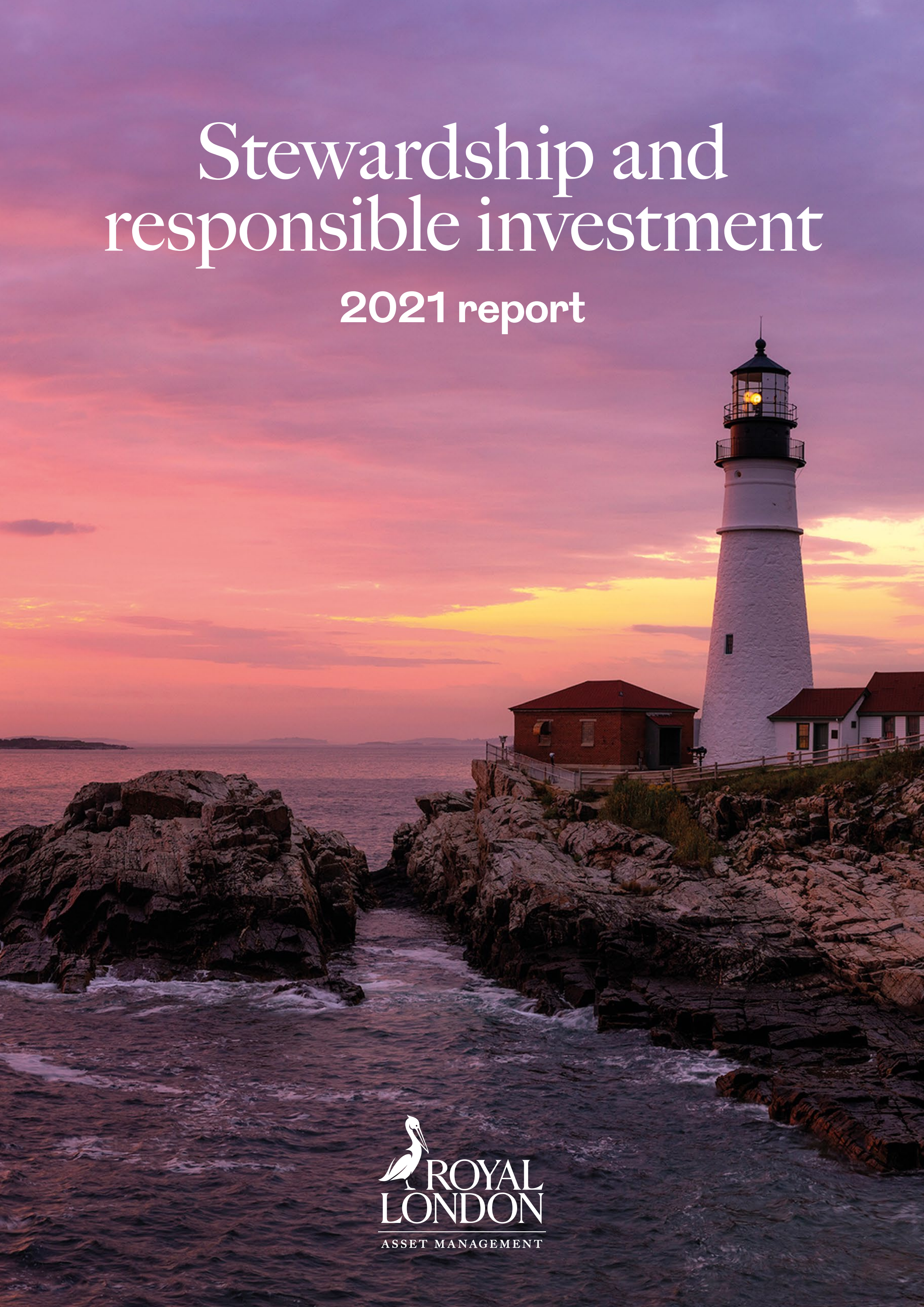
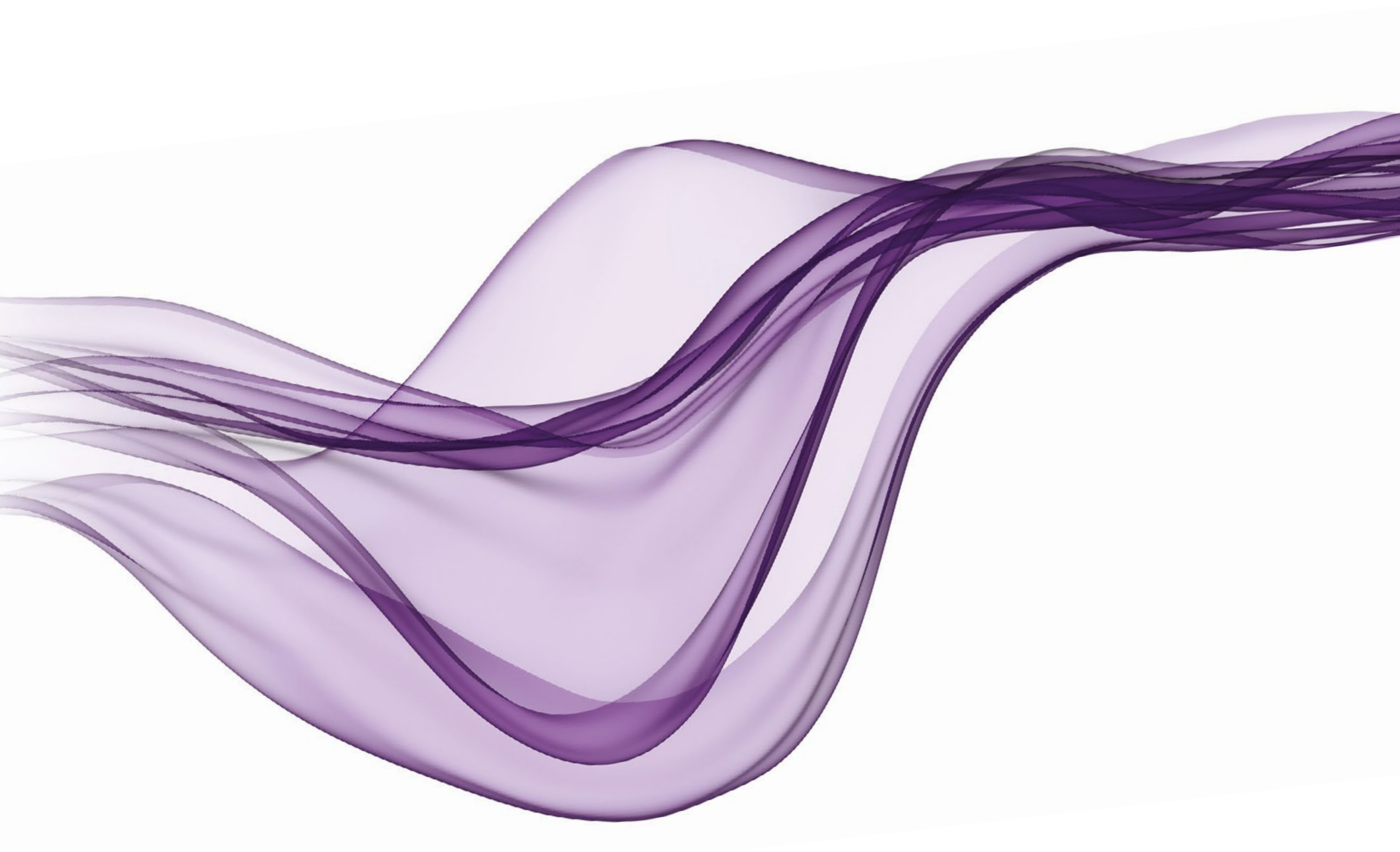
Stewardship and responsible investment

2021 report



ROYAL LONDON
ASSET MANAGEMENT



Contents

Piers Hillier
Chief Investment Officer

> “We engage with the companies we invest in to help them improve their ESG credentials, and it is important that we do the same ourselves.”

Foreword

I am delighted to introduce Royal London Asset Management's (RLAM) Annual Stewardship Report. This report provides an overview of our stewardship and responsible investment activities during 2020.

We first published a Stewardship Report in 2013. At the time, interest in stewardship and responsible investing was relatively subdued, with many seeing this as a 'nice to have' activity. We have long advocated that this is much more fundamental; that investing in a responsible way is the right thing to do, for society and our investors alike, and that integrating responsible investment into the way we manage ourselves and your assets will lead to better returns.

Today it is becoming ever more apparent that this is the case. Arguably the first great shift in our industry was the debate about active and passive; we believe that the second is about the interaction between asset managers (us) and asset owners (you). Asset owners are obviously still interested in returns, but increasingly also looking at using their power as capital owners to bring about change.

It was thought that coronavirus might put responsible investment on the back burner, that we would all have 'bigger things to think about'. But if we look at the tumultuous events of 2020, the pandemic, raging bush fires in Australia and California, Black Lives Matter, we can see that social and environmental issues are now far more prominent in our lives and as such will affect asset prices.

RLAM's approach to responsible investment is multi-layered. We have a Responsible Investment (RI) team, made up of specialists in assessing ESG factors and engaging with companies to try to encourage better management. This team also looks at broader policies such as climate change. However, all of our investment teams look at these factors. In today's world, ignoring or downplaying ESG issues will hurt investor returns. We do manage funds that have explicit ESG-related elements, but every fund we manage now incorporates this approach to some degree.

But responsible investment is not just about fund management. We engage with the companies we invest in to help them improve their ESG credentials, and it is important that we do the same ourselves. Royal London's culture is grounded in our 'Spirit of Royal London' ethos, based on core principles of how we treat colleagues and customers alike. And it's why we made our People Commitment, which looks to build a diverse, skilled workforce, one that helps to create the right conditions to deliver for our clients.

Diversity and inclusion are often seen as a social aim rather than business-related. We disagree. We want to build the best teams and see little point in restricting the potential pool of candidates. We spend a lot of time and resources finding the right people to join our company.

Our approach to stewardship is set out in line with our commitments to the UN supported Principles of Responsible Investment (PRI) and the Stewardship Code of the UK Financial Reporting Council (FRC), and this report is aligned with the provisions of the 2020 Stewardship Code. I hope you find it interesting and informative.

About RLAM

Royal London Asset Management (RLAM) was set up in 1988 as an in-house asset management business for a relatively small mutual life insurance company. The following 30 years have seen both RLAM and its parent enjoy huge success to become significant parts of their relative sectors within the UK financial services industry. Today, RLAM is an integral part of the Royal London Group, the UK's largest mutual life pensions and investment company.

RLAM is a unique asset manager with a mutual ownership structure and managing around £148 billion of assets (as at 31 December 2020). RLAM has a long history of success, delivering key investment strategies in equity, fixed income, property and multi asset for its clients.

Our purpose and strategy

RLAM is an integral part of the Royal London Group, with our direction driven by a shared purpose. **Protecting today, investing in tomorrow. Together we are mutually responsible**. This underpins our strategy to be a growing modern mutual with a focus on delivering for our clients.

For RLAM, delivering for our clients means delivering returns. We believe in the long-term value of active portfolio management, with all of our active strategies drawing on research-led investing, combining the best of top-down and bottom-up analysis when building active portfolios and tailoring this to suit the underlying investment market. We believe that market benchmarks are useful yardsticks rather than a basis for active portfolio construction.

We believe that we need to do more than generate returns, and indeed that generating returns is about more than simply buying and selling assets. We are long-time advocates of the need for asset management firms to be good owners. Environmental, Social and Governance (ESG) issues are increasingly affecting asset prices. We believe that it is in the best interest of our clients for RLAM, where appropriate, to integrate these issues in our investment process with the aim of improving standards, reducing risk and enhancing returns. We believe that this approach enhances returns for our clients, and delivers benefits for our society as a whole.

£148bn AUM
(as at December 2020)

Founded **1988**

We are one of the UK's **leading fund management** companies.

We practise **responsible investment** across fixed income, equities and property.

We are a wholly owned subsidiary of the Royal London Group, **the UK's largest** mutual life pensions and investment company.

Ashley Hamilton Claxton
Head of Responsible Investment

> "We like to focus our intellectual effort on areas less well covered by the market because this is how we add value for clients."

Our approach to stewardship and responsible investment

Amid the unexpected events of last year, 2020 was a watershed moment for responsible investment. I never expected that we would reach the tipping point for responsible investment in the midst of a global pandemic. The emergence of the prolific Black Lives Matter movement, the growing recognition of the social impacts of climate change, and reports of forced labour and internment camps in China are just some of the events of 2020 that highlight the major challenges we face. The social strife, economic stress and global health crisis we have witnessed has brought the message home to many; that our economic, social and environmental lives are so deeply interwoven, that we must think differently about how we invest.

We have seen unprecedented interest from clients in our approach to responsible investing this year. Our clients want to understand how we are working on their behalf to analyse and understand ESG issues, to improve company behaviour, and how we are representing their views and interests when voting or meeting with companies. All clients now expect ESG issues to be integrated into all investment decisions, recognising this can add value and reduce risk. Many clients have made the decision to invest more sustainably, or add sustainable funds onto their buy list, and we've seen record inflows into our sustainable range of funds.

While the spread of the Coronavirus caused worldwide disruption, including the delay of the climate change conference COP26, the world's rising temperatures remains one of the biggest threats to our society. This year RLAM released a standalone climate change policy to inform clients of how we think about climate risk in our investments and operations. We also look forward to publishing our Task Force on Climate-related Financial Disclosures (TCFD) Report in 2021.

We invested heavily in 2020 to improve and enhance our offering to clients. We now have a team of nine responsible investment professionals working alongside our investment teams and supporting our client teams. We have bought new data, started to build new systems, and expanded our proxy voting to cover all of our global equity funds. Our engagement activity has expanded to new markets, and we have deepened our research and analysis to focus on the companies and issues that are the most material. We like to focus our intellectual effort on areas less well covered by the market because this is how we add value for clients. For example, we've focused on decarbonisation in 'rolling stock' train companies, the 'just transition' in the energy utility sector, and improving ESG standards in the social housing sector.

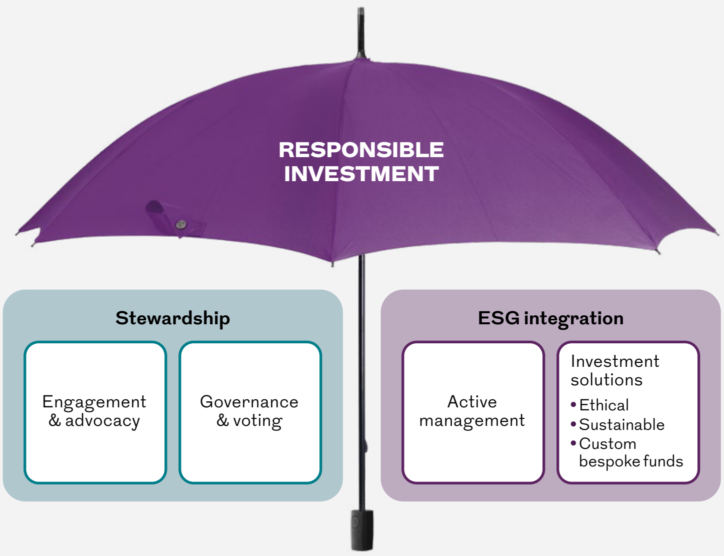
Our longstanding membership of the UN PRI and the FRC's UK Stewardship Code is reflective of our active participation in responsible investment. Our previous Stewardship Code report, published in 2020, was written in adherence with the newest version of the Code, a year before the new standards came in effect.

Appendices III and IV provide an index referencing the alignment between our report and the 2020 Stewardship Code and PRI principles.

Our new company purpose reinforces the value that both RLAM and Royal London places on putting our customers at the heart of what we do, being responsible in how we manage our business and invest our clients' assets. **Protecting today, investing in tomorrow. Together we are mutually responsible.** Our strategy is focused on building financial resilience, promoting long-term savings and strengthening our responsible business activity because we believe this will deliver better value and service for our customers and clients.

Figure 1: RLAM's approach

'Responsible investment' is the umbrella term for our approach to ESG integration and stewardship, which covers all of our investment teams, strategies and funds.



2020 highlights

Awarded A+ by PRI in strategy and governance

59% increase on engagement activity (35% collaborative engagements)

Procured new data and initiated the build of our ESG dashboard

Amplified **social engagement** strategy

85% increase in proxy voting activity

Published standalone **RI policy**

Introduced firm-wide **controversial weapons policy**

Published standalone **climate risk policy**

Published Stewardship Code Report in line with 2020 UK Stewardship Code, **one year ahead** of official release

Launch of new **Group-wide Purpose**

Our investment beliefs

As a member-owned organisation, our investment philosophy is centred on our customers and clients – our **FOCUS**.

Financial outcomes

By working with our clients to understand their needs and expectations, we create strategies that seek to meet their objectives and deliver optimal outcomes, whether that is a tailor-made solution or a fund that is part of their overall investment strategy.

Opportunity orientated

We use our understanding of investment markets to focus on areas where we believe there are opportunities to enhance returns. We use a combination of active and passive solutions to exploit these.

Client-centric risk management

We aim to provide the appropriate mix of risk and return to suit client needs and look to exploit opportunities where risk is being mispriced by the market. Diversification is a powerful risk management tool, but is used for a purpose rather than seen as a goal in its own right.

Unconstrained thinking

We believe in research-led investing – combining the best of top-down and bottom-up analysis when building active portfolios and tailoring this to suit the underlying investment market. We believe that market benchmarks are useful yardsticks rather than a basis for active portfolio construction.

Stewardship and responsible investment

Good investors are good owners. Environmental, social and governance issues are increasingly affecting asset prices. We believe that it is in the best interest of our clients for RLAM, where appropriate, to integrate these issues in our investment process with the aim of improving standards, reducing risk and enhancing returns.

Our commitments

Our FOCUS investment philosophy underpins RLAM's commitment to being a responsible investor. We practise good stewardship of our clients' assets and promote responsible investment and good governance across all of our asset classes. With the support of our responsible investment experts, we empower fund managers and analysts to understand and integrate ESG risks and opportunities into the investment process in order to support and enhance risk-adjusted returns. We engage with the companies we own and pride ourselves on taking an active approach to corporate governance and proxy voting. We often provide thought leadership on important ESG issues and speak publicly where necessary. We disclose our voting record and write to companies in our active funds to explain our voting rationale when we vote against management.

In 2008, RLAM became a signatory to the United Nations supported PRI and in 2020, we scored A+ for Strategy and Governance, up from our 2019 A-rating. In addition, we uplifted our scores to A+ in the Listed Equity – Incorporation, and Fixed Income – Corporate Non-financial modules. These scores are a testament to our continued efforts to become leading in responsible investment. We are engaging with the PRI to understand the current changes to its methodology and how we might need to adapt our practices to capture the required information according to these changes going forwards.

UK Stewardship Code

For a long time, we have been a tier one signatory of the 2016 UK Stewardship Code. That is why we wanted to be early adopters of the 2020 UK Stewardship Code, following its release in October 2019. After implementing the new reporting standards set by the FRC in our 2020 Stewardship report, a year earlier than required, we received highly positive feedback from the FRC and were featured as examples of best practice throughout the FRC's Review of Early Reporting.

Figure 2: Our UN PRI scores

PRI Module	RLAM 2019	RLAM 2020	PRI Median 2020
Strategy & governance	A	**A+**	A
Listed equity – incorporation	A	**A+**	A
Listed equity – active ownership	A	**A**	B
Fixed income – SSA	A	**A**	B
Fixed income – corporate financial	A	**A**	B
Fixed income – corporate non-financial	A	**A+**	B
Fixed income – securitised	A	**A**	B
Property	A	**A**	B

Source: UN PRI assessment report

COVID-19 and calls for a sustainable recovery

As lockdown easing measures began to take hold in the UK, following the events that disrupted life as we knew it, we saw a shift in focus that urged companies and governments to look beyond emergency action in response to the Coronavirus outbreak, towards long-term solutions that integrate environmental and social imperatives rather than just returning to the status quo. The 'Build Back Better' campaign was an example of a movement gaining increasing traction globally, as several stakeholder groups publicly expressed their concerns that the incentive for a just and sustainable recovery could be overlooked amid the urgency of economic growth. The values of the campaign had, at the time, been acknowledged and supported by the UK Prime Minister in a formal address to fellow world leaders.

While we of course recognised the need to tackle the immediate effects of this global pandemic, we believed that decisions made should also consider the longer-term impacts on existing and future environmental and social risks to prevent looming, similar crises. Hence it was essential that commitments to reduce the impacts of climate change for example, one of the biggest threats to our environment and society, were not lost despite the delay of the COP26 summit.

In the summer of 2020, Royal London pledged to maintain focus on long-term outcomes and being advocates for positive change. At RLAM, this means further leveraging our position to urge company boards to be proactive in managing and leading on ESG opportunities and risks. Comprehensive governance measures and exemplary leadership are what we will continue to look for when analysing companies' activity in the aftermath of the pandemic.

We believe that the pandemic presented somewhat of a blank canvas to aid the rebuilding of the economy in pursuit of a renewed vision. Targets set should be ambitious if we are to effectively mitigate the risk arising from climate change and social exclusion in the wake of COVID-19. Performance over the coming months and years will reveal how decisions made in 2020 have taken hold, which will be crucial in shaping our investment decision making.

Our commitment to a sustainable recovery

In the midst of the current global pandemic, we recognise that governments and companies are taking difficult decisions and that, in the wake of this crisis, they may rethink their long-term strategies. We encourage governments and companies to weigh economic, social and environmental imperatives in their analysis. We argue that it remains crucial to avoid unnecessary environmental and social costs and to retain a focus on longer-term sustainable economic recovery.

RLAM, as stewards of our clients' assets, remain focused on the long-term value creation of the companies that we invest in on behalf of our clients. We will continue to analyse the social and environmental impact of companies' decisions, while recognising that for many companies at this time, the global pandemic is their most pressing challenge.

We will fulfil our fiduciary duties as stewards of our clients' capital and encourage sustainable economic recovery by:

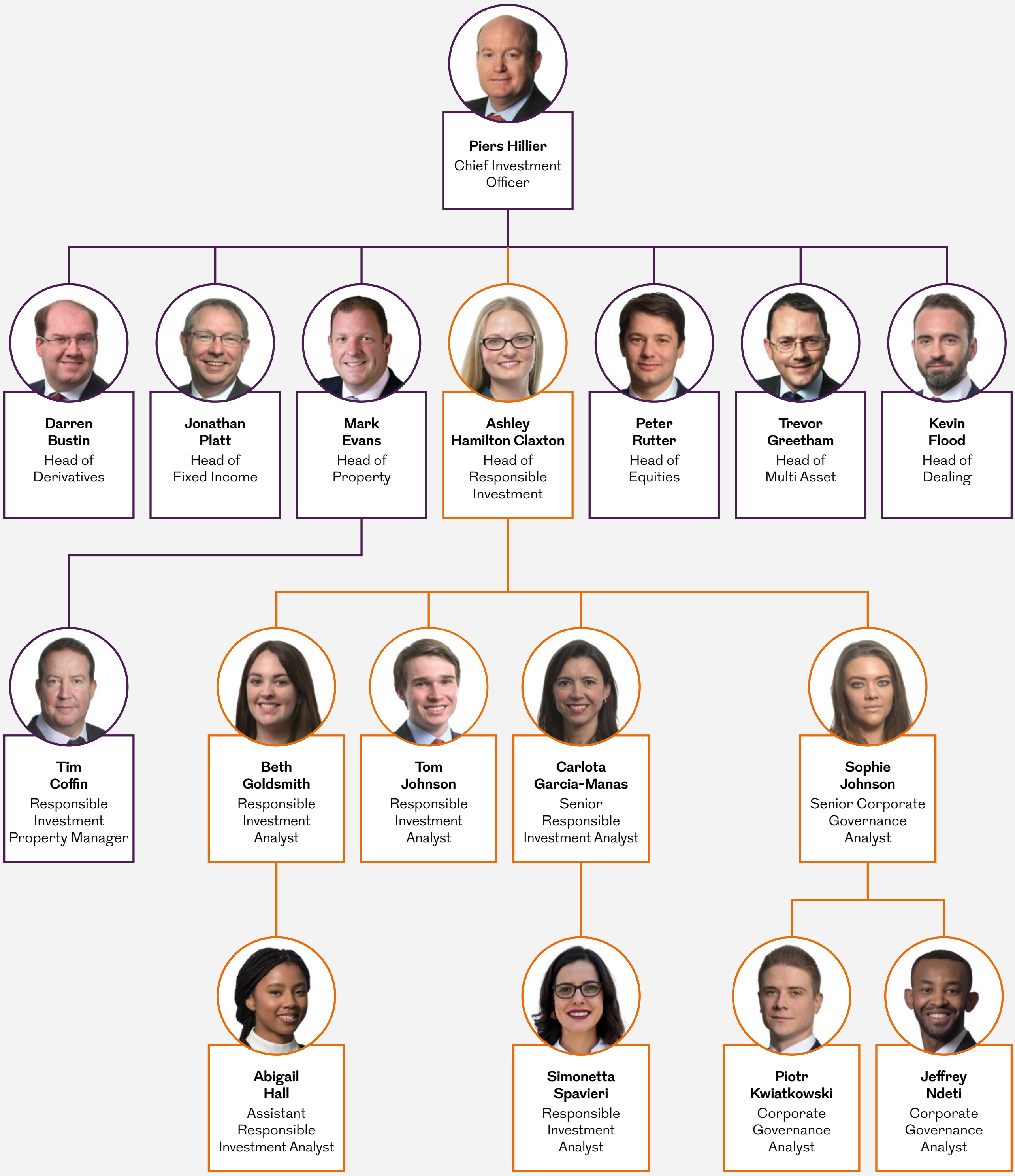
- Continuing to advocate that sustainable business is good business and in the long-term interests of our clients. We will look at public policy interventions and corporate activity through this lens.
- Integrating environmental and social factors into our investment decisions as we believe this can lead to better investment decisions and risk management in our portfolios.
- Using our voting and engagement capabilities to support and where necessary urge company boards to be proactive in managing and leading on ESG opportunities and risks, including those exacerbated by the pandemic, given the potential benefits of this to companies and to the long-term returns investors expect from a more sustainable world economy.
- Encouraging ever greater disclosure and transparency from companies on their contribution to a sustainable economic recovery given the value of this to our clients and the society as a whole.

Our RI team

In 2020, our RI team grew to become a team of nine governance and responsible investment experts. The team is a dedicated resource for implementing our stewardship and responsible investment activity by supporting front office teams to integrate material ESG research into the investment process. The team is led by the Head of Responsible Investment who reports to the Chief Investment Officer and is a member of the Front Office leadership team. The RI team have daily interactions with equity and fixed income fund managers and credit analysts, both on security specific issues and on broader thematic or strategic ESG issues, or company engagement projects.

All senior members of the RI team are certified under the Financial Conduct Authority's (FCA) Senior Management Certification Regime (SMCR). Our RI team members bring a wide variety of experience and diversity to RLAM, something which we feel is important for the strong performance of any team. You can read more about the RI team's experience in the biographies on page 78.

