


# Stewardship Report 2023

April 2024

**Federated  
Hermes**   
Limited

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For professional investors only



On behalf of and in the interests of the investors it serves, the investment industry can be a powerful force in building resilient companies in resilient economies that create wealth sustainably – and at Federated Hermes Limited (FHL), we believe active stewardship is the best way to achieve this objective.<sup>1</sup>

<sup>1</sup> For purposes of this report, references to “Federated Hermes Limited”, “FHL”, “our”, “we”, “our firm” and, unless the context indicates otherwise, “firm” include Federated Hermes Limited and its consolidated subsidiaries, other than Hermes Equity Ownership Services Limited. Hermes Equity Ownership Services Limited (“EOS at Federated Hermes” or “EOS”) will report separately. The statements, references to officers, practices and policies, and discussions in this report pertain to Federated Hermes Limited, and not to other business engaged in by Federated Hermes, Inc. and its other consolidated subsidiaries. Certain statements in this report constitute forward-looking statements, which involve known and unknown risks, uncertainties, and other factors that may cause the actual results, activities or levels of activity, performance or achievements of FHL to be materially different from any forecast results, levels of activity, performance or achievements expressed or implied by such forward-looking statements.

2023 has been another turbulent year for the global economy; as inflation, rising interest rates, tight labour markets and geopolitical shocks fuelled uncertainty.

With catastrophic flooding across 10 countries in 12 days, the hottest ocean temperatures ever recorded, heat waves that scorched the entire Northern Hemisphere, and the worst drought in 40 years across the Horn of Africa – 2023 was also the year climate change became exceedingly undeniable.<sup>2</sup> At the same time, the energy ‘trilemma’ which defined 2022 – managing climate risks while ensuring energy security and affordable access to energy – continued into 2023.

Nonetheless, the US Inflation Reduction Act (IRA) of August 2022 underpinned an increase in renewable energy and clean tech investment and energy prices eased in many markets, helped to reduce inflationary pressures, although the ‘cost of living’ crisis persisted in many markets. This series of environmental and macroeconomic challenges reinforced the focus of our advocacy and stewardship activities in 2023. Geopolitical tensions also remained heightened in 2023, with no sign of an end to the war in Ukraine and the destabilisation of the Middle East through the conflict in Israel and Gaza. Against this backdrop, we continued to engage with companies on how they address geopolitical risks facing their businesses and their approach to safeguarding human rights in high-risk regions.

Amidst all of this, regulators and standard setters remained active in 2023. Disclosure continued to be a focus, including the issuance of the inaugural International Sustainability Standards Board (ISSB) standards and the Transition Plan Taskforce (TPT) Final Disclosure Framework. The publication of the Taskforce for Nature-related Financial Disclosure (TNFD) recommendations reflected the growing focus on nature-related issues. Regulatory focus on ensuring investor transparency continued with the publication of new sustainability disclosure requirements in the UK and review of the effectiveness of the Sustainable Finance Disclosure Regulation (SFDR) in the EU disclosure is, however, not the end in itself. As data availability improves, regulations are emerging to encourage corporates and financial institutions towards concrete action. In the EU, for example, 2024 will see the adoption of the Corporate Sustainability Due Diligence Directive (CSDDD) to require companies to take action to identify and mitigate actual and potential social and environmental adverse impacts in their value chains.

As a business dedicated since our 1983 inception to delivering sustainable wealth creation that enriches investors, and, where possible, society and the environment over the long term, we will continue to invest, engage and act to support the change needed by the planet, its people and the generations to come consistent with client objectives and applicable requirements.



**David Stewart**  
Chair,  
Federated Hermes Limited



**Saker Nusseibeh, CBE**  
CEO,  
Federated Hermes Limited



**Leon Kamhi**  
Head of Responsibility,  
Federated Hermes Limited

<sup>2</sup> FUN Foundation, ‘Year In Review: The Events That Shaped Our World In 2023’ (December 2023).

## Executive summary

### **Stewardship: 'The responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society'. [UK Stewardship Code 2020]**

Following on from our 2022 Stewardship Report, this report describes our continued stewardship work across asset classes during 2023 and the outcomes of these activities. We have followed the structure of the UK Stewardship Code, reporting principle by principle to communicate our policies, processes, activities and outcomes to clients and wider stakeholders.

Building on last year's reporting, we summarise our approach to deforestation and include information from our first report on deforestation risk assessment and mitigation activities across our public markets, real estate, infrastructure, and direct lending portfolios. We have also set out the updates to our diversity, equity and inclusion ("DE&I") Strategy and the formation of six core DE&I project groups. In our latest Climate-related Financial Disclosures Report, we enhanced our climate scenario analysis across our public equity and credit investments and piloted elements of the Taskforce on Nature-related Financial Disclosures (TNFD) recommendations, details of which are included under Principle 4 and 6.

We begin once again by setting out our purpose, our beliefs and our values that drive our strategy and business model. Our stewardship activities flow from this overarching structure, demonstrating how we contribute to building a global financial system that aims to deliver improved long-term returns for investors, as well as, where possible, better, more sustainable outcomes for society.

All of the work we do as responsible stewards of capital is underpinned by our purpose, values and investment beliefs which we describe under Principle 1. From our 1983 inception through to the present day, our purpose has been to deliver sustainable wealth creation for investors over the long-term. We believe there are four mutually reinforcing strands of being a responsible investment manager and steward: ESG-integrated investments; active ownership and management; advocating in beneficiaries' interests; and behaving as a responsible business. Together, these aim to generate sustainable wealth creation for the end beneficiary investors,

encompassing investment returns and their social and environmental impact. This drives our governance structures – designed to put our clients and beneficiaries at the heart of everything we do – and our investment and engagement activities, through which we seek to provide strong risk-adjusted investment performance for clients and in doing so achieve positive outcomes for society and the environment, consistent with client objectives and applicable requirements. It is our contention that long term investment returns and beneficial outcomes for society are often mutually reinforcing.

Whilst stewardship rightly addresses ESG issues, it should not be conflated with ESG. Carried out effectively stewardship is concerned holistically with all aspects of a company's strategy and performance including where material, E, S and G drivers of performance. Similarly, 'ESG integration' ensures that material E, S and G factors are integrated into investment decision-making alongside traditional performance factors.

We continuously strive to reflect on our efficiency and the outcomes we are delivering in order to identify further ways in which we can enhance our approach. Throughout the report we reflect on enhancements made to our approach during 2023, as well as areas identified for further improvement in 2024.

In collating this report, we have taken steps to ensure it is fair, balanced and understandable. We have provided information across asset classes, with the representation reflecting the makeup of our assets under management ("AUM"). In doing so, we have communicated our successes, reflected on our learnings and highlighted the changes we will make in the next 12 months. We also provided examples and case studies throughout the report to demonstrate how our investment approach works in practice. Each section of the report has been reviewed by the relevant business areas, as well as by our Governance Committee. The report has been approved by our Board.

This report also fulfils the entity-level reporting requirements for Federated Hermes Limited – which includes its subsidiaries Hermes Investment Management Limited, Hermes GPE LLP, Hermes Fund Managers Ireland Limited and Hermes Alternative Investment Management Limited (together "FHL Entities" and each an "FHL Entity") – under Annex C of the EU Shareholder Rights Directive and as required by the FCA Conduct of Business Sourcebook 2.2B.

Those investment portfolios managed by Hermes Fund Managers Ireland Limited (other than those of Federated Hermes Investment Funds plc) where discretionary investment management has been delegated to Federated Investment Counseling and/or Federated Global Investment Management Corp. are not in scope of this report.

EOS at Federated Hermes will report separately under the Stewardship Code as a service provider.



# Contents

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Purpose and governance	
1. Purpose, strategy and culture	6
2. Governance, resources and incentives	16
3. Conflicts of interest	26
4. Promoting well-functioning markets	30
5. Review and assurance	49
<hr/>	
Investment approach	
6. Client and beneficiary needs	53
7. Stewardship, investment and ESG integration	57
8. Monitoring managers and service providers	76
<hr/>	
Engagement	
9. Engagement	78
10. Collaboration	96
11. Escalation	100
<hr/>	
Exercising rights and responsibilities	
12. Exercising rights and responsibilities	103
<hr/>	
Glossary	111



# Principle 1

Signatories' purpose, investment beliefs, strategy, and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

**Our goals are to help individuals invest and retire better, to help clients achieve better risk-adjusted returns and, consistent with client objectives and applicable requirements, to strive to contribute to positive outcomes in the wider world.**

## Who we are

From when our first CEO openly challenged a major UK company to improve its governance to when our current CEO Saker Nusseibeh was awarded a CBE for services to responsible business, Federated Hermes Limited (FHL) has always been at the forefront of responsible investing. We are guided by the conviction that responsible investing is the best way to create long-term wealth for investors.

We are an active asset manager with a difference. We were set up to manage the pension funds of British Telecommunications ("BT") and the Post Office in September 1983 and have engaged with companies from day one. In 1983, our first CEO, the late Ralph Quartano, admonished the Marks & Spencer Board for the special loans they made available to directors. He made it clear we were committed to serving the needs of our clients – the 400,000 beneficiaries whose money we part-managed – and that we understood that the investment decisions we made on their behalf helped to determine the shape of the future society in which they would live.

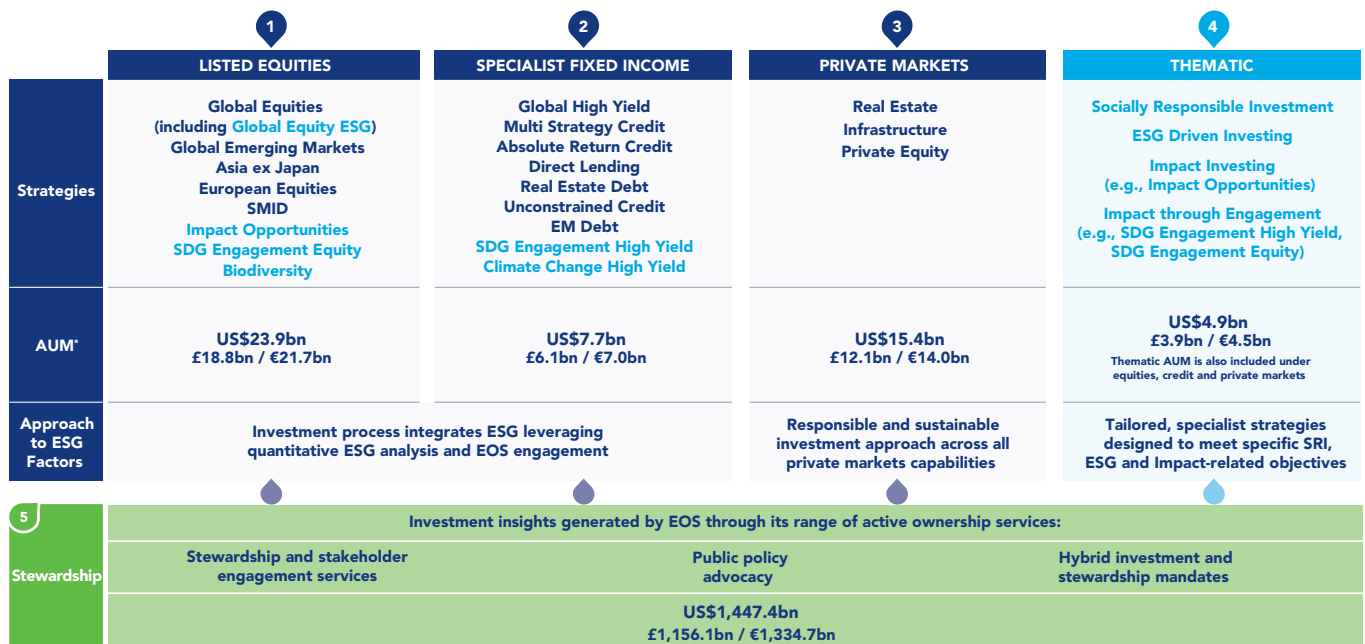
In 1996, we set up a dedicated corporate governance team to engage with companies, make voting recommendations and advise on all aspects of corporate governance and strategy including environmental and social considerations. In 2004, this team evolved into our stewardship business, now EOS at Federated Hermes ("EOS"). EOS was set up in response to demand from pension funds that wanted to be more active owners of the companies in which they were invested.

Our client base has since expanded rapidly, with growth in third-party AUM and stewardship assets under advice ("AUA"). These origins have driven our purpose, investment beliefs and strategy throughout our history, from when we established our Focus Funds business in 1998, to our work challenging boards and pushing for corporate-governance reform, to when we founded EOS in 2004.

Since our beginnings, we have sought to help clients achieve strong risk-adjusted returns through our specialised equity, fixed-income and private-market strategies and, more recently, our multi-asset and proven liquidity-management solutions. Through these strategies and solutions, we continue to aim to help individuals to save and retire better over the long-term.

In February 2020, Federated Investors, Inc. and Hermes Fund Managers Limited formally announced the rebranding of the two companies to "Federated Hermes" (the entity names

Figure 1. FHL's investment capabilities



Key: Investment strategy: Strategies that contribute to Thematic investing

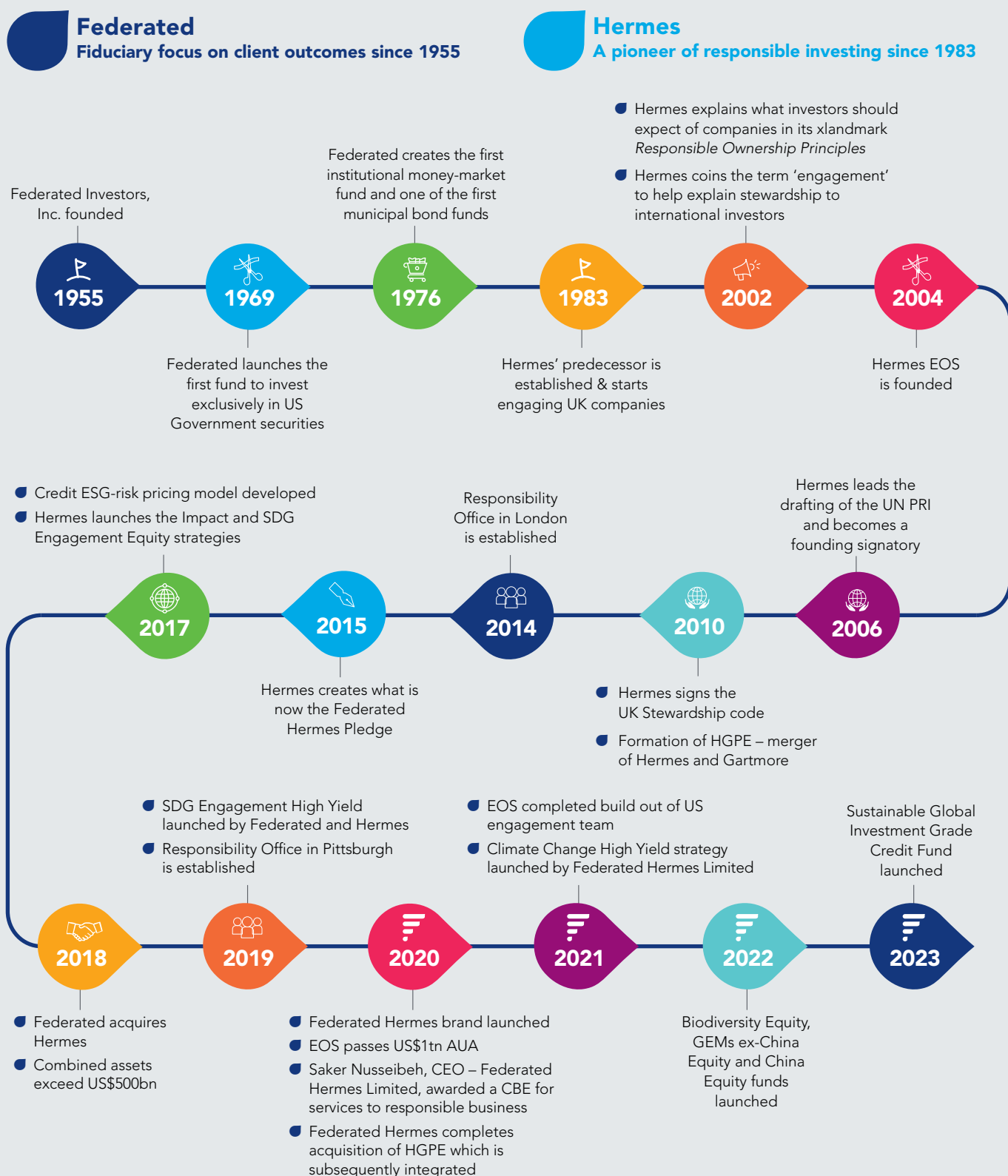
AUM does not include assets under sub advice. Source: FHL, as at 31 December 2023.

changing to Federated Hermes, Inc and Federated Hermes Limited, respectively), strengthening our position as a global leader in active, responsible investment. Federated Hermes Limited ("FHL") has been a subsidiary of Federated Hermes, Inc (FHI) since 1 September 2021. Since Federated acquired Hermes, we have been united by a shared commitment to client-centric responsible investment and long-term business growth.

### Our values

We believe that responsible investment and active ownership is the best way to sustain long-term outperformance. and contribute to beneficial outcomes for investors and companies, as well as, where possible, society and the environment.

Figure 2. Our history as a leading responsible investor has been decades in the making



Source: FHL, as at 30 April 2024.

Since our business began in 1983, we have advocated for and sought to embody a way of investing that enriches investors and companies, as well as, where possible, society and the environment. Sustainable wealth creation is our way of ensuring the capital we invest generates financial outperformance and, where aligned and performance enhancing, environmental and social outcomes – not only for our clients and their investors but for the generations that will follow. We aim to create sustainable wealth for investors through high active share investing, integration of all material factors including ESG considerations and stewardship.

**Since our business began in 1983, we have advocated and sought to embody a way of investing that enriches investors and companies, as well as, where possible, society and the environment.**

In an industry where many peers are awakening to the appeal of sustainable investment, we are energised by the opportunity to advance the leadership position we have long held by driving further change.

We have continued to develop and increase the sophistication of our approach to stewardship on themes, sectors and regions in consultation and agreement with our clients. Our clients, the companies we engage and the policymakers we seek to influence know us first and foremost as a professional voice for investors on sustainability.

**We have continued to develop and increase the sophistication of our approach to stewardship on themes, sectors and regions in consultation and agreement with our clients.**



We aim to act with integrity in everything we do. The Federated Hermes Pledge, first established by FHL in 2015 and adopted by FHI in 2018, compels us to put clients' interests first and to act responsibly. It is a clear expression of our values and reads as follows:

**I pledge to fulfil, to the best of my ability and judgment and in accordance with my role, this covenant:**

- I will act ethically, responsibly and with integrity.
- I will put the interests of our clients first, consistent with our fiduciary responsibilities.
- I will encourage responsible behaviour in the firms in which we invest and on which we engage.
- I will act with consideration for our community and the environment both now and in the future. I will encourage others to do the same.
- I will work with industry colleagues and other key stakeholders to develop and improve our industry's contribution to society.
- I will treat my clients, my colleagues and all other stakeholders with dignity and respect and as I would wish to be treated.
- I will deal with our regulators in an open, co-operative and timely way.
- I will communicate clearly and honestly with all parties inside and outside our firm.
- I will manage conflicts of interest fairly between all parties.

Our fiduciary heritage and expertise in responsible investment ensure that our clients' interests come first.





## Our investment beliefs


**We believe the purpose of investment is to create wealth sustainably for investors over the long term.**


That's why focusing on wealth creation at the expense of the planet and society – the very future for which investors are saving – is counterproductive. Our world faces multiple challenges, including climate change, inequality and navigating the ever-pervasive growth of artificial intelligence.


**Successful sustainable wealth creation should provide investors with income to spend as they get older, an ability to buy goods and services and help to build a world in which investors are happy to live.**

Investment management has a key role in addressing those challenges and the industry must behave in a way consistent with solving the world's problems rather than compounding them. This will have notable positive financial implications for investors and society, guarding against significant risks to the long-term health of the economy. Successful sustainable wealth creation should provide investors with income to spend as they get older, an ability to buy goods and services and help to build a world in which investors are happy to live.

We view responsibility through three lenses. Acting as a:

 **Responsible Investor** – how we integrate engagement insights and ESG considerations including the delivery of sustainable outcomes into our investment decisions.

 **Responsible Owner** – our stewardship activities: engagement, voting, public policy and screening.

 **Responsible Firm** – ensuring we lead by example, be that our commitment to net zero, our approach to diversity, equity and inclusion amongst colleagues and other stakeholders and our charity initiatives and programmes supporting the local community.

**We firmly believe that our ability to mitigate ESG risks and capture the investment opportunities arising from material ESG considerations and engagement insights is essential to achieving consistent investment outperformance for our clients.**

As responsible investors, we embrace high-active-share investing. We take a holistic approach that integrates material ESG considerations and engagement insights into all of our investment products, something that offers our fund managers an additional vantage point with which to assess an asset's potential to deliver long-term sustainable wealth.

We firmly believe that our ability to mitigate ESG risks and capture the investment opportunities arising from these considerations is essential to achieving consistent investment outperformance for our clients.

Acting as responsible owners of the assets we manage on behalf of our clients, we actively engage through dialogue with companies including on ESG issues. We believe this is essential in order to build a global financial system delivering improved long-term returns for investors, as well as, where possible, better and more sustainable outcomes for society.

The importance of environmental metrics was evidenced in recent research from our Global Equities team, with the best placed companies performing ahead or in line with peers, while poorly ranked companies tended to significantly underperform.<sup>3</sup> This followed on from our previous research which confirmed the link between social and governance factors.<sup>4</sup>

**Acting as responsible owners of the assets we manage on behalf of our clients, we actively engage through dialogue with companies including on ESG issues.**



<sup>3</sup> Federated Hermes Limited, 'Despite headwinds, ESG continues to perform', (July 2022).

<sup>4</sup> Federated Hermes Limited, 'ESG investing: How Covid-19 accelerated the social awakening', (December 2020).

Successful engagement can also translate into outperformance: studies have shown how engagement can generate higher annualised returns<sup>5</sup>, while also leading to lower downside risk.<sup>6</sup> There is no conflict between doing good and good investment management – they are one and the same thing.

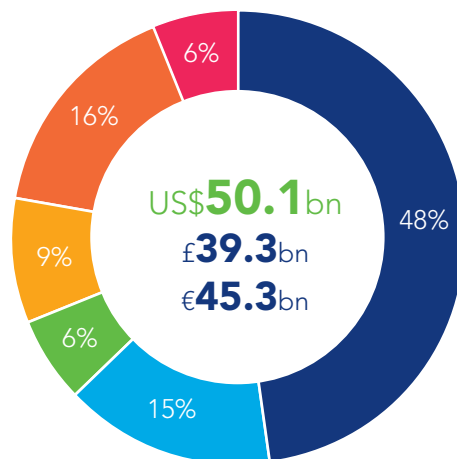
### Our business model and strategy

FHL is committed to delivering superior risk-adjusted investment returns for our clients. In addition to our financial targets, we understand that the way we achieve our investment objectives will have wider societal impacts. As such, we seek to provide both a better financial future for our ultimate stakeholders and, where possible, a more sustainable society. The pursuit of sustainable wealth creation drives the execution of all of our strategies consistent with client objectives and applicable requirements.

Our heritage has enabled us to put this into practice since 1983. We did this first by managing the assets of the BTPS and subsequently by offering our skills to a broad and fast-growing range of global customers that includes institutions and advised private investors. Our specialist, high-conviction investment teams now manage £39.3bn / €45.3bn / \$50.1bn (as at 31 December 2023) of assets across equities, credit, private debt, real estate, infrastructure and private equity.

**Successful engagement can translate into outperformance: studies have shown how engagement can generate higher annualised returns,<sup>5</sup> while also leading to lower downside risk.<sup>6</sup>**

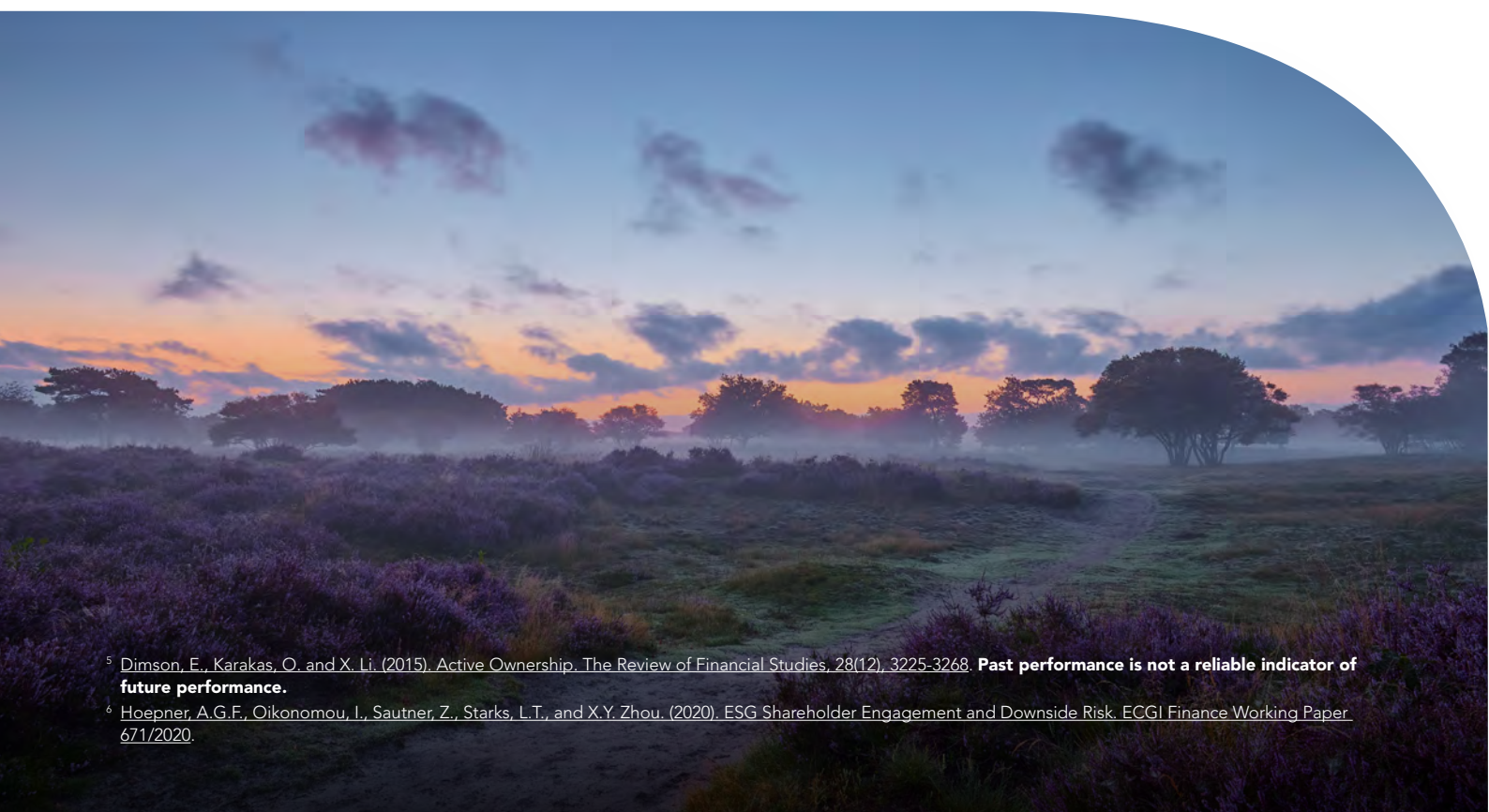
Figure 3. A diversified platform



Total AUM (Millions)	USD	GBP	EUR
Equity	23,943	18,782	21,676
Real Estate	7,684	6,028	6,956
Infrastructure	3,011	2,362	2,726
Private Equity	4,727	3,708	4,280
Fixed Income	7,739	6,071	7,006
Liquidity	2,976	2,334	2,694

'Liquidity' in the pie chart above includes our money market funds. Source: FHL, as at 31 December 2023.

Through EOS – one of the largest stewardship resources of any fund manager in the world – we engage companies on strategic and material ESG concerns to promote investors' long-term performance and fiduciary interests. EOS offers a shared service model, engaging on behalf of both FHL and third-party clients.



<sup>5</sup> Dimson, E., Karakas, O., and X. Li. (2015). Active Ownership. *The Review of Financial Studies*, 28(12), 3225-3268. **Past performance is not a reliable indicator of future performance.**

<sup>6</sup> Hoepner, A.G.F., Oikonomou, I., Sautner, Z., Starks, L.T., and X.Y. Zhou. (2020). ESG Shareholder Engagement and Downside Risk. *ECGI Finance Working Paper 671/2020*.



EOS provides a platform for like-minded investors, creating a powerful force for positive change. The team works on behalf of long-term global investors who entrust us with the stewardship of approximately £1.2tn / €1.3tn / \$1.4tn (as at 31 December 2023) invested in over 10,000 companies worldwide, working collectively in support of shared goals. This pooling of assets increases the influence we can have with companies, which means we can have a more meaningful impact on the issues of most collective importance to our clients.

#### Four platforms

In order to continue to lead and oversee the public markets teams based in Europe, to further expand the private markets offering and to drive the responsible investing agenda for our firm, the Board of FHL has resolved to establish four distinct platforms:

- The **Public Markets** platform – incorporating our Equities and Fixed Income & Multi Asset products and solutions.
- The **Private Markets** platform – incorporating Private Equity, Private Debt, Real Estate and Infrastructure.
- The **Liquidity** platform – which includes a range of sterling-, euro- and dollar-denominated short-term and standard money market funds as well as bespoke solutions for institutional investors. The funds captured within this platform are excluded from this report.
- The **Responsibility** platform – which includes EOS at Federated Hermes, our advocacy team, research, ESG integration and some client advisory activities.

#### EOS provides a platform for like-minded investors, creating a powerful force for positive change.

These form the basis of how we will view our commercial offering and will be supported by all the existing functions necessary to deliver a great client experience – Audit, our Client Group, Compliance, Corporate Communications, Facilities, Finance, HR, Legal, Operations, Marketing, Product, Risk, Sales, Sales Support, Tax and Technology.

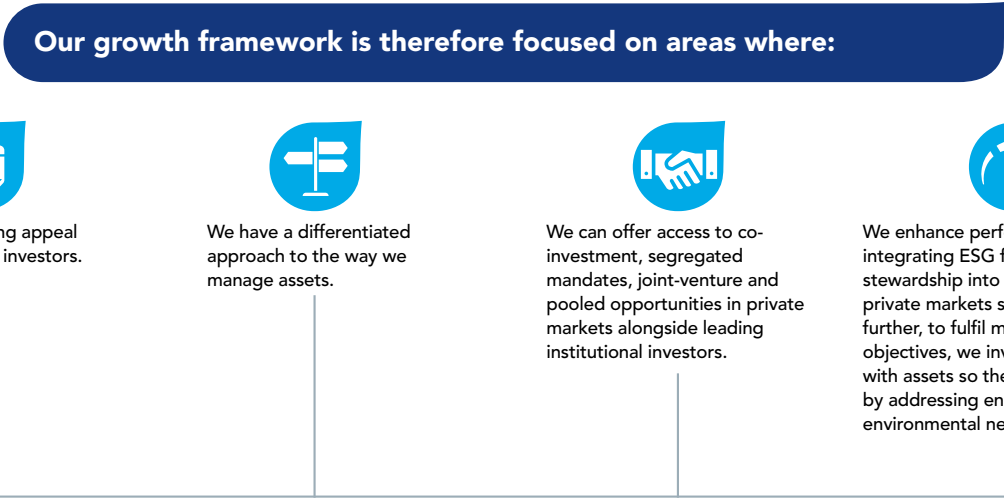
In 2024, now that the four platforms are established, the core area of focus remains on their sustainable development and growth, placing clients firmly at the heart of what we do.

#### Strategy

Our strategy is driven by a focus on delivering sustainable wealth creation for our clients and their investors. That means we aim to provide strong risk-adjusted investment performance for clients and, where possible, achieve positive outcomes for society and the environment.

We seek enduring business growth and profitability, and to make a positive impact as a leader in investment and sustainability. These objectives are firmly aligned with the interests of our clients, the companies in which we invest and engage, and the societies in which they operate.

Figure 4. FHL's growth framework



Source: FHL, as at 30 April 2024.

The priority for 2024 will be to continue our integration efforts with FHL, our parent, whilst upholding our strong heritage. Sustainable Careers remains a priority with the firm, focusing our attention on employee satisfaction, diversity, equity and inclusion, wellbeing, and retention. We will also invest in our competitive strengths in responsible investing and stewardship.

**How we have ensured a culture of effective stewardship**

Our investment beliefs, strategy and culture ensure that stewardship is naturally at the heart of FHL. We believe that creating long-term wealth sustainably through active investment and ownership delivers the best outcomes for our clients. Throughout this report, we highlight some of the actions we have taken to ensure our investment beliefs, strategy and culture enable effective stewardship, including:

-  **Governance:** We have embedded the need for effective stewardship in governance structures across the business, as described under Principle 2. This sends a clear signal of its importance to our business.
-  **Investment integration assessment:** The ESG integration team within the Responsibility Office carries out an annual assessment of the approach to integration of material ESG and engagement insights in each investment strategy.
-  **Integrated in our investment processes:** Driving change through engagement is one side of the coin – effective integration of stewardship insights is the other. As we set out under Principle 7, we systematically integrate stewardship insights into our investment process so that our investment and engagement activities go hand in hand. This creates a holistic understanding of ESG issues and how they intertwine.


**The priority for 2024 will be to continue our integration efforts with FHL, our parent, whilst upholding our strong heritage.**



### **Embedded throughout the product lifecycle:**

Stewardship is incorporated into our product-development process right from the start. A product's relationship to responsible investment and active ownership is a key consideration at the concept development stage and we endeavour throughout the development process to ensure it delivers sustainable wealth creation for clients. Stewardship is also key to our client-service provision. We act as responsible stewards of all the capital in which we invest, through allocation, management and engagement with assets. Through EOS, we also provide broader stewardship services for our clients' public market equity and credit investments in third-party products. An increasing number of clients are enlisting these wider services as there is a growing recognition of the need for high-quality stewardship. As we set out under Principle 2, once a product is live, there is a strong governance process in place to continuously review the effectiveness of the integration of material ESG factors alongside traditional performance drivers and engagement insights for the product and to ensure it continues to deliver the necessary outcomes for our clients.


All of our investment teams integrate ESG and engagement insights into their investment decision making, as we explain in more detail under Principle 7.

