

# The engagement landscape in the UK

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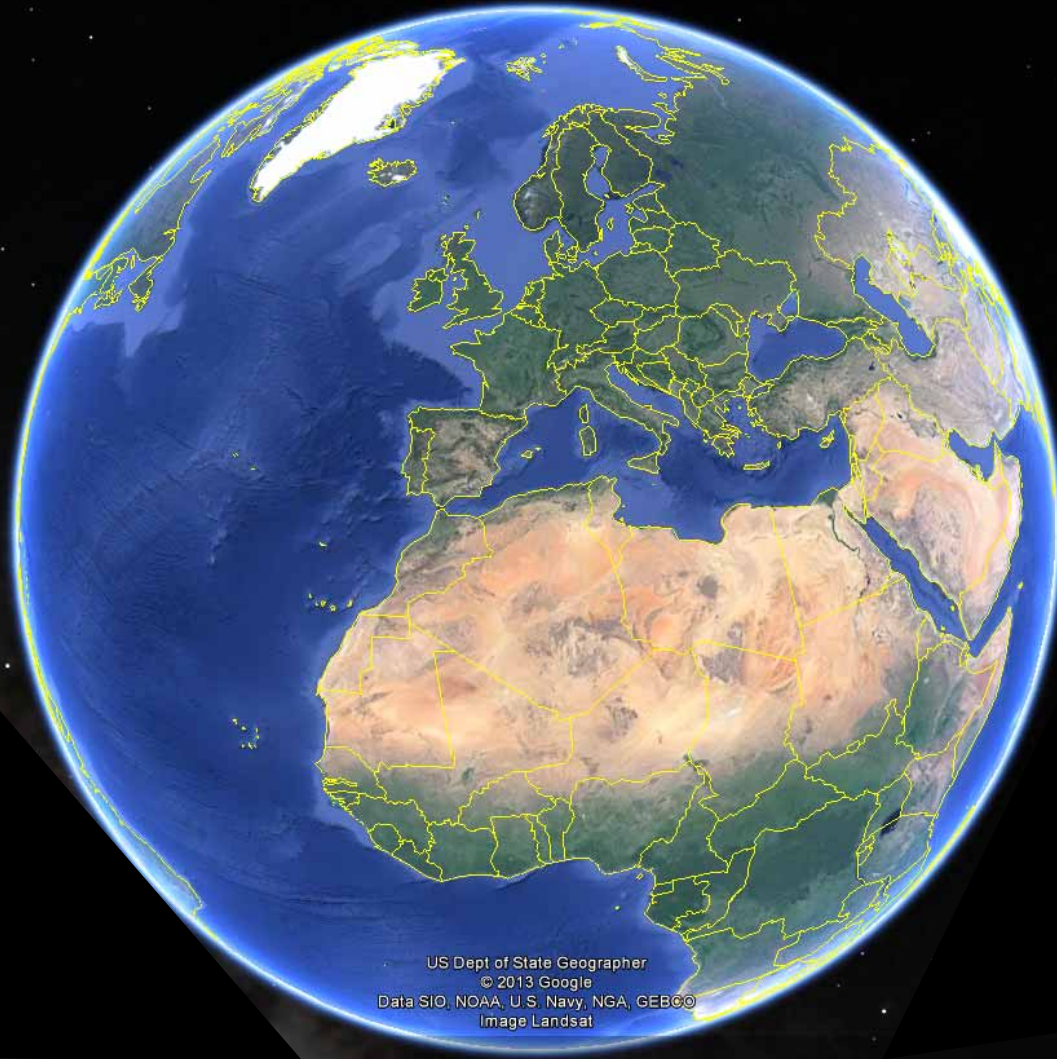
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# A road map for engagement – the Stewardship Code



- Seven principles
- Comply or explain
- 290 signatories
- Focus on UK listed equities
- 90% of pension funds have policy

# 'Emerging from the mist'

- Focus on corporate governance (remuneration)
- Board composition & strategy
- Proactive engagement

# The swampy lowlands of engagement

- Signed up 'in name only'
- Focus on large companies only
- Conflicts of interest

# And the broad sunlit uplands



- Collective engagement
- Importance of long-term holding periods
- Measuring and reporting impact



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## **Investor engagement: Challenges and opportunities**

Yo Takatsuki

14 February 2014

## Leadership

- Europe's first ethical fund in 1984 and investor engagement service in 2000
- 23 external engagement clients, €100 billion assets in advice

## Expertise

- Dedicated in-house Governance and Sustainable Investment (GSI) team of experts conducts all ESG research and engagement

## Global coverage

- Engagement with over 700 companies in 50 markets on key ESG issues

## Proven track record

- €3.7 billion in dedicated responsible investment funds
- Achieving change at 293 companies on key ESG issues in 2013



## We identify high risk companies and stop vulnerabilities developing

- Proactive engagement
  - Regular assessment of exposure to companies, sectors and issues in portfolios
  - Focus on achieving outcomes material to investors
- Identifying targets through analysis
  - Quantitative: ESG rating system to identify high risk companies
  - Qualitative: assessment of company performance beyond disclosures and policy
  - Emergent issues: knowledge of new trends in sectors and countries
  - Examples: supply chain standards, bribery and corruption
- Reactive engagement
  - Event-led: examples include Gulf of Mexico, Fukushima, Libor
  - Respond quickly, but follow-up engagements can be long-term