Figure 3: Organisation chart



RI team values

Here is how the RI team lives the Spirit of Royal London values:

We are trustworthy

We build trust with members and clients by being good stewards of their assets and by being willing to speak up on their behalf. We pride ourselves on being consistent and fair in our approach to voting, advocacy and company engagement.

We achieve

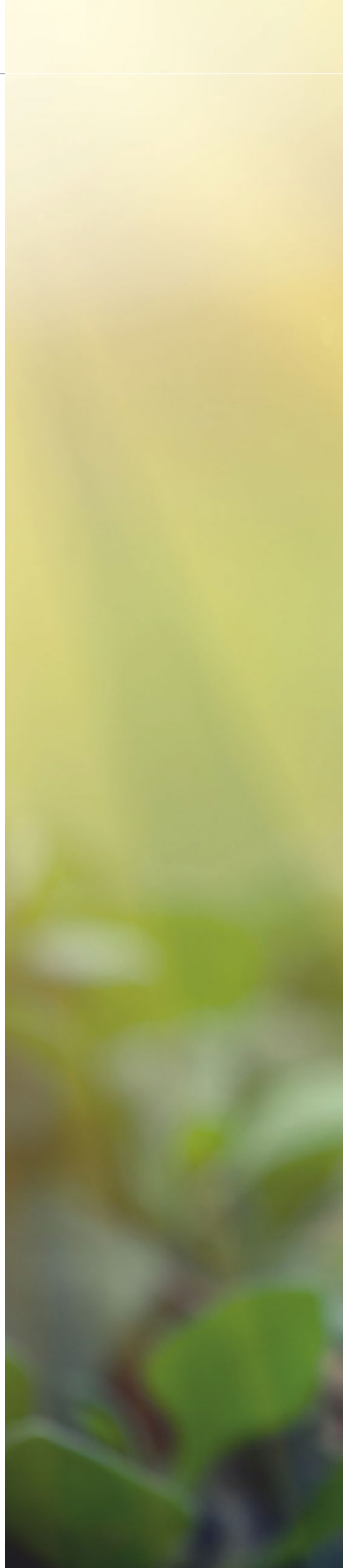
We are focused in our company engagement approach, seeking to prioritise the issues where we can genuinely engage and make a positive contribution. We do not sign up to a large number of initiatives or collective letters, rather we are selective in what we choose to undertake. What we choose to do, we do well.

We collaborate

Voting and engagement is a collaboration between fund managers, analysts and responsible investment experts. We do not view this as a tick-box exercise, but rather a fundamental aspect of our investment approach. Efforts are led and coordinated by the RI team ensuring that RLAM has a consistent message and all stakeholder views are taken into account.

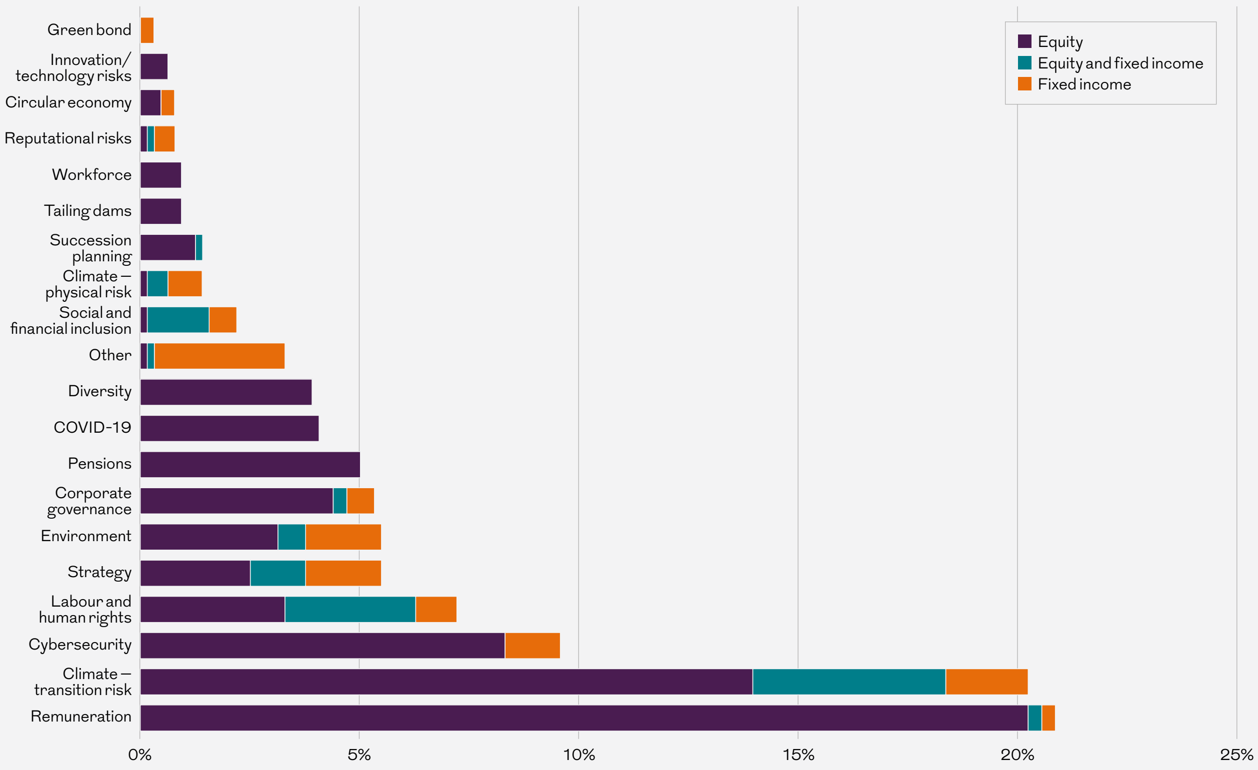
We are empowered

Our analysts are empowered to take a nuanced view of governance issues and voting. We do not adhere to strict voting guidelines or external recommendations; we are cognisant of each company's unique circumstances and approach. Our analysts are encouraged to bring any and all relevant issues to fund managers' attention in both formal and informal ways, and speak up whenever there are ESG concerns, and conduct company engagement.

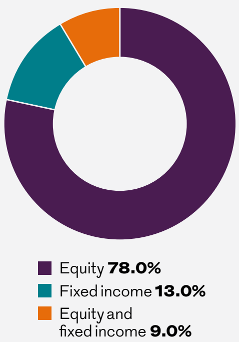


2020 engagement activity

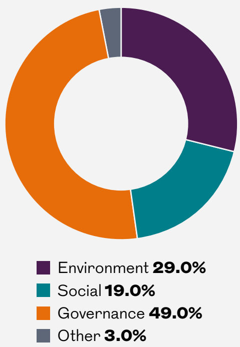
Engagement by asset class



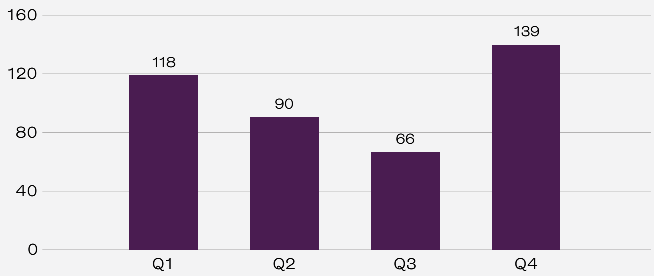
Asset split*



ESG split*



Engagements per quarter



* Figures are subject to rounding and therefore totals may not always equal 100%.

Carlota Garcia-Manas
Responsible Investment Analyst

> "Engagement with investee companies is an activity that many of our clients have come to expect from us as a long-term asset manager."

Engagement and advocacy

2020 engagement activity

In 2020, our RI team engaged with over 200 companies on a total of 413 occasions. Our engagement spanned across a number of topics, notably on matters related to remuneration, climate transition risk and cyber security. Over the year, we observed a significant uplift in engagements compared with activity in 2019, specifically collaborative engagements. We also noted an enhanced focus on social engagements as can be seen in the engagement activity charts.

Our approach to engagement

Engagement with investee companies on strategic, governance, environmental and social risk management issues forms a core part of our stewardship responsibilities. It is an activity that many of our clients have come to expect from us as a long-term asset manager. Engagement may also be used as a tool to help us select and monitor companies in our funds, and to improve their behaviour and performance over time.

We take the view that good company engagement has a positive cumulative effect. It is through successive meetings with either management and/or the board that we can build a better understanding of the direction of travel, discuss our perspective with them, and hopefully build a mutually beneficial relationship. Our ultimate goal is to have a positive influence on corporate behaviour and assist companies with improving internal practices, governance and oversight, and their impact on society and the environment.

Setting engagement priorities

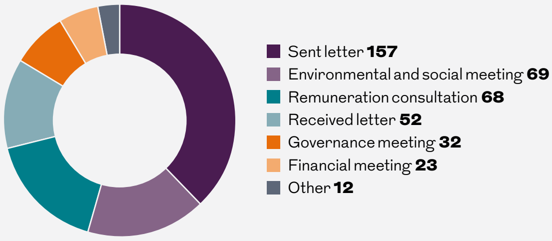
Choosing which topics and companies to prioritise for engagement can be a challenge, because we are faced with an ever-growing list of ESG issues and company requests. In order to achieve the best outcomes for our clients, we have to focus our time and attention on the topics that are most material to our investments and can therefore have the most impact on environmental and social outcomes.

We engage with companies on both a reactive and proactive basis. Our reactive engagement is largely driven by market events such as rights issues or breach of covenants, or governance issues, like remuneration consultations or board changes. It is also driven by company announcements, ESG risk events or company requests. Under these circumstances, we endeavour to respond to as many of these engagement requests as we can; but on occasion, we must prioritise either by the size of our holding or the severity of our concerns.

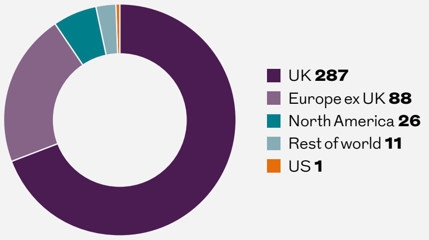
We undertake a full review of our engagement themes every two years in order to amend or set new priority areas. This process is led by the RI team and involves extensive consultations with fund managers, responsible investment analysts, clients and other stakeholders. In 2019, we assessed our portfolio exposures, reviewed academic evidence on engagement, and surveyed external research on new and emerging issues and risks which produced a long list of topics. Of these topics, we selected six themes that we felt were most material to our holdings, fit with our company's culture and values, were of importance to our clients, and represented significant

2020 engagement activity

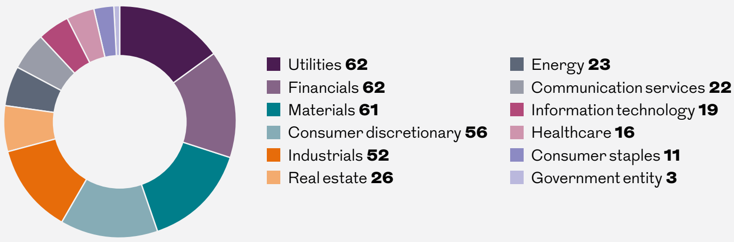
Engagement by type



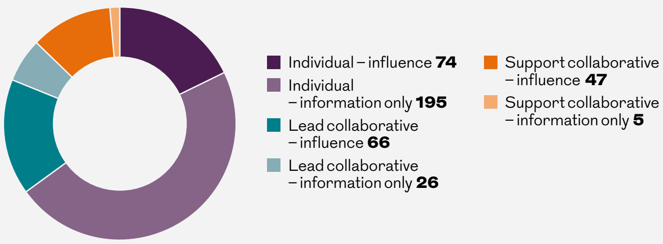
Engagement by geographical region



Engagement by sector



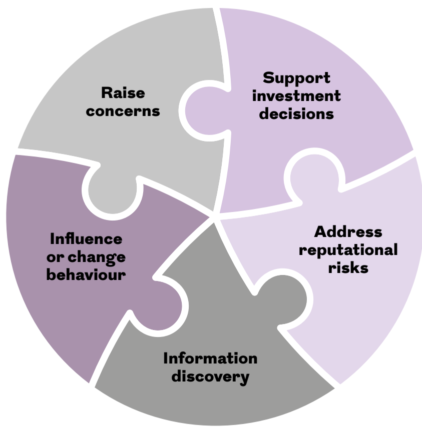
Collaborative engagement



exposure to reputational, operational or financial risks. Our upcoming 2021 review will consider the same factors.

Scope and process

Our engagement spans both equity and fixed income funds because we think good stewardship should be applied regardless of asset class. This requirement is now included in the 2020 UK Stewardship Code and is understood as global best practice. Engagement should serve a clear purpose, meet the needs of our clients, and have clear outcomes. For us, the purpose of engagement is summarised in this graphic:



Engagement criteria

Our engagement topics must meet the following criteria:

- Meet the needs and expectations of clients
- Material and relevant to investment decisions
- Has the potential to impact corporate ESG or financial performance or reduce risk
- Raises best practice standards within a sector or market
- Adds value in advancing thought-leadership and good governance
- Address a principle adverse ESG impact

Opportunities to engage with a company on a topic are reviewed by the RI team in consultation with RLAM's fund managers. New opportunities for engagement arise through a variety of sources, including from internal ESG research or portfolio reviews, client requests, fund manager queries, regulation or company requests. We apply the following filter process when choosing whether and how we engage with companies:

1. Is there a potential material financial or ESG impact?
2. Do we have a significant holding?
3. Is there a significant reputational risk?
4. Does it fit with our engagement themes?

New engagement projects or requests to sign joint letters or public initiatives are approved by the Head of Responsible Investment to ensure it meets our stewardship and responsible investment strategy. We select the companies we engage with based on:

- Evidence of poor performance (or outperformance) on ESG issues relative to peers
- Evidence of ESG risk that has the potential to cause value destruction or significantly affect the reputation of the company or of RLAM and its clients
- Size and nature of any principal adverse impacts
- Percentage of gross exposure within our holdings
- Percentage of the outstanding shares or bonds held by RLAM relative to other companies
- Fund manager or client recommendations

Engagement can take two forms:

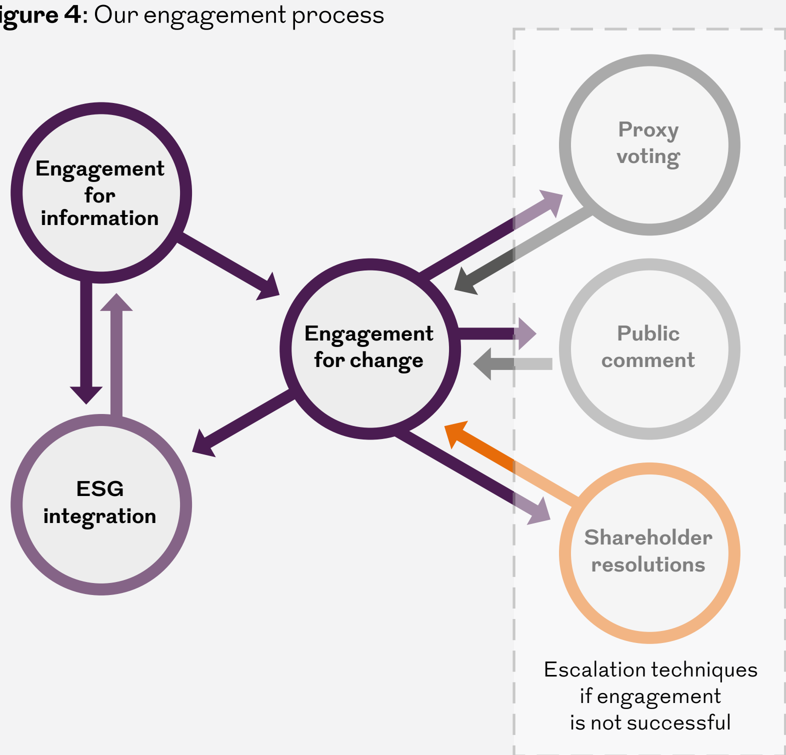
Information discovery: engagements that seek to uncover additional information about company practices, or to identify the need to change or influence behaviour. This type of engagement is less intensive and designed to feed information back into our investment, voting and engagement activities in a dynamic and nimble way.

Change and influence: engagements that seek to influence company decisions and change behaviour. These engagements are resource intensive, time-consuming and can take place over months or years, but may lead to significant changes to company behaviour and ultimately better customer outcomes.

We believe both types of engagement are crucial to being a good steward of our clients' assets.

Figure 4 summarises our engagement process.

Figure 4: Our engagement process



Escalation and public comments

Should we feel that an issue has not been sufficiently addressed by management, we will seek a meeting with the Chairman, Senior Independent Director or other senior executives as appropriate. We may also translate our concerns into votes against relevant directors or other management proposals at the next annual or general meeting. In some instances, when the issue so warrants, we may file or co-file a shareholder resolution.

We will on occasions attend (and speak at) a company Annual General Meeting (AGM), or escalate our concerns to other institutional investors who we believe may share our views (see investor collaboration). We may also voice our concerns through public statements, where we feel the issue is significantly grave enough to warrant this action, or where the company has been unresponsive or has not made sufficient progress on an issue. We will respond to press enquiries where appropriate and use public comments as a tool for improving stewardship and good governance.

We will utilise the full range of tools at our disposal if we judge that value is or may be undermined, while ensuring we are always acting in the best long-term interests of our clients.

Investor collaboration

While as an active asset manager, the majority of our engagements are one-to-one, we understand the need to sometimes work together with others to be more effective in influencing company behaviour. We therefore evaluate the benefits of collaborative engagement on a case-by-case basis.

We favour collaborative engagement with other shareholders when:

- A company has been unresponsive to private engagement, or where the actions of the company are not sufficient to address our concerns.
- The situation is of sufficient seriousness that progression to a collective meeting is appropriate.
- Where partnering with a larger shareholder or bondholder would facilitate greater access to management or the board or provide us with greater ability to influence.
- It is in a jurisdiction where local partners may enhance our ability to engage through their physical presence and/or understanding of local practices.

We leverage our membership with the following organisations to be active in collaborative engagements:

- Principles for Responsible Investment
- Climate Action 100+
- Global Real Estate Sustainability Benchmark (GRESB)
- Institutional Investors Group on Climate Change (IIGCC)
- UK Sustainable Investment Forum (UKSIF)
- 30% Club Investor Group
- Investment Association (IA), Responsible Investment, Stewardship and Climate committees

Advocacy and public policy

As part of our commitment to being a responsible investor, we will engage with regulators, governments, standard-setters and NGOs to advance good governance and responsible investment. This includes providing responses to consultation requests, surveys, and meeting with regulators or others to express concerns or support for policies and practices in relation to good governance. The majority of our public policy work is currently focused in the UK where we have the greatest asset exposure, but we may undertake advocacy in other markets where it is considered important for our clients or material to our investments.

We will also commit our time and expertise as advisors to trade associations or bodies that advocate good stewardship practices, such as the PRI, the IA, the FRC, Climate Financial Risk Forum (CFRF), Institutional Investors Group for Climate Change, and the Investor Roundtable for Tailings Dams. As members of CA100+, we participated in the IIGCC's Portfolio Alignment initiative.

RLAM signed the United Nations Principles for Responsible Investment's (UNPRI's) Just Transition institutional investor statement in 2019, and in 2020 joined the Financing a Just Transition Alliance, an initiative led by The London School of Economics (LSE) to encourage practical steps for companies to connect climate action with positive social impact in the run-up to COP26. The government-backed alliance brings together banks, investors and other stakeholders in the UK, to build on the growing momentum for a just transition.

Our engagement priorities 2019-2021

In 2020, our engagement activity has focused around our six thematic priorities defined by our 2019 consultation. We intend to continue our engagement on these priorities into 2021.

Climate risk

The climate is changing. Companies need to prepare for the energy transition and physical impacts of climate change.

Governance

Checks and balances. Successful companies need strong boards, appropriate pay, and be accountable to their stakeholders

Circular economy

Reduce, reuse, and recycle. Companies need to be designing products and processes of the future that don't hurt our planet.

Innovation, technology & society

Technology is advancing, jobs are changing. Companies need to be cyber resilient, tech-savvy, and responsible users of data.

Diversity

Avoid group-think. Diverse companies are more innovative and create better outcomes for customers.

Social & financial inclusion

Leave no one behind. Companies succeed when everyone has an opportunity to participate and be a productive member of society.

Climate risk

Data & insights

During 2020, RLAM acquired additional climate change data through an expanded number of data providers as part of our broader ESG ambitions. We have long been critics of the quality of carbon and climate data for fixed income, as current existing third party data is not adequate in our view. This year, we have taken the step to create our own proprietary carbon data for fixed income. This has dramatically increased the data coverage for a typical RLAM fund from approximately 50% to over 85%. These expanded and better quality data sets are giving us new and varied insights into the climate risk within our holdings and portfolios, enabling us to make better investment decisions and target our company engagement more effectively.

We are also in the process of developing a climate transition risk framework that amalgamates external data providers' data with RLAM proprietary metrics, and provides an overall climate score for each issuer. This includes three sub-scores showing the company's exposure to climate transition risk, its ability to transition to a low carbon business and its willingness to do so.

TCFD report

In June 2020, RLAM joined the supporters of the Financial Stability's Board TCFD. We published our first standalone climate policy in late 2020. Our first climate risk report aligned with TCFD recommendations will be published in April 2021 along with our financial results.

In the report, we provide disclosure of RLAM's climate governance, risk management and strategy as well as our exposure to climate risk for equities, corporate fixed income, sovereign bonds and property asset classes. We also provide our first estimations of Paris alignment for equities and corporate fixed income asset classes, which amounts to 39% of our assets under management (AUM), and we disclose preliminary stress-testing of these assets against a backdrop of different climate scenarios.

Following the TCFD and CFRF recommendations, in the report, we detail our climate governance, strategies for integration and risk management for each asset class. You can learn more about this work in our Climate Risk Report.

Climate engagement and advocacy

During 2020, climate change was one of our major engagements. Overall, we engaged 141 times on climate change related risk with 71 companies. We were, and remain, active members of CA100+, IIGCC and in November 2020 joined and supported the launch of the Financing the Just Transition Alliance. In 2020, we have stepped up our advocacy role and in March 2020 we were amongst the first to call for 'Green' to be embedded in the COVID-19 stimulus packages. We also joined the CFRF Disclosure working group.

This year we initiated an engagement programme to improve climate disclosure of several US companies we hold in our Global Equity funds. We advanced our long-term engagement with the utilities sector in the UK, scrutinising their net zero plans and promoting a Just Transition agenda in the sector. In the power utilities sector we are also actively contributing to accelerating the transition through our leading role in IIGCC and by engaging with the UK regulator OFGEM. For more information about our activity in the sector read our blog. Also, you can read more about our work in the engagement section of our TCFD report.

Just Transition

What is the Just Transition?

The concept of the Just Transition aims to ensure that social issues are taken into account in moving to a low carbon economy. Rapid climate action that limits global warming to below 1.5°C prevents the worst human and economic costs of climate change. A just transition ensures this climate action also supports an inclusive economy and avoids exacerbating existing injustices, or creating new ones. In simple terms, ensuring that the people affected are taken into account. The Just Transition was part of the Paris Agreement signed in 2015, requesting world leaders to consider the social implications of the energy transition.

Why are we involved?

RLAM is a large investor in the energy utilities sector, which brings power and energy into our homes and workplaces. The sector has a critical role in decarbonising the economy by shifting towards green electrification and away from fossil fuels. There are real risks of social backlash to the energy transition, which may deter it from happening or significantly slow the pace of change. The transition could lead to job losses and further increases in electricity costs before they begin to fall, with an expected addition of over £100 by 2030 to the average annual energy bill for a typical household. Companies who acknowledge this challenge and plan for a Just Transition will be more successful in delivering on their commitment to low-carbon growth. We believe energy utility companies should develop formal Just Transition strategies to manage social risk and ensure they continue to deliver good value for society and their investors. For this reason, we have engaged with the sector with our partner, the Friends Provident Foundation (FPF), since 2018.

What do investors expect companies to do?

A Just Transition strategy for the energy utility sector requires companies to assess the social impact of their decarbonisation plans. Utilities should aim to engage extensively and creatively, bringing the following key stakeholders with them on the journey to net zero in a way that addresses the trade-offs and maximises its benefits.

Workers

- Early engagement and ongoing dialogue with workers and unions.
- Workers reskilling and redeployment, considering increased roles for renewable energy, electrification and digitisation, grid flexibility and demand management, heat decarbonisation, and energy efficiency.
- Provision of good quality new jobs with full adherence to International Labour Organisation (ILO) Core Conventions, e.g. collective bargaining, and improving diversity and inclusion.

Community

- Early engagement ahead of fossil fuel plant closure and community reinvestment.
- Fossil fuel site reuse to maximise retention of good quality jobs and utilise legacy grid infrastructure.
- Partnerships with local authorities and communities, including offering community ownership stakes in new renewable energy generation, and collaborations on local energy markets, demand management, and efficiency.

Supply chain

- Place-based emphasis on suppliers and services for new infrastructure, and seek to add value to communities where they operate.
- Supplier standards covering labour, human rights and sustainability. E.g. adherence to the UN Global Compact and ILO Core Conventions throughout the supply chain.

Consumers

- Energy affordability and fuel poverty alleviation, including energy efficiency and heat decarbonisation, and equitable distribution of system transition costs.
- Support for consumers, including vulnerable groups, to actively participate in the energy transition, including on-site generation, storage, and demand management.

Circular economy

Circular economy is an alternative economic model to the traditional linear model of manufacturing. In particular, it addresses unsustainable trends of increasing production, single-use manufacturing, and poor end-of-life management of materials. A circular economy requires companies to consider the product life cycle and the ways in which products can be reused and repurposed to reduce waste that is harmful to our environment and society. Industries that rely heavily on virgin materials are instrumental in the support for a circular economy and have the potential to shift the world economy to a 1.5-2°C pathway. By adopting a circular economy approach, companies can save on production costs and reduce dependence on external commodities, therefore improving margin stability and minimising energy consumption. Companies leading in circular economy activities are also more likely to be protected from impending regulation and increasing virgin material costs. Technology serves as a key driver of solutions to achieve sustainable development of at-risk industries that focus on recycling and reuse. Our engagement efforts so far have sought to encourage companies to design out the need for virgin components or material and introduce the management of harmful by-products of business operations.

CASE STUDY

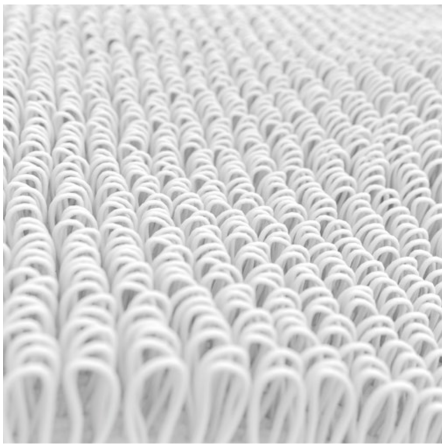
Microfibers

In 2020, we took part in a collaborative engagement programme aiming to assess whether companies are embedding microfiber managing technologies within their products and to encourage the uptake of such solutions in critical sectors.

Microfibers are an unwanted by-product across the global supply chain and within global water systems. The extent of the impact of microfibers is still being researched, though it has already shown signs of increasing death rates when absorbed by humans and wildlife at high levels. In particular, we decided to engage with washing machine manufacturers.