 **Transparency:** Transparency around our activities is key to enabling scrutiny and continuous improvement. We publish a Climate-related Financial Disclosures report annually which is aligned with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). In our [latest publication](#), we also included reporting on nature in line with the Taskforce on Nature-related Financial Disclosures (TNFD). We continue to report as signatories of the UN-supported Principles of Responsible Investment (PRI) and UN Global Compact (UNGC) on our responsible investment activities as well as our work to ensure we behave as a responsible firm. We continue to [publish](#) our EOS engagement plan and quarterly updates, as well as [case studies](#) from public and private markets, along with our Real Estate ESG report. More information is available under Principle 6.

### **We act as responsible stewards of all the capital in which we invest, through allocation, management and engagement with assets.**

 **Expert support:** Our Responsibility Office offers support to all our investment teams in their integration of ESG and engagement information, including through the development of proprietary tools enabling analysts to see ESG data and engagement information for individual companies and their portfolio as a whole. This reflects our core investment belief that responsible investment and stewardship lead to better financial results. More information on our progress during 2023 is available under Principle 7.

 **Long-term focus:** A significant number of our engagements are longer-term efforts, and we carry out a continuous dialogue with companies. For example, 80% of our relationships with the companies in our core public-market engagement programme have been ongoing for at least five years. Our engagement team conducts thorough research and an assessment of each company to ensure the nature of our engagement is focused on the most material issues using up to date information. This allows us to build quality, trusting relationships with these firms. More information is available under Principle 9.

 **Collaboration:** Our collaborative approach – described further under Principles 4 and 10 – acknowledges the significant quantity and quality of resource needed for effective stewardship and the importance of co-operation to deliver maximum impact across asset classes, sectors and geographies. We set out how we have worked with other stakeholders in the system under Principle 4.

### **A significant number of our engagements are longer-term efforts, and we carry out a continuous dialogue with companies.**



## What this means for our approach to investment and stewardship

The recognition that investors' interests lie in sustainable wealth creation over the long term cascades a series of decisions and actions that turns an investor into a responsible owner or steward of capital. We believe responsible, active ownership helps create businesses that are much more resilient to exogenous shocks. These firms are more likely to survive over the long term, and in and by doing so create better outcomes for our investors and society. Indeed, we believe this is the best way to sustain long-term outperformance and contribute to beneficial outcomes for investors, companies, society and the environment.

This is brought to life and complemented by bottom-up fundamental research on material traditional and ESG factors, which, of course, influences the decisions we make in our stewardship and investment processes. We place both stewardship and high-active-share investing at the heart of what we do. This ensures that we invest and engage with

conviction: we build investment portfolios that we believe are meaningfully different from the market – and, as such, we expect to outperform in the long term.<sup>7</sup>

Rather than betting on whether the market goes up or down, this combination of high conviction, high-active-share investing and stewardship means we focus on sustainable wealth creation for investors. In our investment decisions, we take into consideration both ESG data and fundamental research in assessing a company's performance. As responsible owners, we seek positive change in our engagement, not just information. While our engagements with investees cover a broad range of strategic (including ESG) issues, they share a focus on outcomes that create wealth sustainably. Principles 7 and 9 set out how we have continued to maintain high standards of stewardship and responsible investment during 2023 guided by our purpose.



### OUR PURPOSE IN PRACTICE: REAL ESTATE CASE STUDY

## Placemaking in Birmingham, developing impactful partnerships and enhancing biodiversity

From the outset, the regeneration of the Paradise development in Birmingham – a public-private partnership between Birmingham City Council Federated Hermes on behalf of the BT Pension Scheme run by Brightwell, and our development and asset management arm, MEPC – has been viewed as an opportunity to deliver both financial and social returns for the city and on behalf of our investors. The 17-acre site is seamlessly bringing together culture and commerce, combining contemporary new workspace with some of the city's most celebrated listed buildings, delivering a new destination for Birmingham that's rich in both heritage and innovation.



Source: Paradise



Source: Paradise

The development also enhances biodiversity in Birmingham. Bees and bee-friendly planting were established at Birmingham's Paradise development in 2021 as part of a Federated Hermes initiative to encourage greater biodiversity. Now with more than 360,000 bees collecting nectar and turning it into honey onsite, Paradise provides opportunities for occupiers, local residents, schools and community groups to discover the vital job bees carry out and their role at the heart of many ecosystems, including urban ones.

**“Our Paradise bees are a welcome addition not just to the city centre, but to the development and its efforts to help with sustainability and wildlife retention and expansion. By playing our small part – just like the industrious worker bee – we contribute to something larger and more impactful than if we work alone.”**

**– Caroline Rudge, Commercial Manager at Paradise**

<sup>7</sup> Outperformance cannot be guaranteed.

## How effectively have we served clients and beneficiaries?

Throughout this report we seek to demonstrate the outcomes of our responsible investment and responsible ownership, which we believe are in our clients' and their beneficiaries' best interests. This includes financial performance, stewardship outcomes and advocacy successes. We believe our investment approach helps us deliver sustainable long-term wealth creation by building a better world for our clients and future generations.

**External evaluation:** There are several external bodies that have validated our achievements and bolstered the credibility of our claim that we are serving the best interests of our clients.

We are founding members of the UN-supported Principles of Responsible Investment (PRI).

In 2023, FHL received 5 stars in the Policy Governance and Strategy, Fixed Income Corporate, Fixed Income Securitised, Fixed Income Private Debt, Real Estate and Infrastructure modules. We scored 4 stars on the Listed Equity – Active Quantitative, Listed Equity – Active Fundamental, Fixed Income SSA, Private Equity and Confidence Building Measures modules. Since submitting our PRI responses, we have already taken steps which will impact our future reporting, including onboarding a third-party provider to enhance our climate scenario analysis capabilities.

We won a range of awards based on our activities during 2023 in recognition of our leadership in responsible investment, including:

- Investment Manager of the Year for FHL and Investment Team of the Year for our Asia Ex-Japan team at the 2023 Portfolio Adviser Wealth Partnership Awards.
- Asia ex-Japan category winner for our Asia Ex-Japan team at the 2023 Investment Week Fund Manager of the Year Awards.
- The Engagement Award for EOS at the 2023 ESG Clarity Awards.
- Leon Kamhi, Head of Responsibility at FHL, named as one of the fifty most influential leaders in sustainable finance.



**Client input:** We seek client views through a number of fora to ensure we understand how we can best meet their needs. This is set out in further detail under Principle 6.

**Continuous review of client outcomes:** We have a number of governance structures in place (described under Principle 2) to ensure fairness to clients and beneficiaries, including through our Customer Outcomes Group ("COG").<sup>8</sup> The COG supports product governance by providing a forum through which products (including funds and segregated mandates) are reviewed and assessed through a client-centric lens.

We also conduct post-implementation annual reviews on an ongoing basis to confirm that all products and strategies continue to meet a customer need, perform in line with their stated objectives and have continued commercial viability. Each product and strategy is viewed holistically, with data collated across the business using a standard template. Information collated for the annual reviews includes performance figures, client demand and peer-group comparison analysis. Customer feedback may be obtained by a third-party market research agency or directly through the sales and client teams, and this feedback will be considered as part of the review. Any products or strategies that have not met marketed performance targets, do not continue to meet a customer need, or have failed to attract assets will be flagged with the COG for consideration. One-off or ad-hoc reviews may also be conducted in response to market events to ensure the product range remains appropriate within the context of our broader investment and corporate strategy.

We also have pricing committees and complete an internal mapping exercise every year. This considers factors such as each client's AUM in order to identify and address material anomalies between clients. During 2023, there continued to be a number of cases where an investor increased their holding in a fund and subsequently reached the required AUM for a lower-fee institutional share class. At this point, they were able to move into this share class so that they could benefit from lower fees.

**Plans for the future:** We always strive to improve the outcomes we deliver for clients. We recognise this process is never complete, and that continuous improvement and innovation is required if we are to remain market leaders.

Over the coming year, we intend to continue to enhance investment decision-making and engagement effectiveness by further enhancing our thematic approach to biodiversity and human capital management in relation to our investments through targeted portfolio, sectoral and issuer analyses. We also plan to continue to develop our client reporting and to continue to advance our diversity, equity and inclusion efforts across the firm.

<sup>8</sup> HGPE is not within the remit of the COG. For our infrastructure and private equity products, these processes are therefore managed separately within HGPE.

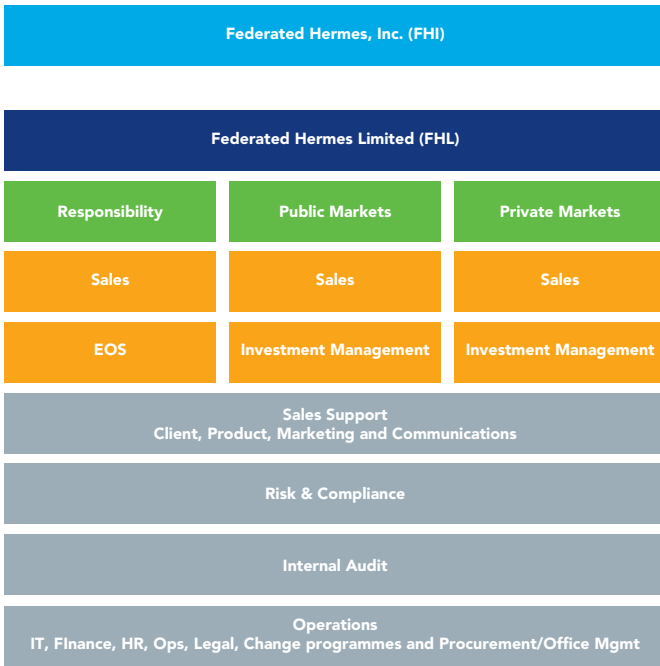


## Principle 2

Signatories' governance, resources and incentives support stewardship.

### Our governance structures

Figure 5. FHL's three-platform structure



Source: FHL, as at 30 April 2024.

All of our staff are responsible for implementing our stewardship approach, although there are several functions within the business that play a particularly significant role:



#### Responsibility Office

Established in 2014, our dedicated Responsibility Office reports through the Head of Responsibility to FHL's CEO and acts as a hub of expertise and support to assist every employee in our business to work towards our core purpose of delivering sustainable wealth creation over the long term. The Responsibility Office houses EOS (see below), FHL's third party stewardship service provider. It coordinates and supports the integration of our responsibility approach and activities across our strategies, funds and stewardship services. This includes quarterly meetings with each of the investment teams to review their ESG and engagement integration activities, as well as asset and issuer-specific discussions related to ESG and engagement. The Responsibility Office is also responsible for leading our advocacy work, as well as holding each department accountable for ensuring that we act as a responsible company. By doing so, it keeps the interests of clients and their beneficiaries at the centre of what we do. To ensure responsibility is embedded in all of our firm's business decisions, Responsibility Office colleagues are members of our firm's key committees (the key committees which oversee our stewardship approach are described in further detail later in this section). The Head of Responsibility is a member of FHL's Senior Management Team ("SMT").



#### Investment Office

Our Investment Office, covering both our public and private markets platforms, is the guardian of the investment outcomes we deliver to clients. It acts independently to ensure our strategies are performing in the best interests of clients and embodies our commitment to acting as a responsible and transparent asset manager.



#### Portfolio managers and investment analysts

Each of our investment teams has formulated their own responsibility plans that explain how, in the context of their particular strategy and investment universe, they incorporate ESG factors and engagement into their investment process. Each team is responsible for undertaking its own fundamental ESG research and the team members are accountable through the performance appraisal system for their part in delivering on our mission.

**The Responsibility Office acts as a hub of expertise and support to assist every employee in our business to work towards our core purpose of delivering sustainable wealth creation over the long term.**







## EOS

EOS is the stewardship service provided by Hermes Equity Ownership Services Limited, a company incorporated in England & Wales and wholly owned by FHL. Its activities and direction are overseen by a board of directors, comprising members of FHL's SMT and a member of FHI's Executive Committee (aka. Executive Staff). Day-to-day operations are directed by the Head of Responsibility as Chair of EOS, and managed by the Head of Stewardship, and directors of the client and business development team and operational management. EOS also has a Client Advisory Board (CAB) which contains client representatives who provide insight, advice and guidance on EOS' business strategy and service offering to ensure that the EOS service is and remains a client-focused offering. The EOS team boasts one of the largest stewardship resources of any fund manager in the world. The team is composed of individuals with a diverse mix of backgrounds, skills and perspectives and has been at the forefront of the development and evolution of responsible investment practices globally. The EOS team leads our public-markets engagement activity.



## Risk and Compliance

The Risk and Compliance teams work alongside the Responsibility Office to ensure that our business continues to, authentically and accurately, report on our ESG objectives and activities. We have in place reputational and sustainability risk frameworks that govern the identification of material ESG risks and monitoring of progress across all key ESG commitments, including compliance with the sustainable finance regulation and scanning for further, relevant emerging regulations or standards.



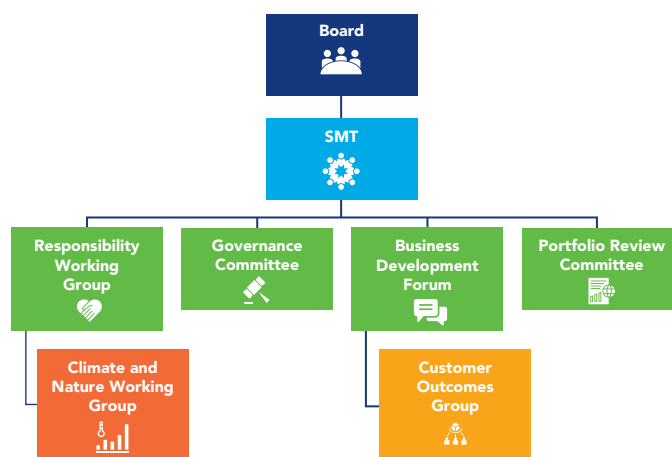
## Internal audit function

The Internal Audit team's primary role is to help the Board and executive management to protect the assets, reputation and sustainability of the organisation. The function is responsible for providing independent, objective assurance to management through a systematic and disciplined risk-based audit approach and assessment of the internal control framework. More information is available under Principle 5.

**The Risk and Compliance teams work alongside the Responsibility Office to ensure that our business continues to, authentically and accurately, report on our ESG objectives and activities.**



**Figure 6.** The internal structure of key stewardship oversight functions of FHL<sup>9</sup>



Source: FHL, as at 31 December 2023.

We have extensive oversight of our responsible investment and stewardship processes, activities and outcomes across our firm – something that is indicative of their importance to our business and how they form a core part of our approach. Accountability for delivering effective stewardship across asset classes is integrated at every level of our governance, including:

#### **Board**

We have a well-established governance structure led by the Board of FHL. The Board is responsible for the governance of the organisation and ensuring its effective operation. It also endeavours to consider all stakeholders when establishing objectives and policies. Among the Board's responsibilities is the implementation of the strategy set by our parent company, FHI. The Board is also responsible for overseeing our approach to climate change.

#### **Senior Management Team ("SMT")**

The SMT is responsible for the day-to-day management of the business and ensuring the objectives agreed with the Board are met. Our CEO leads the development and implementation of our mission and responsibility goals. We believe it is our responsibility to lead discussion and debate about the fiduciary responsibilities of fund managers to our clients, their stakeholders and, ultimately, society at large – tasks that our CEO actively leads and contributes to. In particular, our CEO is the founder of the 300 Club, an independent forum that challenges the orthodoxy of the investment industry and puts forward approaches to align the industry more closely to the goals of beneficiaries. He is also a founding member of the FCA-PRA Climate Financial Risk Forum, and a member of the Sustainable Markets Initiative and the Integrated Reporting and Connectivity Council (previously the International Integrated Reporting Council).

#### **Responsibility Working Group ("RWG")**

Meeting every quarter, the RWG is made up of senior representatives from across the business and is chaired by our Head of Responsibility. This group discusses a comprehensive range of topics that relate to the delivery of sustainable wealth creation for our clients and beneficiaries and shares best practice across the organisation.

#### **Climate and Nature Working Group ("CNWG")**

The CNWG reports to the RWG and meets every quarter. With authorisation from the Board or SMT as appropriate, its aim is to inform the development and implementation of a formal business-wide climate-change and nature strategy and risk-management approach. This includes overseeing progress in meeting our commitments as a member of the Net Zero Asset Managers' Initiative and Finance for Biodiversity Foundation. The CNWG is also a formal Task Force on Climate-related Financial Disclosures ("TCFD") Working Group.

<sup>9</sup> This chart covers key functions overseeing stewardship and is not an exhaustive representation of the internal governance structure of Federated Hermes Limited.



### Governance Committee

The Governance Committee is a formal oversight committee responsible for overseeing the formulation and delivery of our engagement, voting and climate policy. The committee is accountable to and reports to our CEO. The members include the Head of Responsibility; Head of Institutional Client Group; Managing Legal Counsel; Chief Regulatory Officer & Head of Government Affairs; Managing Director, Private Markets; and a representative of the investment teams.



### Business Development Forum ("BDF")

The BDF is responsible for approving or rejecting new products. Its members consider how desirable and suitable a product is from a commercial, customer and portfolio-management perspective. This includes looking at how it is aligned with our responsible investment and ownership approach. The forum is also responsible for setting fees and pricing and reviewing ongoing product and range suitability, target markets and profitability<sup>10</sup>.



### Customer Outcomes Group ("COG")

The COG meets quarterly and supports product governance by providing a forum through which products are reviewed and assessed through a client-centric lens. Good product governance is aligned with our focus on responsible investment management, and we aim to put the customer at the heart of product design and management. The COG makes use of a customer-centric view when reviewing investment products and considering our obligations to investors (both directly and indirectly via distributors). The group operates a dashboard approach to reviewing products at each meeting with detailed information provided to allow topics on individual funds to be explored in greater detail, this includes looking at how well the fund integrates ESG and its engagement progress.



### Portfolio Review Committee ("PRC")

The PRC supports the SMT by assessing and managing the investment teams, their corresponding processes and related activities. It reviews investment performance across all of our firm's portfolios and carries out monthly deep dives into specific investment strategies. As part of this review, the PRC considers the investment

implications – at a portfolio and issuer level – of the ESG performance of holdings and the level and progress made in engagement with the portfolio's assets.



### Responsible Property Management ("RPM") Oversight

The Real Estate team have a Net Zero working group and an ESG working group with relevant representatives from the business to ensure the decision-making process is inclusive and transparent. External experts are also included in these forums as appropriate to ensure project decisions are made with the help of investment managers, delivery counterparts and the Real Estate ESG team.



### Infrastructure Oversight

The Head of Infrastructure, Infrastructure Investment Committee (IIC) and the Federated Hermes Private Markets Governing Body are ultimately accountable for all sustainability matters related to infrastructure.



### Private Equity Oversight

In the Private Equity team, the Private Equity Investment Committee (IC) is responsible for all investment risks, including climate change risk. The Portfolio Review Committee assesses portfolio-level ESG risks including climate change risks quarterly to inform GP engagement. These Committees and the Federated Hermes Private Markets Governing Body are ultimately accountable for all sustainability matters related to private equity.



### Sustainability Investment Centre ("SIC")

The SIC supports the development of our firm's responsible investment capabilities. It facilitates monthly conversations between teams across the business to pool the best ideas in the sustainable space and supports our focus on long-term sustainable wealth creation.

Accountability for delivering effective responsible investment and ownership outcomes for all clients resides with the investment management/fund advisory companies within the FHL group. While the investment management/fund advisory companies of FHL and our parent company, FHI, are also clients of EOS, we have clear policies in place to identify, manage and mitigate potential conflicts of interest as described under Principle 3.

<sup>10</sup> HGPE is not within the remit of the BDF, COG or PRC. For our infrastructure and private equity products, these processes are therefore managed separately within HGPE.

Details of the specific governance we have around managing climate-related risks and opportunities are available in our [Climate-Related Financial Disclosures report](#).

As well as formal governance structures, we have a structured approach to ensuring that we carry out effective engagement and integrate stewardship into our investment processes. This is evidenced in our reporting against Principles 7 to 12, particularly through our ESG and engagement integration approach, engagement selection process and milestone engagement tracking system.

### Resourcing stewardship

All analysts and portfolio managers are responsible for ESG and engagement integration, and a meaningful amount of engagement takes place across all our funds, with the exception of sovereign debt funds as we do not currently engage systematically with sovereigns but may engage on an ad-hoc basis. However, the Responsibility Office plays a key role in facilitating them being informed on material ESG issues for their investments as well as working with them to identify engagement opportunities. The Responsibility Office plays an oversight and support role in ensuring the investment teams have access to the right resources to efficiently integrate ESG and engagement (in conjunction with EOS for public markets).

While the above is the standard process across all of our strategies, we do have specific strategies which engage with all investee companies and where successful engagement is explicitly part of the ex-ante investment proposition. These include the SDG Engagement Equity and SDG Engagement High Yield Credit strategies. Given these strategies' additional focus on engagement and that some of their holdings overlap with other of our and EOS' third-party clients' portfolios, we have dedicated engagers who focus solely on these strategies and work closely with EOS to ensure a consistent approach. More information on these strategies is available under Principles 7 and 9.

**The Responsibility Office plays an oversight and support role in ensuring the investment teams have access to the right resources to efficiently integrate ESG and engagement (in conjunction with EOS for public markets).**

We use a number of third-party data providers which support our efforts to integrate ESG and also inform our stewardship activities. These include Sustainalytics, Trucost, CDP, FactSet, MSCI, netpurpose, Planetrics and Bloomberg. We are also actively engaging with other data providers to ensure our teams have access to the latest and most relevant data for our investment approaches. More details on our use of service providers are available under Principle 8.

### Training

Our investment teams attend regular education presentations and roundtables provided by EOS engagers, portfolio managers and external experts on ESG risks and opportunities



**Our investment teams attend regular education presentations and roundtables provided by EOS engagers, portfolio managers and external experts on ESG risks and opportunities in the context of sectors, themes or country.**

in the context of sectors, themes or country. They are also provided with training on our proprietary ESG integration tools such as the carbon and the environmental tool.

Training sessions provided during 2023 include:

- A number of deep-dive sessions to support the investment teams in their integration of ESG factors, including on net zero and deforestation. The Sustainability Investment Centre is an internal forum open to colleagues from across the firm that meets on a monthly basis to discuss various topics related to sustainability. Recent examples include a presentation on carbon capture, utilisation and storage, a presentation on a new framework for analysing carbon credits and offsets, and a presentation on the latest TNFD guidance. These are discussed with participants across the investment teams, business development and EOS.
- Monthly tutorials are run by the Responsible Investing Office (RIO), an FHI department, for EOS engagers to help build understanding of how investors analyse a company's financial statements.
- Dedicated thematic webinars are run for the investment teams by our EOS engagers. Topics covered in 2023 include Digital Rights, Human Capital Management and Fast Fashion and the Circular Economy.
- A number of training sessions held by third-party data providers on their products and methodology. A recent example includes a presentation on scenario analysis by the data provider Planetrics.
- The Real Estate ESG team held monthly training sessions on a range of different topics, which were open to all private market employees. The sessions were delivered by the in-house team or expert consultants.

The most effective training in responsible investment and ownership in our view is 'on the job'. Portfolio managers and engagers regularly get together to discuss particular investments and often meet companies together. This benefits the engagement service as it can make the engagement more relevant and material. At the same time, the portfolio manager benefits by getting a deeper understanding of relevant engagement (including, but not only, ESG) issues to consider in a company's risk assessment and value opportunities. More information is available under Principles 7 and 8.

Finally, the PRI Fundamentals course continues to be offered to all new joiners, to increase the level of understanding and awareness of ESG integration topics, and our firm's approach to responsibility has been a formal part of all new joiners' inductions since the second half of 2017.

### Stewardship resources – public markets

We have one of the largest dedicated stewardship resources of any fund manager in the world, in the form of our public-markets engagement team, EOS. EOS also draws on the expertise of the Responsibility Office of FHL and others within our firm, a number of whom have had direct engagement experience having previously worked within EOS. There are policies, processes, and controls in place to ensure the management of conflicts of interest, as described under Principle 3.

EOS has intentionally built a diverse, international team of experienced voting and engagement professionals who have the expertise, language skills and cultural knowledge to deliver real beneficial change within companies.

Our diverse engagement team draws on a number of skillsets and our senior engagers come from a range of backgrounds. These include – but are not limited to – banking, law, sciences, academia, climate change, nature and biodiversity, corporate governance, corporate strategy, human capital management and human rights. The team also has strong gender, (53% female / 47% male for permanent staff as at 31 December 2023).

The ability to engage in the native language can be critical to successful engagement, and within the EOS team we have nationals from 20 countries and fluency in 16 languages. The combination of our ability to engage in the local language and our understanding of local culture and business practice are critical to the success of our engagement work. The EOS team is well placed to draw upon and, where appropriate, conduct additional research. It is also well placed to make

judgments about the degree to which companies can reasonably comply with local best practice and where exceptions are appropriate. On a regular basis we update our public voting guidelines and regional corporate governance principles to reflect best practice. More information on the updates to our voting policies made in 2023 can be found under Principle 12.

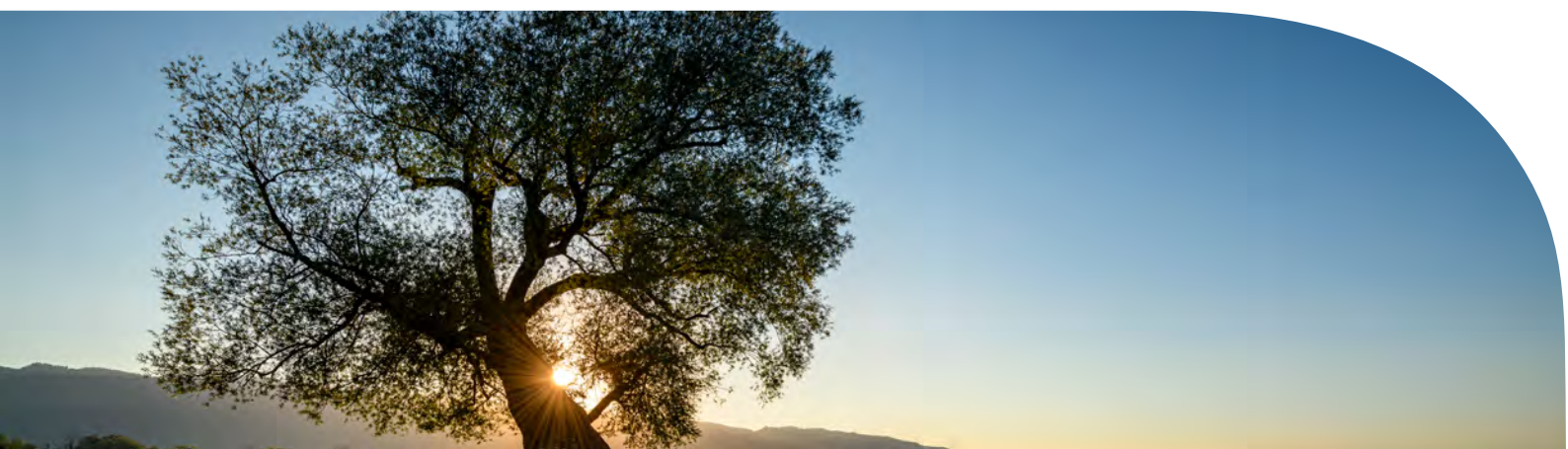
The team's skills, experience, languages, connections, and cultural understanding equip them with the gravitas and credibility to access and maintain constructive relationships with company boards. The depth and breadth of this resource reflects our philosophy that stewardship activities require an integration of a range of relevant skills and experiences. Escalation and intervention at senior management and board director level should be carried out by individuals with the right skills, experience, and credibility.

Our EOS engagement professionals are divided into designated teams covering ESG and strategy-related themes, sectors and regions. This ensures we have experts who can educate the wider team on developments and best practice in their respective areas. Each engager is responsible for engagement, voting recommendations and ESG analysis, focusing on the combination of regions, sectors and themes that they have been appointed to cover.

**The ability to engage in the native language can be critical to successful engagement, and within the EOS team we have nationals from 20 countries and fluency in 16 languages.**

The team is based in the UK and the US. London (UK) staff cover engagement in Europe, Asia and emerging markets and staff in Pittsburgh (US) cover engagement in North America. Our professionals frequently travel to undertake engagements in person where possible at company headquarters and on-site visits to view operations and general conditions, as we believe this is most effective to fully understand company context as well as progress against milestones. EOS also has a number of senior advisers who provide additional resource and expertise specific to some local markets including Japan, the Netherlands and the UK.

Given that the EOS engagement resource operates across our funds, it is critical that engagers integrate effectively with fund managers. Our approach to ensure this is described further under Principle 7.



### Stewardship resources – private markets

The Real Estate business follows an integrated approach in stewardship using tools and procedures that allow investment and fund managers to supervise and effectively manage Federated Hermes' real estate portfolio. With regards to ESG, the team contains a four-person ESG team who work closely with both internal and external stakeholders, including investment managers, external delivery counterparts for technical expertise, property managers and facility managers. The team ensure ongoing engagement with investment managers, property managers, occupiers, and contractors to deliver the ESG plans successfully. The team collaborate with a number of industry working groups such as the Better Buildings Partnership (BBP), the UK Green Building Council, and Institutional Investors Group on Climate Change to ensure they remain aware and contribute to industry trends, best practice and innovation. The team recognise the importance of collecting and sharing ESG information among the various organisational levels of our investment and asset-management process. As a result, the team have developed and integrated a series of ESG tools and procedures that link our strategic investment targets for portfolio strategies and the management of a property's technical characteristics and operational performance.

Our infrastructure team takes a fully integrated approach to sustainability and stewardship, with each member of our team having a duty to ensure a responsible approach is applied to all team activities. As owners, we see ourselves as stewards of infrastructure assets, not only for this generation but also for future generations.

Our private equity team includes one ESG specialist who supports the investment team, which is responsible for assessing ESG risks and opportunities, and ensuring proper process is followed. Our private equity team co-invest both directly in a selection of companies alongside other General Partners (GPs) and indirectly through fund investments. Typically, we are a minority investor for direct co-investments. For a small proportion of our assets where our team have some control and/or the ability to influence company decisions directly, we seek to work closely with investee companies to monitor, challenge and improve ESG performance. However,

in almost all cases our team has limited control and/or ability to influence decisions directly (whether for direct or indirect co-investments). In these instances, the team will work closely with the lead GPs to assess, monitor, and seek to improve ESG performance of the underlying investee companies. As private equity investors, we have a long history of investing in growing businesses across the world. We believe building better business not only translates into better financial performance, but also positive outcomes for individuals, communities, and societies as a whole.

Our private debt team directly engages with the sponsor and management team to remedy any ESG issues that arise during the life of a loan. This engagement is frequently conducted in collaboration with EOS to strive to ensure that the engagement is outcomes-focused and impactful.

### Diversity, equity and inclusion

As outlined above, all of our staff are in some way responsible for implementing our stewardship approach. Our firm-wide diversity, equity and inclusion ("DE&I") approach is therefore of relevance to the diversity of those involved in our stewardship activities. We have a long-standing commitment to increasing diversity, equality and inclusion in our business and acknowledge that we need to make further progress. We aim to foster and promote a culture of inclusion which celebrates all forms of diversity. We aim to appeal to, and retain, a diverse workforce. We encourage innovation and creativity, with a view to helping our employees maximise their potential.

In 2023 the SMT updated our 2023-2026 DE&I Strategy. The Creation of the DE&I Office and rebrand of our employee resource group 'UNITY' to 'Community for All' aligned with our mission to foster and promote a culture of inclusion which celebrates all forms of diversity. We aim to appeal to, and retain, a diverse workforce. In 2023, we launched six core DE&I Strategic projects:

- **Employee Engagement Project**
- **Mental Wellness Project**
- **Baseline Demographic Project**
- **External Charters Project**
- **Disability Project**
- **Menopause Project Team**





In support of promoting an inclusive environment, we launched a number of additional initiatives: ‘Let’s talk about the menopause’ essential training (for all line managers); the Menopause Toolkit; inclusive recruitment training ; neurodiversity training workshops (open to all colleagues); Cultural Competency workshops (for several teams across the business); Building Strategic Partnership inclusion workshops; the @MYSTORY (a campaign that invited colleagues to share their personal story, including insight into their culture and life experiences); LGBTQ+ awareness training (for SMT and a workshop for all employees); several men’s health workshops; and Mental Health First Aider (MHFA) training and MHFA refresher training.

We have continued to collaborate with specialist organisations – including Beyond Education, 10,000 Black Interns, GAIN and Change 100 – to provide internship opportunities for individuals from underrepresented communities. In the summer of 2023, we launched our intern programme for university undergraduates to gain work experience and exposure, with a long-term view of building up an early career talent pipeline.

Throughout our organisation, leaders see the value of DE&I as a driver for growth and innovation. As a result, leaders promote an inclusive and performance led culture that supports the FHL vision statement and mirrors the Pledge and




the Behaviour Framework. Leaders act as the champion of change within the organisation and actively sponsor the firms DE&I-related commitments.

We are committed to having the best talent. This means attracting, developing, and retaining individuals from all backgrounds. Initiatives conducted this year include: the appointment of a Talent Requisition Partner; the roll out of inclusive recruitment training for managers; the launch of the Introduction to Culture workshops for all new employees; providing secondment opportunities; promoting internal and external mentoring schemes; and continuing to run the management development programme.

We continue to commit to voluntary UK charters and pledges including the Women in Finance Charter (WIFC); BITC Race Charter; Change the Race Ratio, Menopause Workplace Pledge, and being a Disability Confident Level 2 employer.

We remain fully committed to supporting the Women in Finance Charter and its objective of attaining gender balance across all levels of financial services. In 2023, we have seen an increase in the proportion of women at the FHL Board level and continue to have a modest increase in women firm-wide in 2023. We have, however, seen the number of women decrease at Senior Management level. This will be a core area of focus in 2024.

Figure 7. Employed women across FHL

Population	Target 2025	2023	2022	2021	2020	2019	2018
 Firm-wide	50%	43%	42%	41%	44%	42%	40%
 Board	50%	40%	33%	31%	31%	31%	31%
 Senior Management (ED+DIR)	50%	32%	33%	29%	33%	31%	28%

Source: FHL, as at 31 December 2023.

## Performance management

Through our performance management process and behaviour framework, that explicitly sets out the visible manifestations of our Federated Hermes Pledge, we look to ensure that our cultural aspirations are reinforced. As such, our philosophy is to reward individual contribution, as demonstrated by the delivery of sustainable results (the 'what') aligned with our business strategy, values and behaviours (the 'how'), which serve the best interests of our clients, their investors and our shareholders while enabling the business to grow to its potential.<sup>11</sup>

As part of the process, performance objectives are set at the start of the performance year and reviewed biannually to assess progress, achievements, and areas for development and growth. This ultimately supports improved organisational performance. To encourage a focus on meeting the needs of clients, their investors, and our shareholders, all individuals are rated equally on their technical performance and their behaviours.