## Engagement tactics change with circumstance

- Access to company vs. no access to company
  - Market and sector dependent: some becoming very open to ESG engagement
  - The worst performers can stone-wall investors and refuse to co-operate
  
- Top-down engagement vs. bottom-up engagement
  - Board and CEO level: in some countries, this is the only way to press for change
  - Operational specialist: building institutional capacity
  
- Solo vs. collaborative
  - Solo can be quicker
  - Collaboration can be more effective than any single investor
  - Institutional Investors Group on Climate Change, Asian Corporate Governance Association

## Key factors for success

- Tenacity – change can take time
- Challenge status-quo
- Specialist knowledge
- Network stakeholders

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Equity Ownership Services

# Challenges and Suggestions to Improve Dialogue Between Shareholders and Boards in France and the UK

14 February 2014

Natacha Dimitrijevic, Head of European Engagement

# Hermes Equity Ownership Services (EOS)

- Hermes Equity Ownership Services (EOS) was **established in 2004** in recognition that stewardship activities require specialist skills and processes
- Hermes EOS is owned by Hermes Fund Managers, which is wholly owned by the **BT Pension Scheme (BTPS)**, one of the UK's largest pension funds (€47.3bn AuM<sup>1</sup>)
- 36 institutional investors in 10 countries delegate to us the stewardship of **over €150bn of assets<sup>2</sup>** invested in over **10,000 companies** worldwide
- We have 23 full-time staff and six senior advisors, who are structured in four regional teams. We also have working relationships with many of the world's largest institutional investors
- Hermes EOS currently acts for clients invested in **listed equities and corporate fixed income**
- **Hermes is a founding signatory** of the United Nations Principles for Responsible Investment. Hermes EOS' Chief Executive, Colin Melvin, **chaired the committee** that drafted the principles

<sup>1</sup> Pension Funds and Their Advisors 2012 BTPS Report & Accounts, 31 December 2012.

<sup>2</sup> Assets under Advice as at 30 September 2013.



## Our rationale for influence

Hermes EOS' mission is to add long-term value to asset owners' investments and manage their risks by engaging with companies and policy makers on environmental, social, governance, strategic and financial issues.

### **Capital markets suffer from two structural weaknesses**

1. The Agency problem: management prioritises their own interests
2. Short-termism: management under-weights long-term risks

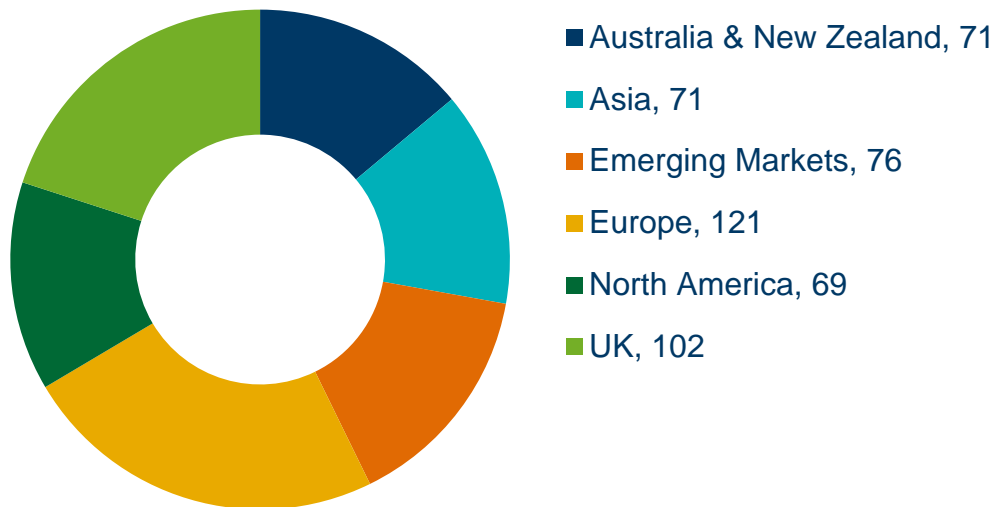
### **These weaknesses can lead to material risks, including:**

- Strategy and finance misalignment
- Governance risks
- Environmental, social and ethical risks

# Engagement

## Global engagement activity

Company engagement by region (510)



## 2012 engagement activity

- We engaged with 510 companies to seek change on 989 separate engagement objectives
- Of the 989 objectives:
  - 49% on governance
  - 19% on social & ethical
  - 18% on environment
  - 14% on strategy & risk management
- All engagements tracked using “milestones”
- We made progress on over 30% of our objectives

Milestone 0	Milestone 1	Milestone 2	Milestone 3	Milestone 4
Objective set	Raised concern at appropriate level	Company acknowledges issue	Company commits to credible change	Change implemented

Source: Hermes



## Priorities for engagement in 2014

### Europe

#### 1- Remuneration

say on pay in France, Minder in Switzerland;

New disclosure requirements in Spain and Germany;  
CRDIV

#### 2- Board balance and accountability

Combined roles and SID; foundations; social  
representation; state/family holdings

#### 3- Minority shareholder rights

Loi Florange en France

### UK

#### 1- Remuneration

Binding vote, single figure; CRDIV

#### 2- Audit quality and board oversight

FRC regulation; Auditors' code of conduct

#### 3- Board diversity and accountability

## Drivers informing the dialogue between boards and institutional shareholders

- Culture, legal rules and historic interpretation of the role of boards
- Company specifics and sectors
- Stewardship codes



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