The washing of garments is one of the most common ways microfibers find their way into our water systems. Regulation is beginning to respond to the reality of microfibers and set requirements for washing machine manufacturers. As a result, in 2020 and as part of the collaborative engagement, we took a lead in engaging with Electrolux Professionals to understand how and if they are responding to the microfibers issue within their products. Based on our discussions to date, it is clear that whilst Electrolux don't currently offer products with microfiber solutions, it is an area which they are researching heavily.

Looking ahead, we are intending to continue engaging with Electrolux Professionals with the aim of pushing them to commit to enhancing their strategy on microfibers and will continue to lead the engagement, with the support of other participant Asset Managers.



Diversity

Diversity is core to our corporate engagement strategy, and remains a priority in our wider stewardship efforts. External research supports that both gender and ethnic diversity enhances company performance with findings which show that more ethnic and culturally diverse companies outperform the least diverse companies by 36% in terms of profitability in 2019; slightly up from 33% in 2017 (Mckinsey & Company, 2020). While companies have made some progress on gender diversity, they still lag behind on ethnic diversity and inclusion. At present, almost half of FTSE 100 boards fall short of the Parker Review recommendation to appoint at least one director from an ethnic minority background by 2021. This increases to 70% for FTSE 350 boards. When assessing our top 10 FTSE 350 holdings across RLAM in June 2020, only 20% of holdings met the Parker Review target. A study also revealed that individuals who find themselves at the intersect of under-represented groups (i.e. ethnic minority, female, disabled) experience the most barriers to career progression, demonstrating the human capital imperative for companies to consider the broader scope of diversity.

CASE STUDY

Gender diversity in Japan – collaborative engagement

RLAM led a collaborative engagement effort with fellow members of the 30% Club to request increased gender diversity and female representation on the board of Japanese company Sumitomo Mitsui Financial Group (SMFG).

RLAM is an active member of the 30% Club Investor Group, which is aiming to reach at least 30% representation of all women on all boards and c-suites globally. The Japanese chapter of the 30% Club has a specific target to achieve 10% representation of women on the boards of TOPIX100 companies by 2020 and 30% representation by 2030. SMFG had never been approached by investors to discuss diversity, so this was the first investor dialogue on the issue. SMFG is one of Japan's largest banks with a large consumer finance business and activity in leasing, brokerage and asset management.

SMFG was selected for targeted engagement as it only had one female representative on its board. However, relative to peers in Japan, the company has good corporate governance building blocks that make it feasible to promote gender diversity and to lead change on this ESG issue in the Japanese market. For example, SMFG describes diversity as a factor in its board selection and has good quality disclosure on recruitment and staff rotation by gender.

During the investor meeting, we found the company had no targets for gender representation on the board and deemed the 30% Club aims unrealistic. Their only gender diversity goal is to increase female senior executives, from 10 people (4%) to 20 people (8%) by 2025. We found that recruitment of female employees had decreased sharply because of digitisation trends and reduction of 'clerk' work. SMFG was not aware of any gender-bias in panels or recruitment firms. They did describe a series of sound policies on childcare but acknowledged that men still only take, on average, two days of childcare leave per year. SMFG made positive comments of understanding diversity as a broader issue, including age, race and skill set.

Whilst challenging we found this engagement to have been positive. The company was open to acknowledging the issue and agreed to escalate our concerns to the Chairman of the Board. We will continue to work with other collaborators on a follow-up meeting in 2021 to seek progress on the issue.

CASE STUDY

Ethnic diversity

The aim is to leverage our engagement efforts to improve disclosure in this area as unfortunately we recognise that, unlike gender diversity data, ethnic diversity data and reporting is in its infancy and remains sparse. In the future we hope this will allow for more comparable assessments across industries and sectors.

There are two phases to our engagement with companies on ethnicity; the first phase aims to 'learn from the leaders' and encourage adoption of formal reporting and target setting on ethnic diversity. The second phase seeks to achieve a commitment in line with the UK Parker Review, which requires FTSE 100 and 250 companies to appoint at least one person from an ethnic minority background by 2021 and by 2024 respectively.

In Q3 2020 we rolled out phase one, which saw us engage with companies such as Ocado Group, Essentra and Paragon Banking Group. The companies we spoke to faced common challenges and hurdles, such as the legal constraints around gathering ethnic minority workforce data. A common finding was that communication with employees is key to success. For example, Paragon Banking Group have partnered with various initiatives like The Women's Association (TWA) - a non-profit group focused on the visibility of women in the workplace from various backgrounds, in order to improve on its diversity ambitions. As part of this initiative, Paragon's CEO (Nigel Terrington) was interviewed by one of the young female participants involved in TWA's Executive Challenge programme; this has subsequently been shared online in a refreshing video that aims to inspire others. In other instances, companies showcased some innovative schemes being developed in the pipeline, one of which includes a board apprenticeship programme to give mid to senior executive candidates the board experience they require to become a non-executive director.

We discovered unique and interesting ways in which companies are addressing ethnic minority representation and inclusion within the workforce. In 2021 we aim to build on this knowledge and start phase two of our engagement with companies we have identified as laggards in this area.

Governance

Governance has long been a key part of our engagement efforts. One of the most high profile aspects of this engagement remains executive pay, which as illustrated throughout this report, is integrated into the investment process for our equity funds. We also use our governance engagement to cover a broad range of topics, including how the board is overseeing and managing all ESG risks, both current and future. During 2020, and in light of the significant and exceptional challenges companies faced as a result of the Coronavirus, we have concentrated our engagement efforts on how the board has managed their strategic response to the pandemic. We have particularly focused on the impact of the pandemic on executive and workforce remuneration, workforce engagement, and diversity as outlined earlier in this report.

CASE STUDY

Engagement with the workforce

In common with our ethnic diversity project, there are two phases to our engagement with companies on this topic. The first phase aims to understand best practice. The second phase seeks to identify and engage with laggards, in order to improve practices and disclosure.

There has been a growing recognition that boards must do a better job at understanding and addressing corporate culture and the needs of the workforce as a whole. The requirement for directors to have regard to the interests of the company's employees was already included in Section 172 of the UK Companies Act 2006, but developments in this area in recent years have enhanced it further through the updated UK Corporate Governance Code. Provision five of the Code gives companies the option to choose one or a combination of the following methods of engagement with the workforce: (i) a director appointed from the workforce, (ii) a formal workforce advisory panel, or (iii) a designated non-executive director. Alternatively, companies should explain what other arrangements are in place and why they are considered to be effective.

The FRC's 2020 Annual Review of the UK Corporate Governance Code[1] revealed that, despite progress and wide-ranging reporting in this area, there is still a risk that the conclusions from workforce engagement activities might not always reach the boardroom. The Review was published in early 2020, before the full outbreak of the COVID-19 pandemic. The pandemic, together with the wider events of 2020, convinced us to prioritise our engagement activity in this area, as employees have suffered some of the most severe impacts this year. Our main focus is to ensure the workforce voice and interests are effectively incorporated into board discussions and decision-making.

In Q4 2020, we rolled out phase one alongside our diversity project, which saw us engage with Essentra, Marshalls, Paragon Banking Group, St. Modwen Properties, and Ocado Group.

For example, at Essentra, due to the size of its international network, the company did not appoint just one but two directors responsible for engagement with the workforce. Having both directors present in different geographical locations helps the company to increase the number of workforce engagement meetings, site visits, and gives the employees based in various countries a more equal opportunity to feed back their views to the board. At Paragon Banking Group, the preference was for an advisory forum of employee representatives, instead of a designated director. The idea is to invite different directors to each forum meeting, in order for the employee representatives to be able to engage with all non-executive directors over time.

One of the most important takeaways from the first phase of the project was the insight into how companies deal with the size, location, and representation of their workforce, in order to maintain adequate engagement mechanisms. Using the knowledge and practical examples we have obtained, our aim for next year is to roll out phase two of the project, with a goal of contributing to the push for improved practices in this area at other companies.

CASE STUDY

Remuneration during COVID-19

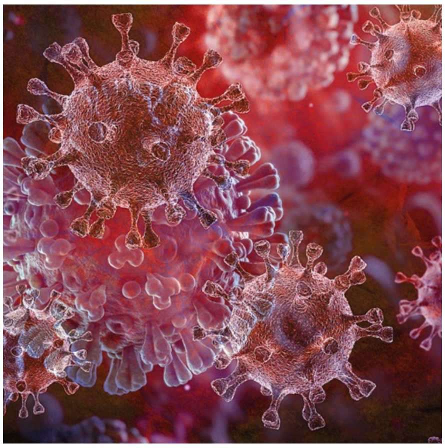
In 2020 with the onset of the global pandemic, remuneration engagement took on a new focus. The calls for increased alignment with the workforce and improvements to existing practices have been circulating for a number of years but really came to the fore over the course of last year. Our engagement aimed to understand what steps companies were taking and to encourage them to fully consider the wider implications of any decisions.

Some of the most positive initial engagement came from companies like Rentokil and Dunelm early on in the pandemic. Board directors and executives took significant salary reductions, bonuses and long-term incentives were suspended and in some cases employee welfare funds were created to help the companies through the first UK lockdown. Later in the year we spoke to these companies again about when and how they planned to reinstate pay. Dunelm again proved to be a positive example when we spoke to them at the end of the summer. As a thank you they provided a small cash bonus to all shop floor staff in recognition of all their hard work re-opening their shops, and for those at head office who would not be receiving their normal bonus, a small share award was made in recognition of their hard work. Another company in the hospitality sector has confidentially consulted with us on similar plans in late 2020/early 2021.

At the other end of the scale, we have spoken to a number of companies who wish to override the formulaic outcomes of their bonus or share awards to ensure that their executives still receive sizable pay-outs despite the negative impact of COVID-19. These situations have proven highly complex with recent financial performance, the use of furlough and treatment of staff being taken into account. In those situations where companies have acted responsibly we are supportive of them rewarding the executives, provided that is reflected in the treatment of their staff. The cases where dividends for shareholders have been cut, redundancies had been made and/or the government furlough scheme has been used to a greater degree we have pushed back, either through our engagement or our voting.

Another emerging trend this year has been companies proposing to change their remuneration structures from a performance based one to something called a Restricted Share Plan (RSP). RSPs generally will provide a greater level of certainty as the value of the award is ultimately down to share price, rather than hitting particular performance conditions. To compensate for this, award levels can be reduced by up to 50%. Whilst most of these conversations remain confidential at the time of writing, our responses to companies have varied. One company, who is highly reliant on the number of people travelling internationally, is understandably struggling to set performance targets and could benefit from this sort of change. Others we have pushed back on, where we do not feel that there is such a degree of difficulty setting targets and we believe the companies should strengthen their proposals.

As with previous years we have had a number of successes and failures in our remuneration engagement this year, but on the whole it has been positive. We have achieved small concessions in areas such as the scale of a proposed award, the minimum financial target used or the addition of an underpin mechanism.



Innovation, technology & society

Technology has become intrinsically linked to the operating structures of modern companies, including the companies held in our investment portfolios. It is our fiduciary duty to mitigate and respond to the potential harm faced by society, and our clients' investments.

Digital disruption has altered the landscape in which businesses and consumers interact. But as companies innovate and change their business models through the use of technology, in search of faster and smarter ways of engaging with their customers, we cannot ignore their exposure to new and emerging threats.

CASE STUDY

Cybersecurity

Cyber-attacks during regional Coronavirus lockdowns rose at an alarming rate, and with a forward-looking trend of increased online usage, we must use our influence to encourage the adoption of preventative action.

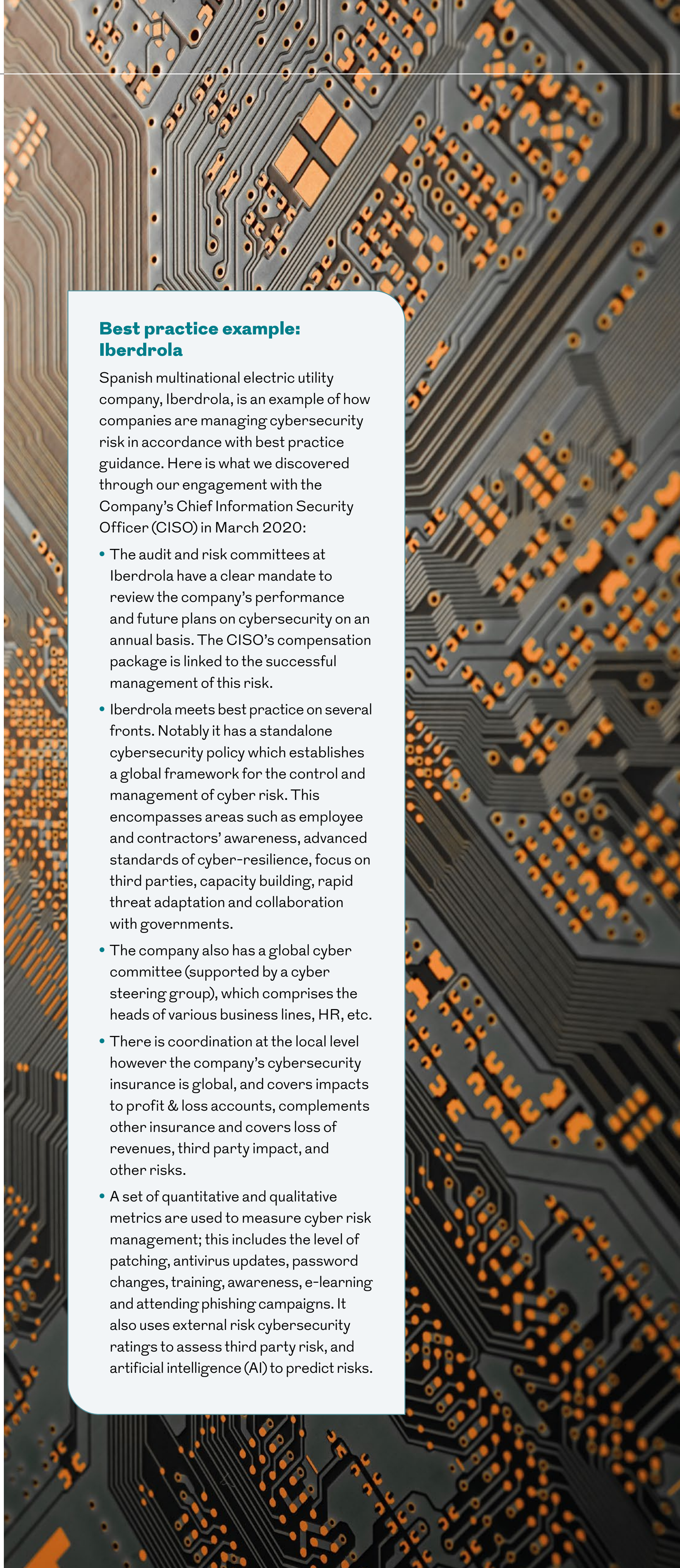
In 2019, the World Economic Forum (WEF) identified cybersecurity as the fifth most likely risk to occur, with the seventh highest impact globally. Cybersecurity poses a significant threat to investors, capital markets and countries alike, a notion we are beginning to see reflected in regulation such as the EU Cybersecurity Act 2019. The impact of cybersecurity was exacerbated not just with the advent of COVID-19 and the increasing exposure to remote working, but also by a massive cyber-attack in the USA which exposed nationally critical industries, government and other companies.

'Technology, Society and Innovation' already forms one of our existing six engagement priorities. And so during the first quarter of 2020, we initiated a collaborative engagement project focused specifically on cybersecurity. We identified 25 companies in our portfolio holdings to contact initially. The large majority of targeted companies were equity holdings and spanned across a number of sectors including healthcare, retail and utilities. Sector distribution was concentrated by design, and in line with the European Cybersecurity Directive's identification of 'at risk' sectors. However, recent company events and breaches also prompted us to include other companies. Over half of the companies we approached responded to our outreach and only one company had declined to engage.

The purpose of our engagement was to understand impending cyber risks faced by the targeted sectors, and to discuss the extent to which the companies' cybersecurity strategies managed this risk. The utilities sector demonstrated the most advanced cybersecurity practices among the companies engaged; an outcome which was highly anticipated on the basis of its National Critical Infrastructure (NCI) status, making the sector subject to tougher regulation. Through our interactions so far, we are establishing a baseline for best practice and disclosure, and are identifying information gaps to agree next steps and areas for improvement.

In some instances, we were asked for recommendations on measures that could be adopted that would align companies with best practice. This demonstrates companies' willingness to improve cybersecurity practices where possible. It was determined that due to the sensitive nature of cybersecurity disclosures, a majority of companies have only partial information published on their websites. One recurrent concern in our discussions was the exposure to cybersecurity risk through third parties. The most robust systems include direct communication of expectations to third parties, vulnerability tests and continuous monitoring, with emphasis on critical relationships and functions.

Overall, we've found the outcome of this engagement to be positive, and companies engaged were generally receptive. Towards the end of 2020, we embarked on phase two of our cybersecurity engagement project, reaching out to a new set of companies in our portfolio operating in sectors deemed as high risk. Our responsible investment analysts will also approach those companies that failed to respond to our outreach in phase one.



Best practice example: Iberdrola

Spanish multinational electric utility company, Iberdrola, is an example of how companies are managing cybersecurity risk in accordance with best practice guidance. Here is what we discovered through our engagement with the Company's Chief Information Security Officer (CISO) in March 2020:

- The audit and risk committees at Iberdrola have a clear mandate to review the company's performance and future plans on cybersecurity on an annual basis. The CISO's compensation package is linked to the successful management of this risk.
- Iberdrola meets best practice on several fronts. Notably it has a standalone cybersecurity policy which establishes a global framework for the control and management of cyber risk. This encompasses areas such as employee and contractors' awareness, advanced standards of cyber-resilience, focus on third parties, capacity building, rapid threat adaptation and collaboration with governments.
- The company also has a global cyber committee (supported by a cyber steering group), which comprises the heads of various business lines, HR, etc.
- There is coordination at the local level however the company's cybersecurity insurance is global, and covers impacts to profit & loss accounts, complements other insurance and covers loss of revenues, third party impact, and other risks.
- A set of quantitative and qualitative metrics are used to measure cyber risk management; this includes the level of patching, antivirus updates, password changes, training, awareness, e-learning and attending phishing campaigns. It also uses external risk cybersecurity ratings to assess third party risk, and artificial intelligence (AI) to predict risks.

Social & financial inclusion

Social and financial inclusion is a wide ranging engagement topic that attempts to encompass any gaps we identify during the course of our work in the way certain groups of people are either expressly or inadvertently excluded. The Just Transition as previously discussed fits into this topic, as could our workforce engagement and diversity case studies. By addressing these gaps companies have the ability to make a positive impact on their public profile, increase their customer base and importantly to make a real difference to people they serve.

CASE STUDY

A just transition for Scottish and Southern Energy (SSE)

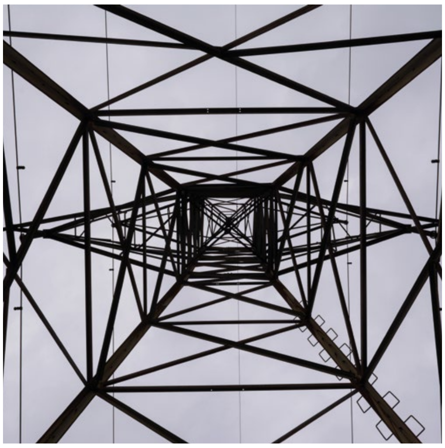
As part of our collaborative engagement with the FPF on net zero and the Just Transition, we met with a number of electric utility companies at the start of 2020, including SSE. SSE is a power generation company and regulated networks business which includes electric and gas distribution and transmission systems.

During our engagement meeting with SSE in the summer of 2020, our responsible investment analysts scrutinised the company's targets and alignment to the UK's 'Net Zero by 2050' commitments. We questioned its assumptions on the role of natural gas, carbon capture, use and storage, hydrogen and energy demand. We also requested details about its contributions to flexibility, storage and demand side response. We discussed the company's strategies to influence public policy, and its views on OFGEM's recent regulatory consultation.

We also proposed that SSE develop a Just Transition strategy and embed it into its decarbonisation plans. SSE welcomed our suggestions and requested we submit a question to the board at the company's upcoming AGM. During the AGM, SSE committed to publishing its strategy by November 2020, alongside mid-year reports, and a statement outlining the company's principles and plans to support a Just Transition.

Now released, SSE's pioneering Just Transition Strategy is the first of its kind in the sector.

We are committed to taking lessons from this engagement and applying it in other contexts. For example, we have leveraged our role as coordinator of the IIGCC Power and Heat Utilities engagement group to produce an investor expectations paper on the utility sector's path to net zero. Learn more about our expectations for the utilities sector on page 23.



Fixed income engagement

Some investors assume that engagement is best left to equity markets, with bondholders merely a passenger on a company's journey. At RLAM, we believe that targeted engagement by bondholders is not just possible, but beneficial to all stakeholders. Whilst our points of influence are more limited in relation to large global companies, our focus on secured debt and more highly covenanted issues gives us greater access to the 'decision makers' and, consequently, allows us to have greater impact both in relation to bond structures and ESG considerations. In addition, we will engage using the full weight of our debt and equity holdings where relevant.

CASE STUDY

Rolling stock leasing companies (ROSCOs)

While the UK economy is relatively advanced in its decarbonisation of power generation, we continue to assess how moves to a lower carbon economy are likely to impact a broader range of sectors. Ideally, our most compelling Fixed income ESG engagement projects share some key characteristics to ensure we target our research efforts as effectively as possible:

1. **Debt specific** – ensuring greater traction and influence with issuers and supplementing a lack of third party research
2. **Material** – focusing on sectors and issuers with the largest potential ESG impact/risk
3. **Enhancing** – creating an ability for information discovery to be reflected in bond selection and pricing and portfolio construction

This engagement framework underpins our rationale for embarking on a new thematic engagement project assessing the impact of decarbonisation on the UK's ROSCOs, who own the majority of the UK's rail fleets. Diesel trains are responsible for over one million tonnes of carbon emissions a year and a recent review has recommended the removal of all diesel-only trains by 2040, and we wanted to understand whether the ROSCOs were prepared for this transition. RLAM therefore wrote to the UK's three largest rolling stock companies, where we have significant credit exposure, in order to understand the approach which each operator was taking. Should certain assets, particularly recent acquired diesel stock, become redundant sooner than current asset lives predict, this could have material credit implications due to the importance of useful economic life to the value of the collateral backing the bonds.

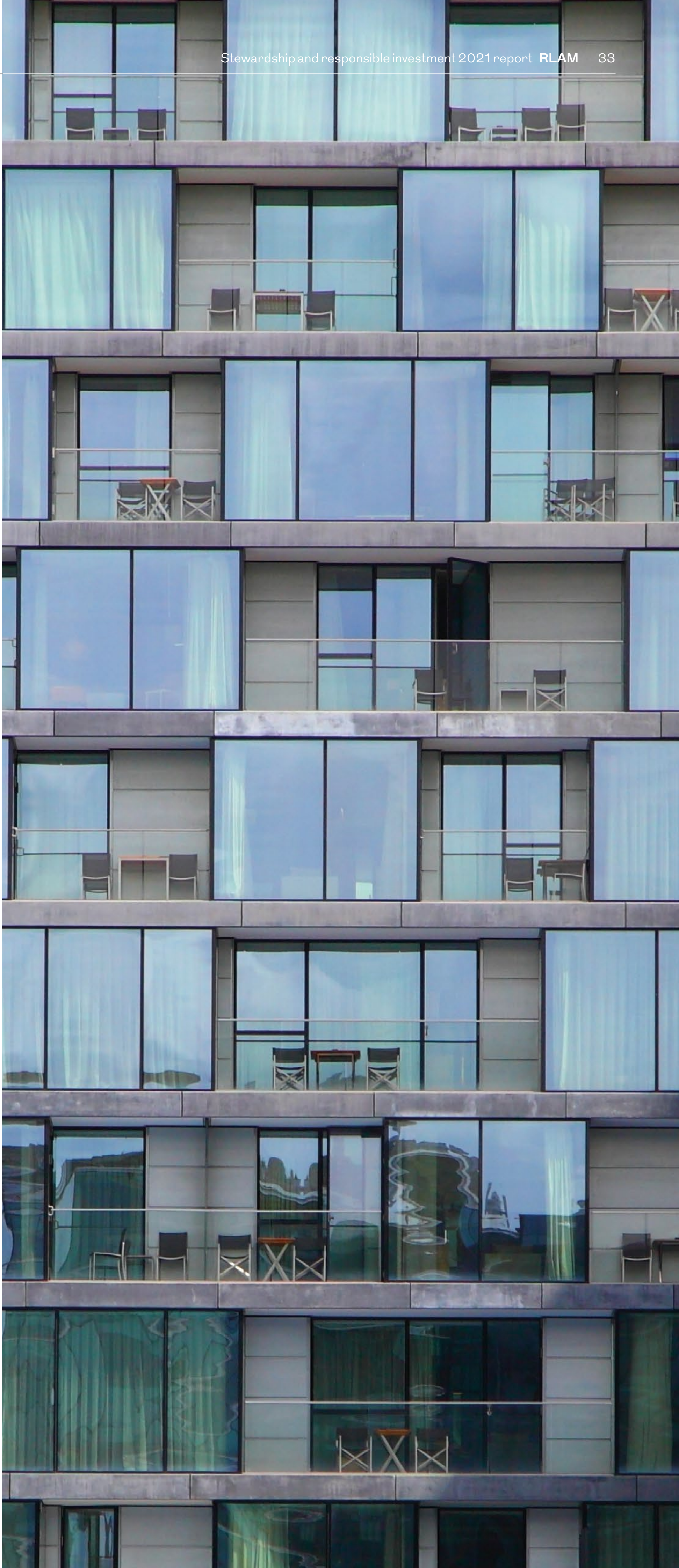
As a wholly privately owned industry, with no public listed equity, this targeted research represents a fantastic opportunity for information discovery, with no 'off the shelf' ESG research available. Our initial discussions have focused both on the role of the existing diesel fleets, each company's approach to investment both in new fleets of trains and re-engineering existing assets, along with the need for further network electrification and the extent to which hybrid technologies might help to decarbonise the rail sector.

CASE STUDY

Housing associations ESG reporting and issuance

We continued to lend to the Housing Association sector despite the near-term sector challenges from COVID-19. Having interacted with a number of issuers, we are generally pleased with both the social and financial reactions from the sector. We were also comforted by the proactivity of the Social Housing Regulator in terms of their oversight of the sector's response to the crisis and their communication with investors and funders. Our funding, which included purchasing secured bonds issued by Optivo, the Midlands based association, and Home Group, whose traditional heartland is more skewed to the north of England, will allow additional affordable housing to be delivered post the 'lockdown' led hiatus of recent months.