We are committed to our business purpose of sustainable wealth creation that enriches investors, and, where possible, society and the environment while being at the forefront of developing industry best practice. Part of this is ensuring that our performance management process, behaviour framework and Remuneration Policy incorporates consideration of stewardship and the integration of sustainable performance and risk in both our firm's investment activities and its wider operations. This is further supported by the co-investment of deferred bonuses in funds to align employees to longer term investment performance after the bonus has been awarded.

In particular we aim:

- To incentivise senior management to drive our strategy and initiatives in line with our business purpose of sustainable wealth creation and ensure that through appropriate stewardship it informs all of our firm's key business and operational processes.
- To promote best practice integration of investor stewardship and ESG factors including the delivery of sustainable outcomes in the investment process and decision making.
- To encourage all employees to develop responsibility objectives as appropriate for their role.
- For sustainability risks to be considered as part of our risk reporting, and for performance against risk appetite and sustainability risks to form part of the Chief Regulatory Officer & Head of Government Affairs annual risk adjustment report. Also, to ensure that adjustments can be made to bonus pools and individual outcomes if the company is operating outside of its risk appetite.

## Reflecting on our governance structures

The efficiency of our governance structure is reflected in the outcomes we deliver for clients, which are evidenced throughout this report.

Assurance and oversight: Oversight of effective stewardship is integrated into all levels of our governance and the structures and processes detailed earlier help us reflect on improvements to support effective stewardship. Our external assurance providers undertook their third limited assurance



<sup>11</sup> For more information, please see our Remuneration Policy: <https://www.hermes-investment.com/ukw/remuneration-policy/>



engagement on the information disclosed as part of the sustainability reporting of FHL in the period from June 2022 to July 2023. Their conclusions are not yet available, however once released, we intend to reflect on these during 2024 in order to enhance our existing approach where needed. We made several improvements based on the recommendations of the external assurance provider's last engagement, the results of which we included in our reporting last year. More information on these improvements can be found under Principle 5.

Our external assurance is complemented by our internal oversight structures. For example, our Governance Committee continued to provide oversight of the formulation and delivery of engagement and voting approaches throughout 2023 by reviewing items such as:

- Several policies relevant to responsible investment and stewardship – as described further under Principle 5 – to ensure our stewardship processes were supported by effective governance. This included approving updates to the Global Voting Policy and Guidelines, which included developments in the climate change policy and a voting policy on human rights, and updating the Engagement Policy and Sustainability Risks Policy to include infrastructure and private equity.
- The EOS Conflicts of Interest Register and the Stewardship Conflicts Log.
- Approach to Controversial Activities.
- The EOS Engagement Plan.
- The FHL 2023 Stewardship Report.

This is also closely connected with Principle 5, where we provide more detail on the internal and external reviews and assurances we have to support continuous improvement.

During 2023, the Governance Committee reviewed progress every six months against commitments we have made, such as the Net Zero Asset Managers initiative, the Finance for Biodiversity Pledge and the Finance Sector Deforestation Action initiative. An annual update was also provided to the Responsibility Working Group. This ensures we have appropriate oversight of our progress against such commitments to ensure we remain on track.

**We continue to engage with companies on how they address geopolitical risks facing their businesses and their approach to safeguarding human rights in high-risk regions.**

As set out under Principles 3 and 4, we have managed all potential conflicts of interest arising during 2023 and our teams have worked hard to develop an effective approach to the systemic risks the industry is facing.

**System improvements:** Following significant enhancement to the EOS operating model in 2022, including the redevelopment of a new Engagement Management System, further improvements have been made to our approach to logging engagements. We have updated the way we categorise our engagements by moving from a two-tier theme taxonomy to a more granular and detailed three-tier taxonomy.

**Continuous improvements:** EOS' engagement plan is reviewed every year to ensure it is up to date and reflects its clients' priorities. Geopolitical tensions remained heightened in 2023, with no sign of an end to the war in Ukraine and the destabilisation of the Middle East through the Israel-Gaza conflict. We continue to engage with companies on how they address geopolitical risks facing their businesses and their approach to safeguarding human rights in high-risk regions. During the course of 2023, biodiversity and artificial intelligence (AI) continued to rise up policy makers' and company and investor agendas, and we will continue to intensify our engagement on these topics. The feedback we received from clients confirmed we were striking "about the right balance of breath and intensity" of engagement.

Under Principle 6 we describe further how we gather and use client inputs into our work, as well as the improvements we have made to our client reporting on ESG factors and engagement.

**Diversity, equity and inclusion (DE&I):** Under the governance of the SMT, in 2023, as part of the new DE&I Strategy we launched six core DE&I Strategic projects, as described earlier in this section. The FHL DE&I Office is accountable for the delivery of the projects over a two-year period. The DE&I Strategy will be monitored and reviewed by the SMT on a quarterly basis, with the FHL Board reviewing progress against plan, including the committed external targets annually.



## Principle 3

Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.

Our public [Conflicts of Interest Policy](#) sets out our commitment to act professionally at all times. We commit to keeping the best interests of our clients and their beneficiaries in mind and to take appropriate steps to identify circumstances that may give rise to conflicts of interest with a risk of damage to our clients' interests. It includes examples of conflicts of interest – such as the receipt of confidential information, conflicts of interest between clients, personal conflicts and conflicts between our business and clients – and the appropriate procedures we have established to manage any conflicts of interest identified and to prevent damage to client interests.

Due to the importance of stewardship to our business, we have also developed a specific [Stewardship Conflicts of Interest Policy](#). We acknowledge our position as a fiduciary for our clients and their beneficiaries and seek always to act in their best interests. Accordingly, we take all reasonable steps to identify actual or potential conflicts of interest. We also maintain and operate arrangements to minimise the possibility of such conflicts giving rise to a material risk of damage to the interests of our clients.

FHL employees are also subject to the Federated Hermes Code of Business Conduct and Ethics.

Across the firm we take all reasonable steps to identify conflicts of interest between:

- FHL, including its managers, employees and appointed representatives or any person with a relevant direct or indirect link to them – and our clients; and
- any one client of Federated Hermes and other clients.

We have summarised key aspects of our policy below and the full version is publicly available online. In addition, we have identified a set of conflicts of interest that are likely to arise in connection with engagement activities and have put in place controls to manage such instances.

### Potential conflicts of interest

#### Ownership

EOS is fully owned by FHL and the Head of Responsibility who leads EOS reports to the CEO of FHL. Any conflict which may arise between clients of the EOS service and other clients of FHL will be addressed in a similar way to conflicts between any of our clients.

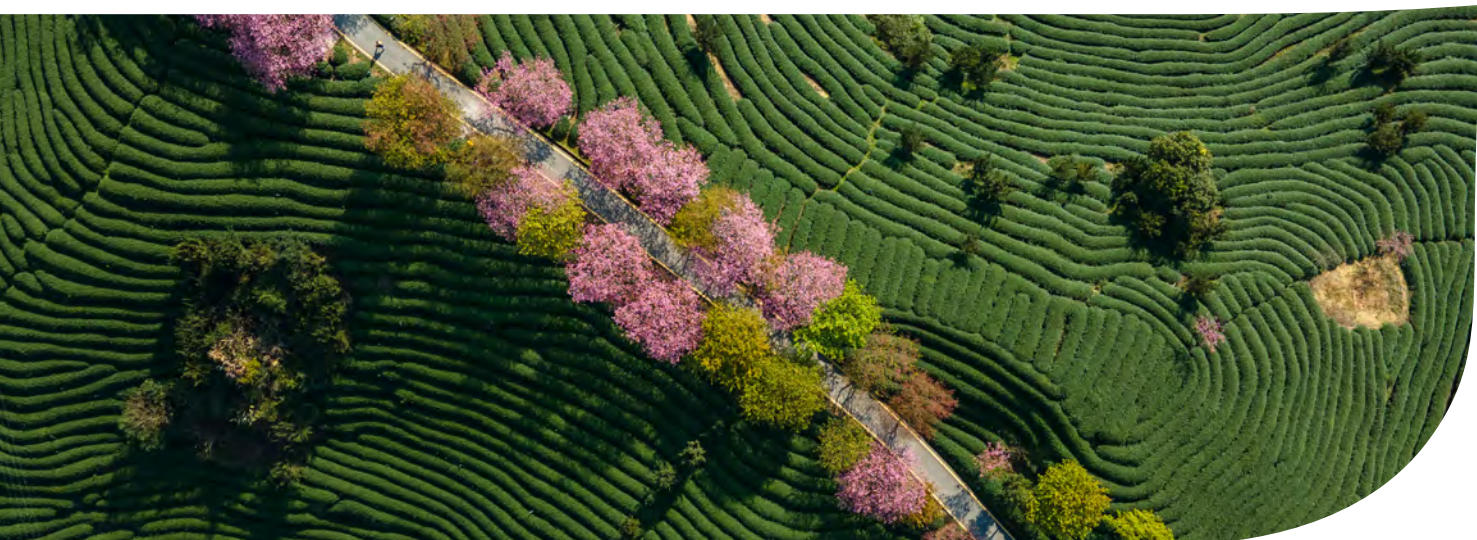
In the instance of EOS clients having the right to vote at an FHI meeting, EOS would not provide a recommendation, but rather would alert EOS clients of the conflict, provide the ISS policy recommendation and enable the client to make their own decision in this circumstance.

#### Clients and prospects

FHL sub-advises a number of FHI products, but also provides services to other institutional investors, including a number of pension funds sponsored by corporations, governments and other organisations, and fund-manager clients. These services include voting recommendations and engagement with companies in which FHL's clients are equity shareholders and/or bond investors.

As a result, the following real or perceived conflicts may arise:

- We may engage with or vote the shares of, or EOS may recommend to a voting services client to vote the shares of a company which is the sponsor of one of our pension-fund clients or is a company within the same group as one of our clients or prospects.
- We may engage with a government or government body that is the sponsor or associate of the sponsor of one of our clients or prospects.
- We may engage with a company which is a tenant of our Real Estate division's property investments.



- We may engage with a company which has a strong commercial relationship, including as a service provider, with FHL and/or with clients or prospects.
- We may vote, or EOS may recommend to a voting services client to vote, on a corporate transaction, the outcome of which would benefit one client or prospect more than another.
- We may engage with a company where certain clients or prospects are equity holders and others are bond holders.
- We may hold meetings with companies for the dual purpose of delivering both our fund management and engagement services.
- We may otherwise act on behalf of clients who have differing interests in the outcome of our activities.

### Individuals

At the individual level, engagers may have a personal relationship with senior staff members in a company in the stewardship programme. If this is the case the engagement activity will be assigned to another engager.

If an engager personally owns securities of a company within the programme they must seek approval from both their line manager and Compliance to ensure there is no conflict of interests with the interests of our clients.

### Stock lending

FHL does not engage in stock lending.

### Short selling

Although FHL's investment teams do not generally hold short positions, those teams which regularly have short positions are prohibited from being involved in any engagement activities for companies where they hold a short position.

**We take all reasonable steps to identify actual or potential conflicts of interest. We also maintain and operate arrangements to minimise the possibility of such conflicts giving rise to a material risk of damage to the interests of our clients.**

### Managing and monitoring potential conflicts

In all our activities, we seek to promote the long-term value and success of the companies in which our clients invest. As such, we engage with market regulators and other actors to influence public policy and regulation to enable this outcome.

Stewardship activities are exercised with the aim of influencing the company's behaviour in line with the long-term interests of clients and their investors. However, these activities are not carried out with the intention of obtaining non-public information, nor is information obtained intended to manipulate the market.

In the event that material non-public information is obtained through stewardship activities, our compliance department is informed, and an information barrier is created for 'insiders' until the information is publicly disseminated. Staff are not allowed to act upon or share the non-public material information.



While we welcome client input and suggestions for engagement, all of our engagements are selected and pursued on the basis of an objective assessment of the severity of the problems faced by the companies engaged or the opportunities available to them, the likely effect of public policy and regulation and the likelihood of success in achieving value-enhancing change or mitigating value-destroying change. We give due regard to the value of the company to our clients and the value at risk given the issues in question.

In our engagements with companies which are the sponsors of (or in the same group as) our clients, we are careful to protect and pursue the interests of all of our clients by seeking to enhance or protect the long-term value of the companies concerned. In the first instance, we make clear to all pension-fund clients with corporate sponsors that we will treat their sponsoring parent or associated companies in the same way as any other company.

In addition, we ensure that in such situations the relevant client relationship director or manager within FHL, including EOS, is not leading the engagement or making the voting recommendation to clients. This same approach would hold true with respect to any engagement with a company with whom we, our owners or our clients have a strong commercial relationship, including suppliers. If we become aware of potential conflicts, they are disclosed, if necessary, to the companies to enable them to be managed effectively. Members of our investment teams have separate processes and management but are encouraged to join engagement meetings with their stewardship colleagues and discuss the implementation of our voting policies. EOS' external clients are also invited to join upcoming engagement meetings on a sustainable and appropriate basis.

**In our engagements with companies which are the sponsors of (or in the same group as) our clients, we are careful to protect and pursue the interests of all of our clients by seeking to enhance or protect the long-term value of the companies concerned.**



The engagement objectives are set out and the voting recommendations made and provided by our stewardship team in line with FHL's voting guidelines, policies, corporate governance principles and engagement plan (or, where agreed, client-specific policies). While carrying out joint engagements may mean that investment teams have access to certain information before it is disseminated to our stewardship clients, we believe the benefits to clients of these joint meetings is substantial.<sup>12</sup> In particular, it produces an enhanced engagement process that focuses on the relevant and material ESG risks through additional insights into financial materiality which also results in a better appreciation of ESG risks in any ultimate investment decision made by the investment team.

We have well-established, publicly disclosed voting principles and guidelines. Based on these and the judgements reached through engagement with individual companies, we provide voting recommendations to our third-party stewardship clients who request to receive our voting recommendation service.

There may be occasions where one of our third-party clients seeks to influence the voting recommendations advice we give to other institutional clients. In such circumstances there would be director-level involvement and an objective judgement reached based upon what we believe to be in the best long-term interest of our clients. All third-party clients retain full discretion over their own final voting decision.

**We consider through our company engagements and voting recommendations not so much the financial effect of a deal for any one client, and more the long term value that could be created or is at risk of being destroyed for our clients.**

Clients and internal investment teams may at times have different immediate interests in the outcome of certain corporate activities, most notably in the result of a takeover bid involving two public companies. In addressing such situations, we are open with clients about the conflict and disclose it where practically possible.

As in other cases, we consider through our company engagements and voting recommendations not so much the financial effect of a deal for any one client, and more the long-term value that could be created or is at risk of being destroyed for our clients.

For our internal investment teams, the voting recommendation provided by our stewardship team will inform their assessment. However, they will make their final judgement independently with a view to their fiduciary obligations to their clients. On the rare occasion that the investment team and EOS disagree on the appropriate voting action, the matter is logged and escalated for a decision to be reached at the Governance Committee (see below).

It is expected that votes cast by our investment teams would be consistent with the voting recommendations we provide to our stewardship clients who request to receive voting recommendations other than in limited circumstances. In a case of divergence between these, the rationale will be documented.

### Review of conflicts of interest

In addition to the broader measures set out above, staff members must flag to their line managers any potential conflict of interest they recognise with a company they are engaging with. We also have policies that seek to avoid any potential conflicts for individual staff members of FHL that arise from engagements with companies in which individuals have personal investments or some material personal relationship with a relevant individual. Where a staff member has a personal connection with a company, they are required to make this known and they are not involved in any relevant engagement activities.

### Recording and escalation

We maintain a register of potential conflicts of interest and the controls to mitigate them. In those limited circumstances where a conflict over our approach to providing voting recommendations (aside from that directed by EOS third-party client-specific policies) or engagement arises which is not able to be resolved in the manner set out above, the matter is referred to an escalation group whose composition is the same as our Governance Committee. The Governance Committee members include the Head of Responsibility; Head of Institutional Client Group; Managing Legal Counsel; Chief Regulatory Officer & Head of Government Affairs; Managing Director, Private Markets; and a representative of the investment teams. The group is guided by our mission to deliver sustainable wealth creation, our published corporate governance principles, voting guidelines and policies and other appropriate industry-endorsed guidance. If there is no majority view in the group, the CEO will make a final decision. All such instances would be documented and reported to the Risk, Compliance & Financial Crime Executive.

<sup>12</sup> If we were to receive inside information, we would not act upon it or share it with clients.

## Real estate

Our real estate business has formal procedures to deal with conflicts of interest. There is a potential for conflict in the allocation of real estate investments between client portfolios. However, it is important to note that each portfolio has its own geographical and structural bias and specific investment objectives in terms of risk, income profiles, hold periods and target lot size. This separation is also compounded by the different timings in liquidity between the various client portfolios. As not all are in the market for new products at any given time, in practice this is rarely an issue.

**On the rare occasion that the investment team and EOS disagree on the appropriate voting action, the matter is logged and escalated for consensus to be reached at the director level.**

Investments are allocated on a first-past-the-post basis. This means that the investment team that first receives the introduction has the first opportunity to acquire the investment. If the property fits into more than one portfolio managed by that Fund Manager or Director, then they will allocate the property on a principle of rotation. The rotation order is determined by when the mandates were awarded and once the mandate at the top of the list has a property allocated then it will go to the end of the list. If a property meets all the requirements but the mandate declines that property, then that mandate will go to the end of the list.

If the opportunity is not a fit for the particular fund, it is made available for other clients managed by FHL. In most cases, it will be clear when a particular investment should be placed between client funds, but where there is any doubt, the allocation decision will be approved by the CEO of our real estate business and the rationale for the allocation set out in the papers presented to the investment executive for formal approval.

Any other type of potential conflict of interest would be reported to and dealt with by our real estate Board, or the appointments committee for matters relating to our FHPUT fund.

## Annual review

We review our Stewardship Conflicts of Interest Policy annually so it adequately reflects the types of conflicts that may arise. This is to ensure they are appropriately managed and as far as possible mitigated. The Policy is publicly available on our website.

## Our conflicts-of-interest approach in practice

Our policy on conflicts may be best understood by considering its impact in practice.

Our EOS conflicts of interest register contains a description of stewardship conflicts, what mitigation procedure and controls were put in place, whether it was then reported to the escalation group if necessary and any follow-up actions and conclusions. It is reviewed by senior management on a regular basis. The following are examples of potential stewardship conflicts which we identified and managed in 2023:

- EOS made a voting recommendation, and FHL voted, to support by exception to our policy the combined chair-CEO. This did not align with EOS' policy and given that FHL had its own holding, a potential conflict of interest was logged based on possible divergent interests between the relevant fund and EOS' stewardship clients. We had recently engaged on the topic and the company had acknowledged our expectation for the roles to be separated in the long term. However, we did recommend voting against a new non-independent director to be nominated to the board to signal that we expected higher independence overall.
- EOS recommended a vote, and FHL voted, to support by exception to our policy a remuneration report and policy. Our policy indicated a vote against the report and policy due to the maximum variable pay awards exceeding our guidelines. Again, a potential conflict of interest was logged based on possible divergent interests between the relevant fund and EOS' stewardship clients. After discussion between EOS and the relevant FHL investment team, we decided to vote for by exception on both items as the company had a history of not exceeding our guidelines when granting awards. We also communicated our position to the company, indicating that we would escalate our voting recommendations towards the company if they moved to further exceed our guidelines.



## Principle 4

Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.

We believe identifying and responding to market-wide and systemic risks will deliver benefits for the economy, environment and society and will ultimately improve outcomes for clients and beneficiaries. As the world becomes more globalised and interconnected, the ability to transmit risks across geographies can cause further global crises to materialise. To truly address systemic risk, collective and coordinated action will be required to provide systemic solutions. Asset managers, working in conjunction with other stakeholders, must join forces to prevent systemic risk and to ensure a well-functioning financial system.

### Global Risks Framework

The key systemic risks we take into consideration across our investment risk, engagement and advocacy work are informed by academic research from the World Economic Forum Global Risks Report and the Centre for Risk Studies at Cambridge University.<sup>13</sup>

**Figure 8.** Global risks framework

Category	Risks
Economic	Ability of macroeconomic policy to prevent a global financial crisis, structural imbalances, chronic inflation, supply chain collapse, labour shortages, stability risks and related dislocations
Environmental	Ability of governments and businesses to address climate change, biodiversity loss, pollution, natural resource shortages and natural disasters
Societal	Risks associated with infectious diseases, inequality and cost of living crises, large scale involuntary migration, human rights, antimicrobial resistance, chronic health conditions, mental health deterioration
Geopolitical	Implications of rising populism, societal and/or political polarisation, protectionism, interstate conflict, evolution in the concentration and sources of geopolitical power and threats to free trade resulting in global governance failure
Technological	Risks associated with technological advances, misinformation, inadequate infrastructure and networks, cyber security, artificial intelligence and other frontier technologies
Governance	Risks associated with unethical business practices, bribery and corruption

Source: FHL, using World Economic Forum Global Risks Report 2024 and University of Cambridge and Citi GPS Systemic Risk Paper (April 2021).

We seek to take an integrated systems-based approach and prioritise and respond to the risks that are most likely, impactful and interconnected in nature. We examine the interlinkages between risks, for example, how climate change can drive biodiversity loss, with the potential to impact global food chains, health and wellbeing, social inclusion/unrest and thereby generate financial and economic crises.

### Identifying and responding to risks

The Investment Office is responsible for the daily oversight of market risk across FHL, as well as the oversight of the underlying portfolio managers' adherence to their pre-defined/client-agreed investment processes.

The Investment Office's main remit is to act as an independent investment risk consultant on behalf of our clients. While the Investment Office can challenge our portfolio managers' decisions, positioning and risk exposures, it cannot force change.

What the Investment Office can do, if the issue is sufficiently serious enough, is to escalate the matter to the Portfolio Review Committee (PRC). The PRC would then meet with the portfolio manager, consider the issue and then, along with the Investment Office and the portfolio manager, agree a resolution.

If no resolution can be agreed, the matter can be escalated to a sub-committee of the FHI Executive team, where the Investment Office can advocate for client communications/disinvestment. The members of our Investment Office take the time to understand individual fund managers' styles so that they can aid and enhance their process.

For our infrastructure team, all risk related matters are considered by the investment teams and are escalated to the IIC (Infrastructure Investment Committee) and if necessary to the Federated Hermes Private Markets Governing Body. The private equity team has a separate PRC (Portfolio Review Committee) which will consider issues the investment teams and the private equity ESG specialist decide to raise.

The Investment Office and portfolio managers have several regular fora where they identify and discuss macro risks and their possible investment implications. Sessions are typically centred around a discussion of market-level investment strategy and shared risk insights from across the investment floor. The aim of these discussions is to ensure that insights are broadly aired and that we have a risk-aware culture across the floor.

Based on the main risk scenarios we identify, we run a series of both hypothetical and historical stress tests across our portfolios that vary according to the asset class and strategy. This includes geopolitical events and shocks to markets, interest rates and currencies.

Given the long-term nature of our investment approach, the purpose of these tests is not to push portfolio managers to make immediate portfolio changes but to enhance their analysis and strategy.

<sup>13</sup> This includes: [SYSTEMIC RISK: Systemic Solutions for an Increasingly Interconnected World \(cam.ac.uk\)](#) University of Cambridge and Citi GPS, 'SYSTEMIC RISK: Systemic Solutions for an Increasingly Interconnected World', (April 2021); World Economic Forum, 'Global Risks Report 2024', (January 2024).

For our infrastructure and private equity teams, we measure, manage, and report on key risks at a fund and exposure level. Risk exposure by key risk characteristics is captured using quantitative and qualitative risk analysis tools to develop a proprietary framework to identify and monitor risk. Effective risk oversight (second line) necessitates strong collaboration with the investment teams. Thus, a risk oversight member is invited to attend the quarterly PRC or similar committee, as well as the Valuation Committee (ValCo), as an observer.

From a second line of defence perspective, our risk identification processes are set out in our risk management framework which recognises thematic emerging and principal risks. Sustainability and ESG risks are integrated into our risk taxonomy as principal risks, as well as our risk appetite statements with appropriate metrics to monitor reputation, sustainability and ESG risks more broadly.

The risk management framework also includes non-financial risk appetite statements to consider drivers of reputation and sustainability risks through a stakeholder lens. This stakeholder-focused approach recognizes the importance of considering ESG issues, including climate change (for example our carbon footprint), from the perspective of their impact both on our firm and also on our clients and wider stakeholders.

During 2023, key sustainability-related risks and the firm's exposure to these risks along with subsequent management activities were reported to our Risk, Compliance and Financial Crime Compliance Executive each quarter.

With respect to sustainability, work continued on the implementation of processes to ensure compliance with the EU's Delegated Acts requirements and implementation of Sustainable Finance Disclosure Regulation (SFDR). Consideration of sustainability risks are embedded within our business plan, governance arrangements and various risk oversight fora including executive reporting.

**Based on the main risk scenarios we identify, we run a series of both hypothetical and historical stress tests across our portfolios that vary according to the asset class and strategy. This includes geopolitical events and shocks to markets, interest rates and currencies.**

### **The Investment Office's main remit is to act as an independent investment risk consultant on behalf of our clients.**

As noted above, regular and ongoing monitoring of product-related ESG metrics and analysis is conducted and embedded within the business and second line of defence. Extensive engagement and collaboration between the risk function and the business is required to ensure a consistent interpretation of sustainability risk and common understanding of ESG integration across our product range. Furthermore, the development of expanded investment risk reporting has allowed for multiple views and articulations of key investment risks at both a product and firm level to support senior management's decision making on ESG matters.

### **Advocacy and involvement in industry initiatives**

We recognise that as investors we have an opportunity and a responsibility to help address market-wide and systemic risks. We engage constructively with regulators and policymakers globally to address environmental, social and other market failures that may prevent the financial system from operating in the best interests of its ultimate asset owners. This includes addressing barriers to responsible investment and stewardship.

We have a public policy and advocacy sub-team in the Responsibility Office, who work with experts across our firm to ensure our advocacy work is well informed, relevant and impactful.

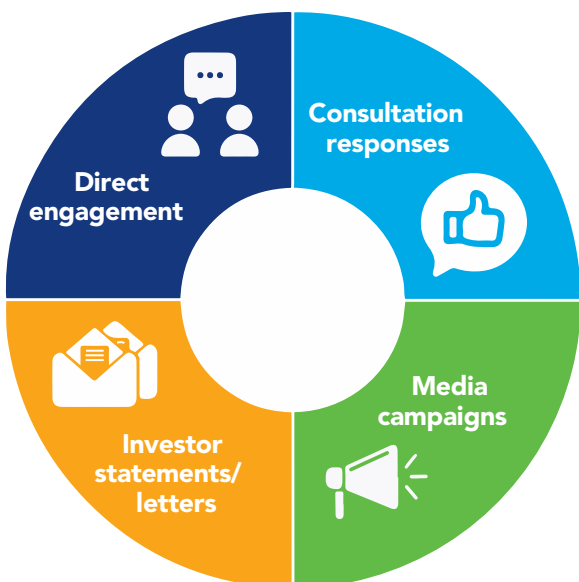




Our stewardship service provider, EOS, also undertakes a comprehensive programme of engagement with legislators, regulators, industry bodies and other standard-setters to help shape capital markets. Members of our investment teams contribute their expertise through collaboration with the Responsibility Office and EOS, as well as direct involvement in external industry initiatives. The result is an advocacy approach that aims to lead rather than follow the policy debate. Given the global nature of our investments, this work spans asset classes and geographies.

Our public policy advocacy can cover a range of themes to help shape capital markets in the interests of our clients and end beneficiaries. We engage on regulation relating to the investment industry and the assets in which we invest. This work may be on a country-specific basis or regulations and codes with a global remit. We identify areas for more in-depth advocacy and engagement where we feel significant change is needed and where we can add value. In 2023 this included climate change, nature and the need for a just transition. More information is included later in this section.

Figure 9. Tools of public policy advocacy



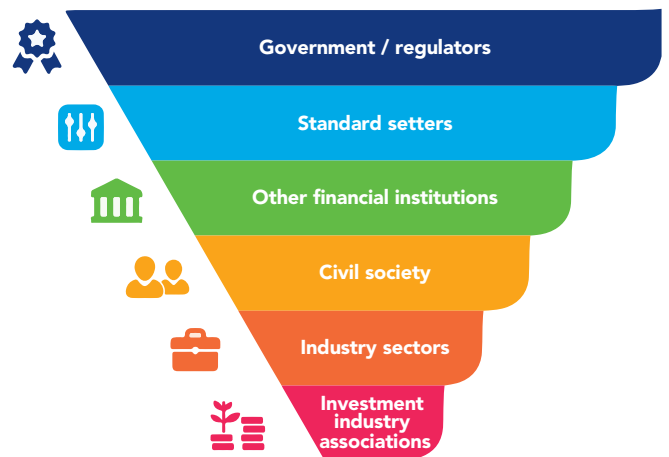
Source: FHL, as at 31 January 2024.

**Our public policy advocacy can cover a range of themes to help shape capital markets in the interests of our clients and end beneficiaries.**

We often engage directly with regulators and policymakers and aim to be a progressive and constructive voice in the debate. We provide practical insights about how proposed policies might play out in practice and help to identify suggested alternatives that might better achieve their responsible-investment policy aims. We also respond to consultations from policymakers to provide constructive feedback, using a networked approach to gain relevant input from teams across the business.

We contribute to policy discussions both directly and in collaborative fora and initiatives. We are a member of several industry bodies and initiatives around the world and are co-founders of many of them. Through these initiatives we engage with others both within and beyond the investment industry to promote responsible investment, including ways that the industry and our investees can respond to market-wide and systemic issues such as climate change. Colleagues from across the business – including the Responsibility Office, EOS, Risk and the investment teams – take on advisory roles in many of these organisations to share our practical expertise. For instance, our private equity team is a member of the Initiative Climat International (iCI) working group, which collaborates to provide structured knowledge sharing sessions that address climate change topics.

Figure 10. We engage with a range of audiences in our public policy advocacy



Source: FHL, as at 31 January 2024.

Over the course of 2023, we responded to 37 consultations or proactive equivalents from regulators, policymakers and industry initiatives. In addition to the advocacy work of the Responsibility Office, EOS also had 60 interactions with regulators, standard-setters and other third parties in the pursuit of public policy and market best-practice objectives.



In the following table, we have categorised our memberships of investment and stewardship-related initiatives or those at which we hold advisory roles.<sup>14</sup>

Tier 1 represents the initiatives in which we play a leadership role, for example chairing a working group; holding a formal advisory role such as on an advisory committee or Board; taking a leading role in preparing or actively contributing content to position papers and joint statements; shaping the strategic direction or leading collaborative engagements.

Tier 2 represents those initiatives in which we actively participate through membership of working groups, contribution to collaborative engagements, reviewing content or position papers, or lending support to joint statements.

**In 2023, we joined nine new initiatives and remain an active member in over 100 different efforts.**

And, finally, Tier 3 represents the remainder of the initiatives in which we are involved where we have light-touch participation such as attending meetings to be informed of developments. There are other organisations that we may collaborate with on an ad-hoc basis.

In 2023, we joined nine new initiatives and remain an active member in over 100 different efforts. Examples of our involvement from each of these three tiers are included in our following 'In focus' sections. We also describe in further detail how we have been involved in collaborative engagement with individual issuers under Principle 10.

**Figure 11.** Investment and stewardship organisational memberships

Tier 1		
Advance	FCA-PRA Climate Financial Risk Forum	Land, Nature and Adapted Systems Advisory Group
Asia Investor Group on Climate Change	Finance for Biodiversity Foundation	Natural Capital Investment Alliance
Associação de Investidores no Mercado de Capitais	Finance Sector Deforestation Action initiative	Nature Action 100
Association of Foreign Investors in Real Estate	Financial Services Culture Board	OECD Biodiversity Advisory Group
British Private Equity & Venture Capital Association	HACT	Quoted Companies Alliance
Ceres	Impact Investing Institute	Reading Real Estate Foundation
CFA UK	Institutional Investors Group on Climate Change (IIGCC)	RENEW Project
Climate Action 100+	Integrated Reporting and Connectivity Council	Sustainability for Housing Standards
Construction Leadership Council	Invest Europe	The 300 Club
Council of Institutional Investors	Investor Initiative on Hazardous Chemicals (IIHC)	UK Sustainable Investment and Finance Association (UKSIF)
CREFC	Steering Group	UN Global Compact
European Leveraged Finance Association	Investors and Indigenous Peoples Working Group	UN Principles of Responsible Investment (PRI)
FAIRR		
Tier 2		
30% Club	Global Canopy Forest IQ Project	Investors Policy Dialogue on Deforestation
Asian Corporate Governance Association	Global Investor Commission on Mining 2030	Net Zero Asset Managers Initiative
Best Practice Principles Group for shareholder voting research (BPPG)	Global Network Initiative	One Planet
Better Buildings Partnership	Healthy Markets Initiative (ShareAction)	ShareAction Long-term Investors in People's Health Initiative
Biopharma Sustainability Roundtable	Human Capital Management Coalition	Social Purpose Ecosystem Research Investor Purpose Action Group
British Property Federation	Impact-Weighted Accounts Initiative	The Investors Policy Dialogue on Deforestation
Business in the Community	Initiative Climat International (iCI)	Thinking Ahead Institute
Central Bank of Ireland Climate Risk and Sustainable Finance Forum	International Sustainability Standards Board (ISSB)	Transition Plan Taskforce
Energy Efficiency Financial Institutions Group (EEFIG)	Investor Advisory Group	UK-China Green Finance Task Force
Eumedion	Investment Association	UK Green Building Council
Financial Reporting Council Stakeholder Insight Group	Investor Action on Antimicrobial Resistance	UK Sustainable Investment and Finance Association (UKSIF)
Financing a Just Transition Alliance	Investor Alliance for Human Rights	Workforce Disclosure Initiative
Focusing Capital on the Long-Term (FCLT)	Investor Forum	World Benchmarking Alliance Investor Alliance
Glasgow Financial Alliance for Net Zero (GFANZ)	Investors for Opioid and Pharmaceutical Accountability	
	Investors in Nutrition and Health (Access to Nutrition Index)	
Tier 3		
British Council for Offices	Global Impact Investing Network	JapanSIF
Canadian Coalition of Good Governance	Global Infrastructure Investor Association	Loan Market Association
CDP	Global Institutional Governance Network	Pensions and Lifetime Savings Association
CECP: The CEO Force for Good	Global Real Estate Sustainability Benchmark (GRESB)	Revo
Dansif	INREV	ShareAction Investor Decarbonisation Initiative
Eurosif	International Corporate Governance Network	Supporter Network of SPOTT
Financing UK Nature Recovery Initiative	Japan Climate Initiative	TNFD Forum
French Social Investment Forum (FIR)	Japan Corporate Governance Network	UK Financial Institutions for Nature Group
Global Alliance for Buildings and Construction		

Source: FHL, as at 31 December 2023.