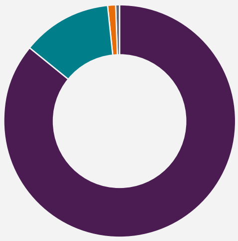
We were also pleased to be invited to comment on the co-ordinated proposals from a number of the larger associations for greater consistency in ESG reporting. Whilst the sector's overarching positive influence on society is extremely clear, there also has to be an acknowledgement that the sector's carbon footprint, as a major landlord of residential property, is substantial. More consistent data provision will help us with our ongoing analysis. In the first instance this aids our monitoring of underlying energy and emission performance and improvement, which feeds into our assessments of collateral quality. More widely, it will also enhance our efforts to create more comprehensive and bespoke portfolio carbon footprints for our clients, across a sector not traditionally captured within third party data sets.



2020 voting activity

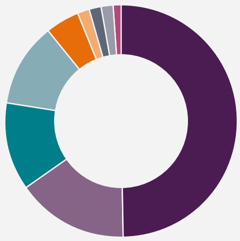
Summary*

Proportion of voting outcomes for all resolutions in 2020



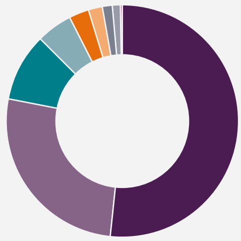
- For **86.1%**
- Against **12.3%**
- Abstain **1.2%**
- Take no action **0.4%**

Votes by category*



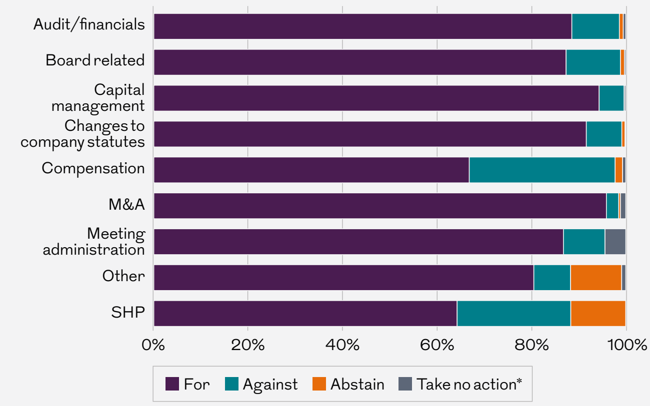
- Board related **50.0%**
- Audit/financials **15.0%**
- Compensation **12.0%**
- Capital management **12.0%**
- Changes to company statutes **4.0%**
- SHP **2.0%**
- Meeting administration **2.0%**
- Other **2.0%**
- M&A **1.0%**

Votes by geographical region*



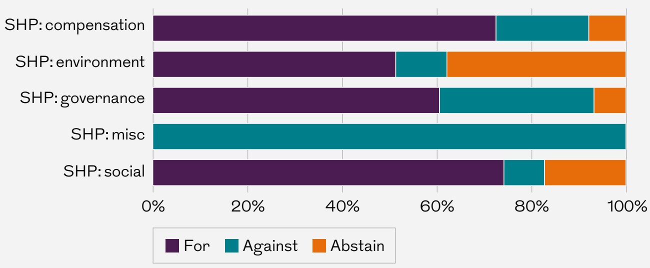
- Europe **51.8%**
- Canada & US **26.4%**
- Asia ex-Japan **9.5%**
- Latin America and Caribbean **5.1%**
- Africa **2.8%**
- Oceania **1.9%**
- Japan **1.3%**
- MENA **1.1%**
- Unknown region **0.1%**

Total voting record



	For	Against	Abstain	Take no action†
Audit/financials	3983	453	37	24
Board related	12628	1665	122	40
Capital management	3230	181	2	10
Changes to company statutes	1206	99	9	2
Compensation	2377	1099	56	24
M&A	257	7	1	3
Meeting administration	434	44	0	22
Other	372	36	50	4
SHP	331	124	60	0

Shareholder proposal votes



	For	Against	Abstain	Take no action†
SHP: compensation	37	10	4	0
SHP: environment	19	4	14	0
SHP: governance	180	97	20	0
SHP: misc	0	2	0	0
SHP: social	95	11	22	0

* Figures are subject to rounding and therefore totals may not always equal 100%.

† Take no action – we endeavour to vote at all meetings other than in markets where voting would result in shareblocking

Sophie Johnson
Senior Corporate Governance Analyst

> "Our voting coverage more than doubled in 2020 to 2,419 meetings across all the markets in which we invest."

Governance and voting

Exercising our voting rights at the companies in which we invest is an important pillar of our stewardship strategy and a way to promote good corporate governance. In 2020, we voted our actively held stocks across our UK, EU, Sustainable and Global equity funds where local market conditions permit. We have also voted all of our passive UK equity holdings for a number of years. During the course of 2020, we added the remainder of RLAM's passive funds to our voting[2].

In January, we started voting our ESG Emerging Markets fund along with our US passive funds, and in October we added our European, Japanese and Asia Pacific passive funds. This has materially increased the coverage of the team, with the number of meetings voted during the year rising from 1,129 in 2019 to 2,419 in 2020. We also vote on our fixed income holdings when the occasion arises as explained further on page 43.

2020 voting activity

RLAM regards every vote as significant for the purposes of SRD II[3], and as such we publically disclose the outcome of all votes on our website in a searchable online database, alongside the rationales for when we vote against management. The following is a high level overview of key votes and our general voting behaviour. We have highlighted those we believe may be of greater interest to our clients due to the subject matter or materiality to the company, and provide an illustration of how we approach a variety of issues when voting. Examples include, but are not exclusively, votes that deal with controversies, diversity, environmental issues, health and safety concerns, shareholder proposals or remuneration.

Proxy voting during a pandemic

2020 did not turn out as any of us expected. Some topics which we were planning to focus on during the year fundamentally changed while others, perhaps unexpectedly given the circumstances, did not. The main proxy voting season coincided with the first UK lockdown, and topics we mentioned in our previous report such as executive pensions, were no longer at the forefront of people's minds. Rather than approving changes in remuneration policies we were seeing companies put their plans on hold, postpone AGMs, forego salaries and suspend bonuses; with everyone unable to plan for the long-term. This made for an interesting, complex, unpredictable, but in some ways quiet voting season, as companies (for the most part) took sensible steps, postponed long-term decisions and there were fewer governance controversies than we've seen in the past.

Diversity, which was always going to be a focus for us in 2020, was thrown into sharp focus by the disproportionate impact the pandemic was (and unfortunately still is) having on people of minority ethnic and disadvantaged backgrounds, and by the re-energising of the Black Lives Matter movement following the death of George Floyd in the USA. While it was too late for many of these events to directly impact our voting this year, which is concentrated in April and May, it has fed into our plans for 2021 and has provoked a shift in the way we all think about and approach social factors when casting our vote.

The enormous strain put on companies trying to survive the economic fallout of the successive global lockdowns has led to succession planning strategies being put on hold and remuneration plans scaled back or cancelled. Many investors, including RLAM, have had to relax some of our previous positions and give companies the space this year to ride out the storm. Wherever possible, we have voted in line with our principles, holding companies to account while accounting for these extraordinary external factors where appropriate, and placing ever more emphasis on engagement. What follows are examples of how we have voted during 2020, providing an illustration of how this has worked in practice.

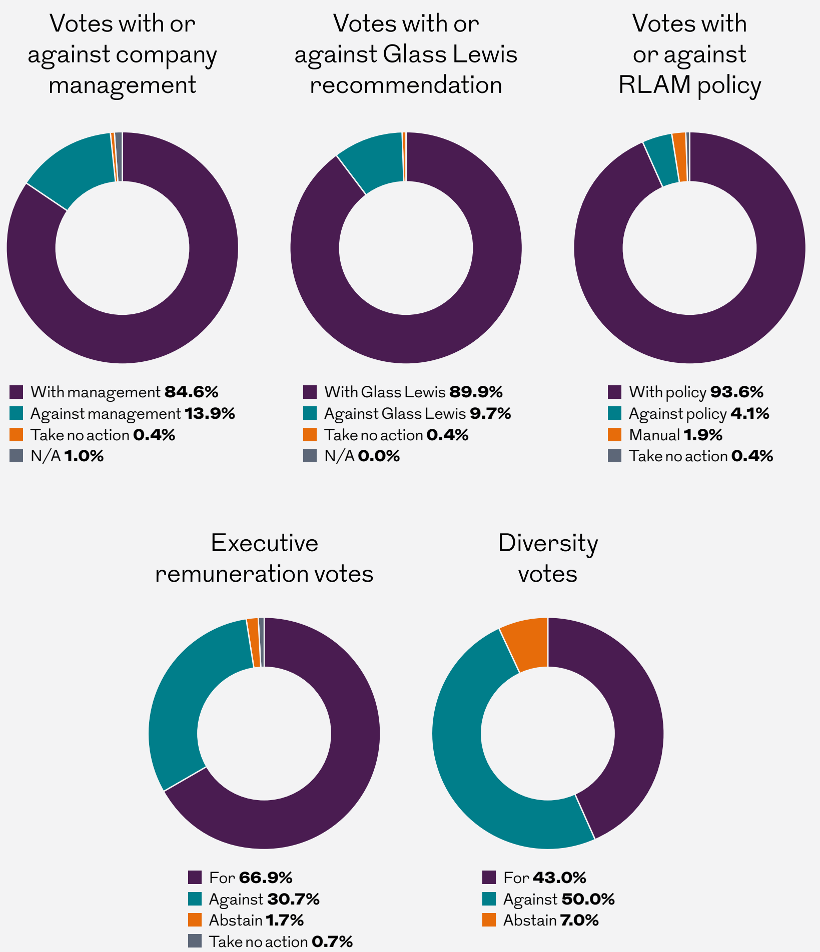
Sophie Johnson – Senior Corporate Governance Analyst

Executive remuneration

As our voting activity has expanded further into global markets we have adapted and refined our approach to suit each of these markets. Our aim as always is to uphold best practice and push for improvements, while remaining cognisant of the particular issues and circumstances for each company.

A large percentage of our active equity assets remain in UK listed companies, where we as a UK business have greater ability to engage and influence company behaviour. As such we focus our efforts around reviewing the executive remuneration of these companies, whether they are large or small, main market or AIM listed. During 2020, we voted against or abstained on remuneration on 221 out of a possible 731 times at 524 companies in the UK; or 30% of the time. We wrote to these companies in advance of AGMs to express our concerns with the remuneration report and/or policy and offered to engage with them further. Globally, including the UK, we voted against or abstained on 1155 out of a possible 3556 times, or 32% of the time on remuneration. We will also send letters to some of these companies if our holding is material or our concern sufficiently serious. When voting on remuneration proposals, we carefully consider outcomes of any engagement with the board. While we strive to maintain a consistent message from year to year, where a company has made meaningful progress on a pay issue, we will often change our vote to Abstain or For in recognition of the willingness to change and improve over time.

2020 voting activity



Figures are subject to rounding and therefore totals may not always equal 100%.

Diversity

As part of our work promoting diversity both in the boardroom and throughout the wider workforce, we escalated our commitment to vote against any UK listed company that did not meet 33% boardroom diversity instead of the 25% threshold we used last year, in line with the recommendations of the Hampton-Alexander review. As part of our voting expansion into global markets we are also starting to apply this voting practice outside of the UK where possible. We have followed local market best practice where targets have been set by the local authorities. Examples include a minimum of one female director in Japan, 30% in Malaysia or 40% in France.

As part of our voting activities in 2020, 112 companies were flagged for diversity concerns out of a possible 553 companies voted across the UK during the period. Of this number we voted against or abstained on the re-election of the Chairman of the Nominating Committee at 54 separate companies or 48% of the time, due to our concerns that diversity was not being adequately addressed. We abstained on seven of these occasions, largely as these were Small Cap companies which have smaller boards resulting in more challenging succession planning. The companies where we did not oppose the director re-election were primarily due to satisfactory disclosure from the companies in question; either that another appointment was soon to be announced, a recent unexpected departure, or a detailed plan of action was presented to shareholders. Globally, including the UK, 159 companies were flagged for diversity concerns, resulting in 90 votes against or abstain, or 57%. We will continue to evolve our approach to diversity in different markets in line with developments in each jurisdiction on this subject.

CASE STUDY

Alphabet Inc.

Alphabet, similar to other large US companies, has proven difficult to engage with, as a smaller European investor. Due to its size and sector there are a number of inherent risks associated with the company. As is often the case with high-profile US companies, there were several shareholder proposals on the agenda at Alphabet's AGM this year. Through our voting our objective was to support calls for the company to provide their shareholders and the public with better disclosure over topical issues at the company, which led to us supporting eight out of ten proposals.

These proposals touched on many human rights related issues, such as improving company disclosure over its whistleblowing policies, developing a human rights oversight committee and better transparency over information takedown requests on Alphabet's software platforms. However, we abstained on a shareholder proposal requesting the appointment of an independent director with human rights expertise to the board; choosing instead to support a proposal calling for a board level human rights committee. We took part in investor calls with the proponent of this proposal before the meeting where we were convinced by the argument for a committee to serve this function, rather than an individual. We also voted against another proponent's request for future shareholder approval on all company by-law amendments. In these cases, there were significant difficulties for the company to implement these changes and we did not consider that there would be a material benefit either for the company or shareholders. Moreover, we found the proponent did not provide sufficient evidence to showcase any failure on the company's part in this regard.

We also voted against the triennial advisory vote on the company's remuneration report. We continue to have concerns with the structure of Alphabet's executive compensation plans which lack sufficient performance conditions and frequently use special one-off awards for directors. We believe the use of one-off awards, whether for retention, promotion or other purposes are inappropriate and a signal that there are fundamental problems with the principal remuneration structure.

We maintain our position with regards to the company, and will very likely continue to support shareholder proposals of this nature until the company becomes more receptive to shareholder engagement, but acknowledge there have been some small improvements in certain areas.

CASE STUDY

Barclays

At the beginning of 2020, ShareAction (a charity focusing on promoting better outcomes in responsible investing) filed a shareholder proposal at Barclays' forthcoming AGM. Their aim was to encourage the business to move away from its carbon intensive lending, particularly in the carbon heavy energy sector. Barclays, in response, told us of their intention to file a counter proposal committing to being a net zero bank by 2050. We held discussions with both ShareAction and senior figures at Barclays to better understand the two perspectives. Our discussions focused on how compatible the resolutions might be from a governance perspective, and on the detail of Barclays' environmental lending policies with a view to ensuring we could support the best outcome for all stakeholders.

On the whole, the outcome of the two engagements was positive. ShareAction were open with us about their concerns and engagement with Barclays prior to filing the proposal. We were also impressed by the scale of the bank's potential response, despite their historically weaker lending policies compared to their European peers. We therefore made the decision to support the Barclays' proposal, welcoming their ambition to become a net zero bank by 2050 across its Scope 1, 2 and 3 emissions; along with commitments to helping the transition of energy and power clients, and to report annually from 2021.

For the ShareAction proposal, we decided to abstain on this resolution, as we believed that the broad ambitions within the proposal were captured by Barclays' own climate strategy resolution. While we understood their arguments and agreed with the bulk of the wording in the proposal, we questioned the very specific focus on a small number of sectors and believed a larger and more strategic focus across all lending would be most beneficial and effective for the bank.

The Barclays' resolution received very nearly 100% support, with the ShareAction resolution receiving 24%. Following this successful outcome we will be monitoring the bank on the implementation of this plan.

CASE STUDY

Amazon.com Inc.

Amazon continues to be a key holding for many of our funds, and despite some negative headlines, remains an innovative and growing company, albeit with some ESG issues to address. As with last year, we saw a large number of shareholder resolutions calling for increased disclosure on a range of issues that affect the company. Our purpose when voting these resolutions, as with Alphabet, is to signal to the company where we believe they can improve when engagement is not effective or possible. We supported nine out of the twelve resolutions.

We decided to vote against a shareholder proposal calling for disclosure on viewpoint discrimination. After analysing the proposal we believed it was reasonable for the company to rely on an exclusion list of potentially controversial charities for its AmazonSmile foundation. We abstained on the proposals regarding community impact reporting and the introduction of a human rights impact assessment. For the community impacts proposal, we appreciated the aims of the proponent, but recognised the steps the company is taking to reduce their impact on local communities and the environment. As for the human rights impact assessment proposal, we noted that unlike the proponent's wording, the company has committed to an enterprise-wide assessment of their supply chain, rather than focusing on just a few high-risk products. We supported all remaining shareholder resolutions regarding reporting on food waste, customer due diligence, human rights impacts of facial recognition technology, disclosure on hate speech and sale of offensive products, independent chair concerns, median gender and racial pay equity reporting, a report on promotion data, the right to call special meetings, and the production of a report detailing lobbying activity.

We will continue to apply pressure where we can to the company, particularly via the support of shareholder resolutions, to ensure that progress is made on these issues.

CASE STUDY

Wizz Air Holdings plc

The company was one of the first we saw following the initial lockdown in the UK to propose a remuneration vote for a financial period that had been impacted by the pandemic. As such this was a test case for how companies should and could respond, and our purpose when voting was to signal just what would be deemed acceptable to both shareholders and the general public.

There is no doubt that the airline industry has been one of the most severely affected by the COVID-19 pandemic and the ongoing global travel restrictions. In line with decisions made by most other companies during lockdown, the CEO of Wizz Air voluntarily reduced his salary by 25% for the second half of March, and agreed to receive no salary for April 2020. For the period between May 2020 and the end of March 2021, he also agreed to a 15% salary reduction.

While we acknowledge the voluntary nature of these salary cuts, at the AGM, we had serious concerns around the company's decision to adjust (and increase) the outcome of bonus awards. The decision was made to apply upwards discretion to the annual bonus, essentially removing the financial impact of the pandemic from the assessment of performance under these grants. We understood Wizz Air's rationale that the impact of the pandemic struck in the last month of the 12 month performance period of the annual bonus, and wiped out the previous 11 months of good performance. However the upwards discretion, which essentially ignored the negative effects of the global pandemic, was not in our opinion appropriate, especially given the wider employee and shareholder experience during the months leading up to the AGM.

As a result, we decided to vote against the company's remuneration report at the AGM in July. 51.6% of shareholders also decided to oppose this resolution and voice their concerns with the arrangements.

CASE STUDY

Adidas

At Adidas' 2020 AGM we had the opportunity to approve the acts of both management and the supervisory board members during the previous financial year. This approval is a requirement for German listed companies, which is usually just a procedural sign off and typically receives high levels of support. This vote can however also be used as a way for investors to signal any issues that they may have with actions taken by management during the year.

This year, RLAM decided to vote against the approval of management acts given persistent allegations of Adidas' failure to address diversity and inclusion issues in both its advertising and across its workforce.

In a 2019 New York Times article, it was revealed that the company faced issues of workplace discrimination and has continually received both public and employee backlash over repeated instances of racially insensitive marketing schemes in past years. Whilst we acknowledge that the former Global HR executive responsible for unhelpful comments around racism stepped down when this came to light, and recognise the slew of positive commitments issued by the company to help tackle the matter, we saw a significant reputational risk to the company given its diverse customer base. We also noted that these changes came mostly as reactionary measures, despite this being an issue that has been raised in previous years.

We recognise that the company has already gone a way towards proving their commitment to tackling this issue and we will keep their approach under review ready for the next AGM. Should these concerns persist and/or little is being done to embed diversity initiatives we will consider escalating our vote to individual board members.

Our approach to voting

Our UK and Global Proxy Voting Policies are publically disclosed on our website. In applying these policies, we use discretion and have due regard for the particular circumstances of the company whilst vigorously pursuing the interests of our customers and clients. We do not automatically support the board, but will analyse each resolution to determine if the company is acting in accordance with our policy and with local best practice. In making our voting decisions, we aim to be consistent from year to year. If we have previously abstained or voted against a resolution, we will change our vote to support management only where we feel the company has made a significant change in its policy or approach. We will also consider any engagement we have had with the company in the year, and reflect our thoughts on the progress of this engagement in our vote and our public and private comments to the company.

Our Voting Policies are reviewed on an annual basis and signed off by the RLAM Investment Committee. In updating our Voting Policies, we will incorporate new and emerging best practice, feedback from clients, changes in local governance or stewardship codes, and our own evolution in thinking.

We are strong advocates of good corporate governance, and our preference is to vote 'as a house.' As a result, all of our funds are voted in the same way. No one fund or fund manager may single-handedly change a vote for their fund; any recommendation to change a vote is considered and discussed as a house. To assist with this our voting process is intentionally managed by our RI Team, who works alongside our investment teams. This is consistent with our Collaborate corporate value, whereby we believe that collaboration and discussion across teams on governance and voting issues will result in the best outcomes for all customers. We believe this 'house views' approach also helps send a clear and consistent message to companies on our governance expectations. It also allows us to engage more effectively to seek improvements to governance standards.

The RI team's role is also to reduce or prevent any bias when voting and to ensure a balance between following our voting guidelines and taking the specific circumstances of the company into account. RLAM's RI team is currently 66% female and 22% BAME, representing eight nationalities and speaking five languages, ensuring that there is a wide variety of views on any given issue. Further details on team members can be found on page 78 of this report.

Voting policies

Every year we update our voting policies to align with emerging best practice, market reviews, targets and developments in our thinking and approach. Our full voting policies for 2021 are available on our website but here we have highlighted the most substantive changes for the forthcoming voting season.

Principle adverse risks

This year we have elected not to detail our approach to specific ESG or sustainability risks, but have included our approach to what we consider to be our principal adverse risks in line with SFDR regulations[4]. These are the most significant risks or impacts which we believe our investments may have; be they environmental, social or governance related and are tied to our engagement themes. We have detailed the stages of escalation should there be a material concern, beginning with supporting shareholder resolutions through to opposing board directors and/or report and accounts.

Climate

As an extension of our previous voting position we will consider voting against the re-election of the Chair of the Board at our most highly emitting companies where following engagement there has not been progress on the disclosure of a climate transition plan.

Diversity

Diversity is a standing item in our policies, and we have formalised our approach in additional areas and markets; we will consider opposing the re-election of the relevant board member if there are no women on the board in Australia, Canada and the US. In line with the recommendations of the Parker Review in the UK for 2021, we will be expecting companies to make progress on the appointment of individuals from ethnically diverse backgrounds during the year.

Restricted stock

We have reviewed and updated our approach to restricted stock plans as they become more common in the UK. We will continue to expect companies to discount the value of an award and to put robust checks and balances in place, but we are sensitive to the current financial situation and uncertainty facing many companies. As such we are more open to these proposals provided there is a strong rationale

The proxy voting process

The RI team is responsible for executing equity proxy votes on behalf of RLAM according to our Standard Operating Procedures. We use Glass Lewis' Viewpoint as our voting platform. All ballots are sent to Viewpoint by our custodians or our clients' custodians. For each agenda item, Glass Lewis applies RLAM's custom voting template which suggests a voting recommendation that reflects RLAM's high level Voting Policies and best practice standards. The RI team then conducts its own review of every vote, considering any unique circumstances facing the company, any engagement we have undertaken with the board, and any discussions with the fund managers. The vote is then approved by a member of the RI team prior to being dispatched.

Because we vote as a house, the RI team will take care to consider internal views on voting issues prior to executing a final vote. We routinely flag any controversial votes to fund managers prior to confirming a vote, to allow time for discussion. Controversial votes may include votes where we are voting against a resolution for the first time, a potentially high profile issue or where we have serious governance concerns. Voting recommendations for our actively held stocks are circulated to fund managers (for their own funds), internal governance experts and the Head of Responsible Investment prior to being executed. This provides full visibility of our votes and an opportunity to raise any objections. In the vast majority of cases, any differences of opinion on proxy votes are discussed and agreed collaboratively. In the rare instance where the RI team and the fund managers cannot agree on a vote, it is escalated to the Head of Equities; or alternatively to the Chief Investment Officer when the vote is concerning funds where the Head of Equities is the named fund manager.

Informing companies of our vote

In cases where we abstain or vote against management in our actively managed funds, we will use our discretion to write to the companies to inform them of the rationale for our vote. We feel this is an effective tool for sharing our views with the Board on key issues where we have concerns, and helps encourage dialogue with non-executive directors on important corporate governance matters.

The scope of voting at RLAM

We make reasonable endeavours to vote all of our eligible shares in the funds where we vote. However, there are occasions where we are unable to vote, or choose not to vote, for example if shareblocking is in place, or if the local market requires us to arrange a local Power of Attorney (POA). We have controls in place to ensure that voting is accurately executed in line with our Voting Policies, and that votes are submitted in a timely manner. There are occasions where we have to submit votes late after the Glass Lewis deadline date. For example this may occur if we receive late ballots due to transactions in the funds, or if the local custodian releases the ballots late. In such cases, we will vote at the first reasonable opportunity after we receive research from Glass Lewis. Any late votes or vote rejections are noted and investigated on a monthly basis.

Client-directed voting

Our preference is to apply a consistent approach to voting across all funds where we retain the voting rights. We value the importance of our clients' views on voting matters and we work with our clients to incorporate their views and speak with one voice on key voting issues. Feedback that we receive from clients is reviewed and considered prior to updating our voting policies each year. Some clients choose to retain their own voting rights and we can advise them on the rationale for our votes so they can consider this when executing their own votes. Where clients have the desire to direct votes in segregated accounts, we will work with them to agree the most efficient and effective way to do this.

In accordance with our 'house views' approach to voting, we currently do not have the facilities to offer underlying clients the ability to vote their share of pooled funds. Should we decide to offer split voting in the future, there is a risk that this would dilute RLAM's strong governance views and could send confusing and conflicting messages to companies when we try to engage. We note that 'split voting' in pooled funds is not technically possible in some European and Emerging markets. However, we do acknowledge that industry discussion and debate on this issue is evolving, in part due to the new UK Stewardship Code. Asset owners are increasingly interested in asserting their own views through the assets managed by third parties such as RLAM. We are committed to working with our clients to better understand their voting needs and will review and evolve our approach as our clients' needs change. Ultimately we want to work with clients to both represent their views and maintain a strong commitment to good governance.

Vote disclosure

We think transparency is important. Our votes are disclosed monthly in arrears in an online searchable database accessible via our website.[5] We proactively disclose the rationale for any votes against management or where we abstain on a resolution. We do not routinely disclose our voting rationale when we vote in favour (for) a resolution as often these votes can be routine, but we are happy to provide an explanation to clients or other stakeholders upon request.

Proxy voting research

We utilise the services of IVIS and Glass Lewis to provide information, highlight controversial ballot items, and provide a platform to execute our proxy votes. However, these voting services are there to inform only; RLAM will use its own voting policies to make the final voting decision, reviewing all votes before execution. We do not rely on external proxy voting advice; we apply our own custom voting policies and we do not rely on auto-voting, each vote is reviewed and manually submitted by a member of the RI team.

Stock lending

We lend stock on a number of our equity and fixed income funds. We have a standing instruction with our custodian, HSBC, to recall shares prior to a vote to ensure that we are exercising our full voting power at shareholder meetings.

Bondholder voting

RLAM's disproportionate exposure to secured and highly covenanted bonds tends to give us a greater degree of creditor control than is normal for fixed income investments, with companies having to put any proposed changes to these bond terms to a vote. As bondholders we do not have the right to vote at the annual shareholder meeting as equity holders do, but we sometimes have the right to vote on issues that affect our credit holdings. These votes often take the form of extraordinary meetings, where we are asked to grant consent for changes that can impact our holdings in a given company. Because there is no set formula to these meetings and the issues proposed are primarily financial, everything is approached on a case-by-case basis and there is no formal policy governing our approach to these votes.

There were 536 votes, across 45 issuers companies where we either gave some form of consent or we exercised our voting rights as bondholders in 2020. Often, due to the nature of our lending position, we were also able to engage directly with the company ahead of any solicitation activity, something which is still relatively unusual for bondholders. Because of the direct financial impact of these votes, we view all as significant and provide our credit clients with an overview of any voting activity on a quarterly basis.

With the impact of COVID-19 dominating the corporate landscape in 2020, issuer requests for waivers and amendments increased materially compared to 2019. Given their extraordinary nature, we always sought to balance providing respite for companies directly affected by the short-term impacts of the pandemic, with ensuring that the underlying economic position of our lending was preserved. Unsurprisingly, our engagements in 2020 centred on those sectors most impacted by COVID-19 and, following in-depth and constructive discussions, we were able to support near-term covenant relief for a range of issuers including the pub companies, Punch Taverns and Marstons, and airport operators, Heathrow and Gatwick.

Away from COVID-19, we continued to support the financial market's transition away from Libor, voting in favour of the future use of SONIA to calculate coupons across a number of floating rate bonds issued by companies such as Skipton Building Society and Lloyds Bank.

Notably, RLAM's emphasis on secured and well covenanted lending means we typically have a preferential level of control and visibility compared to unsecured creditors. Whilst strong covenants will increase the incidence of interactions with our borrowers, critically they also provide earlier and enhanced opportunity to maintain value for our clients. We expect this dynamic to sustain into 2021 and will continue to approach these discussions with the appropriate level of focus and pragmatism.

ESG integration

Use of research

RLAM has an in-house team of professionals that are dedicated to responsible investing and ESG analysis. This team has demonstrated its knowledge and expertise in responsible investing, and are experts at helping fund managers and analysts think about ESG risks and opportunities, and integrate these considerations across both equity and fixed income investment processes. The knowledge and expertise of this team supports and enhances the financial and ESG analysis conducted by our fund managers and analysts. Having an in-house team is essential for providing effective and relevant ESG analysis. In our experience, 'off the shelf' ESG research from third party providers does not always provide sufficient nuance or context, which is required to ensure ESG analysis is additive to the investment process and not simply a 'tick box' process.

We use a mix of internal and external ESG research to inform our investment decisions. For external research we use various third party service providers and sell-side brokers. We monitor the quality of our investment research providers quarterly as part of our MIFID II commitments, including our core ESG research providers. Fund managers and analysts vote each quarter on the brokers or research firms that provide the most value to them. This is done through a systematic and transparent process managed by our Front Office Operations Manager. If providers do not deliver good quality research, contracts will be reviewed with a view to altering or cancelling them. This ensures we are getting the best value for money from our brokers and research providers.

In 2020 we have continued to build and invest heavily in our internal capabilities to consume, analyse and interpret a number of new data sources to help support our investment decisions. In line with our 'unconstrained' investment philosophy, we are keen to consume a wide variety of information and in different formats. Given that many ESG issues are qualitative in nature, there is a significant benefit in being able to quickly search and filter information that is most relevant to us. We are nearing completion of our internal database which will offer all investment staff an easily accessible and centralised way of digesting both RLAM's research and insight from external providers and expect this to be ready in 2021.

Sustainable investing

Sustainable equities

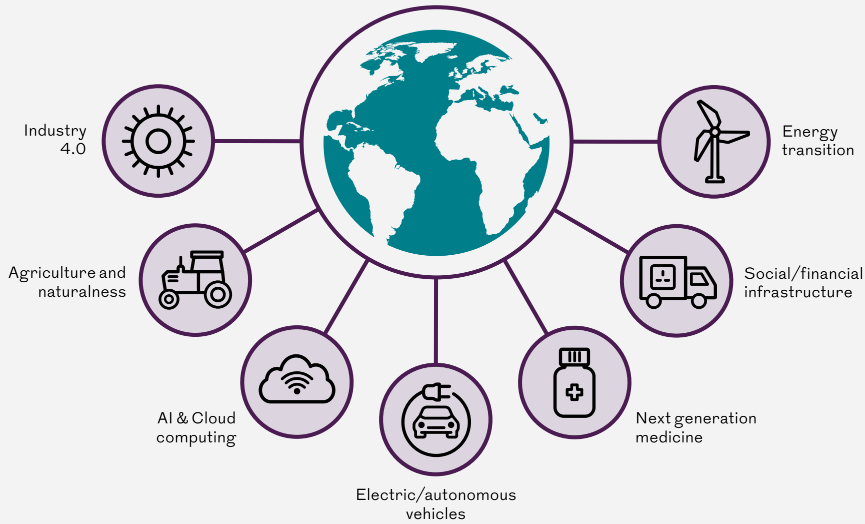
In the Sustainable Equities team we believe that owners and managers of capital play a strong role as a catalyst for positive social and environmental change. We can support a sustainable economy through providing capital to leading businesses and through proactive engagement. We also believe that sustainable investing focuses on an exploitable market inefficiency and that, through a focus on socially and environmentally beneficial products and services and high standards of ESG management within a company, we can identify investment insights that others may miss.

The funds are not rigidly thematic; instead the companies in which we invest tend to be grouped that way. The themes we focus on in the funds can and do change overtime, and are a consequence of our investment process rather than the goal. We think it is important to have the flexibility to evolve as society evolves too, ensuring that at all times we are investing in the most relevant sustainability themes and the ones most likely to deliver strong investment returns.

The type of company that will be a good fit for the funds will have both a compelling financial case, as well as a clear net benefit to society. Often the net benefit that a company presents aligns with several of the UN Sustainable Development Goals (SDGs). Again, this is an outcome of our clear and unwavering focus on investing in companies that support a sustainable future, rather than an explicit goal or mandate of the funds.

As a team, we have a bottom-up approach to investing, extensively researching the credentials of each and every potential new investment. We do not rely on external ESG research. We equally weight the Governance, ESG leadership or positive Net Benefit case with our financial analysis, and draw heavily on the expertise of the fund managers and analysts who run the Sustainable Funds, the RI team and our external Advisory Committee. Everyone has input and an equal voice in the approval process. The Advisory Committee meets at least three times annually and provides us expert external insight and challenge on the companies we review, emerging ESG topics, considerations for the funds, and performance.

The following are examples of companies we have reviewed during the year and why we believe they are worth holding in the Sustainable Funds.



Industry 4.0

Steam was industry 1.0, electricity 2.0, and the computer 3.0. Industry 4.0 is about data and using it to bring together the physical and digital worlds to enhance the efficiency of a range of existing industries. This theme has been accelerated by the recent COVID-19 crisis.

Agriculture and naturalness

Demands on food production will continue to grow as demand for protein is linked to rising wealth, particularly in developing countries. The current system, based on the use of chemicals to enhance production, needs to be changed for smarter, more natural methods of food production.

Artificial intelligence and cloud computing

The exponential growth of data and computing power is allowing data to be used to make better decisions in areas such as healthcare diagnosis and energy usage.

Electric/autonomous vehicles

Transport remains one of the major sources of pollution through the use of the combustion engine. Cars are also the source of many deaths and injuries. Electric and autonomous vehicles offer the opportunity to move transport into a cleaner, safer future.

Next generation medicine

The current healthcare system is based on diagnosis methods and drug treatments that are slow and often ineffective. The ability to extract more accurate and timely health information from our bodies, and the ability to obtain our individual genetic profile, offers the opportunity to significantly enhance the standard of healthcare.

Social infrastructure

Areas such as water and electricity still require significant investment in the future to connect developing countries to these basic utilities and also improve the way they are delivered in developed countries. Other areas such as social housing are also relevant to this theme.

Energy transition

The way we have extracted energy from the sun recently is through fossil fuels. Renewable energy, such as solar and wind, offers the opportunity to extract energy directly from the sun in a cleaner, more sustainable manner.

Wabtec

Wabtec is the leading North American rail rolling stock component and equipment manufacturer and the global leader in freight rolling stock, following its acquisition of GE Transportation. The company started as a manufacturer of train air brake systems and has since diversified into electronics, controls, powertrain components, HVAC, doors and locomotives. At an industry level, railways are the most environmentally friendly way to move freight over land and rail based public transit systems offer positive environmental and social impact versus other alternatives. Wabtec's vision is to 'accelerate the future of transportation by building the safest, most reliable and sustainable freight, transit, signalling and logistics systems and services.' Its products are focused on safety and efficiency and whilst its sustainability reporting could be improved, environmental considerations appear to be incorporated into the company's manufacturing processes, and a focus on health and safety is a key part of the corporate culture. We see many drivers too for future growth at the company and as such, view the company as a good fit for the funds.

IQVIA

IQVIA is a leading global provider of advanced analytics, technology solutions and contract research services to the life sciences industry. IQVIA's insights and execution capabilities help biotech, medical device, and pharmaceutical companies, medical researchers, government agencies, payers and other healthcare stakeholders tap into a deeper understanding of diseases, human behaviours and scientific advances, in an effort to advance their path toward cures. IQVIA enables its clients to improve clinical, scientific and commercial results. It is on the front line of the global public health conversations through ongoing work with non-profit organisations, government agencies, patient advocacy groups and other healthcare stakeholders. Other examples of work in public health include the monitoring and evaluation of drug safety, addressing the opioid epidemic through data analyses, developing an oncology data network, working with the CDC around antimicrobial resistance and enabling Alzheimer's insights. Not only do the products and services of the company facilitate the advancement of health outcomes, but it is at the forefront of the application of data to the healthcare industry, which we think is only at the early stages.

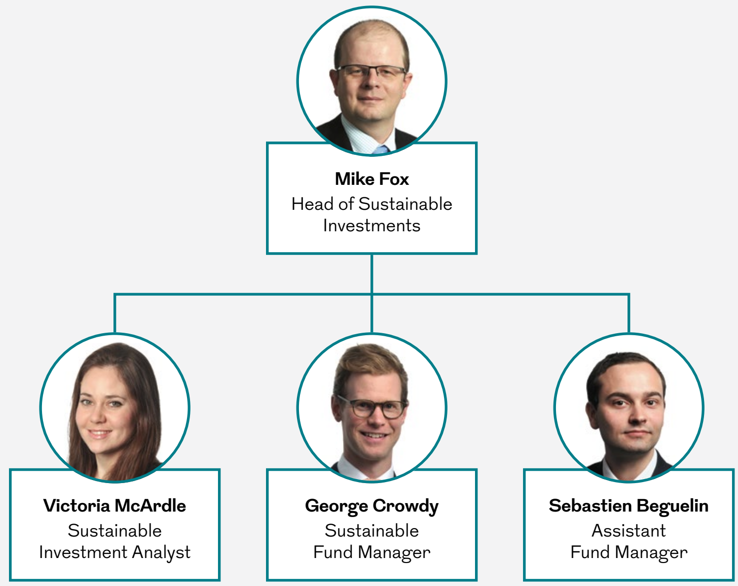
MercadoLibre

MercadoLibre hosts the largest online commerce and payments ecosystem in Latin America. The company's main offerings are MercardoMarketplace, an automated online commerce platform that enables businesses and individuals to list merchandise and conduct sales and purchases online; and MercadoPago FinTech, a financial technology solution platform, which facilitates transactions on and off its marketplaces by providing a mechanism that allows its users to send and receive payments online, and allows merchants to process transactions via their websites and mobile apps, as well as in their bricks-and-mortar stores through QR and mobile points of sale. This latter offering presents the most significant societal net benefit in terms of financial inclusion. MercadoLibre is focusing initially on the bottom and middle segments of the population pyramid (there are huge numbers of unbanked and under-banked people in Latin American) meaning that vast parts of the population can be serviced, particularly those who are not profitable to existing retail banks. The company's purpose is to democratise commerce and money. Its broader ESG practices are also impressive. Ecommerce is growing especially fast in Latin America and we think that MercadoLibre is well placed to be a prime beneficiary.

Greggs

Greggs sells sandwiches and baked goods primarily, positioning itself as affordable food on the go. It rapidly responds to changing consumer demands, owns its supply chain and offers a loyalty scheme. Greggs is also trialling home delivery. Good treatment of its 23,000 employees is a big priority for the company and it has been named one of the happiest places to work. Greggs added nutritional information to its menu before it was required to and also provides free WiFi to customers. It serves food that's free of artificial colours, flavours, added trans fats and MSG. Each year, with support from its 87 partners, Greggs provide six million free wholesome breakfasts to primary school children with its Breakfast Club programme. The main priorities for the company are around customer health, responsible sourcing, community, the environment and its workforce. Greggs has a very clear brand identity and strong focus on the issues that matter most to its customers. Integrity like this can really set it apart in such a competitive market. Its marketing strategy chimes very well with customers, it has proven at times to be a strong social media influencer, and it has been innovative when it comes to its menu offering, which is vital. It addresses all the main emerging trends within the food to go category and its impressive ESG practices make it a great fit for the funds.

Figure 5: The Sustainable Investment team



Sustainable credit

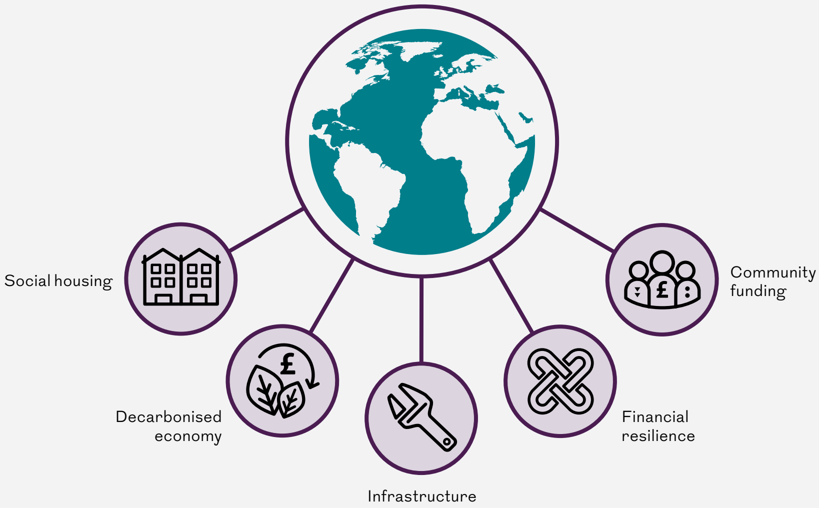
With greater market focus on sustainable investing within the equity market, some investors can overlook the opportunities that fixed income markets present. However, we believe that fixed income markets offer a rich seam of opportunity for investors looking for socially positive investments, without compromising returns.

By investing through debt, we can gain access to socially critical areas of the market that are largely inaccessible to equity investors. This means that we can not only support socially beneficial organisations, but with less market research available in these areas, we can target superior risk-adjusted returns for our clients. Focusing on these areas also dovetails with our sustainable equity funds, preventing a duplication of risk-taking across both asset classes.

As well as giving access to previously hidden sustainable opportunities, fully integrated sustainable credit investing greatly enhances information discovery, helping to improve long-term lending decisions. The ESG insights from our RI team are used in the same way as any other form of credit research – to uncover information that rating agencies and other market participants might be missing, allowing us to see a more complete picture of the risks facing a borrower.

As for the equity funds, we have a clear bottom up investment process, which incorporates a consideration of whether the companies we choose to invest in provide a net benefit to society through their products or services, as well as the financial characteristics of a borrower. For a bond to be included within our funds, both of these elements are required. Our approach to screening for positive choices is bespoke and differentiated – relying on an experienced multi-disciplinary team of individuals working collaboratively. Unlike equities, credit risks are asymmetric; upside returns are capped, while deterioration in a borrower can lead to full capital loss. Therefore, for our financial considerations, we value bondholder protection, such as security and covenants, which can help to protect us if a company does get into difficulty. We also look to run highly diversified portfolios in order to reduce security-specific risk.

All issuers within our sustainable holdings offer a net benefit to society or show ESG leadership. Around three quarters of our sustainable credit holdings fit within a key theme (see overleaf), with the remaining classified as ESG leaders in their industry. The current themes are not an input to our decision making, but an output of our long established philosophy and process, which serves to highlight some of the critical sectors the fund invests in.



Social housing
Charities providing affordable housing to those in need. Credit markets offer the only material way to access this vital sector.

Decarbonised economy
Borrowers playing a key role in the decarbonisation of society, such as supporting the connection of new renewables to our electricity network, or public transportation such as rail ROSCOs that are effectively transitioning to electric trains.

Infrastructure
The provision of vital infrastructure, covering a wide variety of areas from regulated water companies to telecommunications to individual projects.

Financial resilience
Companies providing insurance products that help to support individuals through life's unexpected shocks .

Community funding
Banks and building societies that focus on serving individuals and SMEs.

The following are examples of entities invested in the sustainable fixed income range during 2020:

Greater Gabbard OFTO

This bond is backed by an offshore transmission operator, connecting the Greater Gabbard wind farm near Suffolk to the National Grid. The connection adds enough green energy to power 530,000 homes. The revenues servicing our bonds are very stable, and are not based on the output of the wind farm. Furthermore, we have security over the business and covenants to protect our lending position, making this a great investment from both a sustainable and financial perspective.

Thames Tideway Tunnel

This bond is funding a project constructing a 25km super sewer underneath the river Thames, which once complete will prevent millions of tons of raw sewage spills into the river. In addition to the fantastic environmental benefits, the bond benefits from a strong security and covenant package, as well as excellent visibility on cash flows through a supportive regulatory framework.

Phoenix Group

This company provides exposure to the critically important insurance sector, through provision of Life Insurance and Pension Fund services, serving customers across the UK. Bonds issued by the Group include operating company debt capital at attractive spreads.

GB Social Housing

GB Social Housing is a lender to the UK Social Housing Sector, focusing on smaller housing associations that would otherwise be unable to access bond funding. Lending to smaller housing associations provides a significant net benefit to society providing much needed financing to build new homes. It also provides us with stronger covenants and security values than is typical in the sector which helps protect investors' money.

Principality Building Society

This bond is backed by the mutual building society that provides savings, mortgages and insurance services to 500,000 members and has been operating for over 150 years. As a mutual, it has no shareholders, making bondholders the only route to provide financial support to this key sector.

The green growth

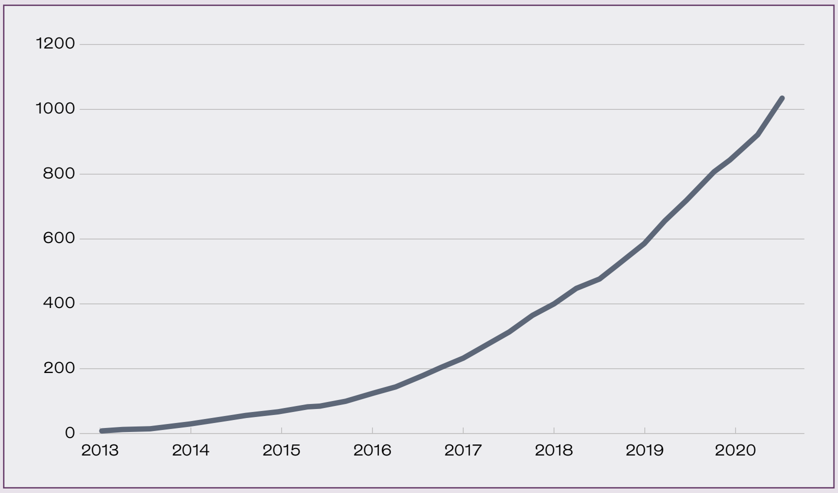
One area of exponential growth over the last few years has been green bonds, lending designed to channel funds raised towards environmentally friendly projects. Fundamentally, we are hugely supportive of any capital flowing towards low carbon and climate-resilient solutions, and any market mechanism that facilitates this.

However, on the ground we sometimes find gaps between this theory and reality. Borrowers' environmental credentials often do not match up to the green label; most green bonds are issued on an unsecured basis, with no claim over the green assets, leaving lenders exposed to the entire business. In extremis, a green bond can turn brown if the company chooses to sell on the green projects during a downturn, potentially leaving bondholders with exposure to environmental polluters elsewhere in the business. Furthermore, there has been surge in the market to demonstrate commitment to ESG investing, with green bonds becoming a key beneficiary as investors buy these bonds on the convenience of the label, leading to potential pricing distortions.

For example, Anglian Water has both green bonds and unlabelled bonds. Despite all bonds being issued under a common platform, and all sharing security over all asset (including some fantastic environmentally friendly projects), the green bonds offer around 0.2% less in yield vs unlabelled bonds of a similar maturity.

Whilst green bonds can offer an 'easy win' for client reporting, in our view relying on labels can lead to investors overlooking opportunities to gain some financial benefits for our clients without sacrificing any green benefits. The only credible solution is through bottom-up fundamental research into each bond's financial and sustainable characteristics. We often see far more attractive opportunities in the 'unlabelled' green bond market than we do in labelled green bonds. Many of the borrowers we lend to have strong environmental credentials but no external labelling. The Greater Gabbard example mentioned is a great example of this – allowing an attractive undistorted spread return for investors willing to put in the extra mile in bottom-up research.

Cumulative green bond issuance ($ billion)



Source: Bloomberg NEF, Bloomberg L.P., based on quarterly issuance from 2007 to Q3 2020

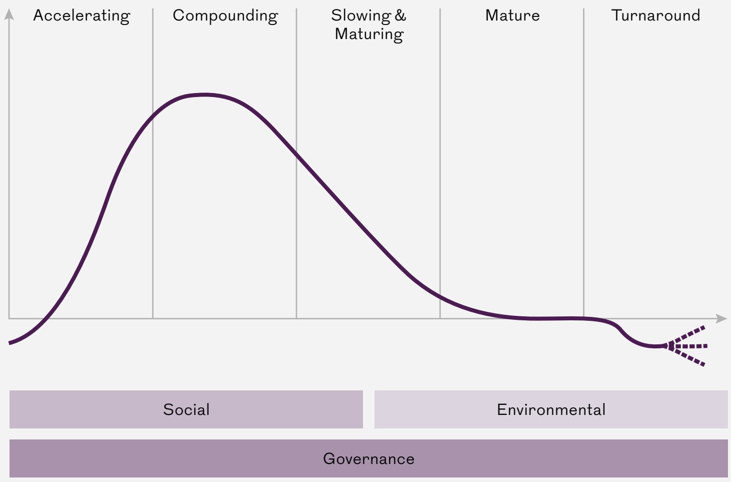
Shalin Shah
Fund Manager

"Our 10-year-plus headstart in sustainable credit has given us time to develop a differentiated investment process based not just on data-driven models or the convenience of green labels. We believe our funds provide an opportunity for our clients to deliver funding to a range of critically important sectors that are not easily captured in equity markets, whilst targeting attractive yields in an ultra-low interest rate environment."

Figure 6: Measure and classify

Investment process	ESG focus
Measure 3,500+ companies	ESG 3rd party data (SASB) framework
Classify 3,500+ companies	Risk flags Climate – transition + physical Life cycle specific
Identify c.600 companies	Stock specific + thematic Materiality – ESG assessments Wealth creation test – positive, challenging, avoid
Value c.200 companies	Fundamental valuation – scenario analysis
Implement Portfolio	Key ESG risks including climate Client reporting & attribution Bespoke solutions
Monitor Portfolio	Stock reviews Portfolio reviews

Figure 7: Identify and value



Source: RLAM for illustrative purposes only.

Portfolio holdings are subject to change, for information only and are not investment recommendations.

Equities

Global equities

The Global Equity team believes integrating ESG issues into our **investment process** strengthens both investment performance and our commitments to be a **responsible investor** and good steward of our clients' capital.

- **Investment performance – lower risk, higher returns**. Future Wealth Creation and valuation are directly impacted by ESG issues, often in a complex and hard to measure way.
- **Responsible investment – be the change**. ESG assessments support more effective engagement, which in turn can influence a better future for our environment and communities. Our ESG integration also enables bespoke client solutions and reporting.

Investment process

We integrate ESG issues into all stages of our investment process and collaborate extensively with the RI team. We use shared ESG data providers, review thematic ESG research to support our stock specific expertise, and participate in monthly independent RI portfolio reviews focused on a wide range of ESG risks, targeting both individual company risks and wider societal risks. We also work closely with the RI team on voting and engagement to support our client propositions.

Portfolio construction

1. **Measure & classify** – data and technology drive our investment insights, idea generation efficiency, and are the foundation for our investment approach. The team integrates an increasing breadth of ESG data with its proprietary Life Cycle analysis.
2. **Identify & value** – the team spends most of its time and energy in these stages, doing deep-dive qualitative and quantitative fundamental analysis to evaluate future Wealth Creation potential, and value the most attractive company specific opportunities.

Wealth Creation – ESG factors can have a critical impact on the Wealth Creation analysis. We believe that ESG materiality is both key to the evaluation and very complex in practice – our Life Cycle concept and qualitative analysis can add nuance and value where simple quantitative ESG data struggles. In situations where ESG risks are deemed very material, and the company is unwilling or unable to mitigate this, ESG factors can be a 'deal breaker' – the company will be avoided in client portfolios.

Valuation – many businesses with attractive forward-looking Wealth Creation potential may also have material ESG risks or rewards. We incorporate these ESG factors into valuation scenario analysis. For example carbon transition risks and carbon taxes can be explicitly modelled into 'bear' valuation cases, and this can directly change our ultimate investment decision.

Challenging but attractive – in Global Equities, we believe companies with material ESG risks can be attractive investments if:

- Risks are understood and acknowledged
- The company is willing and able to mitigate them in future
- Material ESG rewards also exist
- Overall Wealth Creation potential is attractive
- Valuation is attractive even when risks incorporated in 'bear' scenarios

In addition, these companies are often excellent candidates for company engagement. This supports our clients' desire for RLAM to be a responsible investor, and can also lead to better outcomes for our environment and communities.

Nemetschek

Nemetschek is a leading software provider to the architectural, engineering and construction industry. Its solutions enable customers to achieve cohesive planning across the entire project life cycle, which has significant value to an industry plagued by complex and highly wasteful projects. National regulators are demanding ever increasing requirements around mitigating the impact a company has on the climate, not just during construction itself; but also the environmental footprint over the entire life of a building. Nemetschek offers powerful solutions to help plan and mitigate climate impact, which has proven a real tailwind to profitable growth. We consider the long-term potential of this company and the use of its products to be underestimated by the market.

Steel Dynamics

Steel Dynamics is a US steel manufacturer. While the global steel industry as a whole faces transition risks due to high GHG emissions, Steel Dynamics has a different business model. By using primarily recycled steel in efficient electric arc furnaces, the carbon intensity is 80% lower than some global peers, as well as being more profitable. As regulations around carbon emissions increase, Steel Dynamics is well placed to benefit from a shift to 'greener' steel as well as being more resilient if significant carbon taxes are imposed. Despite this differentiation we believe the market is treating the company as a typical steel company, and although there is transition risk associated with any steel manufacturer, we consider Steel Dynamics to be well placed for future success. Market underestimation may also be influenced by the lack of detailed public disclosure from the company and so we are formally engaging with the company to encourage them to improve their reporting.