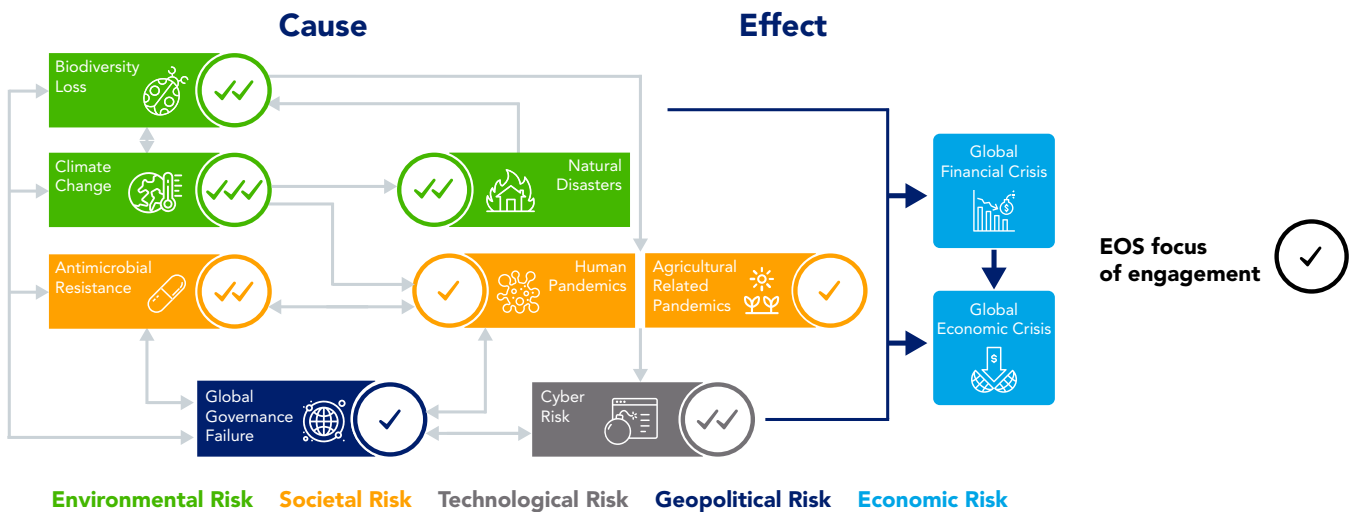
<sup>14</sup> This table is not exhaustive and does not cover all memberships of FHL.

### Engagement with investees

We take into consideration the most important systemic risks when developing our Engagement Plan and prioritising our engagement action. We have examined how the systemic risks highlighted above are interlinked, and often have cascading effects, and overlaid these with the focus areas in our engagement plan. For example, the three big causal systemic risks illustrated in the diagram below – biodiversity loss, climate change and anti-microbial risk – which have cascading causal effects, are important themes in our engagement plan.

In addition, the United Nations (UN) identified systemic risks and developed these into 17 Sustainable Development Goals (SDGs), adopted in 2015 as a global call to end poverty, protect the planet and ensure that everyone enjoys peace and prosperity by 2030. Our view is that the long-term success of businesses and the success of the SDGs are inextricably linked. We believe that all of our engagement and advocacy work is aligned to the delivery of the SDGs either directly or indirectly, enhancing our response to systemic risks.

Figure 12. Risks: Cause and Effects and EOS Engagement Priorities



Source: University of Cambridge and Citi GPS Systemic Risk Paper, and EOS data, as at 31 December 2023.

Figure 13. 1,782 of the issues and objectives engaged in 2023 in public markets were linked to one or more of the SDGs<sup>15</sup>

<b>13</b> CLIMATE ACTION	Climate action	<b>614</b>	<b>15</b> LIFE ON LAND	Life on land	<b>162</b>	<b>11</b> SUSTAINABLE CITIES AND COMMUNITIES	Sustainable cities and communities	<b>66</b>
<b>12</b> RESPONSIBLE CONSUMPTION AND PRODUCTION	Responsible consumption and production	<b>501</b>	<b>9</b> INDUSTRY, INNOVATION AND INFRASTRUCTURE	Industry, innovation and infrastructure	<b>161</b>	<b>6</b> CLEAN WATER AND SANITATION	Clean water and sanitation	<b>63</b>
<b>8</b> DECENT WORK AND ECONOMIC GROWTH	Decent work and economic growth	<b>374</b>	<b>1</b> NO POVERTY	No poverty	<b>149</b>	<b>17</b> PARTNERSHIPS FOR THE GOALS	Partnerships to achieve the goal	<b>32</b>
<b>10</b> REDUCED INEQUALITIES	Reduced inequality	<b>321</b>	<b>16</b> PEACE, JUSTICE AND STRONG INSTITUTIONS	Peace, justice & strong institutions	<b>137</b>	<b>4</b> QUALITY EDUCATION	Quality education	<b>21</b>
<b>5</b> GENDER EQUALITY	Gender equality	<b>224</b>	<b>3</b> GOOD HEALTH AND WELL-BEING	Good health and well-being	<b>131</b>	<b>2</b> ZERO HUNGER	Zero hunger	<b>15</b>
<b>7</b> AFFORDABLE AND CLEAN ENERGY	Affordable and clean energy	<b>183</b>	<b>14</b> LIFE BELOW WATER	Life below water	<b>111</b>			

**1,782** of the issues and objectives engaged in 2023 were linked to one or more of the SDGs

Source: FHL, as at 31 December 2023.

<sup>15</sup> This is the total of unique SDG-linked objectives and issues engaged. Some of the objectives and issues may be linked to more than one SDG. Please note, in our 2022 Stewardship Report we reported the total number of the issues and objectives engaged in 2023 in public markets that were linked to one or more of the SDGs as 2,744. This was incorrect due to an error in the calculation. The actual figure was 1,567.


Where we have identified market-wide and systemic risks, we intend to engage with our investees to ensure they have appropriately assessed, managed and mitigated the risks. This may be through collaborative engagement alongside other investors or industry initiatives, which we discuss in more detail under Principle 10.

EOS focuses its stewardship on the issues with greatest potential to deliver long-term sustainable wealth for investors including through positive societal and environmental outcomes.

The EOS [engagement plan](#) identifies good governance as setting the foundation for managing long term risks and creating value for stakeholders. We seek robust board oversight and management by companies of the most material long-term drivers of sustainable wealth creation affecting each company, as well as those systemic risks to long-term portfolio growth which cannot easily be mitigated through diversified investment strategies. When material and relevant, these factors should drive improved financial performance of individual companies to the benefit of investors, consistent with the long-term fiduciary interests of our clients, and more sustainable outcomes for society. The full taxonomy under Principle 9 identifies 12 key themes and 36 related sub-themes for engagement, many of which could be considered systemic risks as mapped in figures above. Within this, our work maintains a focus on the most material themes.


EOS reviews its [engagement plan](#) every year to ensure it is up to date and reflects client priorities. Further information on continuous improvements to the engagement plan can be found under Principle 2.


Based on EOS' review, in 2024 we will continue our focus on the most material drivers of long-term value, with a focus on four priority themes:

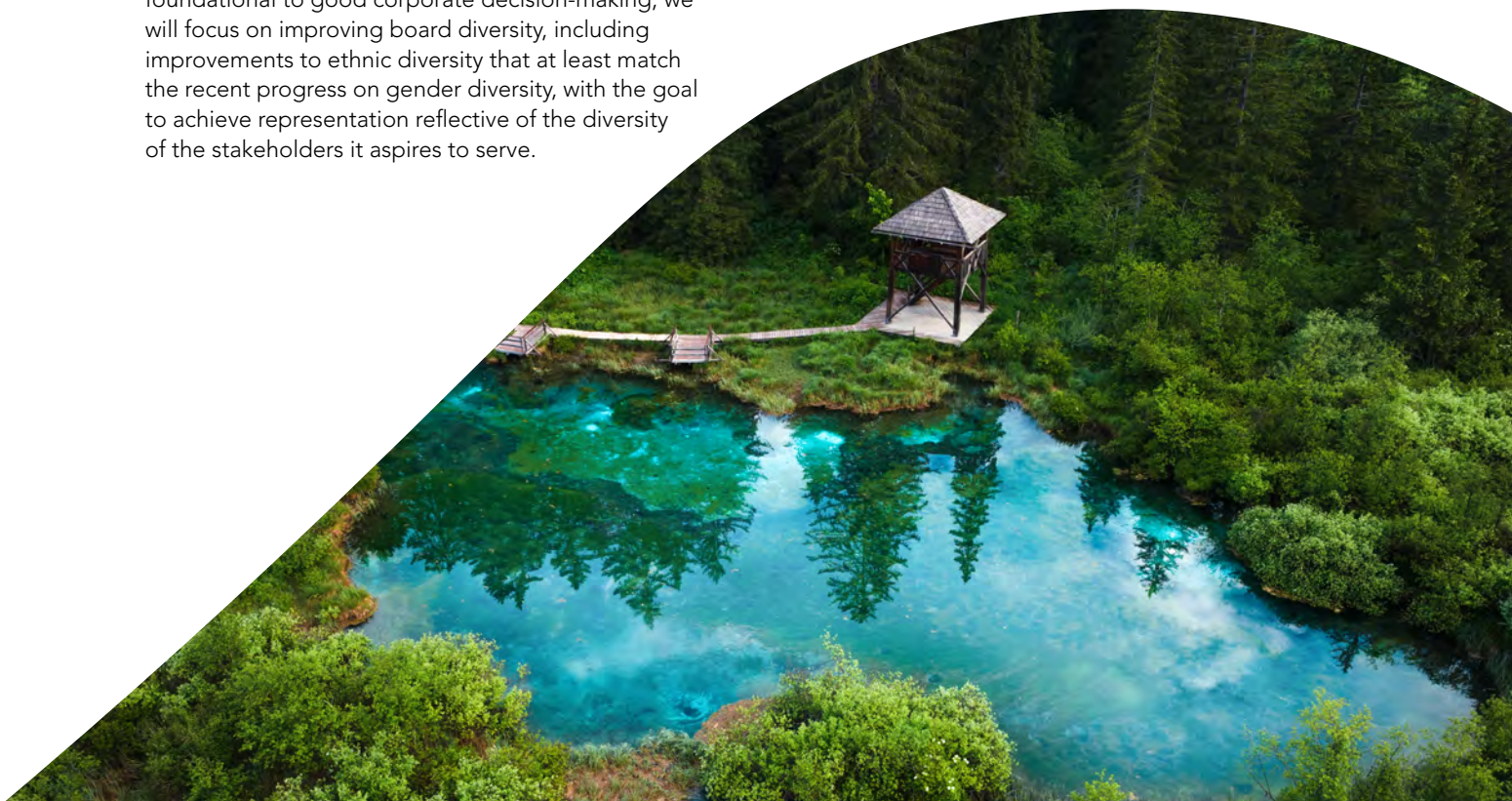
 **Board effectiveness and ethical culture:** In 2024 to enhance the quality of board performance, which is foundational to good corporate decision-making, we will focus on improving board diversity, including improvements to ethnic diversity that at least match the recent progress on gender diversity, with the goal to achieve representation reflective of the diversity of the stakeholders it aspires to serve.

## EOS reviews its engagement plan every year to ensure it is up to date and reflects client priorities.

 **Climate change action:** The emphasis of our engagement remains focused on companies having a strategy and greenhouse gas emissions reduction targets aligned to the Paris Agreement, seeking to limit climate change to 1.5°C, together with aligned financial accounts and political lobbying. In seeking Paris Agreement-aligned transition plans, we will evaluate the credibility of company transition plans including their reliance on technologies and seek to ensure that the governance oversight of investments adequately tests risks and dependencies. We will also continue to engage with companies in high methane emitting sectors to deploy the best available technology to identify and mitigate methane emissions, continue to engage on physical climate risks and work towards a 'just transition' for employees and communities.

 **Human and labour rights:** We expect companies to acknowledge the likelihood that human rights impacts are present within some operations and supply chains and to demonstrate appropriate board- and executive level governance of human rights. We will further focus on the protection of indigenous and community rights, and human rights in high-risk regions such as disputed territories or areas of conflict.

 **Human capital:** We increased our focus on diversity and inclusion, freedom of association, and health and safety, with a particular reference to the employee value proposition in the context of a tightening labour market.



In addition to the above priority themes, we pursued further engagement on three cutting edge topics in 2023: biodiversity, digital rights, and tax. Based on our review, for our 2024 engagement we will continue to intensify engagement on biodiversity and digital rights, two rapidly evolving topics, as follows:



**Biodiversity:** We expect companies to address marine and terrestrial biodiversity loss across their value chains, in-line with the COP15 mission to halt and reverse biodiversity loss by 2030. Given the high impacts and dependencies of the food system on biodiversity and ecosystem services, the retailing and production of food will remain a priority, as well as other sectors with significant impacts, such as mining and agrochemicals. We expect companies to reduce their impacts on biodiversity across the value chain, following the mitigation hierarchy, and aim for a net-positive impact on biodiversity as best practice. Depending on the specific company context, engagement will cover issues including deforestation, water-stress, regenerative agriculture, antimicrobial resistance (AMR), sustainable proteins and chemical runoff management. As we outlined in our [white paper on biodiversity](#), published in February 2021, as a priority companies must identify, assess, and measure their impacts and dependencies on biodiversity and ecosystem services, in line with the 2023 Taskforce on Nature-related Financial Disclosures (TNFD) recommendations. They should use the insights from the TNFD assessment to develop strategies, targets and actions plans focused on their most material risks and impacts.



**Digital rights:** We will continue to engage companies on our [Digital Rights Principles](#) (2022), which outline our expectations for responsible development and deployment of AI. Digital products and services can play a critical role in strengthening human rights but have also brought unanticipated harms and new challenges. We will engage companies on negative societal impacts including problematic content on social media; reinforcement of unintended bias; and

health and safety impacts on children and youth. We expect companies to balance freedom of expression with obligations to remove problematic content and take actions to respect privacy rights online. While the accelerating deployment of AI is creating new opportunities for companies, it also brings with it the potential for workforce disruption, regulatory infraction or reputational damage, and we will be engaging with companies on how they mitigate these risks.

The above represent particular priorities in the years ahead. However, we continue to maintain a comprehensive engagement plan covering a broad range of other themes, including responsible tax practices, increasing resource efficiency through the circular economy, reducing all forms of harmful pollution and seeking positive wider societal outcomes through increased corporate responsibility. More information on our Engagement Plan can be found under Principle 9.

We also use our voting rights as a means of addressing systemic risks. More information on how we use our voting rights is available under Principle 12.

We track the progress of our engagement with investees, including on systemic issues, using our proprietary milestone system. The outcomes of our engagement with investees are described under Principles 9, 10 and 11. We also publish regular case studies from EOS and our investment teams to document our engagement outcomes in more detail.

Throughout this report we have sought to provide a range of outcomes, including where we have not seen the desired outcomes of engagement. Below, we set out in more detail how we have responded to three of the key market-wide and systemic risks in 2023: climate change, nature, and human and labour rights.

These are examples of how our response to identified market-wide and systemic risks can result in changes to our investment portfolios, our engagement with companies and our advocacy efforts. The sections below are also therefore relevant to Principles 7 and 9-12.



### In focus: climate change

We aim to understand both a company’s contribution to climate change and its exposure to related risks and opportunities, which should allow us to play a positive role in encouraging firms to generate lower emissions and reduce the risks arising from climate change.

Our Climate-Related Financial Disclosures report sets out in more detail how we have integrated an assessment and management of climate-related risks and opportunities into our investment decision making. This includes the governance structures we have in place to ensure climate-related risks and opportunities are appropriately managed and that the outcomes of our risk-management processes feed into our business strategy. Our assessment of, and response to, the systemic risk of climate change spans our top-down investment risk and asset-level analysis, our engagement activities and our operational risk management.



As a member of the Net Zero Asset Manager Initiative (NZAMI), our Climate Action Plan sets out our interim targets validated by the Institutional Investors Group on Climate Change (IIGCC). It sets out how we will measure our progress, and the actions we will take to drive improvements. Our approach is focused on driving decarbonisation in the real economy. We have therefore set targets for the proportion of our holdings that will be aligned with a 1.5°C trajectory; these will drive our engagement with portfolio companies to achieve decarbonisation at the company level and not just in our portfolios. The Climate Action Plan also covers our approach to tackling our own operational and travel emissions.

**Our Climate-Related Financial Disclosures report sets out in more detail how we have integrated an assessment and management of climate-related risks and opportunities into our investment decision making.**

Figure 14. Our interim 2030 targets



Source: FHL, as at 31 January 2024.



Through this initiative, we commit to work in partnership with clients on their decarbonisation goals. We reported our progress toward this commitment in our [Climate-related Financial Disclosures Report](#) and will continue to do so on an annual basis.

### Assessing risk in public markets

Our integrated approach to managing climate risk and opportunities is based on our belief that we can create positive feedback loops between investment and stewardship. This should help reduce climate-related risks and maximise the opportunities for the companies and assets in which we invest.

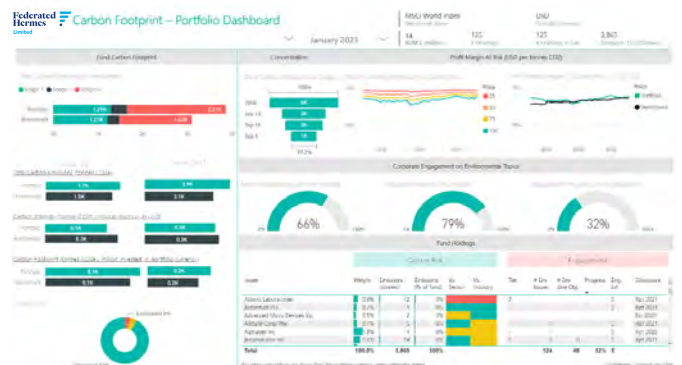
We monitor and measure the greenhouse gas (GHG) emissions of our investment portfolios through our proprietary carbon tool, which measures a fund's carbon footprint relative to its benchmark and calculates its carbon efficiency/intensity. The tool enables portfolio managers to identify whether high-emitting companies in the portfolio are being engaged or whether engagement needs to be initiated and understand the progress on any climate or wider environmental engagements already underway.

The information also helps increase our investment team's awareness of carbon-related risks, which can lead to updated valuations and potentially change investment decisions.

Our environmental tool assesses both portfolios and companies on their carbon, water and waste performance. It also looks to quantify the environmental cost of the impact via the following six lenses; carbon, water, waste, air pollutants, land/water pollutants and natural resource use. In addition, we have incorporated the temperature alignment of portfolios and companies alongside exposures to carbon intensive sectors; namely fossil fuels, mining and thermal coal.

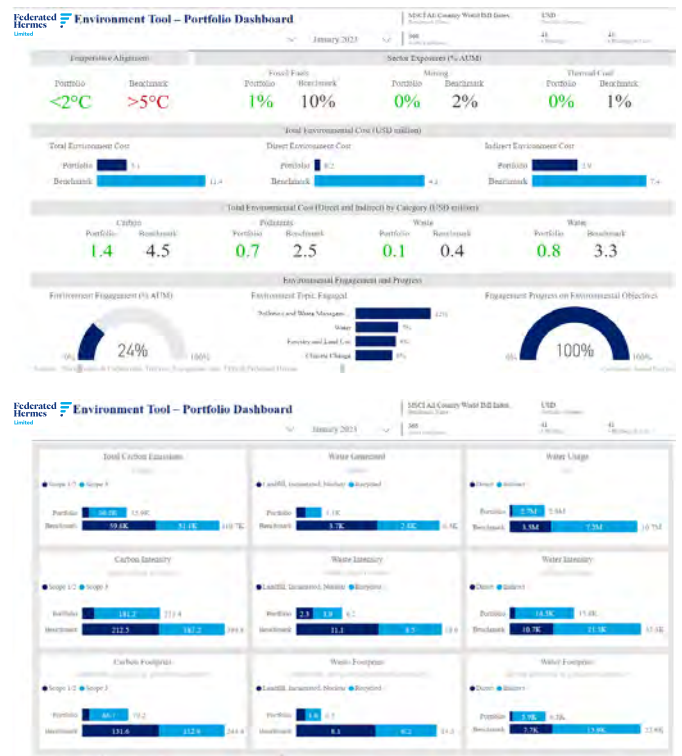
**We monitor and measure the GHG emissions of our investment portfolios through our proprietary carbon tool, which measures a fund's carbon footprint relative to its benchmark and calculates its carbon efficiency/intensity.**

Figure 15. Carbon Footprint – Portfolio Dashboard



Source: FHL, as at 31 January 2024. For illustrative purposes only.

Figure 16. Environmental Tool – Portfolio Dashboards



Source: FHL, as at 31 January 2024. For illustrative purposes only.

We have continued our work in assessing the Paris Alignment of our holdings using our proprietary alignment methodology, outlined in the Climate Action Plan described above. In addition to using this data to identify companies for engagement, this is also a tool for our investment teams in assessing the targets set by portfolio companies, to help flag particular names that may be at risk in the transition to a net zero economy. We will continue to enhance the methodology of our Paris Alignment test in 2024.

In 2023, we enhanced our climate scenario analysis across our public equity and credit investments, in partnership with a third-party, Planetrics. This allows us to understand transition and physical risks and opportunities related to climate change across different regions and sectors. Forward-looking data, such as that from scenario analysis, is becoming increasingly important to integrate into our investment decisions.

We also continue to evolve our work in understanding nature-related risks and opportunities. In 2023, we utilised the ENCORE framework to help understand our impacts and dependencies on nature as well as the Forest500 data to understand exposure to commodity driven deforestation in our portfolios.

### **EOS: engaging on climate-change issues**

Engagement is a crucial element of our approach to managing climate change risks and opportunities – and climate is a specific engagement focus in EOS' public-markets engagement programme. EOS aims for all companies to have a business model consistent with achieving net-zero emissions and an effective transition plan to deliver this in line with the Paris Agreement ambition of 1.5°C.

Our [Climate Action Plan](#) sets out the way we categorise our investees based on their extent of alignment to a 1.5°C world over time, dependent upon further advances in public policy and technology. We use an in-house Paris-alignment methodology for this assessment.

Companies identified as not aligned with 1.5°C are flagged as priorities for engagement and other stewardship actions. Engagement strategies are tailored to the region, sector and company context but include a combination of approaches, such as letters to the board, one-to-one meetings, collaborative engagement, and intensification strategies where appropriate. We engage in line with the expectations outlined in the EOS Engagement Plan, the Federated Hermes Climate Change Expectations for Investee Companies, and best-practice frameworks, such as the Climate Action 100+ Benchmark and the IIGCC Net Zero Investment Framework, Stewardship Toolkit and sector-specific climate change expectations.

### **EOS aims for all companies to have a business model consistent with achieving net-zero emissions and an effective transition plan to deliver this in line with the Paris Agreement ambition of 1.5°C.**

As an overview, we expect companies to publish a climate transition plan that sets out a strategy and greenhouse gas emissions reduction targets aligned with the goals of the Paris Agreement and its ambition to limit global average temperature increase to 1.5°C. Specifically, we request that companies commit to reaching net-zero emissions by 2050 at the latest and set near-term targets that are science-based and aligned with credible 1.5°C scenarios. These targets should be supported with a credible decarbonisation strategy that identifies, and approximately quantifies, key levers for emissions reductions and clearly states any relevant dependencies or assumptions relating to, for example, technology development or policy. We expect this transition plan to provide a coherent and comprehensive roadmap of the business transformation ahead, while recognising the inherent uncertainties that remain.





Additionally, we expect risk management and disclosures to be in-line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). We believe that developing and implementing such an approach effectively will require companies to have competent systems for the governance of climate-related risks and opportunities, including through overseeing that direct and indirect public policy advocacy activities are explicitly aligned to company strategy and to the Paris Agreement. In the short-term, we expect companies to deliver emissions reductions in line with achieving the medium- and long-term goals of the transition plan or to clearly explain reasons for underperformance, whether within or outside the company's influence. Engagement is prioritised based on the materiality of financed emissions and the degree of misalignment to the goals of the Paris Agreement. If companies fail to improve alignment with these expectations or to deliver on transition plans, without mitigating circumstances, we will consider using a range of further engagement tactics, such as voting against responsible directors.

We continued to play a leadership role in the collaborative engagement initiative Climate Action 100+ (CA100+). Since 2017, CA100+ has grown to include over 700 signatories representing over \$68tn in assets under management.<sup>16</sup> Since the initiative's inception, EOS has advised on high-level governance and engagement strategy, as well as leading or supporting a significant portion of company engagement dialogues. In 2023, we acted as lead or co-lead engager for 21 companies, while supporting on a further 13.

In October 2023, the CA100+ Net Zero Benchmark tracked further progress with 77% of focus companies committed to net zero by 2050 across at least Scope 1 and 2 emissions. In addition, 87% of focus companies had set medium-term emissions reduction targets, up from 81% last year. We expect to see more progress on target-setting as companies respond to the Science Based Targets initiative (SBTi) sector guidance. For example, following the publication of the SBTi cement pathway, Heidelberg Materials published 1.5°C-aligned targets.<sup>17</sup>

Some 93% of companies have now disclosed that there is board oversight of climate change, and 91% have aligned their climate disclosures with the TCFD recommendations. However, companies need to translate their climate ambition, risk management, and governance into credible decarbonisation strategies. Just 41% of focus companies have yet to disclose the decarbonisation actions they are taking to achieve their targets. Only 2% have already phased out, or are committed to phasing out, capital expenditure in unabated carbon-intensive assets.

For 2024, we are gearing up to engage companies on these outstanding gaps against the Benchmark, focusing especially on the strategic delivery of emissions targets and climate risk management. We will continue to encourage companies to develop credible and robust transition plans, while also emphasising the importance of governance, lobbying, and just transition considerations in crafting a competitive decarbonisation strategy.

Under Principles 10 and 11 we provide further detail on our collaborative engagements, including our through CA100+, with specific examples of company engagement.

### Real estate – making our assets part of the solution

Our real estate team has integrated climate risk management throughout its investment decision-making and asset-management processes. An ESG checklist is used for every acquisition, and this has been recently updated. It covers specific ESG issues like climate change, with a particular focus on flood risk and mitigation.

Our real estate team's Design Innovation Standard and Responsible Property Management Guide also sets out a series of guidelines and principles for our investment and development managers to follow. This ensures a consistent, start-to-finish approach to sustainable refurbishment and development, making use of key RIBA Stages.<sup>18</sup> The approach also follows BREEAM principles<sup>19</sup>, which adopt sustainable methods of construction to deliver an operationally efficient and sustainable building or refurbishment.

During 2021, the real estate team issued the Net-Zero Pathway document which sets out both the targets and approach to reaching net zero emissions by 2035 across the managed assets included within our UK real estate portfolio. Since then, we have published pathways for our residential, International and real estate debt portfolios.

By taking a proactive approach in developing and operating net zero buildings, we intend to reduce the risks of having stranded assets, asset value declines and potential so-called 'brown penalties' (a higher cost of capital for carbon-intensive buildings). Net zero also presents opportunities for market leadership: to generate income resilience for our clients; support and retain our occupiers; and provide long-term value to our stakeholders.

<sup>16</sup> Climate Action 100+ website as at January 2024.

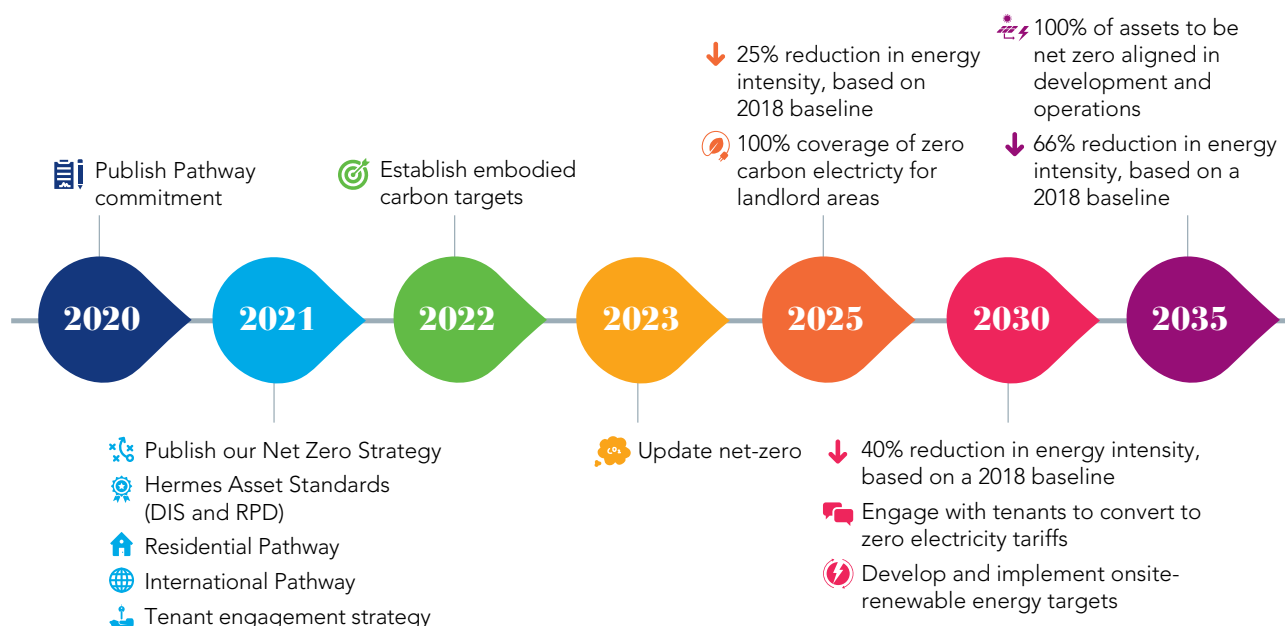
<sup>17</sup> At time of reporting, Heidelberg Materials was not an FHL holding.

<sup>18</sup> The Royal Institute of British Architects (RIBA) Plan of Work organises the process of briefing, designing, constructing and operating building projects into eight stages and explains the stage outcomes, core tasks and information exchanges required at each stage.

<sup>19</sup> BREEAM is the Building Research Establishment (BRE) Environmental Assessment Method, first launched in the UK in 1990. It sets best practice standards for the environmental performance of buildings through design, specification, construction and operation.



Figure 17. Real Estate approach to net zero



Source: FHL, as at 31 December 2023.

We aim to deliver on the net zero aspirations set out in the pathway, with a focus on delivery against four specific pillars of activity:

- 1 **Decarbonisation**
- 2 **Deliver energy efficiency**
- 3 **Stakeholder engagement**
- 4 **Utilise offset opportunities**

More information on the real estate’s team approach to net zero can be found in the Net-Zero Pathway document.

**Addressing net zero transition risk**

Decarbonising existing property portfolios is one of the biggest challenges that real estate industry is facing and will need to respond in the next decade. There is not an one size fit all but at the same time building-by-building approaches also fail to exploit the opportunities presented by portfolio-level investment decisions and economies of scale. With this in mind, we piloted Decarbonomics™ in 2023 on our Milton Park and Federated Hermes Property Unit Trust (FHPUT) portfolios to benchmark performance and develop roadmaps for decarbonisation.

**We continue to develop and implement initiatives across our real-estate portfolio that are designed to reduce carbon emissions and to improve efficiencies in our built environment portfolio.**

**Benchmark**

The first step was to create a baseline to establish the current carbon position, using Decarbonomics™ Carbon Data Insights to plug material data gaps. A five-day, non-intrusive survey representative of the wider estate was then conducted to validate the data.

**Roadmap**

From the carbon baseline, a fully costed roadmap to achieve our 2035 net zero target was generated for each portfolio. To ensure the roadmap was realistic and achievable, Decarbonomics™ combines machine learning analysis with the expertise of building services engineers, whilst taking tenant requirements into consideration.

**Deliver**

We realise that roadmaps are only good if we deliver against them and demonstrate progress through robust monitoring and verification over the course of asset improvement works. This pilot project provided clarity around our asset investment decisions and demonstrated the effectiveness of tools like Decarbonomics™ in supporting our net zero transition plans and decarbonising our portfolios at scale.

We continue to develop and implement initiatives across our real-estate portfolio that are designed to reduce carbon emissions and to improve efficiencies in our built environment portfolio, making use of new technology and best practice gleaned from our active engagement in peer-group benchmarking. A case study on our approach to improving the environmental impact of real estate assets is included under Principle 9.

As part of our commitment to delivering lasting social impact, this year we carried out an innovative new pilot project in partnership with CBRE. Six assets from different classes were analysed across the following ten categories:

Climate, Community and Culture, Connectivity, Diversity and Inclusion, Economic Regeneration, Education, Employment, Environment, Health, and Security and Safety

The resulting scores for each asset were mapped against local area needs, producing a detailed picture of the asset's existing social value and where future improvements might be made. A suite of possible interventions was then plotted across each asset, with the investment required calculated against the social value delivered, leading to an overall Social Return on Investment (SROI) score. This process has enabled us to develop highly bespoke social impact strategies for each asset that took part in the pilot project, and we are now rolling out this industry-leading approach across our portfolio.

### Infrastructure

Our infrastructure team's long-term investment horizon means that climate risk and climate opportunity are integral parts of our team's investment decision making.

Our infrastructure team engages actively with our portfolio companies in our capacity as shareholder, board director and committee member on their approach to climate change. Transition and physical risks such as carbon pricing and extreme weather can be highly relevant to our infrastructure investments. We also see significant opportunity for infrastructure at the centre the transition to a net zero economy, including both 'greening' our existing infrastructure and allocating capital to transition solutions, such as renewable energy generation.

The infrastructure team has set an objective for all portfolio companies to put in place Paris aligned targets (limiting temperature increase to 1.5°C) by 2025. Prospects for alignment are factored into all new investment assessments. Progress against Paris Alignment is monitored annually by the Infrastructure Investment Committee using the FHL proprietary test, developed in line with IIGCC guidance, which classifies companies on a scale of alignment subject to their satisfaction of certain criteria.

During 2022, our most recent reporting year, we engaged with 100% of our Infrastructure portfolio companies, with 42% of our recorded ESG-related interactions focussed on climate change. At time of finalising this report, Q4 2023 statistics were in the process of being compiled.

In 2021, we also undertook whole portfolio scenario analysis, in collaboration with environmental adviser ERM, in order to deepen our understanding of transition and physical risk for our existing portfolio. The outputs of the exercise were shared with companies and are used as an ongoing stewardship tool. This analysis will be refreshed periodically to account for latest climate scenario data and material changes in portfolio company business activities, if any.

The infrastructure team has set an objective for all portfolio companies to put in place Paris aligned targets (limiting temperature increase to 1.5°C) by

# 2025

### Private Equity

In 2023, the private equity team introduced a new framework to assess the climate risk exposure of any potential investments. Significant transition risks will require additional analysis in collaboration with the team's ESG specialist.

The additional analysis will be tailored to the risks identified, whether relating to physical climate risk, transition climate risk or deforestation. The team will seek to avoid making any investments in companies that are not able to thrive as the world transitions to net zero.

### Advocacy: delivering positive industry-wide change

Looking beyond investment and stewardship, we also believe that policymakers have a key role to play in determining the investment risks and opportunities created by climate change. In 2023, we carried out extensive advocacy work on climate-related issues.