ArcelorMittal

ArcelorMittal is an example of a steel business where carbon intensity is actually much higher than the peer average, while profitability and balance sheet robustness is much lower. Although recently announced strategies to become carbon neutral by 2050 sounds positive, in reality we consider it will be very challenging to execute, especially given a difficult starting position. We consider the climate transition risks for the company to be a material negative, and unless we see credible evidence of a viable and profitable transition to low carbon intensity we are avoiding owning the shares because of this.

Positive

Challenging but attractive

Avoid

"Our Life Cycle concept and qualitative analysis can add nuance and value where simple quantitative ESG data struggles."

Peter Rutter, Head of Equities

Integrating ESG in Royal London's UK life funds

As the manager of RLAM's active UK equity life funds, which invest over £2 billion in the UK's largest quoted companies, I have increased the role which ESG factors play in evaluating those businesses in recent years. Royal London's members and customers rely on returns from these funds to help them save into their pensions for retirement and to pay their insurance claims should the worst happen. Although actively managed, the funds apply a low risk approach to portfolio management so their exposure to certain sectors mirrors that of the broader index.

Market bias to energy and basic materials

In the UK, this means an exposure to sectors and companies with a substantial environmental footprint. Over £1 in every £14 invested in the FTSE All-Share Index was in mining and industrial metals at the end of November 2020, including several of the largest publicly held miners anywhere in the world. Oil exploration and production companies occupied a similar proportion of the total index. As they extract the resources which power our economy, these businesses generate carbon footprints larger than some countries, operating on land the size of cities. Understanding how these companies are planning to adapt both their products and their environmental footprint in the face of a changing climate is an essential part of my assessment of business models and outlook for future profitability.

Certain risks are just too big to ignore. In 2019 the Brumadinho tailings dam disaster resulted in a significant loss of life, widespread environmental damage and a potentially large fine for its owner, Vale a Brazilian mining company. Tailings are effectively the waste materials generated during the mining process and are stored along with waste water behind man made dams. Our responsibility as investors is to engage with each of the fund's mining investments, to understand how their own tailings storage facilities are managed. With a better understanding of the risks impacting each company, this year we supported collective efforts which led to the introduction of a new global tailings standard. Now that it's published, we've initiated a new round of conversations with these businesses about how they're planning to meet the requirements of this new standard. For Rio Tinto, which saw an earthquake several miles below one dam earlier this year, discussing their thorough response confirmed how seriously our portfolio companies are now taking these risks.

Looking for changing corporate behaviour

Another area where mining companies held in the funds have made progress this year has been setting new targets to reach net zero carbon emissions within the next 30 years. Our RI team analysed these pathways and this research fed into our most recent quarterly portfolio review, where we discussed both the carbon footprint of the UK Life fund today and the strategies of the companies in the fund most exposed to future risks from climate change. Anglo American stood out for its ambition here, with a target to be climate neutral by 2040, while building materials provider CRH was flagged as having far fewer concrete plans to tackle its footprint. It was also good to see many companies focusing on the efficiency of their operations as part of their steps to lower their climate impact, driving down operating costs associated with energy usage, emissions tariffs and more.

Going forwards, I'm mindful that the funds will need to increasingly focus on emissions from the products which its portfolio companies are producing, particularly the oil majors. While BP and Shell can begin to clean up their own operations through greater use of renewable power and better management of fugitive emissions, but so long as their core businesses focus on the production of oil and gas, building profitable low carbon divisions will be a significant challenge for these companies. While they remain significant parts of the UK market, understanding how they will approach this energy transition is an important part of the investment case for each business.

Engagement is not always enough

In some cases, environmental factors have led to the UK life funds fully exiting our position in a company. While Carnival Corporation had a strong brand and financial profile, our RI team had previously flagged concerns around the company's record on both its levels of pollution and subsequent fines, along with the company's practices relating to upcoming maritime emissions regulation. We spoke with the company on the steps it is taking to clean up its operations and avoid future fines, and came away concerned not just by its environmental strategy, but how effectively its board was providing challenge and scrutiny on these issues. In light of our concerns, we sold our holdings in Carnival in 2019.

I firmly believe that assessing corporate governance factors is an important part of the integration process for the effective management of the life funds. The core of this is a constant discussion between myself as a fund manager and our corporate governance experts. We cover any changes which companies might be seeking to make to their remuneration proposals, combining insights from a financial understanding of the business with their expertise on pay structure and best practice. Our priority is to make sure management interests are aligned with shareholders. We'll meet with the Chairs of companies to discuss their plans to increase the diversity and talent on their boards and will scrutinise any proposals at company meetings brought by dissenting shareholders. While the responsibility for voting sits with the governance team, I'll often provide feedback ahead of votes and at the quarterly portfolio reviews we'll talk through any votes where we went against a management recommendation.

The quarterly reviews are also an opportunity to take a look at any new positions in the funds from an ESG perspective, often throwing up fresh insights on how they operate. From executive pay at Ocado, to Greggs' work to offer more healthy alternatives and ensure best practice when sourcing the tea, coffee and sugar which goes into its hot drinks, these snapshots complement my traditional financial analysis of these companies. They can also better highlight the company's roles within the industries they serve, such as Marshall's decision to track the carbon lifecycle of over 2,000 of its products it sells to building firms. We'll also use each review to discuss a major industry or theme in more detail, tackling the biggest challenges affecting areas such as global pharmaceuticals, tobacco and the banking sector.

Changes in company meetings

These discussions are feeding through into how we have our traditional meetings with company management. ESG issues are now something that I talk about at almost every discussion that I have with management teams. When meeting student housing provider Unite Group earlier in the year, it was important to ask about the company's cladding removal plans and where it was improving its students' experience and helping with any mental health issues, as much as our questions on the integration of their latest acquisition. In a competitive market such as student housing where repeat bookings are a driver of Unite's success, how it approaches these important issues for its stakeholders is important for the business.

So as the world begins to recover and rebuild from the impacts of COVID-19, a better understanding of how UK companies are responding to society's growing expectations for them not just to manage their own impacts but act as drivers of positive changes has never been more vital. For businesses which have dragged their heels on ESG up till now, this will no longer be an option.

Joe Walters
Senior Fund Manager

Fixed income

Our approach to ESG is built off the back of our longstanding investment philosophy which fundamentally believes that credit markets do not accurately price idiosyncratic risk. We use ESG analysis to uncover information that credit rating agencies and other market participants miss, which helps us make better investment decisions for our clients.

We integrate ESG information into our financial analysis, as we see ourselves as long-term lenders of our clients' money rather than short-term traders of bonds. The sustainability of our lending position is therefore critical. We have tailored our approach both to the specifics of fixed income investing, as well as the particular risk characteristics of each sector or issuer. In particular, we identify those sectors where we feel there is most ESG risk and/or limited third party ESG research, and prioritise engagement and analysis on that basis.

Sterling credit

RLAM's Sterling Credit Funds are managed using an embedded approach to ESG integration. We incorporate ESG risk, and have done for many years, as part of our credit analysis. Why? Because we believe that any risk to capital will have a considerable impact on the sustainability of cash flows. This is due to the asymmetric risk of investing in credit whereby investors are at risk of losing all capital invested, with a limited upside based on the value of the income stream of the coupons.

Our Credit team applies a more bottom-up approach to portfolio construction, where ESG considerations are built into our credit analysis process – essentially looking to ensure that the yield on any bond compensates us for the risks that we take in buying and holding that bond. Our stance on risk identification in credit is based on our belief that we are long-term lenders of our clients' capital, rather than short-term traders of bonds.

When investing in corporate bonds, we have to consider all elements that could pose risk to the capital we are investing. Traditionally, the most important consideration would have been credit risk, based on credit risk ratings and the creditworthiness of the borrower. This more old-fashioned approach would focus on the business environment a company is operating in, the leverage on the balance sheet, and the commitment to a particular credit rating or leverage target. The risk as an investor lending over the longer term was that management would change, leverage would creep up, or the business environment would deteriorate. Investors relied, to a large extent, on the point in time when an investment was made, and to the commitment of the status quo from the people running the business. But naturally, businesses, management and the environment they operate in do change. This was one of the reasons we had a preference for lending on a secured basis, when capital invested had higher protections. More recently, credit investors have started to focus on ESG themes as key risks when making investment decisions. This started in areas such as coal-related industries and the concept of 'stranded assets' and the long-term impact of governmental and societal attitude shifts due to climate change. At RLAM, we have always focused on how sustainable a business is when it comes to making an investment. Hence the focus on elements such as covenants, secured assets, and a truly senior position grants us the ability to exercise a significant degree of pre-emptive control over the structure and features of a bond, such as a change in ownership.

Our bottom-up approach therefore means that the Sterling Credit team at RLAM is accustomed to analysing all potential risks, beyond 'just' creditworthiness. ESG research is typically geared towards equity markets, with little focus on companies that are not listed. We therefore supplement poor quality ESG data with insights from our in-house RI team by working collaboratively to uncover risks and opportunities.

Any critical risk can impact the valuation of a bond, and therefore we do not perceive the identification and mitigation of ESG risks as being different to any other credit risk; ultimately it is the impact not the origin of a risk that is central to our credit evaluation.

Environmental

Any risk associated with a negative impact on the environment, beyond what the regulator considers to be acceptable, can impact the ability of a company to raise debt in the bond markets and the pricing of capital for a particular borrower. A good example is the utility sector, but in particular Southern Water, where the company had issues with sewage spillage which resulted in fines from the regulator and a major overhaul of the business. As a result the company had to pay considerably more to access funding from bond markets, which are the preferred method of raising long-term financing for projects, and valuations of existing debt saw a significant deterioration. When looking at investments in areas such as the utility sector, fund managers have to assess the environmental risk and whether the pricing of utility bonds reflect that risk. Clearly, Southern Water bonds prior to the incident had not reflected the environmental risks that the company was undertaking, but subsequently the bonds are priced at a level that reflect more appropriately the riskiness of the business.

As a fund manager in sterling corporate bonds, we have to decide whether the Southern Water bonds are priced at a level that reflects the risks the company is undertaking. How do we do that? Through the intervention of the RI team that are currently engaging with management of Southern Water and can assess whether the company has taken the remedial action to ensure similar problems do not occur in the future; in this case through a major overhaul of the business.

Instead of excluding the bonds, being a responsible investor means that we take a more bespoke approach to assessing ESG risk by considering what actions issuers are taking to address risk events, as well as whether the price reflects the risks associated with the environmental impact.

Governance

Governance is not a new concept for the Sterling Credit team, and has always been a factor when looking at credit. We have encountered numerous instances over the years of companies falling short of minimal governance standards and the impact this has. Examples such as Steinoff and Wirecard are enough to send shudders down investors' backs; both issued long-dated debt in bond markets only to see the pricing collapse after serious governance shortcomings were revealed. We didn't own bonds in these companies however this has always been a risk for corporate bond investors. Less extreme examples such as banks caught up with money laundering issues have also had to pay a high price. Senior managers at Swedbank lost their jobs, and investors saw the valuation of bonds weaken in secondary markets.

Social

Social risk is the more challenging aspect of ESG integration to conceptualise in the context of corporate bond portfolios. At RLAM, the way we have traditionally lent to borrowers with a baked-in emphasis on lending against sustainable, long-term cash flows, has meant that social housing has been a natural destination for capital investment — and we have significant overweights versus the index in this area. The top ten social housing providers which RLAM currently lends to, ranked by the value of the bonds we hold, currently provide nearly 300,000 general needs social housing properties across the UK. They also provide over 30,000 properties for affordable rent and over 30,000 social housing properties for the elderly and those who require extra support in their day-to-day lives. These social housing providers do more than just manage properties however, and between them our top ten social housing providers completed 13,000 new homes in the most recent year, many of which were for social or affordable rents. The sector has attractive credit features such as secured assets and indirect government cash flows as well as attractive covenants. These features make this sector compelling as investments and well suited to our process and philosophy.

Expect more

Traditionally, investors looking at ESG perhaps focused more on their equity exposure, given the greater prominence of issues such as executive pay and the shareholders that vote for and against these items. The increase in interest of responsible investing has led to greater scrutiny on fixed income managers too. We have welcomed the opportunity to demonstrate our thinking in this area — adding regular updates on our website including our Evolution of Responsible Investing report, focusing on fixed income ESG investing towards the end of 2020 — and expect to provide more insights as 2021 progresses.

Paola Binns
Head of Sterling Credit

"Our credit research team does not perceive the identification and mitigation of ESG risks as being different to any other credit risk."

CASE STUDY

COVID-19 impact on credit

During a period of unprecedented economic and social challenge, active ownership of our bond investments becomes even more important. Over the year, we have continued to engage responsibly with the limited number of issuers that required temporary support from creditors during the COVID-19 pandemic.

We approached these discussions in a balanced way with a primary focus on dampening the credit risk impacts of the pandemic. Given the typical strength of our lending position, we have generally been able to offer short-term modifications to bond terms in return for measures that help preserve our clients' economic positions. Another critical benefit of lending on a preferential basis to select issuers is that active engagement and governance oversight is materially enhanced by strong and pre-emptive controls. This has proved particularly relevant against such a fast moving and uncertain backdrop.

The majority of our engagement with bond issuers on this topic was in the retail property and leisure sector, where we approached all these discussions with a common philosophy of balancing the need to be responsible lenders at a time of unprecedented social and economic disruption, whilst ensuring we preserve our clients' economic interests.

For instance, we were pleased to see the early redemption of Arsenal Securities plc bonds in July. Despite the negative commercial impact of the crisis on the underlying borrower, Arsenal FC, a combination of security, protective covenants and a financially strong equity sponsor resulted in the bonds being redeemed at a price materially above prevailing and historic market levels. Such a positive outcome against a negative event backdrop is a direct consequence of highly selective secured lending and further reinforces the ethos behind our long-established approach to investing in corporate bonds.

“We believe that credit markets have an important role to play in the transition to a cleaner, healthier society, directing capital to vital areas of our economy. Our long-established process offers investors access to these opportunities, and delivers a portfolio with robust financial outcomes and lower overall ESG risk.”

Matt Franklin

Environmental reporting in fixed income

RLAM has been interacting with third party providers of environmental and carbon data for well over a decade and, despite our best efforts to improve issuer mapping, the relatively poor levels of coverage of corporate bond indices continues to undermine the credibility and usefulness of carbon footprinting reports for fixed income investors. As well as leaving huge swathes of portfolio and benchmark holdings uncovered, limited coverage also results in significant data skew for those bonds with relevant data, amplifying the problem of measurement methodologies that have never been entirely relevant for debt instruments.

Regulatory requirements are increasing for both asset managers and owners to provide additional environmental reporting on portfolios. Therefore, we are committed to developing a proprietary carbon footprint database for fixed income issuers to help address the key limitations of third party provision. Our coverage levels are already well in advance of what can be captured 'off the shelf' and we continue to interact with debt specific issuers to ensure we have access to bespoke and dependable carbon data. In certain circumstances, this has involved bilateral discussions with smaller and typically non-equity listed bond issuers, such as housing associations and building societies, where reporting and disclosure has not traditionally been as comprehensive as other higher profile bond issuers. We believe issuers are also finding these interactions beneficial; not least the regional building society that was reporting 800,000 tonnes of carbon emissions. Rather than unearthing a previously unreported coal mining subsidiary, our oversight allowed the issuer to identify the wrong unit in reporting, with the true figure actually closer to 800,000 kilograms; a far more reasonable footprint for a regional branch network!

We have always seen the value of targeting our research efforts on lower profile areas of the credit market due to the heightened scope for genuine information discovery, so the advancement of our bespoke in-house carbon footprinting provision to clients along these lines feels like a natural extension of our existing approach. This project is both exciting for us and worthwhile, as we continue to challenge ourselves to help our clients meet regulatory requirements without compromising the credibility of the data for our convenience. We look forward to sharing the outputs of RLAM's fixed income carbon footprinting in the near future.

Global credit

We believe consideration of ESG risks ensures strong corporate citizenship and integrity, and provides longer term sustainability of cash flows from the companies in which we invest. Governance, in particular, is a key part of rigorous fundamental credit analysis in the Global Credit team. Two core principles guide the incorporation of ESG factors into Global Credit and High Yield investment.

Engagement, not avoidance

Our preference is to engage with companies with poorer ESG practices. We don't use exclusions because they tend to avoid weaker ESG-ranked companies, often with no consideration of the financial trade-off. Collaboration with the RI team and credit analysts enhances information discovery and analysis, and supplements third party data where quality and coverage of data is often low.

Rigorous financial impact assessment

ESG analysis provides us with an additional perspective on our traditional credit analysis. We recognise that governance issues may pose the greatest near-term financial risk to companies in high yield markets, while environmental and social issues may have longer-term impacts. Our rigorous credit research process leads to an overall internal rating score which incorporates nine fundamental factors (e.g. free cash flow, growth prospects, etc). As one of our nine factors, ESG issues can move the rating in our internal model up or down one notch. We work closely with the RI team to investigate and understand any significant ESG risks, but the final investment decision resides with the fund manager and takes into account relative valuation.

CASE STUDY

Chemours

Chemours manufactures and distributes performance chemicals for gold producing, oil refining, agriculture, and other industries. Overall we felt Chemours remains a high risk company from an ESG perspective, both due the nature of the industry and its own operational risks, relating to how it manages its operations and the by-products of production, along with potential risks of certain chemicals which it sells. Corporate governance is average by US standards, although the company's remuneration disclosures remain well below par. Despite settlements in November 2018, legacy chemical issues still dog the company along with more recent violations, evidenced by a 2019 New Hampshire lawsuit and a more recent (June 2020) Department of Environmental Quality (DEQ) action relating to non-compliance around testing of waste. While the company is slowly improving its disclosure on production processes, areas such as waste management remain a potential risk. Based on these factors we have assigned a negative ESG score to Chemours and derived an internal rating of B-. As internal ratings are one driver of holding size this meant the strategy exposure was lower than for an equivalent holding with a higher ESG rating. Our rising concerns on litigation risk led us to sell our position earlier in the year (the return over the holding period was in line with the index).

CASE STUDY

Charter Communications

Charter Communications is the second largest Cable TV Company in the US.

The cable sector offers some broad social benefits, particularly internet services, a growth area for Charter where it provides access to online information and services to around 25 million households. In addition, the core video product offers access to some educational content at a competitive rate. However, the long-term health and wellbeing impacts of television habits in the US are a challenge, given that the average American still spends around 3 and half hours a day watching television, even before the impact of any online streaming is taken into account. The industry is currently subject to relatively loose data and customer regulation at a federal level, although state level regulation is a concern, while change in government might tighten federal rules.

Charter's overall approach to ESG reporting is very limited, despite the energy intense nature of its physical networks it provides very few disclosures on its energy management or material sources practices, along with the significant footprint from its 30,000 vehicle fleet. Overall we felt Charter is not a high risk company from an ESG perspective and we decided not to apply a negative ESG score and we derived an internal rating of BB+.

Recent results demonstrated the resiliency of the cable business model and its ability to offset some of the COVID-related expenses. Over the holding period the Charter bonds significantly outperformed the index.

Government bonds

Although effective integration of ESG factors in the government bond market is still in its infancy relative to other bond markets, we do use our position to engage with issuers. For example, we have regular contact with senior figures at the Debt Management Office (DMO) for the UK Government. In addition, we hold occasional one-to-one meetings with representatives from other DMO entities for countries including Australia, New Zealand, Canada and Sweden to discuss our thoughts and raise potential issues surrounding these markets.

Recently, we used one of our formal ESG meetings to discuss government bonds and how their exposure to climate risk could be measured. During this, we looked at the percentage of fossil fuel exports, energy consumption per capita and environmental vulnerability index amongst other factors. The meeting was used as an exercise to both look at RLAM's exposure and discuss the climate metrics available today. This is a discussion that we expect to have frequently as the quality of data and our ability to analyse it matures.

CASE STUDY

UK green gilt

Following the UK Government's announcement in November 2020, which they will issue the UK's first sovereign green bond in 2021, RLAM reached out via letter to the Chancellor of the Exchequer to both offer our support of the announcement and provide some insights on the green bond sector. Whilst RLAM is fully supportive of the goal of green bonds, we often see a range in the quality of the 'green' element of issued green bonds and a significant risk of green washing.

A common issue we see with labelled bonds, which we shared with the Chancellor, is that the debt is often not ring-fenced and therefore there is a risk that debt is serviced by cash produced from other less environmentally friendly activities. For example, whilst the green bond we could be financing is committed towards building wind farms, the cash/interest we receive could in reality be financed from the construction of a new airport runway. As a result, the green credentials of the bond are weakened and in reality not robust to meet what we believe is best practice.

Following on from our letter, we are hoping to secure a meeting with specialists within Her Majesty's Treasury to further discuss our views on green bonds, in the hope that it will help to strengthen the quality of the UK's first sovereign green bond.

Overall, the goal of our engagement is to help ensure green bonds issued by the UK Government are robust so that we can both consider them for inclusion in our funds and contribute to supporting a climate transition in the UK.

Cash

In our cash funds, we are increasingly considering ESG factors, particularly when evaluating our exposure to financial counterparties. Applying high standards of corporate governance to the counterparty banks that we transact with for example aligns closely with the interests of clients. We know our clients' money is safer when deposited with banks that have strong governance and high standards overall. This is a factor we consider when choosing how to invest clients' assets. More broadly, our approach to ESG integration in managing our cash range considers exclusions, research, and engaging on ESG factors to reduce risk, enhance returns and improve industry standards.

Screening

Within our Cash fund range, there is significant client demand to exclude certain sectors from our investment universe. We therefore apply a number of exclusions as standard, and apply exclusion criteria across the entire suite of our cash solutions to eliminate companies that generate over 10% of revenues from tobacco, armaments and fossil fuel extraction.

Research

We are continuously looking at ways we can embed ESG factors into the management of our cash solutions because we believe that ESG factors are crucial to the security risk profile of our investments. Our negative exclusion criteria are therefore coupled with ESG research and scoring. Research from our RI team is combined with that of external providers to determine an ESG score for each security.

Research will pay particular focus to the macro-geographic bias of a given security. Where faced with an equally viable security, our ESG considerations can often be the distinguishing factor over another investment.

Engagement

Our cash specialists and in-house team of responsible investment analysts conduct regular engagement with issuers to ensure information is timely to the short-term emphasis of our cash investments.

CASE STUDY

Lloyds Banking Group

After the announcement that Lloyds Banking Group were committing to halving the carbon emissions they finance by 50% over the next ten years, the Cash team along with members of the RI team undertook engagement activities to understand more about the commitment. The aim of the engagement was to focus specifically on the detail behind the commitment and gauge how stretching this potential target might be.

After several discussions with the bank, it was highlighted that this commitment has placed them at the forefront of the UK banking sector in considering the environmental impact of their lending activities. While at the time of writing we were still waiting for Lloyds to establish a formal baseline, it became clear that the bank is addressing all aspects of their loan book, including hard-to-decarbonise sectors such as their residential mortgage and motor financing arm. The target will require changes in how the bank assesses its lending practices and appears to be an ambitious medium-term target.

Overall, whilst we would like to see more details about the implementation of Lloyds' commitment, we welcome the ambition of the bank and their leading stance within the UK banking sector. RLAM will continue to closely monitor updates, and particularly the impact on Lloyds' mortgage book, as this is the part that may have the greatest direct impact on the bank's environmental performance.

Property

The COVID-19 crisis has presented some significant challenges within property over the past year. Whilst demand for online deliveries has benefitted the industrial logistics sector, the rules governing social distancing and lockdown have exasperated the headwinds faced across shopping centres, retail parks and the high street. The Offices market has also seen great change with so many of us now working from home. The COVID-19 crisis has really brought to the fore the concept of health and wellbeing which for many of us has led to the re-balancing of our working and home lives. It is however also recognised that working together in a face-to-face environment also provides great advantages. This can include learning, sharing and development opportunities. We also contribute towards and benefit from a business's cultural values and beliefs, and the social betterment of being with one another.

Our approach

As at December 2020, we managed 249 assets, with a combined value of £7.65bn. We acknowledge the property we own contributes towards climate change and that there is a real urgency across the sector to address this impact. As part of this, we recognise our buildings will have to be net zero carbon to help mitigate this risk and so we are developing a strategy in order for this to be achieved. The delivery of this ambition will require a number of targets and actions to be met, placing greater emphasis on the ownership and operation of energy efficient buildings, the adoption of renewable energy technology, reducing the embodied carbon within our developments, and offsetting.

RLAM's Property team aspires to be a leader and is developing a Responsible Property Investment strategy which will enable us to achieve this. This will include targets and objectives, procedures, and the monitoring of progress to ensure the real estate funds maintain a programme of continual improvement. This applies throughout the fund's acquisitions, developments and the asset management of all commercial property assets.

We continue to respond annually to benchmarks and reporting requirements including:

- **Global Real Estate Sustainability Benchmark (GRESB)**
  This has become widely recognised as the key measure of sustainability performance. Environmental, social and governance (ESG) performance is assessed against seven sustainability aspects, including information on performance indicators, such as energy, carbon emissions, water and waste. We are very proud to announce that one of our funds achieved a 4-star rating which was an improvement on the previous year's rating of 3 stars, achieving second place out of 59 within its peer group. Furthermore our other two funds both achieved 3-star ratings which was an improvement on the previous year's ratings of 2 stars, achieving 11th and 16th place of 59 within its peer group. We also entered two of our funds into the Development section for the first time and achieved 5-star ratings for both.

- **United Nations Principles for Responsible Investment (UNPRI).** As a signatory this benchmark forms part of RLAM's commitment to reporting on our responsible investment activity year on year across all our asset classes. In 2020 Property received an 'A' against a median score of 'B'.

- **Streamlined Energy & Carbon Reporting (SECR)**. This mandatory government scheme superseded the Carbon Reduction Commitment (CRC) and requires the fund to disclose the following intensity metrics - energy use, carbon emissions and energy efficiency actions.

- **Task Force on Climate-related Financial Disclosures (TCFD).** This is a market-driven initiative which provides a suite of recommendations and consistent climate-related financial risk disclosures in mainstream company filings. In 2020 the government announced TCFD would become mandatory by 2025.

We continue to be active members participating and contributing to the Better Buildings Partnership (BBP), the UK Green Building Council (UK GBC), the British Property Federation (BPF) and the Investment Property Forum (IPF) Sustainability Interest Group.

In 2020 we received 12 Green Apple Awards for a variety of biodiversity initiatives including the planting of wildflower areas, the installation of bug hotels and bee hives.

Property management

With regards to COVID-19 we have been working hard to ensure our buildings are operating normally. We have produced a very detailed guide for tenants on how they can continue to occupy their buildings safely, with clear instructions on how to maintain social distancing. We have also strived to ensure that we have balanced the need to reduce energy consumption with the requirement to provide an excellent flow of fresh air into each building. For example we have carried out extensive assessments of oxygen levels within our office buildings to reassure our tenants that we are maintaining good air quality during the pandemic.

Development

We have around 50 current construction projects within our property portfolios, the majority are for commercial use, both new build and refurbishment. This includes offices, retail, industrial and residential developments of various size and complexity across the UK, and all at different stages of the development process from inception to nearing completion.