Throughout 2023, we have participated in public consultations and meetings with government officials, financial regulators, stock exchanges, industry associations, and other key parties to contribute to the development of policy and best practice to facilitate the transition to a net zero carbon economy. The aim is to protect and enhance value for our clients by improving shareholder rights.

We have advocated for a number of changes to public policy and market best practice, including asking governments to commit to more ambitious climate targets with aligned domestic policies and stimulating investment in required technologies.

With cross-sector guidance on target-setting and transition planning now published by organisations such as the Transition Plan Taskforce (TPT) and Science Based Targets initiative (SBTi), 2023 saw multiple consultations on the financial sector. This included the Monetary Authority of Singapore's (MAS) consultations on Guidelines for Transition Planning for asset managers, the SBTi's consultation on updated resources for the financial services sector and the TPT's consultation on draft guidance for asset managers. We responded in support of the development of these guidelines, with recommendations on how to further enhance their effectiveness. The TPT guidelines in particular offer a framework for high quality, comparable disclosures and are intentionally compatible with the climate-related standards developed by the International Sustainability Standards Board, which creates international applicability. We encouraged the MAS to align their proposals where possible with the TPT's guidance to aid interoperability. We also co-signed a letter alongside a number of our peers to the UK Government on the case for mandatory transition plans for all large companies. The UK Government subsequently committed to consult on requirements for the UK's largest companies to disclose their transition plan if they have them.


**DEEP DIVE: COP28**


**A key focus of our advocacy work in 2023 was COP28 in the United Arab Emirates. We identified COP28 as a significant opportunity to making progress on delivering a just transition.**

**Our asks:** Some of the biggest challenges now facing the transition to a low-carbon economy are social rather than simply technical, and therefore successfully addressing climate change demands the consideration of equity and justice, alongside cost curves and R&D. Reducing greenhouse gas emissions is, among other things, an exercise in large-scale, accelerated change management requiring the consent and support of stakeholders within and outside the business. A company that identifies the social implications of its transition plan and proactively minimises and mitigates these will be better placed to execute this change effectively. Governments, corporates, and financial institutions should ensure that the costs and the benefits of actions taken to advance climate goals are shared widely.

We hoped to see the need for a just transition considered upfront during negotiations. Given the need for equity and justice in meeting adaptation costs as well as mitigation costs, governments need to support finance for Emerging & Developing Economies (EMDEs) for climate mitigation and adaptation, including by building greater confidence in the Global Goal on Adaptation. The operationalisation of the Loss and Damage Fund agreed at COP27 was a key focus going into the negotiations as this could help to plug the gap on adaptation finance, particularly for emerging and developing economies.

**Our actions:** The FHL delegation spoke at 14 panels, keynotes, and roundtables at the COP28 summit on a number of topics and issues. We announced at COP28 that we have formed a partnership with The Global Alliance for A Sustainable Planet (GASP) to work together and find new ways to collaborate on innovative investment solutions. The ambition is to create a scalable platform

that aligns impact-focused patient capital with the development needs of countries on the frontlines of climate change. FHL and GASP will explore the prospects of leveraging concessionary capital as a means to attract private investment to opportunities which will contribute to solving some of humanity's most urgent challenges as articulated in the UN SDGs. This collaboration is motivated by the importance of finding new pathways to sustained prosperity while preserving ecosystems and planetary health.

**Outcomes:** Embedding just principles across decarbonisation efforts was a key theme, while the role of nature and food systems in supporting an equitable transition was brought into the fore. Driven by this momentum on a just transition, COP28 opened with the operationalisation of the loss and damage fund, supported by funding pledges of \$700m.<sup>20</sup> The fund seeks to automatically provide financing to those economies and communities adversely impacted by the effects of anthropogenic climate change. Loss and damage payments have been the subject of intense contention throughout the three decades of COPs, marking the importance of this progress. The emphasis on the fund's role in supporting vulnerable economies reflects greater consensus on the just transition among the international community.

But the loss and damage fund was not the only subject of fraught finance negotiations. Developed countries noted with "deep regret" that the \$100bn a year climate finance target, the overarching annual goal for mitigation and adaptation funding, had never been met and would expire in 2025.<sup>21</sup> Despite the Global Stocktake urgently calling for the significant scaling of adaptation finance commitments to equitably build resilience and conserve access to water and food, the agreement over this finance was shelved for 2024.<sup>22</sup> A separate UN adaptation fund raised only half of its target \$300m by the end of the conference.<sup>23</sup> Meanwhile, communities and their food and water systems are more vulnerable than ever to the changing climate.

<sup>20</sup> World Resource Institute, 'COP28: Outcomes and Next Steps' (December 2023).

<sup>21</sup> [edie](#), 'COP28 into overtime following 'disappointing' draft Global Stocktake text – here's what's included' (December 2023).

<sup>22</sup> UNFCCC, 'First Global Stocktake High-level Committee' (December 2023).

<sup>23</sup> Reuters, 'COP28 calls for adapting to warmer world without resolving how to pay' (December 2023).

## In focus: nature

Throughout 2023, worrying reports of deforestation, water pollution and soil depletion continued to dominate news headlines, ensuring that preservation of biodiversity and the natural world remained high on the investor agenda. There is a growing recognition of the financial risks associated with companies' impacts and dependencies on nature and the ecosystem services it provides. These services include pollination, water quality management and fertile soils, all vital for life to thrive.

## Engagement

We responded to this challenge by engaging with companies in the sectors with the biggest exposures, such as food and beverage producers, encouraging them to develop strategies to avoid and mitigate their most material impacts on nature, whilst aiming for an overall net-positive impact. Our biodiversity engagement covers different sub-topics, and a focus area in 2023 was regenerative agriculture and pesticides. We continued to engage companies on their targets and strategies to implement regenerative agriculture in their supply chains and encouraged them to measure the outcomes of their approach on soil health, water, carbon, and biodiversity. Our focus on reducing pesticide use is important because pesticide runoff can cause widespread pollution and contaminate soils, water, and air. We expect companies to oversee how pesticides are used within their agricultural supply chain. This may include mapping their exposure and setting expectations for suppliers to limit pesticide use, starting with eliminating the most hazardous pesticides. Our engagement on pesticides is in line with the Kunming-Montreal Global Biodiversity Framework (GBF) which sets out the need to reduce the overall risk from pesticides and highly hazardous chemicals by at least half. We also expect companies to monitor and respond to the potential regulatory and reputational risks associated with the misuse and overuse of pesticides.

## Collaborative engagement

Engagement on biodiversity is growing and we are working in collaboration with others in the industry to strengthen and streamline approaches, including as co-chair of the Engagement Working Group within the Finance for Biodiversity Foundation.

We are also part of the Farm Animal Investment Risk and Return (FAIRR) collaborative engagement on waste and pollution and antimicrobial resistance (AMR), and Nature Action 100, a new collaborative engagement initiative on biodiversity launched in 2023. We were pleased to see the Nature Action 100 initiative kick off, with letters sent to 100 companies asking them to consider including nature in their business models, strategies, and climate transition plans.

We also joined the PRI's Spring collaborative initiative for nature and are a member of the Advisory Committee. This will focus on preventing biodiversity loss by engaging companies on their advocacy work on deforestation. We are members of the signatory advisory committee for this group and have held regular meetings to provide input into the investor statement and the methodology developed to select target companies.

Our public policy work is aligned with our engagement on regenerative agriculture and pesticide use. In 2023, we co-signed an investor statement coordinated by the FAIRR initiative calling on G20 finance ministers to repurpose their agricultural subsidies in line with climate and nature goals. This statement follows the GBF's target to identify incentives, including subsidies harmful for biodiversity by 2025, and eliminate, phase out or reform them in an effective way.

In recognition of the need for better disclosure frameworks on nature-related issues, including deforestation, we also joined the Taskforce on Nature-related Financial Disclosures (TNFD) Forum and provided feedback on the draft recommendations. Following the publication of the TNFD recommendations, we piloted elements of the TNFD disclosure framework in our latest Climate-related Financial Disclosures Report. We also formally signed up as an inaugural TNFD Early Adopter.<sup>24</sup>

<sup>24</sup> TNFD, 'TNFD Early Adopters' (January 2024).





## DEEP DIVE: Deforestation

### Halting and reversing tropical deforestation will be essential if we are to avoid the consequences of severe climate change and biodiversity loss.

Deforestation and forest degradation, mostly driven by beef, palm oil, soy and other agricultural commodity production, has continued despite the immense value of tropical rainforests. Following our commitment to strive to eliminate commodity-driven deforestation from our portfolios by 2025 at COP26, deforestation remained a priority in 2023. We recognise the need for investors to conduct sustained and outcomes-focused engagement with companies in forest-risk sectors and with regulators in order to seek more sustainable production and consumption practices in support of climate goals.

#### 2023 progress

In line with our commitment, in 2023 we published our first reporting on deforestation risk assessment and mitigation activities across our public markets, real estate, infrastructure and direct lending AUM. In public markets, for example, we disclosed the proportion of AUM which is on the Forest 500 list. Global Canopy's Forest 500 list ranks the most influential companies driving tropical deforestation. The list focuses on the 350 companies with greatest influence on tropical deforestation, based on their exposure to forest-risk commodities, and the 150 financial institutions which are providing the most finance to them. It ranks them based on the strength and implementation of their commitments on deforestation and human rights. We also looked at the engagement coverage of these companies on the issue of deforestation. Approximately 50% of names held by FHL in our public markets' strategies on the Forest 500 list were being engaged on deforestation as at 30 September 2023. In 2024, we will continue to enhance our deforestation exposure analysis and reporting in public markets as data availability improves.

As well as publishing this report, we have completed the annual review of our Deforestation Policy Statement. As part of this process, our real estate debt and private equity portfolios have now been brought into scope of the policy statement.

In 2023, we deepened our engagements on deforestation with food and beverage companies, commodity traders and fast fashion companies and have continued to play a role in the collaborative initiative Finance Sector Deforestation Action (FSDA).

FSDA was launched to support investors who made the commitment to eliminate commodity-driven deforestation through engagement and due diligence. Following the letters on deforestation that we sent to the target companies as part of the FSDA group, we had good engagements with numerous companies on the FSDA list. This included Adidas (a German sportswear apparel company), Yum! Brands (a US restaurant chain), Bunge (a US agribusiness and food company) and Archer-Daniels Midland (a food processing and commodities trading company).



For example, EOS met with the chief sustainability officer of Yum! Brands on multiple occasions as part of our direct engagement, and with the FSDA collaborative engagement, and asked the company to increase commodity traceability in its supply chain. It underlined the challenge of tracing the soy in its cattle feed back to its origin. We shared some deforestation tools that the company could use to help improve traceability, which it agreed to consider.

We hold the chair or other responsible directors accountable through voting where we believe companies' actions are materially misaligned with the goals of the Paris Agreement and/or where companies are not responding sufficiently to the risks and opportunities posed by climate change. This includes a particular focus on companies that are involved in activities that are clearly incompatible with limiting global warming to safe levels, such as causing deforestation and the expansion of coal-fired power. We assess companies using a range of frameworks and benchmarks, including Forest 500.<sup>25</sup>

We have also been involved in the development of ForestIQ. ForestIQ is a new data platform launched in 2023 for financial institutions which brings together a range of data sources on corporate exposure to deforestation. The platform has been developed by an alliance of not-for-profits – Global Canopy, the Stockholm Environment Institute and ZSL – in close consultation with several financial institutions, including FHL. This project aims to improve the usability, quality and scope of data available to investors to allow more accurate portfolio risk assessments and to inform engagement.

Since COP 15, we have been advocating for ambitious implementation of the Global Biodiversity Framework at national level. For example, we supported the Global Witness campaign on the proposed amendment to the UK Financial Services and Markets Bill to extend the due diligence requirements to the financial sector when investing in or lending to forest risk sectors. This amendment had broad support and passed through the House of Lords but was defeated in the House of Commons. The UK Government agreed to explore other options to encourage or require financial institutions to conduct due diligence on deforestation. We have since attended roundtable discussions with representatives of HM Treasury and the Department for Environment, Food & Rural Affairs (DEFRA) in the UK focusing on aligning financial flows with the Glasgow Leaders' Declaration goal of reversing forest loss and land degradation by 2030.

<sup>25</sup> Forest 500.

## In focus: human and labour rights

A failure to protect and respect human rights undermines not just the wellbeing and dignity of individuals but also damages the wellbeing of economies and societies. The Universal Declaration of Human Rights is clear that 'every individual and every organ of society' has responsibility to promote and protect human rights. As noted in the UN Guiding Principles on Business and Human Rights, this responsibility also applies to companies and investors.

Protecting and respecting human rights is also central to our duties as an investor, given that human rights issues can have a material impact on our investments. For example, human rights issues can present operational risks (e.g., delays to projects, interruptions to business continuity, loss of a company or a project's social licence to operate), regulatory risks (e.g., the EU's non-financial reporting directive, the UK and Australia's Modern Slavery Acts, the US Alien Tort Claims Act) and reputational risks (e.g., negative media attention). We recognise that human rights are not just matters for individual companies but can also represent systemic risks to financial markets through, for example, harming certain economic sectors or exacerbating instability in particular countries or regions.

The business case for corporate action on human and labour rights is therefore compelling.

### Human Rights Policy Statement

In September 2023 we published our inaugural Human Rights Policy Statement. This statement sets out our commitment to respecting human rights in accordance with the United Nations (UN) Universal Declaration of Human Rights; the International Labor Organization's (ILO) Declaration on Fundamental Principles and Rights at Work; the UN Global Compact; and the UN Guiding Principles on Business and Human Rights (UNGPs). This commitment applies to all of our investments, in all asset classes and in all geographies. We are committed to integrating human rights issues (as one aspect of wider sustainability and governance issues) into our investment analysis and decisions across all asset classes. We are also committed to using our influence as a large asset manager to engage with the companies we invest in to protect and respect human rights.

## Engagement approach: Human and labour rights in supply chain

Many of the problems linked to human and labour rights can be disproportionately found in supply chains. It is in part due to their complex, dynamic and opaque nature that poverty, modern slavery, and inequalities persist. Regulations continue to come into force to tackle human rights issues, with modern slavery or supply chain transparency/due diligence regulations now in place in the UK, Australia, California, Canada, France, Germany, and Norway, among others. Investors and companies must get ahead of these, or run the risk of fines, lawsuits, or reputational damage.

Our engagement with companies focuses on their responsibility to respect human rights as outlined by the UNGPs. This begins with aspects such as policy and governance, but also encourages companies to do more to undertake effective human rights due diligence to identify potential supply chain impacts and provides remedy as needed. We engage on how a company can provide meaningful grievance mechanisms that allow affected workers to be heard and provide feedback for solutions.

We also encourage companies to move beyond the relatively standard process of auditing supply chains - which may provide only limited assurances over the occurrence of human rights concerns in supply chains - to consider how their own actions may be exacerbating human rights issues, and how to address these.

We updated our voting policy in 2022 to consider recommending votes for relevant proposals or against directors where a company was in clear breach of its applicable regulatory human rights responsibilities or those outlined in the UN Guiding Principles on Business and Human Rights. We applied the policy in 2023 and recommended votes against a number of company directors.

Companies should also use their leverage and collaborate with each other, recognising that transformative change requires collective action. We engage companies on how they work collaboratively with such alliances, to promote change across a sector or industry.



 CASE STUDY

## Hon Hai Precision Industry



**Hon Hai Precision Industry Co., Ltd. (known internationally as Foxconn) is a Taiwanese multinational electronics contract manufacturer.**

We have engaged with Hon Hai on the topic of labour policy and practices since 2010, including improving its human capital management strategy to address labour rights concerns. In April 2023, we were invited by the company for a production campus tour in Zhengzhou, China where we could see first-hand the implementation of the company's human capital management strategy.

### Engagement

We began engaging on labour standards in 2017 after controversies arose surrounding working conditions. Despite being an employer of over one million people globally, Hon Hai did not appear to have a robust human capital management strategy. It recognised that staff turnover was high, with most of its human resources work focused on administration, and it was unclear to what extent the issue was on the board's agenda. Although the company was tracking various human capital metrics, none were disclosed.

In 2017, media reports claimed that student workers aged 17 to 19 were working long hours and overtime, which violated local law.<sup>26</sup> The company acknowledged that there were operational oversight issues. We discussed responsible remedial actions including the termination of the existing student worker programme and for the company to raise the working age to the international labour standard of 18 years old, rather than adhering to the local standards in China of 16 years old. We continued to engage with the company on human capital management topics over this period.

In October 2022, we turned our attention to ensuring that the company demonstrates that working conditions across its supply chain outside of China meet international standards. Following media reports that indicated subpar working conditions in the company's Indian plant<sup>27</sup>, we pressed for better disclosure of audit results and actions taken to address labour standards, with more emphasis on grievance mechanisms, employee engagement and welfare.

In early 2023, EOS was invited by the company to a factory tour in Zhengzhou, the location of the protests. One of the aims was to understand the circumstances leading to employee protests and to conduct a due diligence visit at the social and living facilities for employees. EOS was the only investor representative to gain access to the site, providing a unique opportunity for direct engagement with the most senior management of the Zhengzhou plant.

During the tour, we were able to visit most of the social facilities, including the learning and development centre, job training centre, canteen and, most importantly, the living quarters. Positively, the company allowed EOS to select any room, floor and block of any dormitory in an effort to meet our due diligence requirements. Our EOS engager stayed in an employee dormitory during the two-day tour and also dined in the assembling worker canteen before departure.

### Engagement outcomes

In addressing our labour rights concerns over the years, the company stated in 2020 that it had developed a labour strategy, approved by the board, which prevented students under the age of 18 from working in production. In May 2022, we were pleased to see the company's new long-term social goals as part of its ESG strategy.

During the 2023 engagement, the company provided an update on its revised value chain code of conduct. It also provided updates on its recent labour issues, which included a comprehensive update on how issues arose and were resolved. The company added that 100% of its production plants are internally audited as well as an independent third-party audit of its principle customers. It also confirmed that it would expand disclosure of data outside of China in its next ESG report, due for release in 2024.

We believe that through these and other measures, Hon Hai has made significant positive steps towards a more holistic human capital management strategy.

<sup>26</sup> Financial Times, 'Apple's iPhone X assembled by illegal student labour' (November 2017).

<sup>27</sup> Reuters, 'Foxconn India's iPhone plant restarts production after December protests' (January 2022).

In 2023, both FHL and EOS participated in the PRI's Advance initiative, the collaborative stewardship initiative for human rights and social issues launched in 2022. The objective of the initiative is to advance respect for human rights, minimising negative outcomes and drive positive outcomes for people. The metals and mining and renewables sectors were selected as the initial focus based on an assessment of the highest risk sectors and the practicality of engaging with these sectors. 40 focus companies have been selected for engagement, 25 metals and mining and 15 renewables companies. Three key expectations have been set for the focus companies: to

implement the United Nations Guiding Principles on Business and Human Rights (UNGPs), to align their political engagement with their responsibility to respect human rights, and to deepen progress on the most severe human rights issues in their operations and across their value chains. As participants both FHL and EOS committed to take on the role of lead engager with at least one company as well as supporting other engagements. As of 31 January 2024, FHL and EOS combined are leading engagements with three companies and supporting with a further eight companies.



### DEEP DIVE: Indigenous peoples' rights



We believe that how a company manages its human rights strategy is of critical importance for its licence to operate, its impact on people's lives and ultimately its ability to create and preserve long-term value. We focus on Indigenous Peoples' rights within our human rights engagement theme. We have set objectives on Indigenous Peoples' rights with more than 30 companies, mostly in the oil and gas, mining, and financial services sectors. Through our collaboration and involvement with the Investors and Indigenous Peoples Working Group, we consider Indigenous perspectives when setting priorities for engagement and researching companies.

International standards for Indigenous Peoples' rights are documented in the UN Declaration on the Rights of Indigenous Peoples (UNDRIP) 2007. UNDRIP, which is endorsed by most countries, recognises Indigenous Peoples' right to give or withhold Free, Prior and Informed Consent (FPIC) to business activities on or near their lands.<sup>28</sup> FPIC is an avenue through which Indigenous Peoples seek to secure formal recognition of their right to their traditional lands and natural resources.

Additionally, there is a strong overlap between Indigenous Peoples' rights and some of our other engagement themes, for example, natural resource stewardship. While Indigenous Peoples own, occupy or use 25% of the world's surface area, they safeguard 80% of its remaining biodiversity.<sup>29</sup> In the Amazon rainforest, Indigenous Peoples

can play an important safeguarding role because of their deep knowledge and understanding of the Amazon's ecosystem.<sup>30</sup> But in recent years this has been undermined by illegal logging, mining and fossil fuel extraction. Therefore, protecting Indigenous Peoples' rights offers strong benefits for biodiversity as well.<sup>31</sup>

In our engagement, we encourage companies to adopt a policy commitment to Indigenous Peoples' rights, separate from or included in its Human Rights Policy, which includes support for Free, Prior and Informed Consent (FPIC) and UNDRIP. For example, we engaged with BHP Billiton to share feedback on its policy for protecting Aboriginal heritage sites in Australia. In 2023, the company published a new reconciliation plan that covered FPIC and laid out a five-year plan for community engagement.

We encourage companies to report on the implementation of their policy commitment to Indigenous Peoples' rights and have suggested the metrics used within the International Sustainability Standards Board standard for mining. The standard requires that companies disclose the percentage and grade of proved and probable reserves located in or near areas considered to be Indigenous Peoples' land, and the due diligence practices and procedures with respect to Indigenous Peoples' rights, including the FPIC processes. For more information, see EOS' [Q3 Public Engagement Report](#).

<sup>28</sup> United Nations, 'United Nations Declaration on the Rights of Indigenous Peoples' (2018).

<sup>29</sup> World Bank, 'Indigenous Peoples'.

<sup>30</sup> WWF, 'Governments recognize the urgency of avoiding the point of no return in the Amazon' (August 2023).

<sup>31</sup> Convention on Biological Diversity, 'Indigenous Communities Protect 80% Of All Biodiversity' (July 2022).



## Principle 5

Signatories review their policies, assure their processes and assess the effectiveness of their activities.

### Ensuring our policies support effective stewardship

The latest versions of our policies are available on our Policies and Disclosures webpage. We regularly review our policies to ensure they remain effective. The process for doing so depends on the specific policy:

- Our Conflicts of Interest Policy is reviewed annually. No material changes were made to this policy in 2023.
- Our Stewardship Conflicts of Interest Policy is reviewed annually by the Governance Committee to ensure it adequately reflects the types of conflicts that may arise. This means we can ensure that they are appropriately managed and as far as possible, mitigated. No material changes were made to this policy in 2023.<sup>32</sup>
- Our Engagement Policy and Sustainability Risks Policy for FHL are reviewed annually by our Governance Committee. The Engagement Policy fulfils our requirements under the Shareholder Rights Directive II (SRDII) to have an engagement policy covering our public equity engagement approach and the Sustainability Risks Policy fulfils our requirements under the EU Sustainable Finance Disclosure Regulations.<sup>33</sup> In 2023, infrastructure and private equity were brought into scope of these policies.
- EOS' Engagement Plan is a key policy for public-markets engagement and covers the next three years. It is updated on an annual basis using a structured horizon scanning exercise which considers extensive feedback from our investment teams and EOS third-party clients, as well as an external scan of industry issues. This ensures that we consider fresh perspectives and continue to identify the key themes which cover our clients' priority areas, ensuring we carry out effective stewardship.
- EOS' Global Voting Guidelines act as a policy which inform EOS' voting recommendations to our investment teams as well to EOS clients who request to receive voting recommendations. The FHL Global Voting Policy and Guidelines, which are aligned with EOS' Global Voting Guidelines, inform the voting decisions made by our investment teams. Our Guidelines are informed by a hierarchy of external and internally developed global and regional best-practice guidelines. This is further supported by public regional voting guidelines, available on our website, which set out our fundamental expectations of the companies our clients invest in. We also have nearly 50 country-level policies. The primary policy-development cycle for EOS voting guidelines is an annual process and runs in conjunction with the policy-review process at ISS<sup>34</sup>, which informs its benchmark research. EOS looks at feedback from clients, evolving best practice in each market, as well as the changes made at ISS in view of resolution-level data for past voting seasons, to consider what additional changes are warranted. Further input is provided by our Engagement Plan, which identifies thematic priorities for engagement. These can often be boosted by enhanced vigilance and potentially escalation through our voting recommendations. EOS completes its major policy changes before the main voting season in each market. Once changes are applied, the policy is monitored to ensure it is having the desired effect and is adjusted further where appropriate. Our Global Voting Policy and Guidelines are approved annually by the Governance Committee. The regional voting guidelines are approved by the Head of Stewardship and regional team leads and noted by the Governance Committee.
- Our approach to controversial activities is reviewed at least annually by the Governance Committee. This standard applies across asset classes.
- Our Design Innovation Standards, which were issued in 2021, and our Responsible Property Management Refurbishment guide also help us embed sustainability principles into development, refurbishment and maintenance. This internal guidance is reviewed at least annually or if there is a relevant major legislation change. It is reviewed by our third-party delivery partners where appropriate.

<sup>32</sup> As HGPE does not hold listed equity of any length of time it is not in scope of the Stewardship Conflicts of Interest Policy.

<sup>33</sup> HGPE are not currently in scope of the FHL Engagement Policy and have a separate Sustainability and ESG Risks Policy which is reviewed by the governing body of HGPE and updated when required.

<sup>34</sup> ISS is a provider of corporate data, analytics and insight. Its services include proxy-voting services. The way we use ISS research is explained further under Principle 12.

## Our approach to assurance

We have several internal and external processes in place to maintain high standards of stewardship.

### Internal processes

The Risk and Compliance departments, together with senior management, continue to augment and embed our firm's compliance framework, which includes:

- Managing any potential conflicts of interest.
- Monitoring of regulatory and client-specific guidelines by using the appropriate systems.
- Ensuring that the risks associated with new products, instruments and markets/locations are adequately considered.
- Staff inductions and regulatory training, including Know Your Customer, Anti-Money Laundering, and Anti-Bribery and Corruption training.

Our internal audit function's primary role is to help the Boards and executive management to protect the assets, reputation and sustainability of the organisation. The Internal Audit team is independent of the day-to-day operations and management of the company and is responsible for providing independent, objective assurance to the Boards through a systematic and disciplined risk-based audit approach and assessment of the internal control framework across our firm. Internal audit reports are published at the conclusion of each audit. The individual reports highlight any control weaknesses noted, along with agreed remediation actions, owners and expected resolution dates. Updates on all reports and the status of open internal audit issues are provided to management and the relevant Boards.

Responsibility matters including ESG integration remain key areas of continued audit focus. Specifically, these were considered in the 2023 Audit Plan through reviews of: ESG Corporate Data Reporting; Global Equities and Impact and Sustainable Equities investment processes; Real Estate Investment Process; and Product Lifecycle.

## Our internal audit function's primary role is to help the Board, its committees and executive management to protect the assets, reputation and sustainability of the organisation.

To maintain the quality of our public-markets engagements, we have established a quality-assurance programme. Day-to-day operations and quality assurance are managed by the EOS & Responsibility leadership team, consisting of the Head of Responsibility; the Head of Stewardship; the Regional Team Leads (North America, Europe and Asia and Emerging Markets); the Head of Policy & Integration; the Head of Client Service & Business Development; the Director of Business Management; and the Sustainability Director.

In relation to engagement quality, each year we plan a series of director-led engagement clinics to confirm that engagement is focused on the right objectives and issues and review the proposed approach to engagement.

Our independent Responsibility Office meets quarterly with each of the investment teams to review portfolios holdings and discuss any existing and/or emerging ESG risks.

Our Real Estate ESG team has a comprehensive monitoring programme to measure, monitor and report on our ESG performance. The progress is published annually in our Real Estate ESG report, available to the public. All data used in Real Estate ESG reporting are verified and assured by a third party in accordance with relevant industry standards.

### External assurance

Prime Advocates Limited, an independent external assurer, undertook a third limited assurance engagement on the information disclosed as part of the sustainability reporting of FHL in the period from June end 2022 to July 2023 (inclusive). The limited assurance engagement related to our stewardship and ESG integration within our public equities, credit, real estate and infrastructure investment portfolios.<sup>35</sup>

The selected subject matter for stewardship & ESG assurance was as follows:

- The scope of FHL stewardship & ESG integration (including EOS engagement) policies and procedures;
- FHL (including EOS engagement) policies and procedures, systems and controls regarding FHL [stewardship and ESG integration] implementation;
- Representations and assertions in FHL reports and financial statements about ESG matters;
- Compliance with regulatory requirements and best practice standards;
- Internal systems, controls and processes for ESG integration; and
- ESG and engagement outputs and reasonable verification.



<sup>35</sup> Private equity were not in scope of the external assurance engagement.

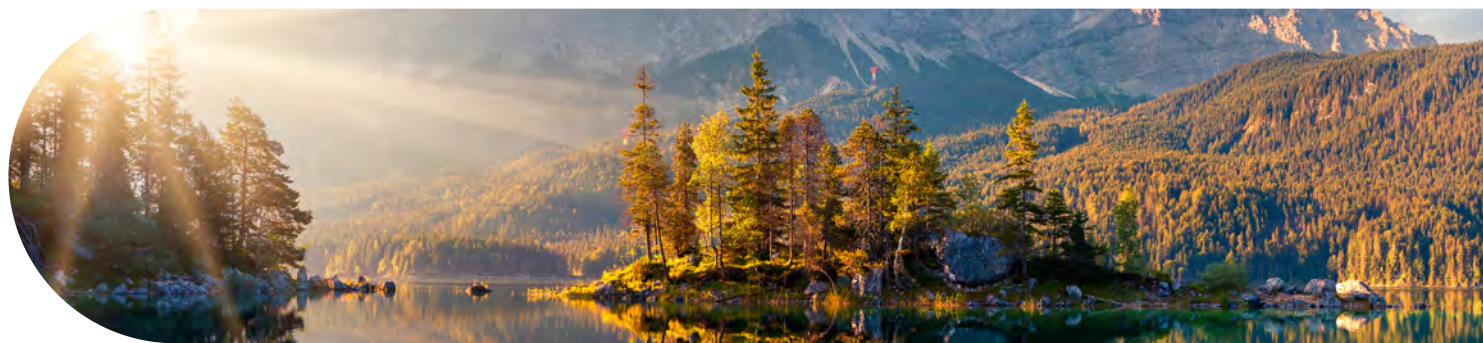


Figure 18. Assurance Summary – stewardship and ESG integration

Overall: Meets/Exceeds ✓ ◆	Scope of conceptual stewardship & ESG application	Processes, procedures and implementation
Equity (listed)	◆	✓ / ◆
Credit (listed)	◆	✓ / ◆
Real Estate	◆	✓ / ◆
Infrastructure	✓ / ◆	✓

✗ Fail ✓ Meet ◆ Exceed  
 Source: Prime Advocates Limited, 2023.

**Conclusion:** The assurer’s report contained the following conclusion: ‘Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that FHL’s [stewardship and ESG integration] within its portfolio investment for public equity, public credit, real estate and infrastructure has not been prepared, in all material respects, in accordance with the identified applicable appropriate criteria. We are satisfied, subject to our limited reasonable assurance, that FHL exceeds regulatory requirements and current best practice for [stewardship and ESG integration].’

The assurer also identified the following areas of attainment and areas for improvement:

**Areas of attainment/ excellence:**

- FHL’s enhanced excellent **holistic, adaptive and material ESG data-driven focused approach to [stewardship and ESG integration]**, pervasively applied and accessible across all investments and strategy types. [All]
- **Expert internal senior ESG expertise** of the Responsibility Office applied across all asset classes to varying degrees, reinforced by **cross-departmental collaboration** via FHL’s Responsibility Working Group. [All]
- FHL’s “sustainable wealth creation” pedigree and leading industry position. **Utilisation of FHL’s market-leading Public Policy/ advocacy teams** allowed for FHL to influence and innovate on ESG themes, progressing the market and assisting their portfolios’ [stewardship and ESG integration]. [All]
- **Effective leverage of the market-leading EOS stewardship engagement service**, adding deep [stewardship and ESG integration] expertise and investee relationship power and knowledge, active management, oversight controls and stewardship/ ESG issue engagement power. [All]

- **Application of EOS’ engagement methodology** and Public Policy expertise for better sustainability engagement for FHL Infrastructure’s long term assets. [Infrastructure]
- FHL attained **best practice** on the collection, management, independent due diligence and disclosure of quantitative ESG data across its investments. Further internalisation of ESG data management, further direct data sourcing and product development commenced for technology gains (with commitment for further automated meter reading systems improvement). [Real Estate]
- FHL outperformed **best practice on the conceptual scoping and practical solution development for [stewardship and ESG integration] of sustainability systems risks and opportunities**. FHL exceeds best practice with the integration of material sustainability investment considerations of key market factors including natural capital, reversing biodiversity loss, deforestation, halting Anti-Microbial Resistance, tax (well-functioning societal health etc.), digital rights and diversity. [All]
- FHL’s progressive work on **climate change (transitional and physical factors) and automated [stewardship and ESG integration] processes** (including data collection, scenario analysis and good standards setting) as developed in house or by collaborative market leadership or developed with experts to enable effective integration methodologies. [All]

**Areas for improvement:**

- Irrespective of FHL’s leading work on measurement and target setting on progressive sustainability areas (see below), such areas lack market data and are estimate dependent. **Continued primary data gathering and quantitative tool innovation is needed for areas pertaining to reduction in Biodiversity loss, Deforestation and non-gender diversity**. We note FHL’s market leading biodiversity and natural capital tools/ approaches coming live outside of this Assurance period. [All]
- **Further transparency and FHL senior periodic (reported) oversight** on the determinants of, and the application of, **engagement “viability” considerations**. [Equity/ Credit]
- Application of a **publicly reported Transparency and Accountability Framework** further to the implementation of the Controversial Activities Policy. [Equity/ Credit]
- **Additional KPI data, integrity checks and verification processes needed where assets are not majority owned or are tenanted**. Continuation of the work commenced on the application of bespoke data capture questionnaires and direct ESG data point collection processes. [Real Estate/ Infrastructure]

## Our Real Estate team have a checklist to ensure the appropriate sustainability due diligence is carried out on all ESG factors when acquiring new assets.

The Real Estate ESG team completes Global Real Estate Sustainability Benchmark (GRESB) reporting to benchmark our real-estate assets against their peers. In the most recent GRESB results, which were issued in 2023 on 2022 data, Wellington Place, NOMA, Hestia, and centre:mk have all achieved a stellar 5-star rating, with NOMA and Wellington Place developments scoring 100/100 performance score. The recognition further exemplifies our commitment to creating community-engaged spaces and our ongoing pursuit achieving net zero. More information on GRESB can be found under Principle 9.

All data is managed and verified by a qualified third party and is submitted to the relevant certification scheme. This data output and analysis is fed back to the internal teams on a quarterly basis through update reports by property managers. We also have a checklist to ensure the appropriate sustainability due diligence is carried out on all ESG factors when acquiring new assets.

In 2021, we also developed internal Design Innovation Standards, which we detail earlier in this section.

Our infrastructure team has encouraged portfolio company participation in the GRESB Infrastructure assessment and complete the assessment on behalf of a selection of their portfolio companies, primarily those which do not have a strategic sustainability framework in place and therefore benefit from participating.

## Fair, balanced and understandable stewardship reporting

As described above, we have internal and external assurance processes in place to ensure the quality of our stewardship. EOS also undertakes a competitor analysis review on a regular basis. In the introduction to this report, we set out the steps we have taken to ensure that our reporting is fair, balanced and understandable, including representing a range of outcomes in our reporting and describing lessons learned. We have sought to proportionately represent the breakdown of asset classes and geographies in the examples and case studies that we use and been clear about any differences in approach.

Relevant business areas have reviewed the content of this report relating to their business area, and the report has been approved by our Board.

## Continuous improvements

We use these assurance processes, reviews and learnings from our investment and stewardship practices to continue to make improvements to our stewardship approach. This ensures we continue to provide best-practice services for our clients.

We made several improvements based on the recommendations of the external assurance provider's last engagement, the results of which we included in our reporting last year. For instance, we obtained new datasets to broaden the ESG integration team's analysis, now perform regular Paris-alignment analysis of the investment teams' portfolios and have a broader, firm-wide project to streamline the consumption of ESG data. We will consider any recommendations of our external assurance provider's third engagement in relation to stewardship and ESG integration during 2024 once their outcomes are made available.

As described under Principle 2, we have made further changes in response to internal and external assurance.

## We have internal and external assurance processes in place to ensure the quality of our stewardship.

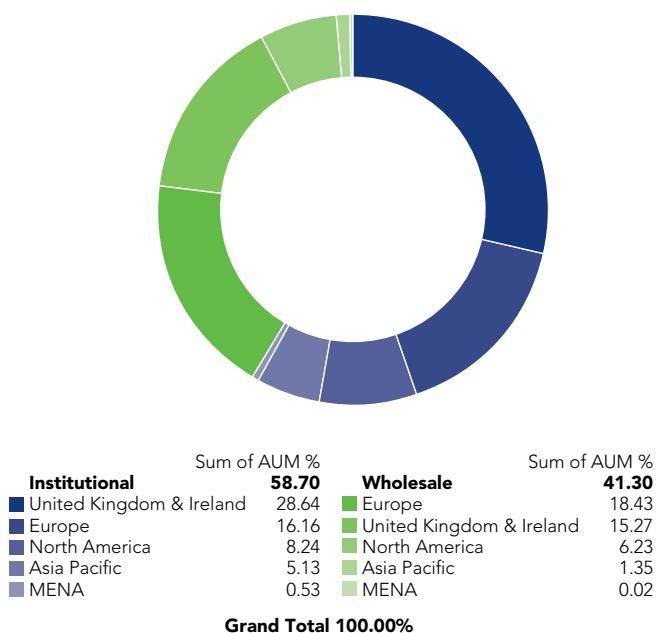


## Principle 6

Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.

### Our client base

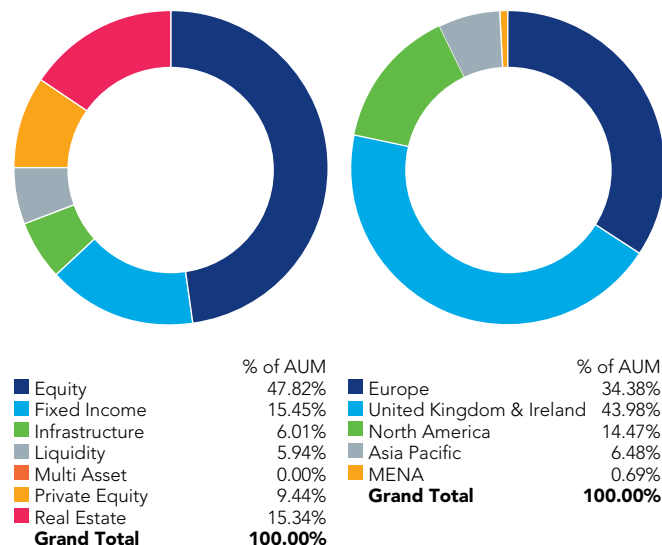
Figure 19. The breakdown of our client base:



Source: FHL, as at 31 December 2023.

### Our assets under management

Figure 20. The breakdown of AUM by asset class and geographies



Please note, due to rounding the Grand Total does not correspond with the sum of the separate figures. 'Liquidity' in the pie chart above includes our money market funds.

Source: FHL, as at 31 December 2023.

### Our investment time horizons

Our approach is to seek opportunities to deliver long term sustainable wealth creation for investors. It is this understanding that informs our belief that we have a duty to consider the longer-term risks and opportunities when investing. This means carrying out extra work when analysing companies to understand externalities, governance practices, environmental impacts, treatment of workforces and the influence of operations on local communities. It also means using our influence to improve the behaviour of those companies in which we have invested, the operations of the assets that we directly manage and advocating for systematic improvements to the financial system in which we participate. Some engagement initiatives will take a number of years to come to fruition.

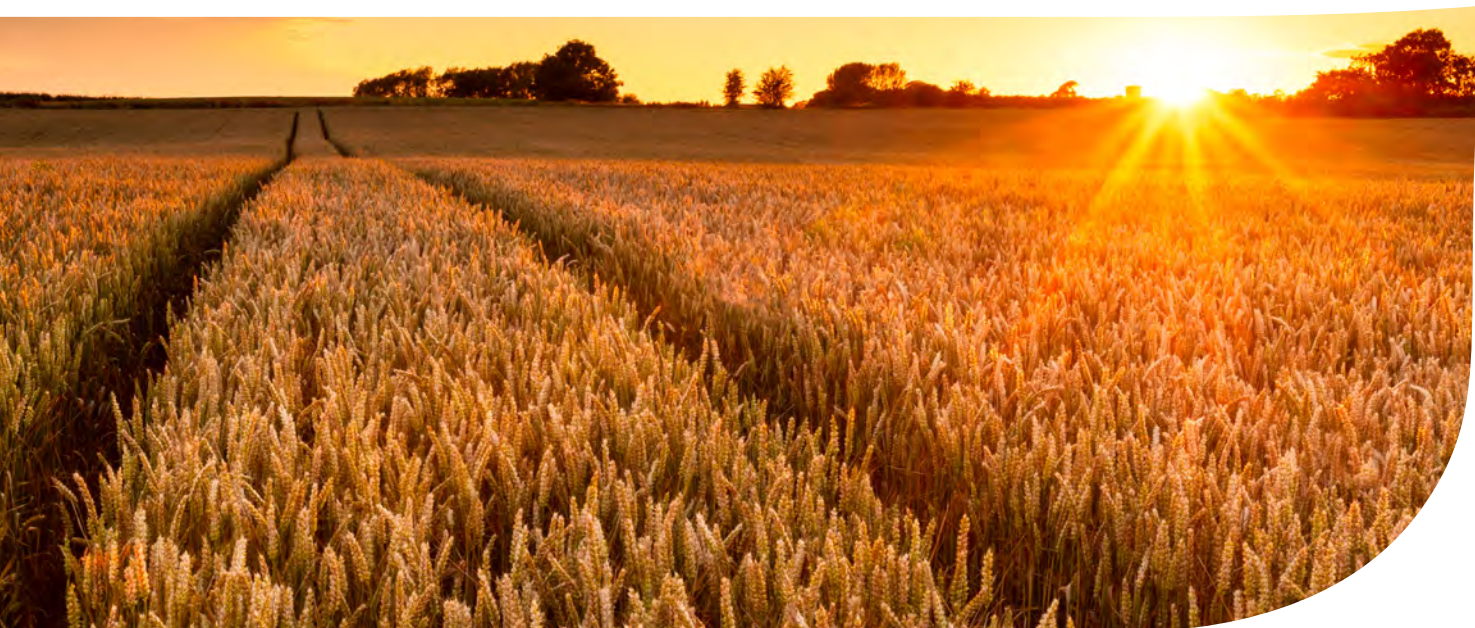
All of our strategies adopt a long-term investment horizon. While this will vary depending on the investment strategy and the markets within which they invest, a typical time horizon adopted by our investment teams is three to five years. This aligns us with our pension-fund clients who typically invest over the long term.

### How we have sought and incorporated our clients' views

We seek client views through a number of fora to ensure we understand how we can continue to best meet their needs. We meet regularly with our clients, in-person and/or virtually, to seek their views and feedback. We held regular webinars for our clients across our strategies to apprise them of market trends, portfolio performance and attribution, as well as our outlook and resulting positioning. Furthermore, we held regular client conferences and seminars, including our ESG Academy.

The majority of our clients have an appointed client team to meet their needs, which consists of Client Directors, Sales managers and Client-Services managers. Several of the teams also involve members of senior management or other parts of the business. These client teams are responsible for developing a deep understanding of their client, their needs, views and approach. The client teams are trained to listen to clients, support them, and develop new ideas in tandem with them.

Through this approach, we have developed a number of commingled funds with existing clients. These funds are a testament to our ability to work closely with our clients, take their views and needs into account and launch strategies that are appealing to like-minded clients.



We established the Federated Hermes Academy, an education hub developed by our experts for our clients and prospective clients seeking to understand responsible investing and how the integration of environmental, social and governance and stewardship can help create long-term wealth sustainably. In 2024, we will launch a new Academy hub, which will host the existing content as well as upcoming content.

As we set out under Principle 1, we use our Customer Outcomes Group (COG) to conduct post-implementation annual reviews on an ongoing basis.<sup>36</sup> This is to confirm that all products continue to meet a customer need, perform in line with their stated objectives and have continued commercial viability. Client feedback may be obtained by a third-party market-research agency or directly through the sales and client teams, and this feedback will be considered as part of the review.

We continue to receive positive feedback from our clients on the service we provide, our thought leadership and the way in which we manage their assets. This is a strong indication that our clients feel that their views are being heard and that we are providing a service that meets their needs.

### Finding the right fit

We offer a range of strategies across asset classes, each with their own investment style and stewardship approach, so that clients are able to invest in products that meet their needs. All of our products are high active share, integrate ESG considerations and engagement insights in investment decision making and deploy best practice stewardship. The stewardship approach will be informed and aligned to our firm-wide policy, as articulated in various policy documents (see Principle 5).

While each investment team is responsible for the investment and stewardship decisions within the strategies that they manage, we are in regular dialogue with our clients for their views and inputs on certain topics or issues. This ensures that the client is front and centre of every decision that we make.

Our investment offering is structured on three strategic pillars of Active ESG, Sustainable and Impact. Each product managed is mapped to the EU SFDR classifications where applicable and aligned with one of these investment categories to outline the level of ESG integration adopted by that particular strategy and ensures complete transparency with our clients.

Our Active ESG products offer best-practice integration of ESG analysis and engagement insights, with the objective of delivering long-term outperformance.

Our Sustainable products offer thematic exposure to companies we consider to be leaders in offering environmental or social products and services or mitigating their environmental impact. These portfolios also have a clear set of exclusions to ensure that potentially harmful activities cannot be invested in and an additional objective to deliver a reduced environmental footprint vs. their benchmarks.

Our Impact products seek to deliver real-world measurable positive change either through investment in companies that provide products and services which help to solve the world's environmental or social challenges or through companies that, with effective investor engagement, can make a greater material positive contribution to the world.

While these approaches differ and may appeal to different client types, each is underpinned by our best-practice integration of ESG analysis and engagement insights and the delivery of sustainable outcomes through effective stewardship.

**We offer a range of strategies across asset classes, each with their own investment style and stewardship approach, so that clients are able to invest in products that meet their needs.**

<sup>36</sup> HGPE is not within the remit of the COG. For our infrastructure and private equity products, these processes are therefore managed separately within HGPE.

The EOS Engagement Plan was developed to provide clients with a clear articulation of the approach to engagement being carried out acting as a statement of our stewardship priorities and objectives on our clients' behalf. Under Principle 9, we identify our 12 key themes and 36 related sub-themes for the next three years. We find this breadth of coverage is necessary to reflect the diversity of the issues affecting companies in our global engagement programme. The Engagement Plan is developed utilising the engagement team's specialist expertise and is informed by input from EOS' third-party clients and our investment teams. This ensures that the themes represent client priorities and those of their underlying beneficiaries. Through the EOS annual survey, we have seen that a consistent majority of clients say that engaging for impact and outcomes is a priority.

To ensure that we continue to manage our assets in line with the approach we market to prospects and agree with clients, our Compliance department monitors fund guidelines, IMA and prospectus rules which include fund objectives and constraints, through order management and trading system (OMS) ThinkFolio. All active portfolios undergo pre- and post-trade compliance. Pre- and post-trade portfolio parameters, counterparty limits and other guidelines are coded (where possible) into ThinkFolio before the fund go-live and any limits which are not codable are covered by manual monitoring. A member of the Compliance department undertakes the guideline coding, while another member conducts a second review before rules activation. Portfolio manager and client team sign-off is also conducted prior to the fund go-live to ensure all rules are correctly captured, interpreted, frequency of manual monitoring and usage of data. The ThinkFolio rules are also coded to prevent any trade in a prohibited counterparty, sanctioned entities or jurisdictions at pre-trade stage.

The Compliance team also runs a daily post-trade breach report in ThinkFolio, which shows when investment guideline limits have been exceeded. This is irrespective of whether the breach has occurred as a result of passive market movements, cash inflow/outflow or a corporate action.

The Investment Office monitors adherence to internal risk guidelines and provides an early warning of potential breaches. If any internal risk guidelines are breached, the situation will immediately be flagged to the appropriate investment team and the portfolio manager will usually adjust their position. However, in cases where investment teams believe it is more appropriate to continue with an outlying position or challenge the internal risk guideline, the situation will be escalated for discussion at the Portfolio Review Committee (PRC) to agree a resolution.

**The EOS Engagement Plan was developed to provide clients with a clear articulation of the approach to engagement being carried out, acting as a statement of our stewardship priorities and objectives on our clients' behalf.**

### Communicating with our clients

We are committed to being open and transparent. As noted earlier, the [Federated Hermes Pledge](#) underpins our firm-wide commitment to always put clients first and to act responsibly.

Reporting is critical to demonstrate our activity on our clients' behalf. We therefore continue to build out our suite of high-quality, activity-based, qualitative and quantitative communications to support internal and external stakeholder communications.

We publish our annual [Climate Related Financial Disclosures \(TCFD\) report](#), where we lay out our approach to identifying and managing climate-related risks and seizing opportunities as a business. These include how we are involved at the policy level in developing climate-related initiatives and how we ensure that everyone in the business factors the weight of the climate emergency into the work that they do. In our [latest publication](#), we enhanced our climate scenario analysis and also included reporting on nature in line with the Taskforce on Nature-related Financial Disclosures (TNFD).

We regularly [publish](#) detailed case studies and periodic reports that cover a range of asset classes, alongside thought pieces, blogs and podcasts on topical and emerging ESG issues. We also make [publicly available](#) a quarterly EOS engagement and voting recommendations report covering thematic ESG topics and EOS' annual report, which includes statistics, case studies and public-policy information.





Following the launch of the upgraded company website in 2022, further developments and additions continued to be made throughout 2023 to enhance client experience and support evolving regulatory and reporting requirements. We established the Federated Hermes Academy, an education hub developed by our experts for our clients and prospective clients seeking to understand responsible investing and how the integration of environmental, social and governance and stewardship can help create long-term wealth sustainably. In 2024, we will launch a new Academy hub, which will host the existing content as well as upcoming content. The new areas we will focus on are Biodiversity, Engagement, Sustainable Credit and Regulations.

ESG analysis and engagement insights, where material, are integrated into all of our investment decisions across each of our strategies. We continue to improve our reporting on ESG so that our clients can fully understand our approach to responsible investment and plan to roll out further enhancements on ESG reporting as tools and technologies evolve. For our equity funds, we aim to provide clients with carbon performance and high-level engagement and voting information relevant to the portfolio on at least a quarterly basis. Our ambition to roll out equivalent reporting on carbon performance and engagement to our public fixed income reporting remains a priority. We also continue to report on our water and waste performance for our Global Sustainable Equity Strategy with an objective to outperform the benchmark on these factors. We provide detailed quarterly and half-year reporting on both ESG and engagement information to the clients of our SDG Engagement and Impact funds.

Our real estate team publishes an annual ESG report, which publicly discloses environmental and social outcomes for our real estate funds. We have also published several reports to measure the social and economic outcomes of our real estate placemaking initiatives.

Our infrastructure team have issued an annual Sustainability and Stewardship Report for clients since 2019 and issued their first public report in 2022. The annual reports provide an overview of their sustainability and stewardship approach and activities over the year. The client-facing annual report provides detailed data-driven analysis of sustainability performance at portfolio and individual investee company level. Summaries of material ESG matters at individual companies as well as performance against engagement objectives are included in the quarterly investor reports.

**Our real estate team publishes an annual ESG report, which publicly discloses environmental and social outcomes for our real estate funds. We have also published several reports to measure the social and economic outcomes of our real estate placemaking initiatives.**

Our private equity team also issued their second, enhanced ESG reports for some of our latest funds with the aid of a third-party provider in 2023.

Typically, we offer clients annual meetings where the client director and portfolio manager review the portfolio and provide insight into ESG activities undertaken. However, we aim to meet the needs of each client and can be available to meet at more frequent intervals or via conference calls as required. We hold regular webinars for our clients across our strategies to apprise them of market trends, portfolio performance and attribution, as well as our outlook and resulting positioning. Furthermore, we held regular client conferences and seminars including our Academy.



## Principle 7

Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.

At FHL, we believe responsible investment requires integration of material E, S and G factors in the investment process alongside material traditional performance factors and active ownership of assets through stewardship.

Holding this focus across all of our strategies, while also behaving responsibly as a firm, is integral to delivering sustainable wealth creation.

**Figure 21.** Creating wealth sustainably



Source: FHL, as at 31 January 2024.

We do not see the integration of ESG factors and engagement insights within investment decisions as a separate category of investing. Instead, we believe material ESG risks and opportunities should inform all investment decisions. That is why we integrate ESG considerations and engagement insights into our investment processes in all of our products, across all asset classes. As our research has demonstrated, investors do not need to sacrifice returns to invest responsibly. On the contrary, our research shows that companies with good environmental, social and governance performance indicators tend to outperform others over the medium and long term<sup>37</sup>. In the credit space, our research on ESG risk in CDS spreads and sovereign credit further evidence the importance of ESG

in investment decisions.<sup>38</sup> For this reason, we aim to ensure that investors' capital is deployed to create wealth sustainably, delivering sustainable growth and helping to build a better society and planet for all – dual perspectives that we believe should not be separated, but considered as one.

We believe there are four mutually reinforcing strands of being a responsible investment manager: ESG-integrated investments; active ownership and management; advocating in beneficiaries' interest; and behaving as a responsible business. Together, these aim to generate sustainable wealth creation for the end beneficiary investors, encompassing investment returns and their social and environmental impact.

Figure 22. Our strategy



Source: FHL, as at 31 January 2024.

## Prioritising issues for assessment of investments

Taking an active approach is a central part of our investment proposition. As a result, our portfolio managers are able to take a selective approach by only investing in companies with the necessary characteristics, in the team's opinion, to be sustainably successful over the long term. This approach stems from our values and investment beliefs, which we described earlier under Principle 1. We consider all material investment factors, including those relating to material ESG issues and insights from engagement.

While the most pressing material risks are those that will crystallise in the short term, we are long-term investors that strive to deliver sustainable wealth creation for our end investors. This means that our definition of materiality is necessarily wider. We believe that a wider range of risks will ultimately become material over a longer timeframe and that we need to engage proactively to mitigate them.

The key medium- to long-term risks – many of which may also present threats over shorter timescales – that we factor into our investment analysis and engagements include climate change, natural resource scarcity, pollution, human rights, human capital and labour rights, conduct, culture and ethics, corporate governance and strategy, risk and communications. More detail about how we engage on these issues and the outcomes we seek is available under Principle 9.

An ESG issue will rarely be the sole or standalone driver behind any investment decision. Instead, material ESG factors are integrated into fundamental analysis and inform the teams' investment decision making. The impact on the investment decision will vary depending on the mandate of the fund. For a fund that integrates ESG but is not a thematic fund, the presence of ESG risk does not necessarily preclude investment, but rather helps investment teams reach a more holistic view of the risk profile of a company and the actions needed post-investment to mitigate risk.

<sup>37</sup> FHL, 'Despite headwinds, ESG continues to perform', (July 2022).

<sup>38</sup> FHL, 'Pricing ESG risk in credit markets: reinforcing our conviction', (December 2019); FHL, 'Pricing ESG risk in sovereign credit', (March 2020).

Investment teams may also identify opportunities in companies that are improving their ESG practices, particularly given our strong engagement capabilities. For our funds with a thematic focus and/or our impact funds, the existence of ESG risks and opportunities and the prospect of creating or increasing positive outcomes will be significant where it is one of the main drivers of investment decisions.

Research and analysis by all of our investment teams includes an evaluation of performance on strategy, financials, material risk and ESG factors, and the interplay between these elements. Insights from engagement with company management, boards, subject specialists and other shareholders and stakeholders – including the extent of engagement progress – is also a key input into this process and investment decisions at a portfolio and individual asset level. Such engagement is carried out in a co-ordinated manner both by our investment teams and by EOS to maximise the impact of our engagement. These factors influence decisions to invest and are also actively monitored after investment, with the potential to influence decisions to sell an asset or increase the size of our investment. Where concerns arise in relation to one of our existing investments, engagement is often a means to both raise concerns with the company and, where effective, reduce the investment risk and enhance the opportunity from the investment.

The ESG Integration team within the Responsibility Office also works very closely with the investment teams to help identify material ESG issues that are specific to the investment manager’s strategy. The ESG Integration team organises sector-level knowledge-share sessions between EOS and the investment teams and also works with the investment teams to develop frameworks which assess the materiality of ESG risks at the company level. Finally, the ESG Integration team obtains data from third-party providers, which is overlaid in our proprietary tools by insights gleaned from our engagement with the company and is also used by analysts and engagers in their company research and portfolio analysis.

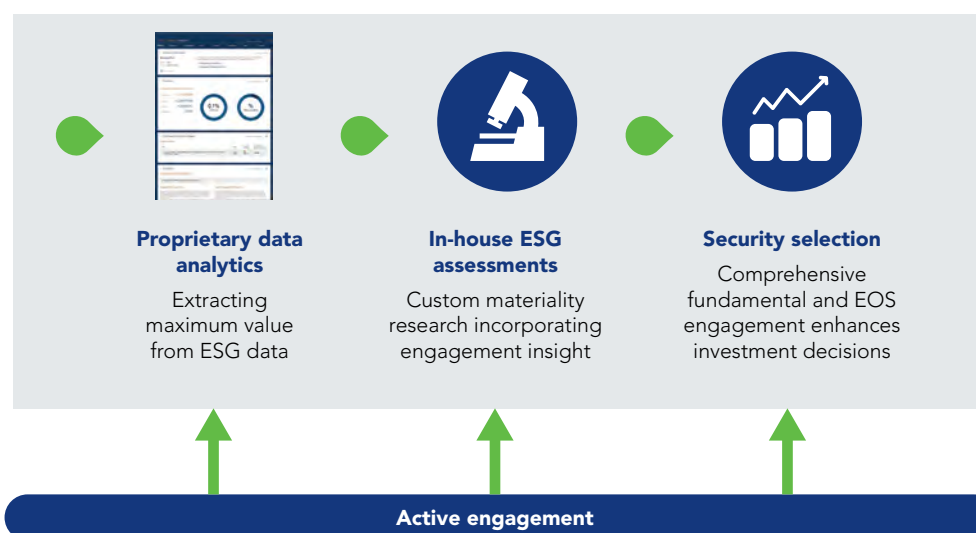


We encourage our fund managers to use their own expert judgement when considering ESG issues, just as they would with other fundamental investment factors – for example, the strength of a company’s structural competitive position or the quality and depth of management.

Climate change continued to be a key priority across our investment teams in 2023, demonstrated by the work of our CNWG. To enhance our work in this area, we have explored scenario analysis in 2023, in partnership with Planetrics. Biodiversity also remained a firm focus during 2023; we continued to assess our exposure to deforestation risk across a range of asset classes in line with our commitment and began to assess our exposure to nature-related risks and opportunities. More detailed explanations of our work on climate-change risk and opportunities, biodiversity and social issues are available under Principle 4.

### How we integrate stewardship and investment across our products

Figure 23. ESG and engagement integration: leveraging market leading engagement capability to enhance investment performance



Source: FHL, as at 31 January 2024.

**A tailored approach with centralised support:** All our investment activity is supported by our dedicated Investment Office and Responsibility Office, both of which report directly to our CEO. Regular meetings are held between the two offices and with the investment teams to ensure proper coordination and integration of ESG factors and engagement insights. However, it is the responsibility of our investment teams to effectively integrate ESG and engagement information into their investment processes and ultimately our fund managers have discretion on investment decisions. This ensures that ESG factors are fully integrated into investment analysis and decision making.

**Developing a holistic view:** Research and analysis by all of our investment teams includes an evaluation of performance on strategy, financials, risk and material ESG factors (including from a range of proprietary ESG and engagement tools), and the overlaps between these elements. Insights from engagement with company management, boards, subject specialists and other shareholders and stakeholders – including the extent of engagement progress – is a key input into this process and investment strategy. Such engagement is carried out both by our investment teams and by EOS on their behalf. These factors influence decisions to invest and are also actively monitored after investment, with the potential to influence decisions to increase/decrease our exposure to the asset as well as sell an asset. Where concerns arise in relation to one of our existing investments, engagement is often a means to both raise concerns with the company and seek to reduce the risk.

**Stewardship integration:** Our experience suggests that a systematic engagement approach, combined with tried and tested methods of escalation such as collaboration or shareholder meeting interventions, is needed to accelerate change at companies, such as those failing to prepare for the low-carbon transition. Driving change through engagement is one side of the coin – effective integration of stewardship insights is the other.

The principal objective of stewardship is to maintain or enhance the value of an asset. The beneficial outcomes sought through engagement include those of a governance, strategic, environmental or social nature.

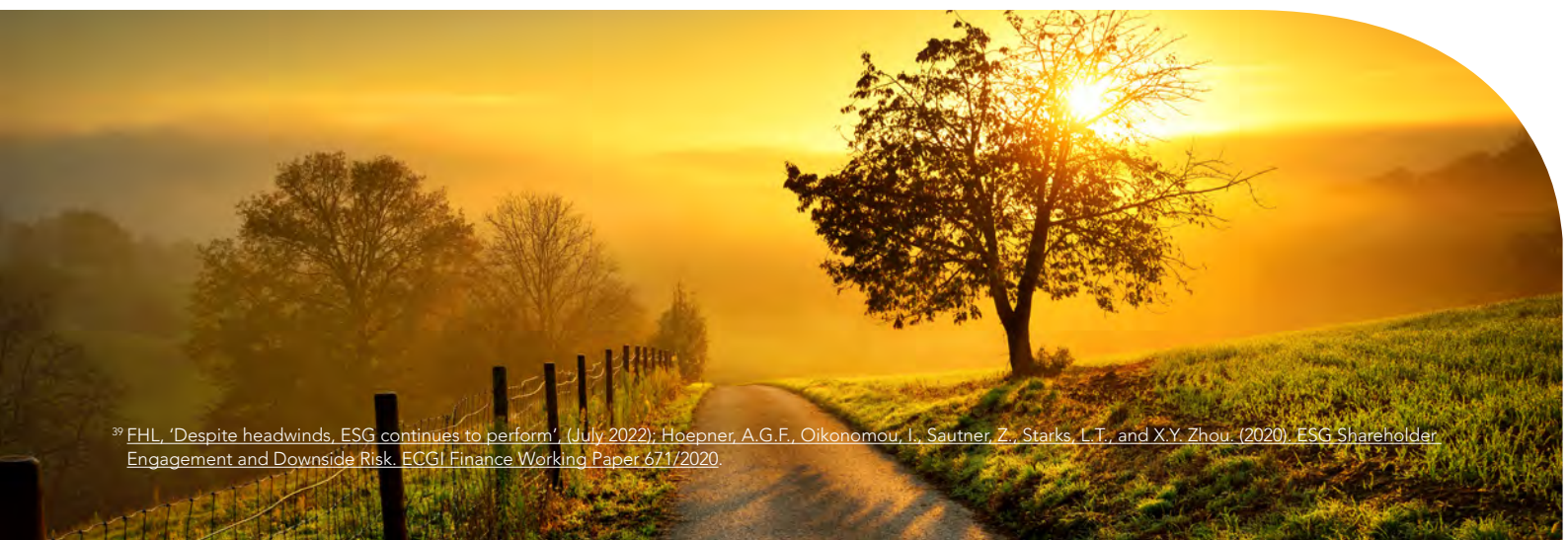
In addition, we believe that investors that integrate ESG should not rely on data alone, as it is often backward looking and updated infrequently. As such, active ownership is an

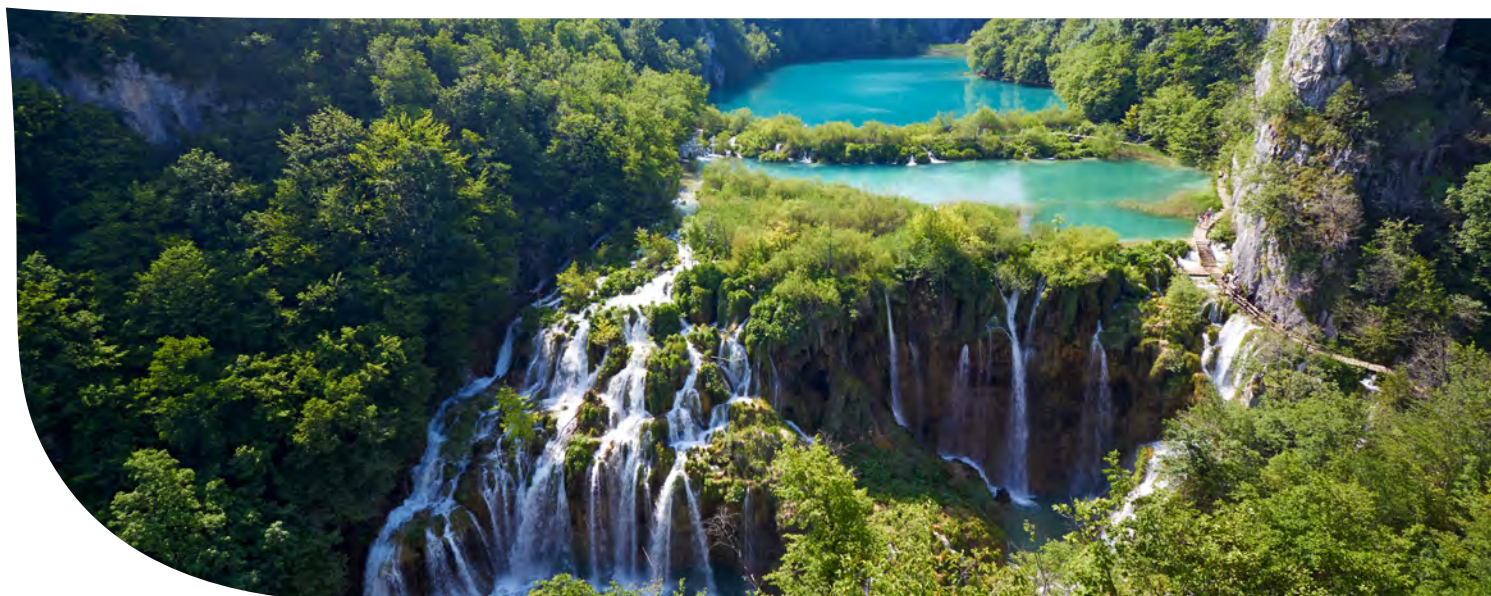
important pillar of our investment approach. Engagements can deliver useful investment insights (although engagers and analysts must always seek to avoid acquiring any inside information). The voting recommendations and engagement activities of our stewardship team can promote positive change within companies, unlocking hidden value and also providing a forward-looking view of ESG and broader performance that can lead to opportunities.

The investment teams assess and continue to monitor strategy, financials, risk, material ESG factors and the overlaps between these elements throughout the life of the holding. The monitoring of strategy, financial and non-financial performance and risk and capital structure is done through carrying out a financial analysis of company reports, attending analyst meetings and investor presentations, using media sources and third-party research and attending engagement meetings. Each investment team is responsible for looking at the financial performance, risk and capital structure of investee companies. All teams also have access to ESG data and proprietary tools, including engagement information. When a concern is identified, this will inform engagement and investment decisions.

The information we gather through stewardship enables us to develop a more comprehensive view of both the risk and opportunities a company is exposed to and to factor this into valuations and investment decisions. Such assessments are not a one-off but rather form an ongoing feedback loop. Monitoring this information informs our engagements, while engagement insights inform our investment decisions. Our fundamental research benefits from our ongoing dialogue with investees, as well as that between our public-markets investment teams and stewardship arm. We invest time and resources to encourage companies to strengthen their governance, give our views on strategy and encourage companies to take a long-term view, particularly on sustainability issues. The insights we glean from these interactions help us to better understand a company's complex strategic challenges – something that ultimately helps us serve our clients. Our latest research has confirmed the importance of environmental metrics as a performance indicator, as poorly ranked companies tend to significantly underperform over the long term.<sup>39</sup> This reinforces our aim to generate sustainable wealth creation for the end beneficiary investor, encompassing both investment returns and their social and environmental impact.

<sup>39</sup> FHL, 'Despite headwinds, ESG continues to perform', (July 2022); Hoepner, A.G.F., Oikonomou, I., Sautner, Z., Starks, L.T., and X.Y. Zhou. (2020). ESG Shareholder Engagement and Downside Risk. ECGI Finance Working Paper 671/2020.





We also consider the environment that an asset is operating in when assessing risks, including ESG risks. For example, because emerging markets are not as transparent as developed markets, the risks are higher. As a result, our Global Emerging Markets team recognises that investors need to be more prudent and seek a margin of safety – something that can be secured by integrating ESG factors. Similarly, for our Asia ex-Japan fund, assessments of corporate governance factors are particularly important when considering potential investments in countries such as China and South Korea. The team has a varied and lengthy list of warning signs that they consider and seek to visit and/or speak directly to management prior to investing in a stock.

Given the integrated approach of all of our investment teams, information gathered through stewardship directly informs our investment decisions (alongside other factors such as more traditional financial analysis).