In 2020 a thorough review was undertaken of our Development Sustainability Targets. This included a benchmarking exercise comparing our own position against our industry peers leading to the creation of a new enhanced set of targets which we consider are both aspirational and market leading. The targets, which have been branded as the 'Property Development Sustainability Standards' are now grouped into eight new sustainability categories including energy, materials, waste, water, climate resilience, bio-diversity, health/safety/wellbeing, and community. There are 52 targets in total, including:

- All major development and refurbishment projects to undertake both an embodied carbon and operational energy net zero carbon feasibility assessment at the early stages of the design process.
- A minimum Energy Performance Certificate rating of 'A' to be targeted for all new-build development projects and a 'B' targeted for all refurbishment projects.
- All new and major refurbishment projects to achieve a Building Research Establishment Environmental Assessment Method (BREEAM) 'Excellent' and develop a pathway to achieving BREEAM 'Outstanding'.
- For all new build and major refurbishment projects an operational energy net zero carbon feasibility assessment should be undertaken. This should clearly set out how the scheme can be readily adapted in the future to achieve net zero carbon.
- All timber products used in construction shall be from sustainable sources accredited by the Forest Stewardship Council or the Pan European Forestry Council.
- A feasibility study of low and zero carbon technologies such as district heating networks, combined heat and power (CHP) and renewables shall be undertaken for all new build and major refurbishment projects.
- To actively consider, and where possible, incorporate bio-diverse green and brown roofs on all appropriate roof space for new and major refurbishment schemes.
- Contractors to support at least one community engagement activity each year, where team members give time to a project that benefits and supports the local community.

Some examples of the sustainability aspirations embedded within our development pipeline include the following:

Statesman House, Maidenhead

A 110,000 sq ft new build office, currently submitted for detailed planning consent and forming part of a wider master plan for the site that includes a further 186 residential units and a separate 70,000 sq ft office. The initial phase will deliver the larger office building commencing in 2021 and will be targeting ambitious sustainable criteria. These include BREEAM Outstanding, WELL Building Gold Standard, EPC A, and Net Zero Operational Carbon. Additionally the development is part of the Design for Performance Pioneer Programme targeting reduced operational energy levels which will assist in achieving the funds wider Net Zero Pathway strategy, and reduce running costs for tenants.

The Distillery, Bristol

This development is an office development in the Temple Meads area of Bristol due to practically complete at the end of Q4 2020. It has been benchmarked against our new Property Development Sustainability Standards and is a strong performer. It should achieve an embodied carbon emissions figure of 469kgCO_2/m^2 against a target of 600kgCO_2/m^2, it is BREEAM Excellent, achieves an EPC of A, as well as incorporating a green 'living' wall and a diversion from landfill rate of 95%. The building design responds well to new COVID-19 occupational requirements as it has natural ventilation, semi-external access to each floor level, the heating and cooling plant is installed as separate systems on a floor-by-floor basis and a large communication stair between all floors reduces the use of passenger lifts.

The Earnshaw, London

The Earnshaw (previously known as Castlewood House) is a new build mixed use office development in the West End of London, comprising 139,000 sq ft office space and 27,000 sq ft retail space. The development is targeting best in class credentials which includes all electric building systems removing the need for gas powered plant and equipment, a WELL Building Gold standard, as well as BREEAM Outstanding and the incorporation of on-site solar PV for renewable electrical energy production. The building design responds to the requirements of occupiers in relation to COVID-19 through the incorporation of multiple individual WC cubicles for both women and men, the utilisation of SMART technologies to enable building users to access reception and individual floors without the need to push or pull buttons and door handles, as well as improved fresh air ventilation rates over and above current industry benchmarks.

Hotel, Bristol

A 200-bedroom hotel is currently under construction as part of the same master plan as the office building above and will complete in Q1 2021. The development has been benchmarked against our new Property Development Sustainability Standards and achieves a number of these including an embodied carbon emissions figure of 350kgCO_2e/m^2 (600kgCO_2e/m^2 target), a 40% reduction in water use through the selection of low flow sanitary ware, with 97% of waste being diverted from landfill. Furthermore, five student work placements have been facilitated during the course of the development. The development is an all-electric building meaning that gas powered plant and machinery have been designed out at commencement whilst the heating and cooling system uses a majority water based solution to function rather than using harmful refrigerant products that have a high global warming potential.

Tim Coffin
Responsible Investment Property Manager

"RLAM's Property team aspires to be a leader and is developing a Responsible Property Investment strategy which will enable us to achieve this."

Multi asset

Our multi asset funds serve a range of clients and are the backbone of our Group parents' workplace pension proposition. Many of our clients invest with us to take advantage of our active Tactical Asset Allocation (TAA) investment process, which makes tactical choices about where we allocate capital depending on various economic and financial factors. The Multi Asset team does this by applying a systematic framework for allocating to various asset classes and regions, with investment decisions informed by a range of quantitative models. Our strategy aims to provide excellent long-term value to our clients by taking advantage of low cost investing options, such as passive equity funds and futures overlays.

Asset allocation rather than stock selection is the main driver of our multi asset proposition, and therefore ESG integration is achieved through investing in RLAM's range of active and passive funds. The fixed income portion of our multi asset proposition is invested in RLAM's active fixed income funds where ESG is integrated through targeted credit analysis, and is reviewed regularly by the RI and Credit teams. Whilst the equity portion of our multi asset funds is predominantly invested in index trackers for cost efficiency, Emerging Markets exposure is provided via an ESG-screened index to mitigate risks associated with parts of the world where corporate governance is less developed. As described in detail in this report, RLAM takes an active approach to voting and engagement, and clients that are invested with us through our multi asset propositions benefit from our efforts to improve outcomes for customers by reducing ESG risks and encouraging improved behaviour by companies.

We are currently investigating how we can consider ESG factors when investing in derivatives such as futures contracts. Product development in this space is in its infancy and there is not yet sufficient liquidity in these solutions to be suitable for our clients. However, we know the marketplace is rapidly evolving and we will continue to seek opportunities that allow us to further integrate ESG into our multi asset portfolios while delivering great customer value.

Private equity

Totalling just 0.2% of our AUM, RLAM's involvement in private equity is purely as a Limited Partner (LP). ESG issues often have both greater impact, and offer more opportunity for direct management, while under private ownership. Private equity holding periods are longer than average public equity holdings, and the level of ownership by the general partner as a majority shareholder is enough to give it special rights and influence.

Formal ESG policies are increasingly an inherent part of our private equity managers' operations both at the management company and portfolio company level. We have reviewed our existing private equity relationships for any risk outliers. As part of RLAM's due diligence in deciding whether to commit to a new fund, we will review the adequacy of the general partner's ESG policy and it's resourcing to execute on the policy.

External managers

The vast majority of our assets are managed internally. In the rare instances where we outsource investment management to a third party we consider whether bidding parties meet a high minimum standard on integrating a responsible investment approach. Our requirements regarding responsible investment and ESG are made clear in the Investment Management Agreement and the manager must report to us regularly on implementation.

Disclosure and transparency

Reporting our progress

In keeping with our corporate values, we are committed to being transparent and open about our approach to stewardship and responsible investment. We regularly disclose our voting and company engagement activity via publications such as this Stewardship and Responsible Investment report, 'Responsibility Matters' and on our website through blog posts, articles and press comments.

Our Proxy Voting Policies are reviewed annually by the RLAM Investment Committee and published on our website. In addition, our comprehensive online database discloses our proxy votes monthly in arrears, explaining where we vote against management or abstain.

Our clients receive quarterly reports which provide details on how we have implemented responsible investment and stewardship within their fund. These reports may include voting data, engagement examples and case studies, and investment commentary highlighting how ESG considerations were factored into investment decisions in the quarter. We also regularly meet to discuss ESG issues with clients, and we make our investment staff and RI team available to provide their expert insights. In addition, we disclose our annual PRI Assessment results on our website.

We are happy to respond to any specific requests for information on our stewardship and responsible investment activities.

Review and assurance

RLAM's Investment Committee, Executive Committee and Board reviewed and approved this Stewardship and Responsible Investment Report. In doing so, they consider the report to provide a fair and balanced view of our approach to stewardship and responsible investment.

Our Board has also considered whether our stewardship activities are effective and where we can make improvements. As mentioned, RLAM has worked closely with our parent, Royal London Group, to make a significant investment in improving the scope, depth and quality of our stewardship and responsible investment activities in 2020. As such we have allowed for further alignment in our strategies, with the Royal London Group having recently defined its engagement priorities. The growth of the RI team in 2019 and 2020 has enabled us to expand our proxy voting coverage to include our global passive funds, and has allowed us to work more effectively with our investment teams to deliver more consistent ESG analysis, integration, and engagement.

The external auditors regularly review our procedures and controls as part of our Audit and Assurance Faculty (AAF) Control review to ensure we are meeting the standards we have agreed with our clients. The external auditors last completed an AAF Control review in October 2020, which included reviewing our proxy voting processes.

Outside of the AAF, we do not seek specific external assurance for our stewardship activities. We do however have internal controls in place to ensure we follow our own procedures and policies, in particular regarding Proxy Voting, Conflicts of Interest, Personal Account Dealing, Execution and Allocation, and Gifts and Benefits. These policies and procedures are monitored by the Risk and Compliance team and periodically subject to review by both Compliance and Internal Audit.

What's next?

We look forward to 2021 with excitement and optimism. There is no doubt that we will face significant global financial, environmental, social and health challenges, and that things may get worse before they get better. However at RLAM we feel there is an exceptional amount of opportunity as we work with our clients and our parent company to build a purpose-driven and customer-led organisation. There is a deep and growing desire from our clients to further integrate ESG factors into investment decisions, and to ensure that their financial future is aligned with positive long-term social and environmental trends. We also know our clients want to work with companies that share their values, goals and beliefs, and we think our new corporate purpose will help us align behind a mutual commitment to responsible investment.

We have taken the time this year to invest in our people, build new systems and data, and further embed our responsible investment function into the business. These are the building blocks that will support our growth ambitions. We know there are always things we can improve, so we will be working with our clients to better understand their needs, improve how we communicate our ambitions and goals around responsible investment, and blend technology and data with deep qualitative insights to add value to our funds. 2020 was an exceptional year for many reasons, but we believe the momentum behind responsible investing is growing and we look forward to the opportunities this brings.

Further reading

Our culture and values

Our values are a reflection of the culture we are cultivating internally. Our aim is to deliver a great experience for our people, members and customers where our shared values shine through. These shared values are described through the Spirit of Royal London, our culture.

Our values

We are empowered
We enable, challenge, support, we are responsible

We are trustworthy
We are reliable, open, we build relationships

We achieve
We deliver, we improve, we celebrate success

We collaborate
We learn, enjoy, we are a team

Our people strategy

Our people commitments

Leadership
Career
Inclusion
Wellbeing

At RLAM, we recognise the importance of creating an inclusive culture. Across RLAM and the Royal London Group, we have designed a people strategy that we believe will help our people perform at their best, a strategy we are confident will contribute to us achieving our collective vision to become the most trusted and recommended life assurance, pensions and investment provider.

Diversity and inclusion

Diversity and inclusion continues to be an area of great focus for Royal London, particularly in light of some of the high profile events that we have seen in the external environment during 2020.

We fundamentally believe that differences equate to strengths, and employing people from a range of backgrounds, genders, ages and sexual orientations provides a diverse range of skills and life experiences which contributes to our combined success.

During 2020, we developed further our focus on black, Asian and minority ethnic (BAME) inclusion, and in late 2020 we launched a prioritisation plan aimed at improving the attraction and appointment for BAME candidates. This plan, based on accepted industry best practice, focuses on three main pillars: our talent pipeline; our ways of working; education and development.

Diversity highlights 2020

- In 2020, we received recognition of our commitment to diversity from the Employers' Network for Equality and Inclusion (ENEI) – the UK's leading promoter of equality and inclusion in the workplace. ENEI awarded us their Gold standard in its annual benchmark after being ranked 11th among 98 entrants. ENEI are helping us to achieve best practice in equality and inclusion.
- In 2018, we signed up to the Disability Confident scheme and became a Disability Confident Employer in 2020. Our membership will support or objective to successfully recruit and retain disabled people, as well as maximise their potential within Royal London.
- We signed up to Business in the Community's Race at Work Charter and also signed up to the #100BlackInterns initiative.
- We launched a campaign to encourage our people to volunteer their demographic data so we can accurately measure the diversity of our workforce. As a result, 40% of our people have now updated their records (as at 7 January 2021).
- We organised and supported activities for International Women's Day, Pride Month and Black History Month. We also joined more than 3,000 businesses and organisations in celebrating National Inclusion Week.

To ensure we remain on track, we have defined a three-year D&I Strategy and Roadmap which will run from 2021 to 2024, and will address the following key areas:

- Continuing to build our inclusive culture, aligned to our values and working closely with our employee inclusion networks.
- Driving an absolute focus on robust data disclosure, capture and tracking for all protected characteristics, across our key life cycle elements.

- Taking positive action to improve gender balance across all grades, with specific focus on increasing the number of women in senior roles by supporting internal progression and attracting women to externally advertised senior roles.
- Taking positive action to increase ethnic origin diversity across all grades, specifically to support BAME colleagues achieve internal career progression and attracting more BAME applicants to apply for externally advertised roles.
- Finally, we will continue to proactively focus on ensuring other under-represented groups are supported.

Our employee diversity networks

We operate the following Group-wide employee networks:

- Women's Network – 750+ members
- BAME Network – 150+ members
- Pride Network (lesbian, gay, bisexual, transgender and related communities) – 300+ members
- EARL (Enabling disability confidence At Royal London) – 100+ members

Gender pay gap

Through our analysis of our gender pay data to date we have been assured that we do not have an equal pay issue. We have ascertained however that, while women make up 46.5% of our workforce (in line with the overall UK workforce statistics), women remain over-represented (58%) in our most junior grades. Consequently, the impact of the pay gap is the greatest at more senior grades. We are determined to reduce this gap and have lasting impact. Please see our latest gender pay gap report for more information.

Employee engagement

In 2020 Royal London introduced a new employee engagement tool for all colleagues across the Group to express views and insights about their experiences of working at Royal London.

Following a pilot which began in 2019 involving almost 800 employees, Peakon replaced the company's annual Your Views survey. Peakon which is run on a continuous basis provides a platform for employee voices to be heard. Each month, individuals receive a summary of their own engagement based on their feedback to reveal what they are most and least satisfied with. The tool also provides for People Leaders to respond directly to comments made anonymously, encouraging an open and honest dialogue. The tool has proven particularly useful for ensuring employees feel supported while working remotely.

The engagement score for RLAM's front office staff as at January 2021 was 7.7/10. This engagement score is an overall indicator of how engaged employees are based on a series of targeted questions.

Other workplace initiatives

At Royal London we want our employees to feel as though they are supported on issues that are important to them. That is why we have the following internal forums in place to create awareness and drive changes that benefit the wellbeing of our staff:

- Eco champions
- Mental health first aiders
- Employee Engagement committee

How we are governed

We are regulated by the FCA and comply with the SMCR. Our Chief Investment Officer is a regulated Senior Management Function (SMF) and is accountable for our responsible investment function. He is a member of RLAM's Executive Committee and chairs the Investment Committee. The Chief Investment Officer is supported by the Investment Committee which meets monthly to discuss investment issues. The Head of Responsible Investment attends these meetings and presents papers for discussion. Our Stewardship and Responsible Investment Statement is signed off annually by the RLAM Board. Our proxy voting policies are approved annually by the RLAM Investment Committee, and our policies and practices around voting are subject to AAF controls[6] and are reviewed by our external auditors on an annual basis (see Assurance section).

Supporting our clients' needs

Our clients will naturally have different needs and time horizons, and our investment strategies are aimed at supporting these; whether it is for meeting shorter-term cash requirements, such as for universities or charities, or for very long-term requirements like saving for retirement. We offer a variety of investment options to our clients and engage with them to help them find the proposition that best meets their requirements. However, we fundamentally see ourselves as long-term investors and we look for ways to enhance our clients' capital over the long-term.

Royal London Mutual Insurance Society (Group)

Our largest client is our parent company, Royal London Mutual Insurance Society (RLMIS). We manage approximately £101.7bn of assets for RLMIS and work closely with our colleagues in the Group Investment Office to ensure our investment strategy and responsible investment activities meet their needs. As discussed throughout this report, we have been working very closely with Royal London Group throughout the year on stewardship and responsible investment. You can read more about Royal London Group, its investment strategy and governance in our Annual Report, which is available on our website.

All of our other clients can be divided into two segments; institutional and wholesale.

Figure 8:
Institutional AUM split

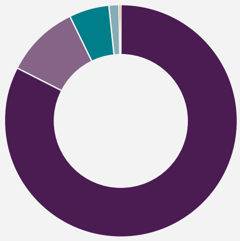


Figure 9:
Wholesale AUM split

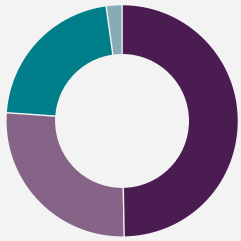
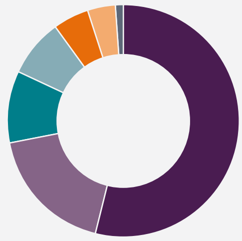


Figure 10:
Institutional client split



Figures are subject to rounding and therefore totals may not always equal 100%.

Source: RLAM

Institutional

We manage £23.5bn in assets for approximately 255 external institutional clients. These include local authorities, charities, universities, corporate pension schemes, and insurance companies. The vast majority of these clients are UK-based, with seven clients located outside the UK. We work closely with our institutional clients to understand their stewardship and responsible investing preferences and to ensure our propositions are aligned with the needs of their underlying beneficiaries. Our RI team is available to help answer client questions and address any specific stewardship, ESG or exclusion requirements. We have seen a significant increase in the number of clients engaging with us on responsible investment issues, which we have used as an opportunity to review and further refine our approach.

Wholesale

We manage approximately £19bn in assets for advisory and discretionary firms in the wholesale space. We ensure assets are managed in line with client goals and expectations and provide access to key investment information and data through documentation such as factsheets and investment commentaries which are available on the RLAM website. We will answer due diligence questionnaires and host fund update meetings which some clients use as part of their ongoing monitoring on our funds. Where appropriate RLAM funds are also risk mapped to risk mapping tools available in the market which are in turn used by advisers and wealth managers to ensure the selected fund is aligned to their clients' attitude to risk.

Understanding how responsible investing forms part of the RLAM approach at both company and fund level is becoming more important to wholesale clients and we spend time engaging with clients to enhance their knowledge in this area. We have held numerous webinars such as videos through BrightTALK, and have sponsored educational sessions on Asset TV, where clients can gain professional development credits.

Product development

We have a structured product development process which we use to bring new solutions to the market. The first stage of this is to complete an idea proposal, for which target market and client needs are among the key requirements. Target market and client needs, along with the business case are at the core of the product design phase. During this phase, the RI team, heads of investments desks, distribution teams and marketing challenge the investment philosophy, drawing on direct client experience and interaction. It is this process that helps to shape an idea into a viable proposition that addresses a client need and ensures new products are aligned with our responsible investment ambitions. Once the concept is defined, we undertake direct client testing conducted through our existing client base. Where we may introduce a product offering very different from our current product suite, we seek to target and engage with potential clients on the concept and materials that will support the potential launch.

Whilst the above is all conducted prior to a launch, it is equally important to ensure that the product continues to meet the needs of clients once it is available to the market. We undertake a substantial review after the first year of a product launch. More broadly, we conduct annual reviews on all funds. In compiling the annual review, we consider any feedback we have received from clients and distributors; sales numbers, client types and investment performance are amongst other metrics.

In 2020, we produced our first Assessment of Value report – a requirement that came out of the FCA's Asset Management Market Study, whereby the RLUTM Board is asked to act on behalf of clients to ensure that products provide value for money. The Board reviewed our service, pricing and value added benefits and made recommendations on where we may improve customer outcomes. As part of our new Climate Risk Policy, we have also made a commitment to embed climate risk considerations when developing new products.

Through the annual reviews and the assessment of value, we continue to challenge ourselves internally and invite our clients to do the same. Given the competitiveness of the market we recognise that to retain our client base we must ensure we are continually meeting the needs of our clients by developing and evolving our products to deliver expectations.

Performance management and reward

As we are a member-owned business, we have a natural alignment with our clients. We aren't seeking to maximise quarterly returns to shareholders, but rather are focused on building our business in the best long-term interests of our members. Remuneration for our people, including fund managers and analysts, is intimately tied to our successful delivery of better outcomes for our customers through a scorecard approach to bonus delivery, which considers a wide range of metrics. The continued development of RLAM's responsible investment strategy is a key pillar of our strategic vision for 2025. As such, our progress on responsible investment is tracked through the RLAM Business Scorecard. This has a direct link to the calculation of discretionary bonuses for all staff, dependant on year-end outcomes. We evaluate our people's performance on both 'what' they deliver as well as 'how' they deliver it – paying particular focus to how they deliver good customer outcomes and demonstrate the Royal London values.

Starting in 2021, our investment professionals will also have a specific performance goal relating to responsible investment and integrating ESG considerations into the investment process. The impact of ESG on investment risk should be considered for all investment decisions and documented. In addition, ESG and sustainability impacts of investment decisions should be understood with a view to minimising and/or mitigating those impacts in accordance with the objectives of the fund. This performance goal supplements existing remuneration incentives for investment specialists and the wider senior population, which are tied to the long-term financial performance of our funds. RLAM's remuneration is structured in a way that incentivises our people to deliver the best outcomes for our customers over the short- and long-term while considering ESG risks and opportunities, and without taking excessive risk.

Training and education

Our investment teams receive a mix of practical on-the-job and formal training on stewardship and responsible investment. Daily engagement and interaction between our investment teams and ESG specialists provides ongoing practical training for fund managers and credit analysts on what types of ESG issues to look out for and what questions to ask management. In addition we undertake regular ESG portfolio reviews with a number of our investment teams, which provide a formal opportunity to sit down and highlight specific ESG risks or opportunities within the investment fund and have a discussion about the relative risk to the fund from a financial perspective. Finally, we undertake other formal training sessions, such as workshops, with our specialist research providers, or internal training conducted by our RI team.

In 2020, our investment teams each received small group coaching sessions on responsible investing which was tailored to each of their strategies. The coaching sessions included key topics like industry terms and definitions, best practice standards, frequently asked client questions, key messages on responsible investment from the fund manager's own perspective, and examples where ESG factors have directly affected investment decisions. In addition, specific training was provided on upcoming EU regulations on sustainable investing and on climate risk and net zero.

Risk management and monitoring

RLAM employs a decentralised risk management model under which risk management framework is integrated into our business processes. We have a clear and well-documented organisational accountability covering the board, committees, functions and individuals which are laid out in terms of reference for the board and committees, as well as in policies and procedures. RLAM's approach to risk management recognises the fiduciary nature of our business and our duty to act in the best interest of clients and members at all times. There are two integral components of our risk management framework; enterprise risk and portfolio risk. The Board Risk Committee has an oversight of the overall risk management framework to ensure it is appropriate for the services we provide to our customers, interests of our Group parent and aligned to industry-wide practices.

Enterprise risk management is based on the Royal London Group-wide risk taxonomy and covers RLAM's proprietary risks which can be financial, operational or strategic in nature. As part of a forward-looking enterprise risk management approach we monitor emerging risks, geopolitical developments, as well as the overall market landscape. This allows timely identification of any market-wide or systemic issues and supports our commitment to stewardship and responsible investment. Identified risks are swiftly escalated internally in line with the risk management approach and an adequate response is defined by the business.

In 2020, we made a number of improvements to our responsible investment risks and controls. This included adding responsible investment and climate risk to the terms of reference of the RLAM Investment Committee, the Board Risk Committee (climate only) and the RLAM Board. We also published our first Climate Risk policy, which was approved by our board, and confirmed that our Chief Investment Officer serves as our Senior Management Function responsible for climate risk.

In addition, we made the following improvements to our responsible investing risk framework:

- Adopted a controversial weapons policy, which restricts RLAM from investing in any companies involved in the production of cluster munitions, land mines and chemical and biological weapons.
- Undertook a full review of the risks and controls governing how we manage sector or stock exclusions.
- Added a new regulatory risk to our risk register.
- Adopted new procedures for financial counterparty approvals to include an ESG assessment.
- Improved our compliance disclosures relating to the Shareholder Rights Directive II.

Our in-house economist, Melanie Baker, provides support to portfolio managers in making strategic investment decisions, whilst the Investment Risk team carries out an independent monitoring of risk exposures in the portfolios we manage. In case of any wider market events, it is the responsibility of portfolio managers to take adequate actions with regards to portfolio allocation and any potential restructuring or strategy adjustments. This includes a review of risk tolerance levels and investment objectives to identify and appropriately address unintended sources of risk resulting from market developments and forecasts.

Risks reviewed in 2020

Climate risk

We undertook a significant amount of work reviewing our climate risks in 2020, both operationally and strategically. Much of the work involved interrogating, cleansing and understanding climate and carbon data, and educating and coaching our investment teams internally.

We consider climate risk to be a systemic financial risk, that manifests through transition risk and physical risk. Climate transition risk is associated to the socio-economic transformation to a net zero economy, while physical climate risk relates to the impacts of chronic changes and extreme weather events from an already altered global climate. We manage climate investment risk in three ways; incorporating material climate risk considerations into investment decision-making processes, using proxy voting and engagement as tools to influence company and regulator behaviour, and ensuring it is integrated into our risk framework. With climate risk oversight now formally a part of the terms of reference for the RLAM Board and Board Risk Committee, we can ensure it is appropriately monitored and reported on regularly. In addition, we have training planned for 2021.

A more detailed account of climate risk management can be found in our Climate Risk Policy and TCFD disclosure.

Operational and disaster recovery

RLAM mobilised its operations and technology teams quickly in response to COVID-19, setting over 90% of its staff up to work from home. While the RLAM business continues to operate from a predominantly working from home model, a small proportion of key staff are still based in our London offices, including individuals that are in the office for wellbeing and productivity purposes. To enhance our operational resilience, a contingency back-up solution has been successfully implemented to support our virtual desktop infrastructure which has proven to be robust and effective to date. In addition, a second contingency Internet Service Provider has been implemented. Further work is being undertaken with an external consultancy to develop and embed an operational resilience framework. The business' response to COVID-19 has been and will continue to be aligned with UK Government guidelines, and people's safety and well being are placed at the heart of our return to workplace strategy.

Brexit

As described last year, Brexit was top of mind this year for our risk and investment teams, particularly as we moved closer to the end of the year. In preparation for the exit of the United Kingdom from the European Union, Royal London Asset Management (RLAM) implemented a formal business-wide programme to monitor and take appropriate actions to respond to any detrimental impacts on its client assets and its business from the UK's exit. Following agreement on terms of a Free Trade Agreement (FTA) between the two parties and the end of transition period on the 31st December 2020, the risks of the UK exiting without an agreement failed to materialise and/or were mitigated. However, the FTA failed to outline the terms for financial services, in particular a ruling on the granting of equivalence. Therefore the programme will continue to monitor developments and take action where appropriate.

Managing conflicts of interest

RLAM is fully committed to the highest degree of professionalism, integrity and governance in doing business and ultimately to treating our customers in a fair and consistent manner. RLAM has a detailed conflicts of interest policy that all members of staff are required to read and adhere to. Overall responsibility lies with RLAM's senior management who are responsible for ensuring that RLAM systems, controls and procedures are adequate to identify, manage and monitor conflicts of interest. RLAM's senior management has responsibility for ensuring that RLAM staff are aware of the aspects of the policy relevant to them. The policy is updated annually by the Risk and Compliance team.