The nature of engagement, as described here and in Principle 9, varies between asset classes. Engagement is also influenced by sector and geography and each investment team tailors its own ESG and engagement integration approach to suit their investment philosophy (see Principle 6 for a breakdown of our asset classes). ESG factors and engagement insights can be a component of a screen, a source of ideas, an input into fundamental analysis or an adjustment to valuation drivers and/or a portfolio construction factor. But common across all of our funds is a set of shared investment beliefs, as set out in Principle 1, which influences every aspect of the investment process. ESG factors and engagement insights are integrated into investment decision making, whether it is deciding to avoid, buy, hold or exit a position.

The Responsibility Office oversees and supports all of the below ESG and stewardship integration activities. This is achieved through a number of different activities, such as coordinating knowledge-share sessions between teams (including EOS), working with the investment teams to develop frameworks to assess different ESG risks and coordinating conversations with EOS to ensure there is good engagement across the strategies. The investment teams also meet formally with the Responsibility Office at least every quarter to discuss their ESG and engagement integration activities.

## Public markets

For public markets, our firm's proprietary ESG tools are of particular note:

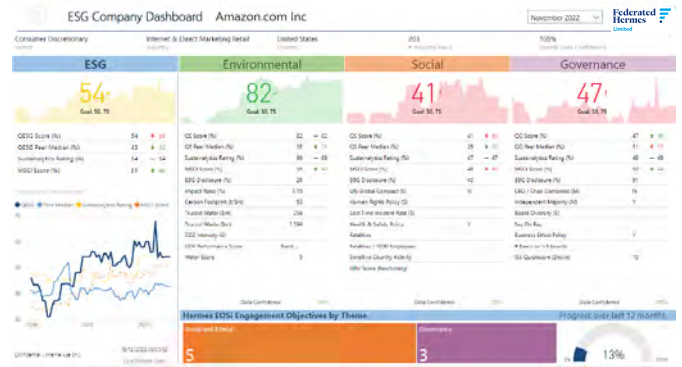
- Our **Carbon Tool** enables fund managers and engagers to identify carbon risks in portfolios and companies that currently exist or may develop in the future. Importantly, the tool incorporates our stewardship activity and intelligence and is able to identify companies that are priorities for engagement and their progress against environmental objectives.
- Our **Environmental Tool** assesses both portfolios and companies on their carbon, water and waste performance. It also looks to quantify the environmental cost of the impact via the following six lenses; carbon, water, waste, air pollutants, land/water pollutants and natural resource use. In addition, we assess our portfolios and companies alongside exposures to carbon intensive sectors, namely: fossil fuels, mining and thermal coal. This tool also incorporates our stewardship activities with a focus on environmental engagement at both portfolio level and company level.
- Our **Corporate Governance Tool** provides a breakdown of corporate governance characteristics, such as information on board independence, diversity and audit tenure. This tool compares the governance of companies to the expectations we have set and flags any companies that do not meet the expected standard.
- Our **ESG Dashboard** includes our proprietary Quantitative ESG (QESG) Score and identifies stocks with positive ESG characteristics and/or stocks demonstrating positive ESG change. The QESG score captures how a company manages its ESG risks. The dashboard includes a snapshot of what themes that company has been engaged on along with progress made.
- The **Portfolio Snapshot** allows us to examine ESG ratings and controversies and identifies contingent risks. Our portfolio managers use this tool to evaluate a strategy's ESG performance over time. It also provides insights into engagement and the progress made, and our voting choices relative to the benchmark.

Figure 24. Carbon Footprint – Portfolio Dashboard



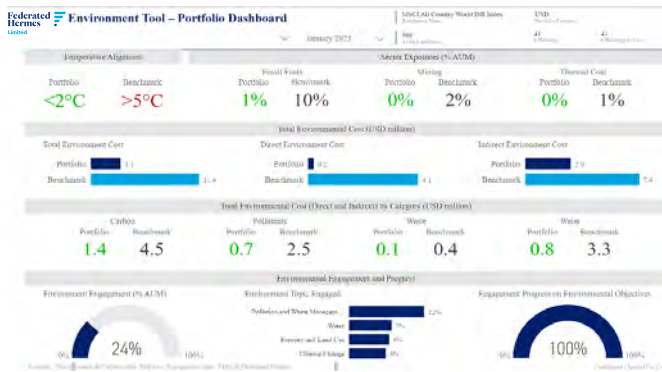
Source: FHL, as at 31 January 2024. For illustrative purposes only.

Figure 27. ESG Dashboard



Source: FHL, as at 31 January 2024. For illustrative purposes only.

Figure 25. Environmental Tool – Portfolio Dashboards



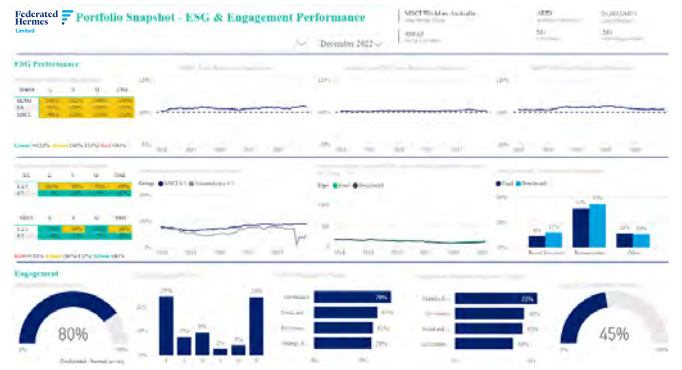
Source: FHL, as at 31 January 2024. For illustrative purposes only.

Figure 26. Corporate Governance – Company Dashboard



Source: FHL, as at 31 January 2024. For illustrative purposes only.

Figure 28. Portfolio Snapshot – ESG and Engagement Performance



Source: FHL, as at 31 January 2024. For illustrative purposes only.

Through these tools, along with additional EOS engagement information, the public equities and fixed income teams have access to third-party ESG data, as well as insights on engagement carried out by EOS with investee companies and the broader investable universe. These sources are a valuable input to the investment process, as well as to the ongoing monitoring of and engagement with companies.

We believe that ESG-aware investors should not rely on ESG data alone. The information provided by companies may not be comparable with peers. In addition, it is often backward looking, updated infrequently and with a time lag. As such, engagement activities and voting information can be used by our teams to provide a forward-looking view of ESG characteristics and the broader performance of a company. As well as accessing EOS' engagement portal – which includes the engagement history and progress against live objectives – portfolio managers can, and are encouraged to, attend engagement meetings with the engagers. The benefit of these joint meetings is substantial and results in more robust engagement that focuses on the relevant and material ESG risks and opportunities. Our investment teams also regularly discuss salient ESG issues with company management directly.

Our investment teams regularly interact with the relevant sector or regional lead within EOS to better understand the ESG issues within their investment universe, and also discuss specific companies with the relevant engager. Such interactions can help the portfolio manager discern whether a



particular ESG issue is material or not, something which cannot always be gleaned from raw ESG research data. Therefore, we believe that to implement a credible and successful ESG integration approach it is of utmost importance that engagement information is part of the ESG information universe.

Because our EOS engagement team engages globally in respect of both our internal holdings<sup>40</sup> and the holdings of EOS' third-party clients, its coverage extends beyond our own holdings. This coverage allows our analysts to benefit from these engagement insights when looking at prospects, as well as in relation to ex-post monitoring.

While there are principles that govern our ESG and stewardship integration across our investment teams, we believe in developing processes that are relevant to the investment strategy. Therefore, the method of this integration can vary by investment team. Below is an outline of our public credit team's approach.

### Public Credit

The public credit team believes there is a direct link between ESG risk and credit risk and sees no separation between ESG-integrated investing and more traditional investing based purely on financial metrics. Their approach not only relies on inputs from various external data providers, but also builds on the extensive experience of our EOS engagement platform and the bottom-up work of individual analysts. The methodology aims to capture the positive movement in a company's ESG characteristics and not rest on annual data inputs. The insight gained from engaging with companies is an important ongoing additional input into the fund managers' investment considerations as a strong focus is placed on driving positive change within investee companies. The team believes that there is an opportunity to add alpha by investing in companies that may score poorly in ESG characteristics as measured by the traditional data providers

but show an earnest desire to improve those ESG behaviours. This can be achieved by investing and engaging with the company prior to its ESG risk reduction being priced into market consensus.

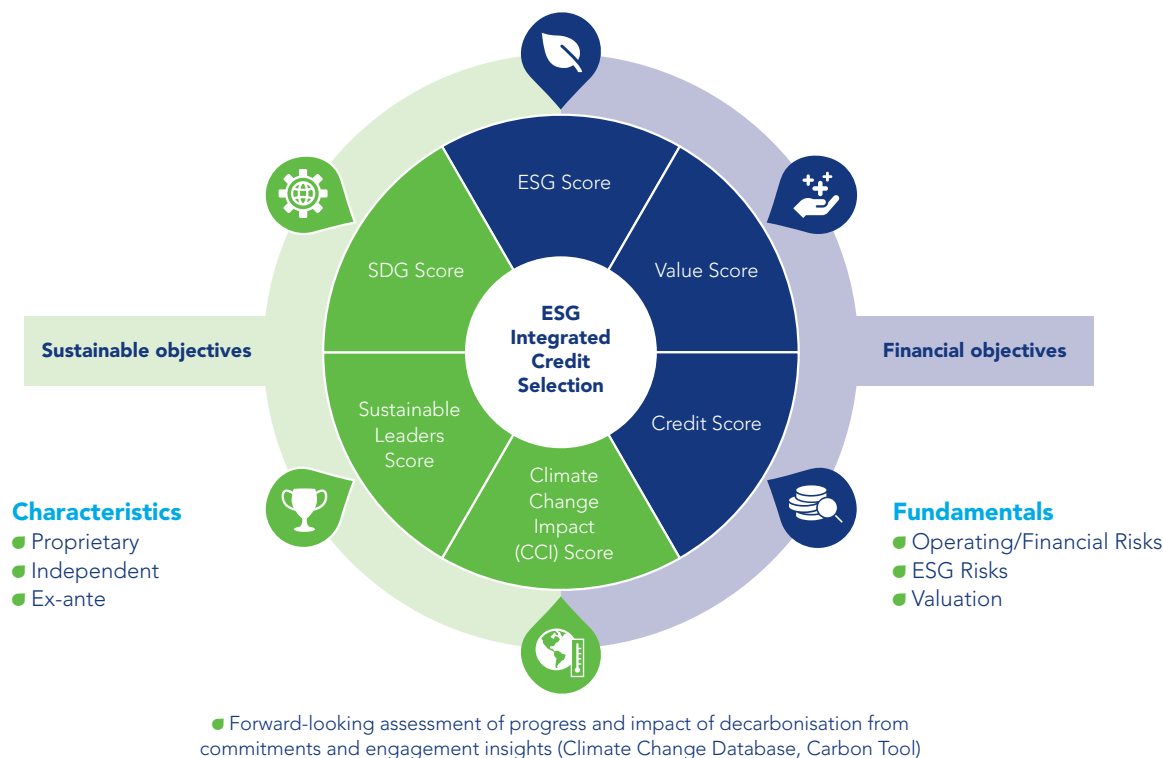
The team's holistic approach to ESG integration considers ESG factors within all stages of the investment process, from initial universe screening through to stewardship and advocacy. The process begins when screening global credit markets to create the core investible universe (the universe from which portfolio managers can select securities). They are able to 'screen in' securities on which we have high conviction from a sustainability perspective (as indicated by their proprietary sustainability scores) but which are not already captured by other criteria. This means they are able to include securities that would not necessarily screen highly if considered from the purely financial angle of the investment process. In addition to this, the team operates a minimum ESG threshold for investment. Using the proprietary and forward-looking ESG scoring system (detailed below), the lowest scoring issuers from an ESG perspective are excluded from portfolios.

For investment solutions governed by a sustainable investment objective alongside a financial investment objective, the sustainability analysts take the lead in the development and maintenance of sustainable investment processes and proprietary sustainability scores. For the purposes of these solutions, the sustainability scores allow us to screen the investible universe to ensure the portfolio is constructed in a way that feeds into the sustainable objective of the strategy.

**We believe that to implement a credible and successful ESG integration approach it is of utmost importance that engagement information is part of the ESG information universe.**

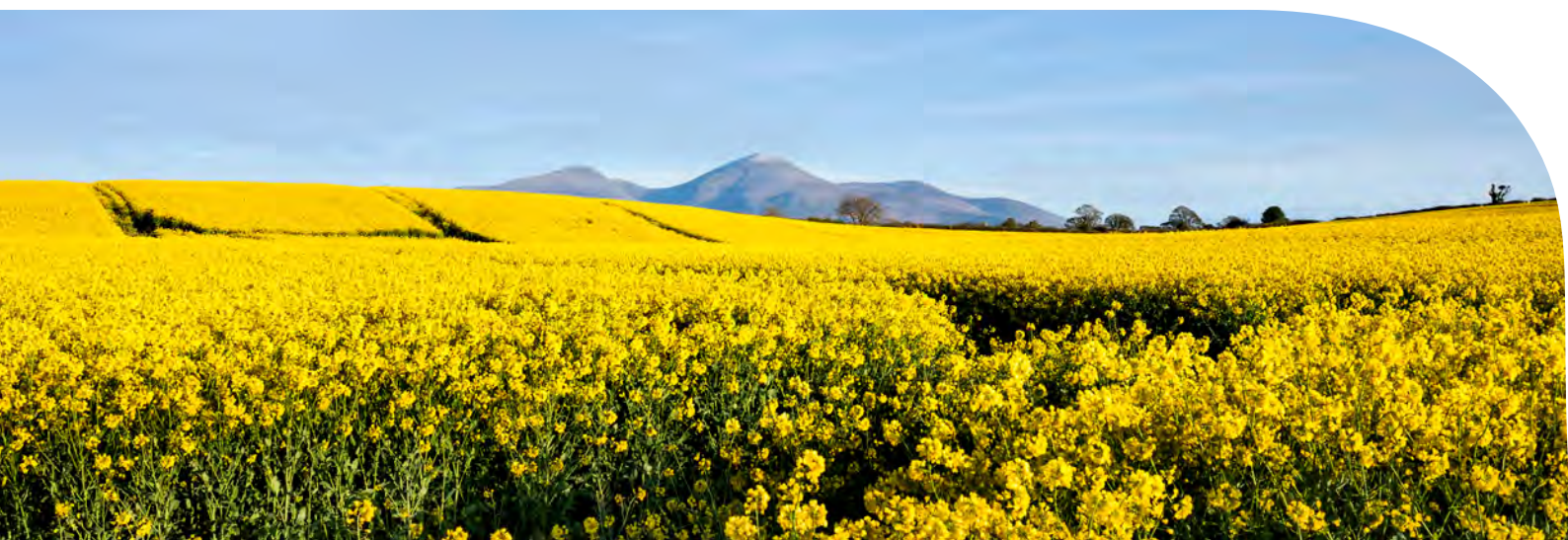
<sup>40</sup> Throughout this report, references to FHL holdings relate to the holdings that we manage on behalf of clients.

Figure 29. The team's suite of proprietary ESG and sustainability scores



Note: The QESG score is a quantitative assessment of a company's ESG metrics compared to its peers and how its ESG profile is changing.  
Source: FHL, as at 31 December 2023.

- **ESG score** (from one to five) – assesses the potential forward-looking impact of non-fundamental factors on a company's enterprise value. The scores are assigned by credit analysts as part of their bottom-up assessment of each issuer, alongside more traditional financial scores of credit and value. Within their assessment, the analysts will consider the FHL QESG score, as well as the sustainability scores assigned by the engagers, which are considered in the ESG score for each issuer.
- **Sustainable Development Goals (SDG) Score** (from one to five) – determines the ex-ante potential for a company to effect positive change on society and environment. SDG scores assess a company's willingness and ability to manage its operating process and/or the products it produces in a purposeful way for the benefit of society and/or the environment.
- **Climate Change Impact (CCI) Score** (from one to five) – assesses the climate change credentials of a company along two dimensions: 1) how credible is the company's process and progress in decarbonisation compared to its own goals – if any – and compared to its sector peers (i.e. scope and ambition of decarbonisation plans; near-term and mid-term goals innovation; capital expenditure; reporting) and 2) the impact of decarbonisation on the company and on the wider economy (i.e. materiality; time frame; avoided emissions; value change contribution).
- **Sustainable Leaders (SL) Scores** (from one to five) – a sector-weighted, ordinal assessment of the sustainability leadership of companies, derived from the sector-weighted average combination of our proprietary scores overlaid by views from credit analysts and engagers.







The credit research analysts and engagers discuss the ESG and sustainability scores in detail at the credit committee when evaluating credit selection. Engagers work closely with the credit research analysts throughout the process and take ownership of evaluating each issuer for the sustainability scores.

If a company advances through the initial screening, then it is included in the investment universe. These scores are reviewed on a regular basis to ensure any updates are taken into consideration.

Once in the universe, the credit research analysts will assess various factors to understand how much the company's behaviours jeopardise or enhance its enterprise value. The criteria do not differ across jurisdictions or sectors; however, the team recognises that certain sectors are more vulnerable to ESG behaviours which can lead to sudden degradation in firm value. To that end – while the team looks at the relative standing of a company within its sector for each of the three components of ESG – for each sector they might emphasise one ESG factor more than others. The main criterion for the governance category is the earnestness with which a company seeks to improve all of its behaviours and their responsiveness to the team's engagement. The analyst assesses management's desire and ability to build a sustainable business that will support and perpetuate firm value.

Once issuers have gone through our screening and bottom-up research process, they are available for selection by portfolio managers across our range of credit funds. Our suite of ESG and sustainability scores have a direct effect on the sizing and selection of securities, depending on the fund's objective.

**Once in the universe, the credit research analysts will assess various factors to understand how much the company's behaviours jeopardise or enhance its enterprise value.**

#### **The team's approach to stewardship**

The fixed income team's stewardship work is supported by a team of dedicated ESG professionals. Its approach to engagement is based on the intellectual capital, systems and quality control developed by EOS. It identifies engagement opportunities with investee companies through the assessment of their ESG practises. This tends towards companies with weak ESG practices but which present room for improvement and demonstrate a willingness to engage. In addition to its own engagement work, the team also rely on EOS to engage with a broader pool of companies. Regardless of who is leading the engagement, EOS or the fixed income team, there is only one assigned engager within the business. This is so the company being engaged hears a single message coming from FHL.

Wherever possible, the relevant credit analyst will attend joint engagement meetings. If this is not possible then credit analysts will sit with the engagement lead before or after meetings to share knowledge, perspectives and ideas. Likewise, engagement analysts are invited to present on engagement progress at credit committees.



## SDG ENGAGEMENT HIGH YIELD CREDIT STRATEGY CASE STUDY

**The company is among the largest food companies in the world, being a global player with leading brands in various large product categories.**

The company reduced its leverage target to 3x from 4x at the end of 2022, and positively reported leverage below its target in the latest Q3 results. This was partly accomplished through divestiture of low growth businesses using proceeds to repay debt in recent years. The company is committed to maintaining an investment-grade rating.

In its Q3 2023 results, the company showed sequential improvement in volumes with softer pricing, in line with expectations, and profitability performed better than expected, with the company raising projections for the year. We have been engaging with the company on the following:

- Tackling supply chain human rights risks [SDG 1, 8, 10]** – The company faced several supply-chain and human-rights allegations in 2019-2020, and has sought to reset its approach to human rights, working conditions and safety in agriculture and supplier value chains since conducting a global human rights assessment in 2019.

During a Q2 2022 engagement, we suggested the company take a materiality-driven heat map approach to identify where human rights action should be prioritised and provided strong examples from the technology sector's efforts to combat supply chain human rights risks. Progress was made in 2023, with the company's publication of its global anti-deforestation policy, which enshrines free, prior, and informed consent (FPIC) for communities and indigenous peoples. It has also committed to publishing a Global Vigilance Plan and Modern Slavery Statement, which will outline its overarching strategy for addressing environmental and human rights risks, though the timeline for its publication is unclear.

- Targeting deforestation-free supply chains [SDG 2, 12, 15]** – As a major, global agricultural commodity buyer, the company has the power to build farming and processing resilience and climate adaptation in its supply networks and collaborate with suppliers to optimise the environmental impact of commodities, including palm oil and dairy. The company has responsible sourcing targets for eggs, broiler chickens, tomatoes, palm oil and animal welfare to be achieved during 2022-2026. The company has completed much of this work for palm oil sourcing. However, it is a number of years behind several peers that lead the market on deforestation, land use and biodiversity policy and implementation, including auditing and remediation. We believe it needs to accelerate its work and increase its overall transparency across its top 10 commodities.

In Q4 2022 and Q2 2023, we engaged the company on its plans to develop this work well beyond palm oil and learned about ongoing sustainable sourcing and anti-deforestation efforts for several sourced commodities. A couple of weeks after our Q2 2023 engagement, the company published its global deforestation and

conversion-free policy. The policy commits the company to ensuring there is no deforestation, no peat, no exploitation (NDPE) or natural vegetation conversion in its highest-deforestation-risk commodity supply chains. Importantly, on biodiversity, the policy requires conservation and protection of water resources and biodiversity in its supply chain, and recovery or restoration if losses or negative impacts have occurred. The publication of this policy is a positive step forward. In future engagement, we will provide feedback and seek dialogue on how implementation for the highest-risk commodities is progressing. Before completing the objective, we would also like to understand how it will report on supplier performance and audits, non-conformance to the policy and how such issues have been resolved over time.

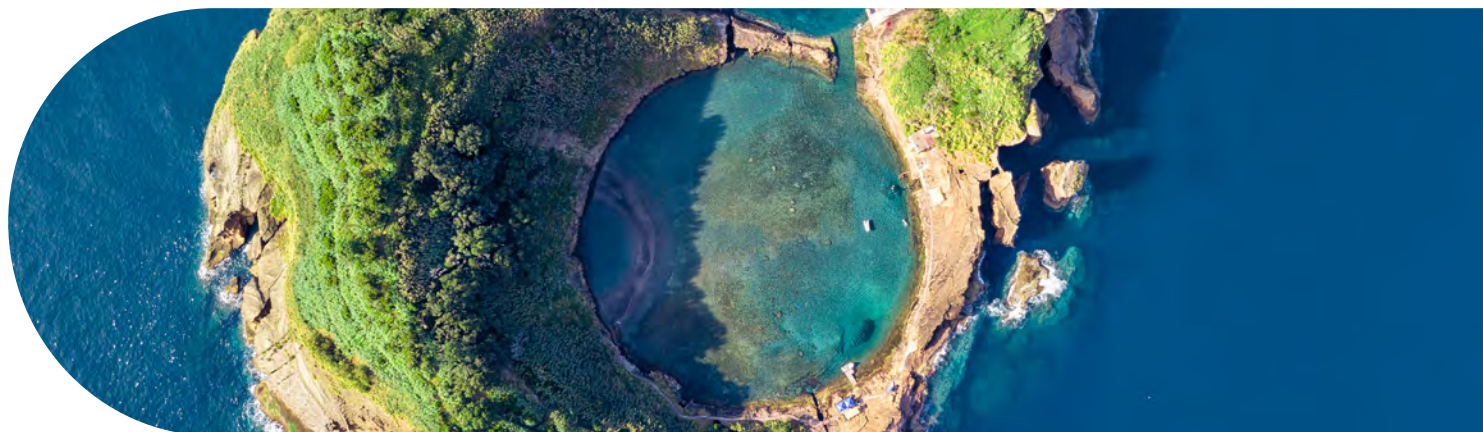
- Developing a healthier, more nutritious product range [SDG 2]** – The US, the company's largest market, recorded an adult obesity rate of almost 42% between 2017 and 2020.<sup>41</sup> Our engagement objective is for the company to aim higher than its post-2025 targets for 'negative nutrients' such as salt and fat, and calorie reduction, and focus on 'positive nutrients' within its targets and nutrient profile model. We believe the company has an opportunity to focus on micronutrient deficiencies in its largest, most material markets, and to move beyond a single global lens (predominantly North America). Furthermore, we believe the company can set new healthy-food innovation and growth goals beyond its plant-based 2025 goal to capitalise on the significant demand for affordable, nutritious packaged foods.

The company has set a series of 2025 targets focusing on reducing salt, sugar and caloric content in its products by 2025. These initiatives are crucial, as besides potentially contributing positive health impacts, the negative health impacts of products with significant salt and sugar content will remain a reputational, market and licence-to-operate risk for the company unless sufficient action is taken. Over several engagements in 2022 and 2023, we raised the opportunity for the company to move further in its own strategy. We built a stronger understanding of why the company is focusing on reducing unhealthy nutrients first. It is considering what kinds of targets might be set beyond 2025, and we suggested that positive micronutrient-based targets should be evaluated as a possibility.

### Future engagement and ongoing objectives

The company has been catching up to some peers on sustainable agriculture and value chains, biodiversity, deforestation and land use, human rights in supply chains and engagement on healthier products. We will continue to engage on the development and delivery of more ambitious goals on nutrition, more comprehensive targets and reporting on human rights, and on the implementation of its deforestation commitment, seeking to influence its approach and provide feedback on material impact drivers.

<sup>41</sup> Centre for Disease Control and Prevention, "Adult Obesity Facts" (2023).



Further examples of how some of our investment teams integrate ESG and stewardship in their investment decision-making processes are below:

### Global Emerging Markets

The investment team analyses ESG risk and opportunity as part of its fundamental research of companies. To understand a company's ESG trajectory, the team believes both quantitative and qualitative analysis is critical, particularly in emerging markets where accurate ESG data is less available. It is only through a detailed understanding of the social and environmental challenges facing a company – in the context of its actual business and the beliefs of its board and management – that one can truly invest responsibly.

In 2023, the team introduced a high-level climate risk framework to deepen its understanding of the physical and transition risks facing companies and to model the financial impacts. This involves three key steps as laid out by the figure below.

Engagement is also a key feature of the investment strategy and, in the team's experience, it has been a powerful way to foster change in emerging market equities, more direct than

exclusion. The team, often in tandem with EOS, engages with companies on material ESG issues – many of which are relevant to the SDGs. These engagements – which are outcome-based and subject to regular progress reviews – seek positive impact across companies' value chains.

The team draws on a wide range of ESG data including FHL's own proprietary ESG tools and EOS, combined with its own qualitative assessment, to generate an overall ESG rating for the company (i.e. below, average, above, leader). This takes into account whether the company is demonstrating positive momentum and a commitment to addressing ESG challenges and opportunities.

The team prefers to invest in stocks that perform well on ESG but may invest in 'below average' companies where they show commitment to improve and are engage-able. In 2023, the team introduced an engage-ability score to evaluate whether companies would be receptive to engagement and whether they have the capacity to engage. The score reflects a company's willingness and capacity to engage on material ESG issues with scores ranging from 1A at the top end to 4D at the bottom.

Figure 30. Global Emerging Markets Equity climate risk framework

Key steps	Transition risk	Physical risk
<b>1.Vulnerability assessment</b>	Assessing exposure based on the nature of the business, location of its operations and how and where its revenue is generated.  Focus on emissions intensity and carbon regulation risk.	Assessing geographic exposure and resilience to acute and chronic <sup>42</sup> physical climate risks. <sup>43</sup>
<b>2.Contextual adjustment</b>	Adjusting for likelihood, severity and timing of transition impacts, considering mitigating factors.	Understanding the likely operational and supply chain impacts, including impacts on people (eg. safety, physical and online connectivity); productivity and business continuity; impacts to local infrastructure; and climate-related opportunities.
<b>3.Modelling financial impact or risk premium</b>	Key financial impacts to consider may include: inflationary costs, regulatory costs, capital expenditure (CapEx) requirements, revenue loss, stranded assets.	

Source: FHL, H2 2023 GEMS Materiality Report.

<sup>42</sup> Acute physical risks refer to those that are event-driven, including increased severity of extreme weather events, such as cyclones, hurricanes, or floods. Chronic physical risks refer to longer-term shifts in climate patterns (e.g., sustained higher temperatures) that may cause sea level rise or chronic heat waves.

<sup>43</sup> This draws on the Notre Dame Global Adaptation Index's climate scores which consider each country's vulnerability and readiness. Country Index // Notre Dame Global Adaptation Initiative // University of Notre Dame.

### Global Equities

Assessment of the ESG characteristics of a company is a vital part of the team’s investment approach and the team uses ESG research in both proprietary models and in discussion with EOS.

The team have built a bespoke quantitative assessment of the most important ESG issues, the QESG Score, which evaluates a company’s ESG characteristics and identifies positive ESG change. The team believes that companies less exposed to ESG risks than peers will outperform over the long term. Further, it believes that companies that are improving their ESG profile through positive change can unlock shareholder value.

The QESG Score is designed to capture a company’s behaviour on various ESG issues, as well as observed change in its ESG behaviour. The score combines data from EOS, Sustainalytics, MSCI, CDP, ISS, Trucost, FactSet and Bloomberg and is weighted 50% governance factors, 25% environmental factors and 25% social factors. The score is shown in the ESG Dashboard. The weightings used are based on the expertise of the EOS team. Following research into the growing impact of ESG factors, the team found a meaningful correlation between the ESG scores and stock performance.

The QESG Score is a valuable component of the ESG Dashboard, which is used in the subjective part of the process and provides a concise digest of the ever-increasing amount of data on ESG risks. As such, all of the team’s investments are analysed from an ESG perspective.

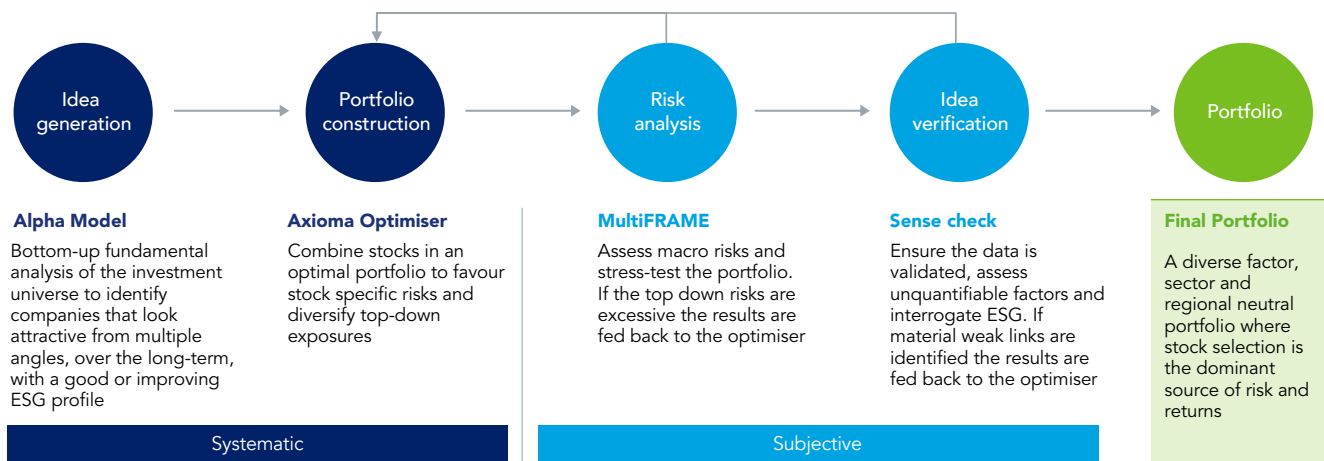
**The expertise of EOS has also helped define the key performance indicators or risk factors on which each company is measured.**

In 2023, the QESG Score was refreshed and version 3.0 is in active testing. The latest version incorporates the framework built for the team’s Sustainable Opportunities score, introduces new factors and data sources, and expands the granularity of the underlying indicators where possible. The team are currently using version 3.0 to inform their analysis of companies and will introduce within the quantitative framework during 2024.

The expertise of EOS has also helped define the key performance indicators or risk factors on which each company is measured. These are either generic, such as board structure, or sector specific, focusing on the major risks by industry – such as CO2 emissions and fleet consumption for the automobiles industry, paper sourcing for media and energy efficiency for airlines. The team uses it to identify ESG risks within companies and determine the materiality of these risks. Any change in the level of ESG risk and progress on current engagements are key factors that could influence an investment decision.

The ESG integration approach adopted by the team is complemented by direct dialogue with businesses that is made possible through EOS, which ensures the team remains active owners of the companies held in the portfolio.

Figure 31. Global Equities Investment Process



Source: FHL, as at 31 December 2023.



## SDG Engagement Strategies

While all of our strategies integrate engagement into their investment processes, we have a selection of strategies with a specific focus on selecting companies with engagement potential. Our SDG Engagement Equity strategy and SDG Engagement High Yield Credit strategy seek to achieve a meaningful social and/or environmental impact as well as a compelling return through investing in and engaging with companies to drive positive change in line with relevant SDGs. The SDGs provide an ideal framework to identify ex-ante potential for creating positive societal and environmental change through engagement to create more impactful and sustainably profitable companies.

Given the added focus on engagement for these strategies, we have dedicated engagers based in the relevant investment teams who focus solely on these strategies and work closely with EOS to ensure a consistent approach (see Credit section above for additional detail). All investments are formally reviewed by the lead manager and lead engager, while the relevant analysts and team members also provide input every six months. These meetings investigate whether the original engagement thesis is still valid and also measure progress towards any specific objectives. In addition to the case study below, case studies for our SDG Engagement strategies are available under Principle 9.



### SDG ENGAGEMENT EQUITY STRATEGY CASE STUDY

#### SSP Group



One of the largest employers in the SDG Engagement Equity Strategy is SSP Group – the world's second-largest travel food and beverage concessions operator. Effectively in hibernation during the initial period of the pandemic, SSP began rapidly hiring in 2022 and 2023. As at the end of 2023, the company employed about 42,000 people – a 20% increase from 12 months earlier.

The company is in essence a people business. Its employees serve millions of customers each year in airports and railway stations around the world. Its ability to create and sustain long-term partnerships with clients and partner brands relies on its teams delivering a commercially viable and sustainable offer. To that end, retaining core talent in what can be a very seasonal business requires focus.

Employee turnover is high (c.40% when seasonally adjusted, or >100% in absolute terms) and average salaries are a modest £24,700. Pay increases for the lowest paid were up 6% vs. 3% for the wider workforce and supportive benefits were expanded too. The company's labour costs are roughly 30% of sales.<sup>44</sup>

Our conservative estimates<sup>45</sup> based on FY23 figures for SSP's UK business (25% of sales in FY23) suggest that moving its UK employees to at least a living wage level (as per the Living Wage Foundation<sup>46</sup>) would cost about £5m (assuming 60% of employees are currently paid the UK minimum wage which is known as the UK National Living Wage). While this cost is immediate, we believe that there is scope to realise cost savings from turnover reductions and like-for-like revenue gains from more engaged and productive employees. If voluntary turnover were to reduce to 30% annually, then the saving from this change alone could be upwards of £5m each year. Recognising that many of the benefits are hard to quantify, we would suggest that over the medium term the potential benefits are greater.

Pleasingly, the company's management team, led by CEO Patrick Coveney (who joined the company in March 2022), recognises this correlation. During a meeting in Q2 2023, the CEO committed to continue to raise pay for the company's lowest-paid employees at a higher rate than for the wider workforce in the coming years. Costs will be passed on through pricing and absorbed through productivity enhancements achieved through deployment of further technological investments. We continue to engage with the company on this issue and the practical and short-term commercial challenges of moving to a Living Wage Plus model of employment.<sup>47</sup>

<sup>44</sup> Turnover figures obtained via engagement and salary figures obtained from company filings.