RLAM is 100% owned by RLMIS. RLMIS believes incorporating material ESG issues within the investment process is in customers' best interests. These functions report directly to RLMIS Board which is ultimately accountable for the management of risk within the Group and reviewing the effectiveness of internal control, including those related to conflicts of interest. Failure to adhere to our policies may be held to be a breach of an employee's contract. Failure of a person to declare an interest will be regarded as misconduct and may lead to disciplinary action being taken against the individual concerned.

Potential conflicts of interest:

- Where an investment is also a client
- Where the interests of two RLAM clients conflict
- Between RLAM and Royal London Group
- Where an employee of RLAM is a director of an investee company

The policy provides detailed guidance with respect to management of conflicts that might arise in relation to the order and execution of trades, access to inside information, management of client accounts, voting and engagement, confidential client information, gifts and entertainment, additional employment or consulting activities, and new product launches. RLAM's policy is to take all reasonable steps to properly identify and manage conflicts of interest and always to act in the best interest of our clients, so that transactions are effected on terms which are not materially less favourable to the client than if the conflict had not existed. The business maintains a Conflicts of Interest Register and a Conflicts of Interest Events Log. Should a conflict be unavoidable, RLAM will strive for appropriate and sufficiently detailed disclosure to the client. The disclosure must include the general nature of the conflict and/or the sources of that conflict and be provided before undertaking the relevant business for the client. This will allow the client to make an informed decision on whether to accept the conflict or terminate the activity.

A summary of our Conflicts of Interest policy is available on our website and the full policy will be made available on request.

Relationship with Royal London Group

RLMIS and RLAM have complete commitment to the highest standard of integrity and governance in treating our customers fairly, and take all reasonable steps to identify actual or potential conflicts of interest. We operate and maintain arrangements to minimise the possibility of such conflicts giving rise to a material risks which may damage the interests of our customers.

However, potential conflicts of interest may rise from either the relationship between RLMIS and RLAM; or due to management across different customer cohorts.

To address risks around our relationship with RLMIS, RLAM has put in place a specialised team dedicated to managing the relationship between Royal London and RLAM. The Strategic Partnership team can identify potential conflicts before they arise and communicate with RLMIS on a day-to-day basis.

The RLMIS Investment Office and Investment Proposition teams interface directly with RLAM through the Strategic Partnerships team. Any conflict of interest between RLAM and RLMIS is dealt with through the Strategic Partnerships channel.

RLAM, through the Strategic Partnerships team, are responsible for ensuring its clients are not materially disadvantaged as a result of its relationship with RLMIS, its single largest investor.

Additionally, RLMIS implements two assessments to ensure RLAM's appropriateness to manage the majority of RLMIS's assets. The first is a triennial review of RLAM's suitability, which includes a review of our governance, investment philosophy, investment performance, and fees amongst other things. The last review was conducted in 2019, and it was concluded that RLAM continues to be an appropriate manager of RLMIS's asset. The second is a Responsible Investment Monitoring Programme that RLMIS uses to review its asset managers' responsible investment capabilities. This involves detailed questionnaires and increased quarterly monitoring of RLAM's responsible investment activity.

A potential conflict of interest may also arise when managing the interests of different RLMIS policy holders. For example, when a new RLAM product is initially funded by RLMIS and subsequently invested in by other policyholders, we report a possible conflict of interest. The conflict would be if the initial seed investment was returned, this could adversely impact other policyholders' investments. Ongoing monitoring is in place where this particular risk is considered and reviewed.

Conflicts arising in 2020

The RI team logged one instance of a conflict of interest during the year. RLAM was contacted by a company disputing RLAM's decision to vote against resolutions at the company's annual meeting. While this type of correspondence is normally routine for the RI team, this particular company stated very clearly in our correspondence that they were also a client of Royal London's pensions business. We followed our conflicts of interest procedures and escalated the matter to the Risk team, Head of Equities and Chief Investment Officer. It was decided not to change our vote, and to arrange a meeting with the company to discuss their concerns.

Inside information

When engaging with companies, it is our strong preference to not be made an insider, as this restricts our ability to trade. However, on occasion, we will voluntarily agree to be given inside information in order to aid in our discussion with management or the board. Should we agree to be taken inside, the company is immediately put on our Restricted Stock List. The List is programmed into our trading systems and all fund managers in the business will be unable to trade the security. Once the information is made public, a member of the Executive Committee will provide sign-off to allow the fund managers to lift the trading restriction.

There are occasions where we have been taken inside involuntarily or inadvertently in our discussions with a company. In accordance with our Market Conduct Policy, RLAM staff are required to immediately put the stock on the Restricted Stock List, as described above, if they feel they were provided information that is not in the public domain. Staff are provided training and assistance by our Compliance Advisory and Legal teams to help identify and understand what constitutes inside information. If the situation is unclear as to whether the information disclosed to us is considered inside information, we err on the side of caution and place the company on the Restricted Stock List.

Glossary

Acronym	Explanation
AAF	Audit and Assurance Faculty
AGM	Annual General Meeting
CFRF	Climate Financial Risk Forum
DMO	Debt Management Office
ESG	Environmental, Social and Governance
FCA	Financial Conduct Authority
FPF	Friends Provident Foundation
FRC	Financial Reporting Council
GRESB	Global Real Estate Sustainability Benchmark
IA	Investment Association
IEMA	Institute of Environmental Management & Assessment
IIGCC	Institutional Investors Group on Climate Change
ILO	International Labour Organisation
LP	Limited Partner
PRI	Principles for Responsible Investment
RI	Responsible Investment
RLAM	Royal London Asset Management
RLMIS	Royal London Mutual Insurance Society
ROSCOs	Rolling Stock Companies
RPI	Responsible Property Investment
SMCR	Senior Management Certification Regime
SMFG	Sumitomo Mitsui Financial Group
SSE	Scottish and Southern Energy
TCAM	The Co-operative Asset Management
TCFD	Task force on Climate-related Financial Disclosures
TWA	The Women's Association

Notes

1 https://www.frc.org.uk/getattachment/53799a2d-824e-4e15-9325-33eb6a30f063/Annual-Review-of-the-UK-Corporate-Governance-Code,-Jan-2020_Final-Corrected.pdf

2 We may elect not to vote some of our equity holdings due to local market issues, such as shareblocking. More information can be found in our voting policies.

3 EU Shareholder Rights Directive II.

4 Sustainable Finance Disclosure Regulation (SFDR) https://www.rlam.co.uk/institutional-investors/about-rlam/sustainable-finance-disclosure-regulation-sfdr/

5 The voting database includes RLAM's voting record from January 2015. It also includes the voting records of The Co-operative Asset Management (TCAM) for the period of January 2002 to December 2014. The voting record is only available for the funds where we vote.

6 For the period of 1 October 2019 to 30 September 2020. Proxy voting is no longer in scope of the AAF review from October 2020.

APPENDIX I

Record of company engagement 2020

Below is a list of companies we engaged with in the year.

3i Group
AA
Adidas
Admiral Group
Agilent Technologies
Air Liquide
Airbus
Akelius
Allegiant Travel Co
Allianz
Alphabet
Amazon
AMPIL
Angel Trains/The Great Rolling Stock Company
Anglian Water
Anglo American
Ansys
AP Moeller Maersk
Aperam
Aptitude Software
Arcelor Mittal
Assura
AVEVA Group
Avon Rubber
Bandai Namco
Barclays
Barratt Developments
Barry Callebaut
BASF
Bellway
Berkeley Group
Berkshire Hathaway
BHP Group
Biomerieux Sa Npv
BMW
Bodycote plc
BP plc
Brewin Dolphin
British American Tobacco
British Land
BT Group
Bunzl
Cadent
CDW Corporation
Center Parcs
Centrica PLC
Chesnara
Clarkson
Close Brothers
Coats Group
Continental
Co-operative Group
CRH
Croda
Daimler
DBS Group Holdings
De La Rue
Dechra Pharmaceuticals
Derwent London
Deutsche Lufthansa
Deutsche Post
Deutsche Telekom
Diploma
Disney
Drax
DS Smith
Dunelm Group
E.ON
Eastman Chemicals
Easyjet
Electricite de France
Electrolux Professionals
Empiric Student Properties
Endesa
Enel
Engie
Eni
Equinor
Essentra
Euromoney
Experian
Facebook
FDM Group
Fiat Group
Fidelity National Information
FirstGroup
Fresenius
Fuller, Smith & Turner
Galp Energia
Gamma Communications
GCP Student Living
Glencore
Great Portland Estates
Greggs
Halma
Hargreaves Lansdown
Henkel
Hennes and Mauritz
Hill & Smith
Hilton Food Group
HSBC
Iberdrola – ScottishPower
IG Group Holdings
IMI Group
Infineon
Informa
Intermediate Capital Group
Intertek Group
Intuit
ITV
James Fisher & Sons
Japan Tobacco
JD Sports Fashion Plc
John Wood Group
Johnson & Johnson
Johnson Matthey
Koninklijke Philips
Lafarge-Holcim
Lancashire Holdings
Landesbank Baden-Wurttemburg
LandSec
Linde
Lloyds Banking Group
Lloyds of London
London Stock Exchange Group
Londonmetric Property
Magenta-1 2020
Marshalls
McCarthy & Stone
Medica Group
Mediclinic International
Melrose
Merck & Co
Microsoft
National Grid
Nationwide
Natwest
New York Life
Next
Ninety One plc
Ocado
Ofgem
Old Dominion
OMV
Onesavings Bank
Orange
Orpea
Orsted A/s
Paragon Banking Group
Pearson
Pennon Group
Pernod Ricard
Persimmon
Personal Group
Porterbrook
Primary Health
Progressive
PRS REIT
Prudential
PSA Peugot
Rathbone Brothers
Red Electrica
Reliance Steel & Alluminium
Renault Group
Rentokil Initial
Repsol
Restaurant Group
Ricardo
Rio Tinto
Roper Technologies
Royal Dutch Shell
RPM International
RWE Aktiengesellschaft
Saga
Saint-Gobain
Samsung
Segro
Senior plc
Severn Trent
SHOPIFY
Siemens Healthineers
Ag Npv
Signature Aviation
Sika AG
Smith & Nephew
Softcat
Southern Water
Speedy Hire
SSE PLC
SSP
St. Modwen
Standard Chartered
Standard Life Aberdeen
Steel Dynamics
Stobart Group
STV Group
Sumitomo Mitsui Financial Group
SUNCOR
Swedbank
Tate & Lyle
Taylor Wimpey
Telenor
Tesco
ThyssenKrupp
TI Fluid Systems
Total
TP ICAP
Transport for London
Tritax Big Box
TSB
Tyman
UK Government
Ulta Beauty
Unilever
Uniper
Unite Group
Verizon
Vinci
Vistry Group (Bovis Homes)
Vitec Group
Volkswagen
WH Smith
Wolter Kluwers
Workspace
Yew Grove REIT
Yorkshire Water

APPENDIX II

Meet the team

Piers Hillier
Chief Investment Officer

Piers joined RLAM in January 2015 as Chief Investment Officer, with responsibility for managing and developing RLAM's investment capabilities. Piers has over 25 years of investment experience, including roles as Head of International Equities and a member of the Strategic Policy Group responsible for setting Asset Allocation for multi asset portfolios at Kames Capital. Prior to this, Piers was CIO and Head of Asset Allocation for LV= Asset Management and previously CIO European Equities for WestLB Asset Management. He also previously held the position of Head of European Equities at Deutsche Bank and Schroders. In his current role, Piers is a director of RLAM Ltd, Royal London Unit Trust Management, a member of the RLAM Executive Committee, and chairs the RLAM Investment Committee. Piers holds a Bachelor's degree from the University of Bristol and Masters degree from the University of Oxford.

Ashley Hamilton Claxton
Head of Responsible Investment

Ashley joined RLAM in November 2013 following the acquisition of The Co-operative Asset Management (TCAM) by the Royal London Group. Ashley is responsible for RLAM's responsible investment strategy across all of our asset classes. She oversees a team of seven people, and has management responsibility for our company engagement, ESG analysis, and proxy voting. Before joining RLAM, Ashley worked with the UK's local authority pension funds on company engagement as a Shareholder Engagement Executive at PIRC and the Local Authority Pension Fund Forum (LAPFF). Ashley is Canadian, and started her career working with Canadian pension funds, foundations and mutual funds as a research analyst and corporate engagement consultant for SHARE, a non-profit based in Vancouver, Canada. She has a Master of Arts degree (Political Science) and a Bachelor of Arts degree (Political Science and Sociology) from the University of British Columbia. Ashley is RLAM's subject matter expert and spokesperson on responsible investing and corporate governance, and provides regular press commentary. She sits on the Sustainability and Responsible Investment committee of the Investment Association.

Sophie Johnson
Senior Corporate Governance Analyst

Sophie joined the RLAM Sustainable Investment team as an analyst on a fixed-term contract in March 2016. After a brief period working for another wealth manager, she returned to RLAM in November 2017. She is responsible for managing the proxy voting process, corporate governance analysis and focuses on company engagement on governance and social issues. Sophie joined from Institutional Shareholder Services (ISS) where she worked in both the Client Account Management and Custom Research teams. She holds a GDL and LPC from the University of Law Bristol; a LLM in International Corporate and Commercial Law from the University of York and a BA (Hons) degree in History and Archaeology. Prior to this Sophie lived and attended school in Grenoble, France for seven years.

Tom Johnson
Responsible Investment Analyst

Tom joined the team as a Responsible Investment Analyst in May 2018. He carries out a lot of the day-to-day company research, particularly in the investment grade and high yield fixed income space, both for RLAM's sustainable funds and more broadly. He also works closely with a number of equity teams and provides corporate governance support when required, particularly during proxy season. Before this Tom spent nearly three years working in Royal London's Group press office, focusing in particular on the asset management business. Tom spent a number of years growing up in Singapore, Malta and Hong Kong and has a degree in Politics and Philosophy from Cardiff University.

Beth Goldsmith
Responsible Investment Analyst

Beth joined the team as a Responsible Investment Analyst in June 2019. Day-to-day Beth maintains oversight of quarterly ESG reviews and helps to ensure that fund managers have continued access to the latest ESG information. Additionally, Beth also helps to ensure RLAM's Responsible Investment Strategy continues to have sound and robust processes and is aligned with upcoming regulation requirements and ongoing market demands. Prior to this, Beth spent five years working at KPMG, working with FTSE 250 companies on ESG disclosure and risk management. Beth holds a BA in Environmental Management from the University of Leeds.

Carlota Garcia-Manas
Senior Responsible Investment Analyst

Carlota joined from the Church of England National Investing Bodies, where she spent three years running high profile corporate engagements focused on climate change, international corporate tax, and board diversity (among others). Before joining the Church of England, she was the Director of Products and Services at a tech start-up (Datamaran, formerly eRevalue) where she led the research team to develop software for sustainability benchmarking. Prior to that, she spent ten years and was Head of Research at EIRIS (now Moody's following its merger with Vigeo) where she led global ESG research and product development. Carlota has a deep interest in analytics and the integration of externalities (environmental and social) in corporate assessment. She uses techniques learned during her business development and sales role at eRevalue in her company engagements. Carlota has studied Corporate Governance at The Chartered Governance Institute (ICSA), she is a Civil Engineer with an MSc in Environmental Economics.

Simonetta Spavieri
Responsible Investment Analyst

Simonetta joined the team as a Responsible Investment Analyst in March 2020 to work on the expansion of RLAM's engagement strategy. Prior to this, she worked at the Green Finance Institute in London and she spent four years working at the Foreign and Commonwealth Office working as Climate Change and Energy Officer. Simonetta studied International Relations and Public Administration and holds an MSc in Environmental Change and Management from the University of Oxford.

Jeffrey Ndeti
Corporate Governance Analyst

Jeff joined the RI team in October 2019 as an analyst working on proxy voting, company engagement and corporate governance analysis. Previously, Jeff spent nearly three years at ISS where he worked as a custom research analyst in providing bespoke proxy voting solutions and corporate governance consultations to several institutional investors. While Jeff currently resides in the UK, he often travels to his birthplace country of Kenya to connect and spend time with his extended family. He holds a Masters in Economics from the University of Exeter and a BSc (Hons) Economics degree from Swansea University.

Piotr Kwiatkowski
Corporate Governance Analyst

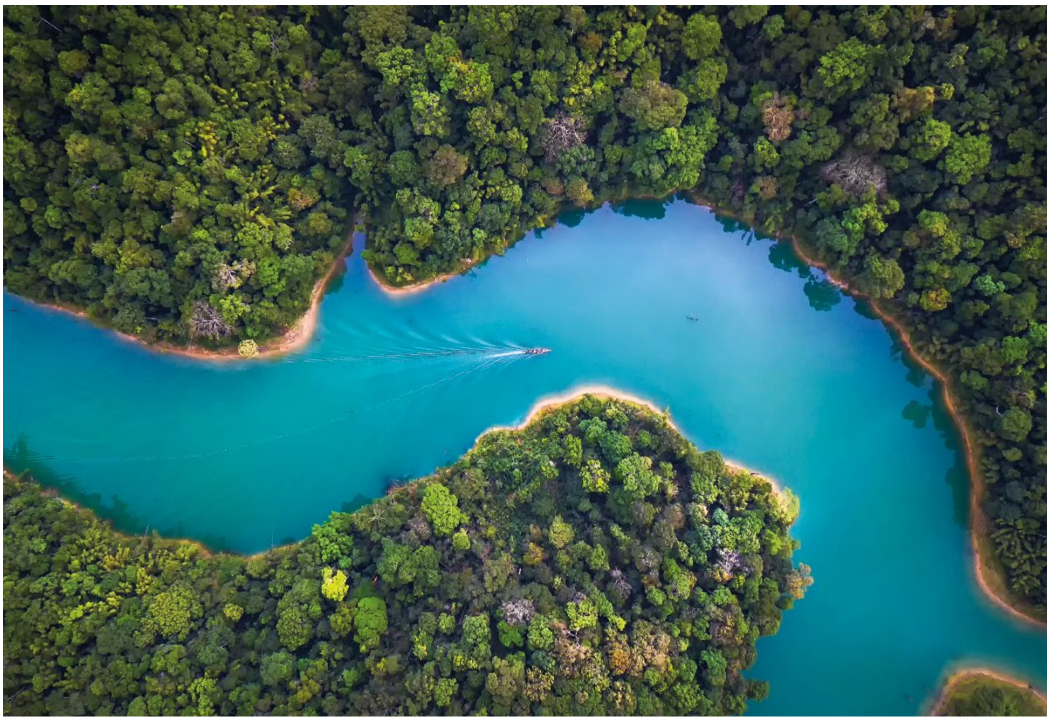
Piotr joined the team as a Corporate Governance Analyst in October 2019, to work on the expansion of RLAM's proxy voting and governance activities. Piotr has joined from ISS, where he worked as a custom research analyst, providing institutional investors with bespoke proxy voting recommendations. Piotr has a Masters degree in Business Law and LL.M. in Corporate and Commercial Law from Maastricht University. Prior to moving to the UK, Piotr spent almost seven years gaining his educational and work experience across continental Europe while living in Poland, France, Netherlands, Portugal and Belgium.

Abigail Hall
Assistant Responsible Investment Analyst

Abi joined the RI team in November 2019 as an Assistant Responsible Investment Analyst. She moved over from the RLAM Marketing team where she had spent the last three years as a Marketing Executive, servicing both institutional and wholesale channels. Prior to joining RLAM, Abi held sales support and project roles at Schroders and EY respectively. Abi provides general support to the RI team in terms of research and data analysis, and assists in providing more agile and effective responses to client queries, due diligence questionnaires, and RFPs. She is also responsible for helping the team to convey its 'story' to key stakeholders through the effective use of communication channels. Abi has a BA (Hons) degree in Business Management from the University of Greenwich.

Tim Coffin
Responsible Investment Property Manager

Tim joined the RLAM Property team in 2019 as RPI Manager. His primary focus is to ensure the funds actively integrate ESG property investment and management considerations into the entire process. He also acts as the RPI champion and expert within the RLAM Property team, bringing technical experience in resource (energy, waste and water) efficiency, transactions, compliance/regulation and benchmarking. Prior to joining RLAM, Tim worked for 9 years at the pension fund USS, within the Property team as their RPI Manager. Tim holds a BA (Hons) in Business Environmental Management from Brunel University. He is a Practitioner Member of the Institute of Environmental Management & Assessment (IEMA).



APPENDIX III

The UK Stewardship Code

Principles for asset owners and asset managers

Purpose and governance	Document reference
1 Purpose, strategy and culture	Our purpose and strategy, page 6 Our culture and values, page 67
2 Governance, resources and incentives	Our responsible investment team, page 12 How we are governed, page 68 Performance management and reward, page 70
3 Conflicts of interest	Managing conflicts of interest, page 72
4 Promoting well-functioning markets	Advocacy and public policy, page 20 Product development, page 70 Risk management and monitoring, page 71 COVID-19 and calls for a sustainable recovery, page 12 Engagement priorities, page 21
5 Review and assurance	Review and assurance, page 65

Investment approach	Document reference
6 Client and beneficiary needs	Supporting our clients' needs, page 69
7 Stewardship, investment and ESG integration	Our approach to stewardship, page 8 ESG integration, page 44
8 Monitoring managers and service providers	Risk management and monitoring, page 71 Proxy voting research, page 43 Use of research, page 44

Principles for asset owners and asset managers

Engagement	Document reference
9 Engagement	Engagement and advocacy, page 17
10 Collaboration	Investor collaboration, page 20
11 Escalation	Escalation and public comments, page 20

Exercising rights and responsibilities	Document reference
12 Exercising rights and responsibilities	Our approach to voting, page 41 Bondholder voting, page 43

APPENDIX IV

The UN Principles of Responsible Investment

Principle	Document reference
1 We will incorporate ESG issues into investment analysis and decision-making processes.	Our approach to stewardship and responsible investment, page 8 ESG integration, page 44
2 We will be active owners and incorporate ESG issues into our ownership policies and practices.	Our approach to stewardship and responsible investment, page 8 ESG integration, page 44 Engagement and advocacy, page 17 Governance and voting, page 35 How we are governed, page 68 Supporting our clients' needs, page 69
3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.	Engagement and advocacy, page 17
4 We will promote acceptance and implementation of the Principles within the investment industry.	Our approach to stewardship and responsible investment, page 8 Escalation and public comments, page 20 Advocacy and public policy, page 20
5 We will work together to enhance our effectiveness in implementing the Principles.	What's next?, page 66 Investor collaboration, page 20
6 We will each report on our activities and progress towards implementing the Principles.	Disclosure and transparency, page 65

Signatory of:

PRI Principles for Responsible Investment

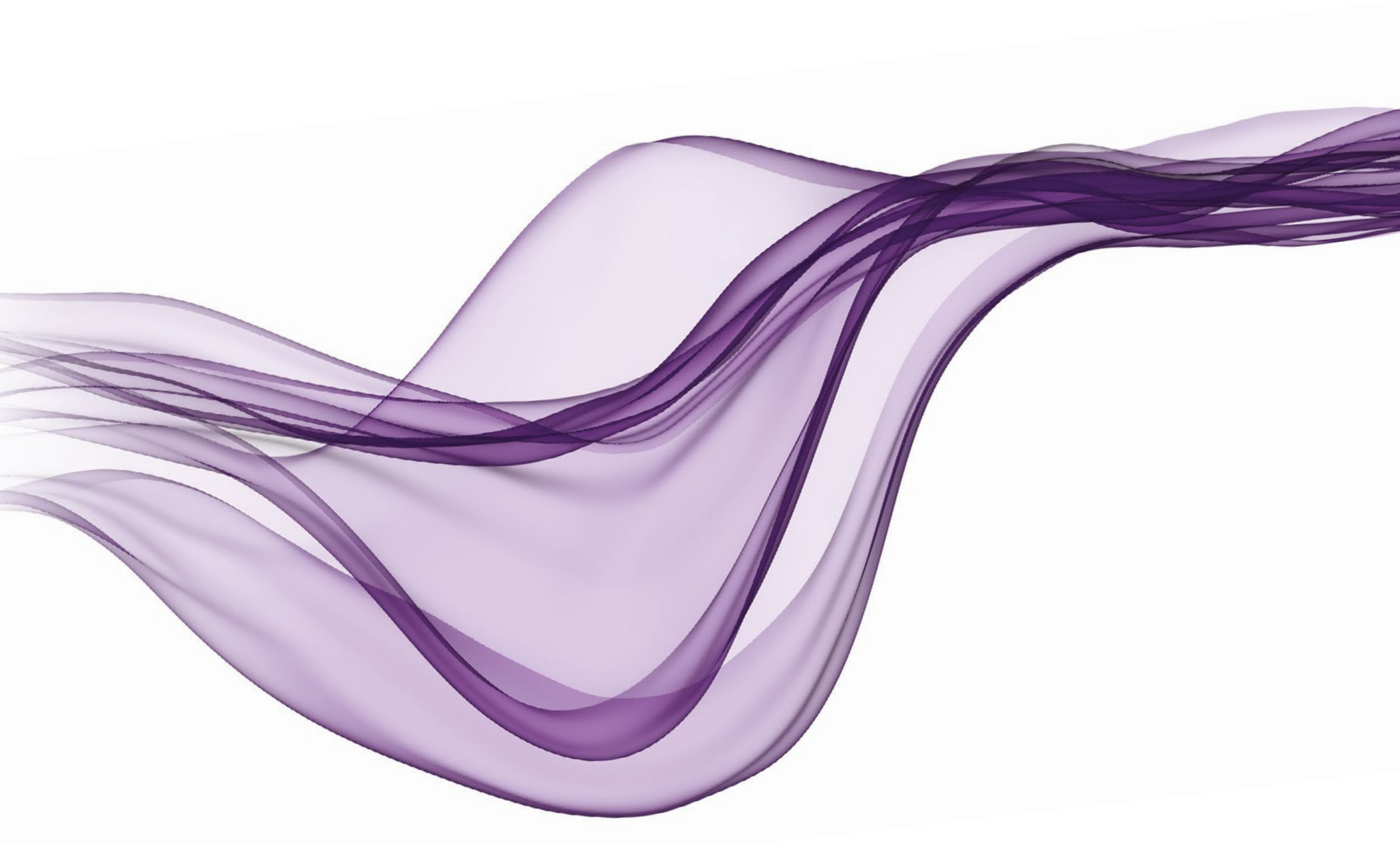
Useful links

RLAM Responsible Investment web page
www.rlam.co.uk/institutional-investors/our-solutions/responsible-investment/

RLAM Sustainable Investing web page
www.rlam.co.uk/institutional-investors/our-solutions/sustainable-investing/

UK Stewardship Code 2020
www.frc.org.uk/getattachment/5aae591d-d9d3-4cf4-814a-d14e156a1d87/Stewardship-Code_Dec-19-Final.pdf

PRI Definitions and terminology
https://d8g8t13e9vf2o.cloudfront.net/Uploads/d/t/z/maindefinitionstoprireportingframework_127272.pdf



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