<sup>45</sup> We have assumed 60% of UK employees are paid a minimum wage and calculated wages using personnel expenses – executive director compensation / number of employees. For costs of turnover, we have used a 30% of average salary cost.

<sup>46</sup> The Living Wage Foundation is an NGO whose purpose is to encourage employers to play their part in tackling in-work and post-work poverty and provide a decent standard of living by paying the real Living Wage, adopting Living Hours and Living Pensions as well as wider good employment practices.

<sup>47</sup> The Living Wage Plus entails a range of extras on top of the basic Living Wage. The extras will not be added to the Living Wage, but users can pick components, such as car ownership, expenses for cinema/culture, eating out, the provision of care.

### Private markets

In private markets, ESG data is often less readily available. As such, the teams are heavily reliant on their due-diligence process and have developed their own frameworks for assessing ESG risks within their investments.

### Private debt

The private debt teams consider ESG behaviours when carrying out credit analysis for each potential investment. ESG considerations are a fundamental part of the research presented, and discussed, for all new transactions tabled at the Investment Committee. Material ESG issues will often form part of engagement with the company prior to investment and once invested.

For our direct lending team, the key is to identify meaningful ESG risks (both current and potential) before investing. Due to the difficulty of divesting and the capped upside, it is important to manage the downside and engage where possible ex-ante. The direct lending team undertakes enhanced due diligence on industries that are deemed controversial, such as energy, chemicals, forestry and agricultural commodities, manufacturing and mining and metals. They also undertake transaction specific ESG analysis by carrying out an assessment on ESG risks for every investment opportunity. In addition, the team focuses acutely on the sensitivity of the company's cashflows to the identified potential ESG risks. With that in mind, the direct lending team will evaluate if investors are adequately remunerated for the ESG risk(s) of the transaction.

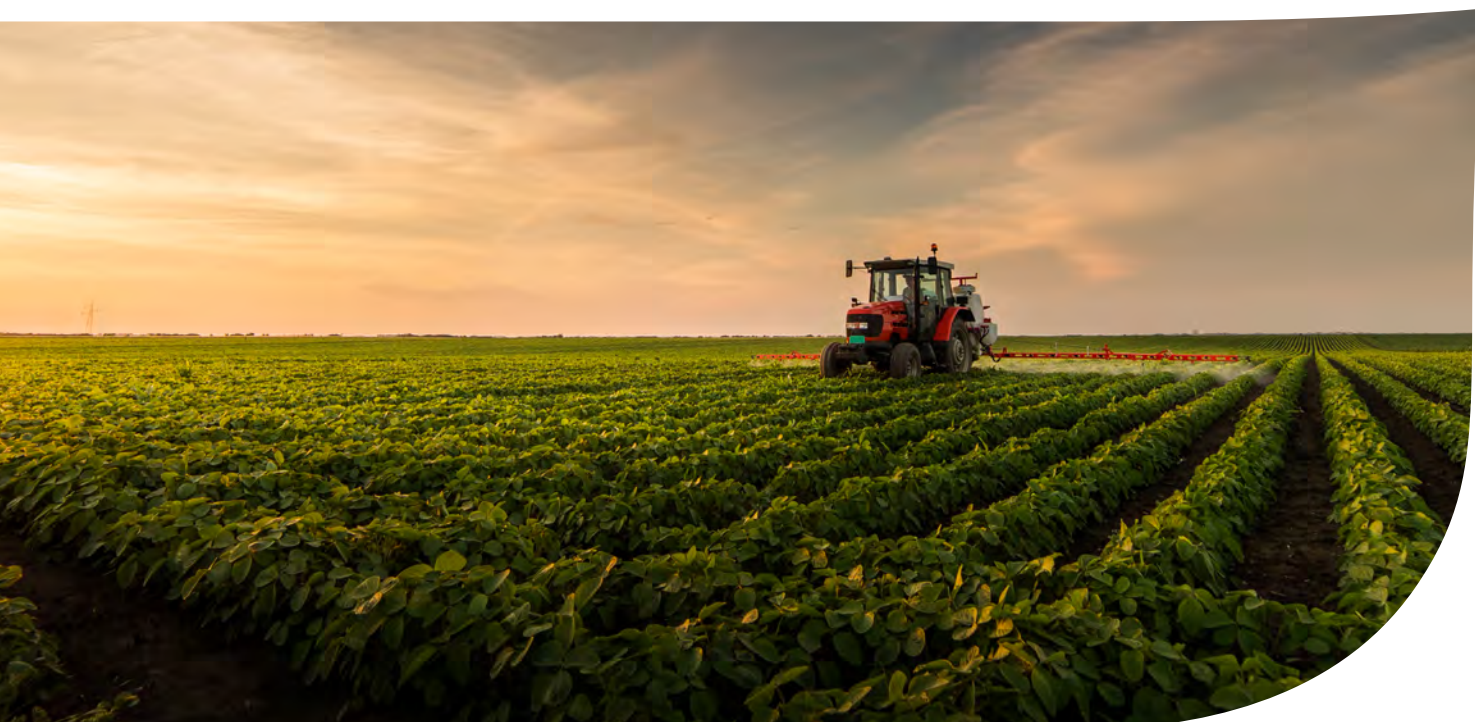
As with our direct-lending investments, it is important for our asset-based lending team to identify risks that may impact on a borrower's ability to repay their loan. We have integrated our responsible property investment (RPI) principles and programme into the debt-investment procedures. This is done as follows:

## CASE STUDY

### Direct Lending



Our direct lending team reviewed the opportunity to lend to a Swedish producer of polyethylene film and sustainable high-performance film. The company's differentiated product portfolio, with a clear focus on ESG leadership through circular plastic technologies, pioneering recycling processes and closed loop solutions presented a compelling prospect. The proposed debt financing was to support the expansion of the company's product offering, manufacturing facilities and geographic footprint via a strategic North American acquisition. To ensure the borrower continued on its journey to improve sustainability practices, an ESG margin ratchet was included in the loan documentation which, depending on the meeting of certain ESG-related criteria, impacts the quantum of interest paid by the borrower on the loan. These criteria include the reduction of greenhouse gas emissions, the percentage of recycled materials used in their production and their employee engagement index score.





- Underwriting and due diligence:** The focus of our responsibility programme is on ensuring a strong due-diligence process, including assessments of ESG and climate risks and opportunities before agreeing new loans.
- Loan origination and documentation:** The business plan agreed is included in the loan documentation at the loan-origination stage. This includes all mitigation activities identified and detailed in the asset business plan, asset refurbishment plans and/or planned and preventive maintenance programmes.
- Management and monitoring post closure, asset upgrade finance:** We collect and manage the sustainability information we hold on the borrowers and the underlying assets.

Where we provide capital for refurbishment in accordance with the business plan, refurbishment agreements include a review of our responsible refurbishment guide and minimum requirements.

## Real estate

ESG is integrated into the investment strategy and working practices of all of our real-estate portfolios. A consideration of ESG principles is embedded into the property selection and investment process, including through initial screening and due diligence and as part of the investment decision.

At the transaction stage, we use a number of procedures and tools that have been developed internally and through our sector engagement programme. This includes an initial screening, where the team assesses the risks and opportunities for value-add from ESG characteristics. This is then followed by a responsible investment due diligence for any new acquisitions, where surveyors and environmental consultants collect relevant data on the buildings to identify risks and opportunities. As part of our due diligence process, we inquire to understand the level of community and occupier engagement in the assets being considered. The findings from this then inform the asset-management plans and processes.

Sustainability regulatory risk assessments are then used to identify typical risks that should be incorporated when devising the parameters entered into the investment models (using discounted cash flow analysis). Typically, the team integrates ESG information that can affect investment fundamentals such as refurbishment budgets, risks of voids, lease lengths and obsolescence. ESG criteria and assessments are integrated into the investment decision papers submitted for approval to the Investment Executive Committee. The ESG team reports to the Real Estate Chief Operations Officer who sits on the Investment Executive Committee to review and ensure that ESG integration is appropriately covered.

ESG and engagement information continue to be integrated into the development and monitoring of our real-estate assets after purchase:

- Setting ESG requirements:** through our internal responsible property development requirements we have set minimum requirements that assets must meet when undergoing refurbishment or new construction. This is monitored through an online platform.
- Monitoring and data collection:** we work with our property managers, facilities managers and consultants to monitor ongoing implementation and improvements. This is reported back to the business on a quarterly basis. Annual key performance indicators (KPIs) are set and progress against them is measured.
- Engagement:** we work with our property and asset managers on site to engage with the delivery teams, occupiers and visitors. Site-specific annual surveys and other engagement activities are carried out successfully.

For our real estate team's indirect and international investments, we carry out active engagement on governance matters and on ESG policies and strategies with property developers, property management teams, tenants, lawyers and agents. We include commitments to develop a joint ESG strategy on acquisitions for jointly managed assets.



## Infrastructure

ESG and sustainability considerations are fully integrated into all of our infrastructure products and activities. As investors, we integrate an assessment of ESG risks and opportunities related to a prospective investment into our investment analysis and consider the long-term sustainability of each investment with reference to internationally recognised sustainability objectives. As owners, we see ourselves as stewards of infrastructure assets, not only for this generation but also for future generations. We engage actively with our investments on all areas of potential ESG risk and opportunity supported by robust data monitoring.

We select investments based on strict investment criteria and restrictions in accordance with our clients' needs. ESG matters are considered together with all other risks and opportunities identified in the course of due diligence. They are factored into Investment Committee papers at each stage of our investment process. Conclusions are factored into the investment decision, investment valuation, transaction documentation and/or transitioned to our asset management team for further engagement post-completion.

We identify potentially material ESG matters which may pose a risk (to value or reputation), represent significant opportunities or have significant environmental or social impacts using a proprietary GRESB<sup>48</sup>-derived materiality matrix. We then undertake internal due diligence or appoint third party advisers to deep dive into areas of focus where appropriate. We further undertake a high-level assessment of alignment of key business activities with the SDGs. Our most recent investment assessments take into account whether an investment has the capacity to reduce its emissions on a trajectory aligned with a 1.5°C warming scenario pursuant to the Paris Agreement, and/or whether the investment

represents a solution with reference to the climate mitigation and adaptation criteria within the EU Sustainable Finance Taxonomy. We will decline investments which are unlikely to achieve stable, sustainable returns over our long-term investment horizon (e.g. which bear stranded asset risk) and where an opportunity lacks the governance, information or alignment with co-shareholders to enable us to influence material ESG matters over time.

**Figure 32.** ESG Integration in investment process



Source: FHL, as at 31 December 2023.

<sup>48</sup> GRESB is the global real-estate sustainability benchmark for real assets.



Where we invest, we will transition any identified ESG risks or opportunities identified in due diligence to the ongoing asset management team. The asset management team is fully integrated into the investment process, with informal and, if required, formal input being provided at each Infrastructure Investment Committee approval stage and a 100-day transition plan for the investment being developed during the final stages of investment due diligence and execution to ensure a smooth transition, including of key relationships. In addition, where practicable, the ongoing asset management team will include team members who have undertaken the original acquisition.

Sustainability is fully integrated into our ongoing strategic asset management framework. Given the long-term nature of our investment, engagement is the primary means to tackle ESG risks post-completion.

### Private equity

Our private equity team invests both directly in a selection of companies through co-investments alongside other General Partners (GPs) and indirectly through fund investments. Typically, we are a minority investor for direct co-investments. Our private equity team have identified four key megatrends that they believe will reshape global economic activity over the next 10-20 years and drive the growth of certain companies in niche sectors regardless of economic cycles. It is these fast growing, noncyclical businesses in the EMEA, North America and APAC, which are our investment targets. Within the megatrends we look for investable growth themes, and then drill down to the sectors most likely to benefit in order to find companies capable of generating sustainable long-term alpha. All investment opportunities are subjected to our rigorous, systematic investment process which we have developed over many years. As well as driving our co-investments, our fund selection also closely follows the key themes we have identified. When investing in funds, we form close relationships with the GPs we back, often initially via a co-investment relationship. This gives us valuable insight into the experience of the team and how value is created.

The team firmly believe that acting responsibly does not impede results. Creating a positive effect on society and the environment – sustainable investing – is closely aligned to our objective of delivering above market returns for our investors.

### The team assess all investments using a proprietary responsible investment framework to guide decisions. The team has one framework for funds and one for direct co-investment.

The team considers both ESG risks and opportunities ahead of each investment. Due the nature of the asset class and our position as a co-investor, our private equity team aim to identify ESG risks at the point of investment due to the difficulties faced in escalating activities during the investment hold. The team assess all investments using a proprietary responsible investment framework to guide decisions. The team has one framework for funds and one for direct co-investment. The aim is to protect investors from the impact of 'bad' investment decisions, avoiding businesses that are later penalised for failing to meet legal, regulatory or public standards of conduct.

The private equity team considers the ESG practices of managers ahead of making fund investments. The team assesses managers capabilities across 5 key areas: (i) policies and commitments to standards, (ii) governance and mindset, (iii) investment process, (iv) climate risk and (v) communication and reporting. Each manager is scored on each dimension using a standardised and proprietary matrix that leverages Institutional Limited Partner Association and UN PRI recommendations. The assessment of managers capabilities is included in the Investment Committee papers and contributes to the investment decision.

For direct co-investments, material ESG risks and opportunities are presented (at a minimum) in the Investment Recommendation Paper (IRP), (for example, practices, company culture and board composition). ESG considerations are tabled across the investment process in local team discussions and formally considered and discussed at the Investment Committee where each investment is scored on a proprietary ESG framework. Based on a risk-based approach, only investments which have risks within tolerable limits are progressed to investment. For these investments, material ESG issues and KPIs are identified to be monitored post-investment. Deals are routinely rejected when they do not clear the ESG risk threshold and good ESG practices are considered positively into the investment thesis.





Our private equity team collaborate with various industry initiatives and subscribed to the ESG Data Convergence Initiative in 2021. The initiative aims to improve disclosures of ESG KPIs in private equity by selecting a limited series of KPIs that subscribers of the initiative shall aim to collect and share with their own investors. As part of this initiative, we now engage with each new company or lead investor as part of the investment process to receive the KPIs from the ESG Data Convergence Initiative on a yearly basis.

We seek to improve and protect the financial value of investments through assessing, monitoring, and seeking improvements to material ESG risk areas. Our private equity team takes a risk-based approach to effectively identify, monitor, and manage ESG risks, opportunities and impacts identified across its portfolio. For direct co-investments, we receive quarterly reports from the GP that include both financial information and qualitative data. These reports often contain ESG information. In addition to this, we often have a quarterly call with the GP where we discuss the reports and any other topics we wish to raise. For fund investments we also receive quarterly reports and are invited to participate in AGMs. In a minority of cases, we are part of the limited partner advisory committee (LPAC) and hence part of the fund's governance structure. We can raise issues with managers in those forums or bilaterally.

## The Responsibility Office

Our Responsibility Office is tasked with monitoring and overseeing every investment team's integration approach. To that end, the Responsibility Office meets with every investment team on a quarterly basis to review the portfolio holdings to assess ESG risks and opportunities and flag, if necessary, particular holdings that might present an issue. A combination of in-house and external tools are used to review the ESG performance and engagement coverage of our holdings.

The Responsibility Office also conducts an assessment using our proprietary ESG Assessment Matrix on an annual basis to determine where each of the investment teams are in their ESG and stewardship integration journey. The matrix contains 30 indicators across 4 key areas of assessment and aims to assess the teams on the following:

- **Investment process and philosophy** – how well the team understands material ESG factors for its universe and how they stay abreast of developments, where in the process the team integrates ESG and stewardship insights and how this impacts investment decisions to the benefit of clients and their investors. Within the stewardship sub-category – the teams are assessed on their proactiveness in identifying areas of engagement, their interactions with EOS and how involved they are in the engagements, how regularly the teams assess the progress made on engagements and how this influences their investment decisions.
- **Sustainability commitments** – how actively the team is monitoring their progress in meeting FHL's various commitments, such as FHL's net zero commitment.
- **Communication** – how clearly the team articulates, for clients and their investors, the ESG and stewardship approach of an investment strategy, and how it reports on its ESG performance.
- **Advocacy** – how actively the team is involved in initiatives in clients and their investors' interests, both internally and externally, on ESG themes as well as ESG and stewardship integration in asset management.

**Figure 33.** Identifying opportunities and avoiding harmful or controversial behaviour

	 Uninvestable	 Potentially attractive	 Attractive
<b>Behaviour</b>	<ul style="list-style-type: none"> <li>■ Reliance on harmful products (eg: Tobacco, coal, weapons)</li> <li>■ Significant ESG Controversies</li> <li>■ Breach of UN Global Compact</li> </ul>	<ul style="list-style-type: none"> <li>■ Good company but products have little societal benefit</li> <li>■ OK company, but limited ESG improvements</li> <li>■ Challenged company, but reducing exposure to harmful products</li> </ul>	<ul style="list-style-type: none"> <li>■ Sustainable products that benefit society</li> <li>■ Robust processes &amp; effective management of ESG risks</li> <li>■ Leading and improving governance standards</li> </ul>
<b>Outcome</b>	<ul style="list-style-type: none"> <li>■ Alpha Score severely reduced</li> <li>■ Major financial &amp; reputational risks</li> </ul>	<ul style="list-style-type: none"> <li>■ Alpha score driven mainly by financial characteristics</li> <li>■ Engagement vital in understanding &amp; controlling risk</li> </ul>	<ul style="list-style-type: none"> <li>■ Alpha score enhanced to reflect the lower risk and higher quality company</li> </ul>

Source: FHL, as at 31 December 2023.

## How we have aligned our approach with client investment time horizons

Under Principles 1 and 6 addressed earlier in this report, we set out our belief that the purpose of investment is to create wealth sustainably over the long term. This informs our view that we have a duty to consider the longer-term risks and opportunities when investing, which aligns with the goals of our pension-fund clients who typically look out over the long term. All of our strategies adopt a long-term investment horizon. While this will vary depending on the investment strategy and the markets in which they invest, a typical time horizon for investment decisions adopted by our investment teams is three to five years. As such, depending on the investment being considered, its fundamental or ESG performance drivers are likely to be relevant in any evaluation for significantly longer than three to five years.

All of our strategies look to deliver sustainable wealth creation over the long term and our combined approach to responsible investment and responsible ownership is the key to catalysing positive change within companies and generating financial gain over the long term. We believe we cannot deliver long-term returns without identifying and working towards mitigating material ESG risks and, where possible, seizing positive opportunities.

We consider our clients' and potential clients' needs throughout the entire product-development process. As such, stewardship and ESG integration is built into the investment process at the outset and clearly articulated in any legal and marketing documentation for the strategy. The Customer Outcomes Group (COG) then uses this documentation to monitor the investment teams at least annually to ensure they are acting in line with the parameters they have set for themselves. More information about the COG and other processes that ensure we continue to meet client needs is available in our reporting under Principle 1.<sup>49</sup>

**We consider our clients' and potential clients' needs throughout the entire product-development process.**

## Service providers

Our stewardship is undertaken in-house by our investment teams and EOS, as described under Principles 7, 8 and 9. In the case of private equity, the team work with lead GPs in instances where they do not have the ability to engage directly. Likewise, the investment teams are responsible for integrating ESG and engagement information into their investment processes (with the support of the Responsibility Office, which promotes best practice).

We also use third-party data providers, as described under Principles 7 and 8. In some cases, we integrate this third-party data into our proprietary tools to enable our investment teams and engagers to access and compare a wide range of data quickly. The parameters for such services are clearly set out in the relevant contracts and the ESG Integration team within our Responsibility Office monitors the provision of such services on an ongoing basis. Key parameters that we consider when assessing a data provider are data quality, methodology used for any calculated or modelled data points, frequency of update, data delivery mechanisms and coverage.

As described in more detail under Principle 8, our real estate team use external property managers for all day-to-day property management. To ensure our expectations are clearly understood, ESG requirements and commitments are included in their contractual service agreements. The managers are responsible for the implementation of our ESG programme and health-and-safety measures, as stated in their service agreement. As described under Principle 8, our private equity team make direct and indirect co-investments and monitor the GPs.

<sup>49</sup> HGPE is partly within the remit of the COG. Currently the COG covers products that are managed by HFML, HJML and HJML, therefore the more recent HGPE products that have launched with HFML as the Manager are in scope.

## Principle 8

### Signatories monitor and hold to account managers and/or service providers.

All voting recommendations to our investment teams are made internally by EOS and engagement activity across asset classes is carried out by EOS personnel or the investment teams themselves, with the exception of some engagements for our private equity funds as described below. More detail on how we use ISS research to inform our voting decisions – and how EOS use ISS research to inform voting recommendations to voting services clients – is available under Principle 12.

As noted earlier we use a number of external ESG data providers, as each data provider has developed their own methodology which can result in differing views. Taking this range of views into account, along with our qualitative fundamental analysis and insights from engagement by EOS or the investment teams, helps us to form a more comprehensive view of the company.

As part of our ongoing research into assessing sustainability within companies we have spoken with a number of data providers on their frameworks and how these are applied to companies and sectors. Having worked with data providers over many years we are able to critically assess the strengths and weaknesses of the approaches and feed this insight back to the service providers.

**Having worked with the data providers over many years we are able to critically assess the strengths and weaknesses of the approaches and feed this insight back to the service providers.**

We may also engage with data providers when we identify incorrect information. Over the course of 2023, we identified instances where environmental data received from the data provider did not match our expectation of the company's performance on those factors. We have had ongoing dialogue with data providers around data quality and have since seen the data providers improve their data quality practices. We have also developed our own approach to data management; this includes the creation of a dedicated team to monitor the data quality and implementing automatic checks to flag data discrepancies, where possible. In 2024, we will continue to improve our work on data management and implementing an infrastructure that enables efficient data consumption and creation of analytics.

Assessing nature-related risks and opportunities has been an area of focus in 2023 and we have been in dialogue with a number of third-parties to partner with to create a framework that allows us to integrate these risks and opportunities in our investment process, engagement and for external reporting. As this is a nascent space, it allowed us the opportunity to share our requirements for consideration to the third parties as they develop their products.

In 2023, our impact team enhanced their impact database along with one of our data partners to introduce new biodiversity metrics. This is primarily being used to assess the investments in our Federated Hermes Biodiversity Equity Fund.

The database draws on data from company, sector, and impact related industry reports. It provides theme specific KPI outputs including, but not limited to: number of species preserved; hectares of land restored or conserved; megawatt hours (MWh) of renewable energy generated and metric tonnes of CO<sub>2</sub> avoided (Energy Efficiency); cubic metres of water saved (Water); and metric tonnes of food waste/loss avoided.

For our real estate team, all day-to-day property management – including rent and debt collection and active responsible property management – is dealt with by external property management agents. They are selected following a rigorous process that includes ESG considerations, while ESG requirements and commitments are included in their contractual service agreements. The performance of property manager agents – and any other agents appointed for work on activities such as rent reviews, lease renewals, transactions property maintenance, health-and-safety issues and environmental issues – is closely monitored by our internal investment managers. The property managers are contractually responsible for implementing the ESG programme and health-and-safety measures, as stated in their service agreements. Their requirements include risk management, refurbishment and development, utilities measurement and reporting, ESG business plans, energy management, water management, waste management, transport, procurement and supply chain, environmental risk and management, occupier engagement and quarterly monitoring of progress against targets. In 2023, there was also progression on social value implementation, the detail of which can be found under Principle 4.

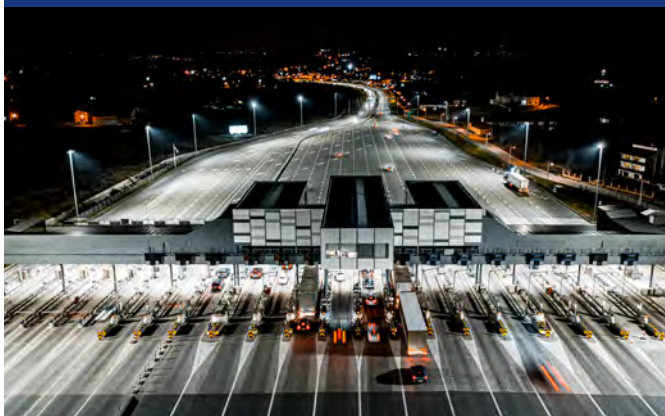
Our infrastructure team is primarily a significant minority shareholder in operational businesses with robust governance rights, typically including Board representation. We engage via day-to-day asset management with operational teams, as board and or committee member and as shareholder. We also have some majority shareholder investments in energy and transport assets at which we engage directly with Operations and Maintenance (O&M) providers in the day-to-day running of the assets. Collaboration on sustainability matters with the O&M providers is a key priority at these assets and we value positive relationships with aligned counterparties.

We also have two legacy indirect (fund) investments which are part of our infrastructure fund, HIF I. Engagement with managers for our indirect investments, including on ESG and sustainability considerations, is integrated into our asset management approach. However, our approach necessarily changes where holdings are indirect. Where ESG reporting and engagement by underlying managers is limited, we remain focussed on foundational, open questions focusing on risk mitigation.



## INFRASTRUCTURE CASE STUDY

### Iridium Hermes Roads



As an example, at the time of the majority stake acquisition in 2020, Iridium Hermes Roads (IHR), a shadow toll road portfolio across Spain, did not have emissions reporting in place. This was deemed a critical first step to put in place so that targeted action could be taken to decarbonise the business and reduce emissions, focusing on the areas that contribute most to carbon emissions (directly or indirectly), and so that progress can be tracked.

In 2021, the infrastructure team developed a reporting template which would capture scope 1, 2 and scope 3 (where available) emissions from different emitters (the latter being O&M subcontractors) across the six concessions. The emissions template has been a useful tool to guide targeted action on the easy to decarbonise areas and large sources of emissions at each of the projects.

Through collaborative engagement with co-shareholder and O&M provider, Iridium, a number of decarbonisation initiatives were implemented in 2022 and 2023, including the switch to renewable electricity tariffs (the most significant driver of emissions reductions, in particular in the largest concession in the portfolio), and the installation of solar panels and LED lighting.

In 2024, with the help of co-shareholder and O&M co-shareholder Iridium, IHR will be populating the template for latest emissions performance and it is expected that impacts of recent decarbonisation-related capital expenditure will be visible in the emissions reported.

When investing in funds, our private equity team form close relationships with the GPs we back, often initially via a co-investment relationship. This gives us valuable insight into the experience of the team and how value is created. ESG risk assessments are conducted on lead GPs for all new co-investments and fund investments. The private equity team considers the ESG practices of managers ahead of making fund investments. The team assesses managers capabilities across 5 key areas: (i) policies and commitments to standards, (ii) Governance and mindset, (iii) Investment process, (iv) climate risk and (v) communication and reporting. Each manager is scored on each dimension using a standardised and proprietary matrix that leverages Institutional Limited Partner Association and UN PRI recommendations. The assessment of managers capabilities is included in the Investment Committee papers and contributes to the investment decision. We seek to improve and protect the financial value of investments through assessing, monitoring and seeking improvements to material ESG risk areas. Our private equity team takes a risk-based approach to effectively identify, monitor and manage ESG risks, opportunities and impacts identified across its portfolio. For direct co-investments, we receive quarterly reports from the GP that include both financial information and qualitative data. These reports often contain ESG information. In addition to this, we often have a quarterly call with the GP where we discuss the reports and any other topics we wish to raise. For fund investments we also receive quarterly reports and are invited to participate in AGMs. In a minority of cases we are part of the limited partner advisory committee (LPAC) and hence part of the fund's governance structure. We can raise issues with managers in those forums or bilaterally. We describe in more detail under Principle 9 how we work with GPs when it comes to engagement with investee companies.

In terms of our investment operations, our middle office is responsible for monitoring outsourced functions on a day-to-day basis. We also have a Supplier Review Group, which chaired by FHL's Chief Operating Officer, that is responsible for the oversight of material outsource arrangements and critical supplier arrangements, where regular reviews of the risks and performance of these arrangements are overseen, in particular key risk indicators are used to monitor any deterioration in the service and/or risk profile. Furthermore, our contracts with material third parties include a service level agreement (SLA) where applicable. The SLA details service standards we expect from our third parties – which include several agreed key performance indicators (KPIs), and where applicable, dependencies and escalation requirements in respect to risk incidents. The contract and/or SLAs include details of the required governance structure and frequency of service reviews between the third party and our business.

As part of the governance structure, significant or persistent issues can be escalated to the Risk, Compliance and Financial Crime Executive. In addition to the service reviews, periodic on-site visits and due diligence reviews take place and the latest SAS70 reports (or equivalent controls report) and credit worthiness are reviewed to identify any adverse conditions that may have an impact on the service provider and the services provided.



## Principle 9

Signatories engage with issuers to maintain or enhance the value of assets.

### How we identify issues for engagement and develop objectives

Our approach to engagement is driven by our purpose and investment beliefs. We believe that the purpose of investment is to create wealth sustainably over the long term and that investing responsibly is the best way to sustain long-term outperformance and contribute to beneficial outcomes for investors, companies, society and the environment. We aim to generate sustainable wealth creation for the end beneficiary investor, encompassing both investment returns and their social and environmental impact. As a result, our engagement is outcomes-driven and focused on ensuring that the companies we invest in are creating wealth sustainably. Given the time horizons of our strategies to meet our clients' needs (as described under Principle 6) we are able to engage on particular issues over multiple years to encourage fundamental change within our investee companies. We believe that this approach delivers the best results for our clients and end beneficiaries.

We adopt a systematic approach to identifying companies for engagement. We select companies and tailor the intensity of engagement based on the size of our investment, materiality of the risks and issues and feasibility of achieving change through engagement. We believe that this enables us to most effectively serve our clients' needs by focusing our efforts on where they are needed the most and can have the most impact.

Our EOS [Engagement Plan](#) and related corporate governance principles and voting guidelines, as well as our FHL Voting Policy and Guidelines which are updated each year drawing on our extensive experience as an active and engaged shareholder, set out a number of expectations which we believe should exist between owners, boards and managers to create a framework for communication and dialogue.

While we can be robust in our dealings with companies, the aim is to deliver value for clients, not to seek headlines through campaigns that could undermine the trust that would otherwise exist between a company and its owners. We are honest and open with companies about the nature of our discussions and aim to keep these private. Not only has this proven to be the most effective way to bring about change, but it also offers a level of protection for our clients by ensuring their positions will not be misrepresented in the media.

In 2022, we published our Climate Action Plan which takes an engagement-driven approach. As climate change continues to be the biggest single issue of concern for long-term investors, the emphasis of our engagement is on matching long-term commitments with a Paris-aligned strategy and targets. We also support action to ensure that published financial accounts and political lobbying are similarly aligned. Our [Policy Statement on Deforestation](#) sets out our engagement-driven approach across asset classes to deforestation.

In 2023, we published our [Human Rights Policy Statement](#), as described under Principle 4, which sets out our expectations of companies relating to human rights and our engagement approach across asset classes.

### Public markets

EOS has established a detailed public markets [Engagement Plan](#) on a rolling three-year basis, with themes ranging from human and labour rights to circular economy and zero pollution. EOS focuses its stewardship on the issues with greatest potential to deliver long-term sustainable wealth for investors including through positive societal and environmental outcomes. The full taxonomy below identifies 12 key themes and 36 related sub-themes for engagement. This breadth of coverage across the whole programme is necessary to reflect the diversity of issues in our global Engagement Plan, which covers all regions and sectors, including those which are most material to the individual companies. The selection of these themes is developed in line with input from the investment teams at FHL, as well as EOS' third-party clients.



Figure 34. Engagement themes: our stewardship process to achieve long-term sustainable returns on investment



Source: FHL, as at 31 December 2023.

We review our engagement plan every year to ensure it is up to date and reflects client priorities. Geopolitical tensions remained heightened in 2023, with no sign of an end to the war in Ukraine and the destabilisation of the Middle East through the Israel-Gaza conflict. We continue to engage with companies on how they address geopolitical risks facing their businesses and their approach to safeguarding human rights in high-risk regions. During the course of 2023, biodiversity and artificial intelligence (AI) continued to rise up policy makers’ and company and investor agendas, and we will continue to intensify our engagement on these topics. In response to client feedback, over 2022 and 2023 EOS increased the intensity of engagement with certain companies and modestly reduced the number of companies in the Engagement Plan. In light of these changes, client feedback confirmed we were striking “about the right balance of breath and intensity” of engagement.

Based on the review, our work in 2023 continued to focus the four priority areas – climate change, human and labour rights, human capital, and board effectiveness – as these remained the most material themes. Information on the four priority themes can be found under Principle 4.





We annually review, develop and publish a rolling three-year engagement plan. The EOS engagement selection process is a key structure which enables us to support client stewardship. We select around 320 companies for the core EOS Engagement Programme, of which approximately 125 are also held by FHL's equity and credit teams (as at 31 December 2023). These companies are formally identified on an annual basis and reviewed for continuing materiality throughout the year. The three key considerations are:

- 1 Size of holdings.** EOS take into consideration the aggregate holding size of FHL and EOS clients.
- 2 Materiality of identified ESG and financial risks.** This is assessed by EOS engagers using quantitative and qualitative data sources, including inputs from external providers like Planetrics, NetPurpose, Sustainalytics, MSCI, Trucost, CDP, BoardEx, ISS, FactSet and Bloomberg. EOS also considers the output from our quarterly screening tool, the Controversial Companies Report, which looks at any severe controversies and a number of internal norms and standards including the UN Global Compact Principles and the OECD Guidelines for Multinational Enterprises. It also uses the proprietary ESG Dashboard and QESG score, which captures how a company manages its ESG risks and whether it is improving. All this data is scrutinised by the EOS team, alongside insights from engagement and voting recommendations history, media flow, investment management intelligence, public policy and market best-practice trends.
- 3 Feasibility of engagement.** We endeavour to allocate our engagement resources efficiently and towards companies where we can affect change.

This combination of analysis supports our pursuit of stewardship through our shared service model.

Each company in our core engagement programme is given an appropriate intensity tier, based on the likely impact of engagement and ultimate benefit to the value of the underlying investment. We then assess the required intensity or depth of the engagement needed to resolve the issues:

**Tier 1+** – a small number of companies sometimes termed 'Super Tier 1' companies with material client holdings that have more significant or numerous long-term sustainability or corporate governance issues with the opportunity of feasible engagement and where intense engagement and possibly time spent collaborating with other investors, supported by detailed research, is anticipated to be required in order to achieve material change, with the expectation of approximately eight to ten interactions per year.

**Tier 1** – Companies with material client holdings that have more significant or numerous long-term sustainability or corporate governance issues with the opportunity of feasible engagement and which we consider require more time and effort to progress, including more detailed research, leading to typically more intense engagement, with the expectation of approximately five interactions per year.

**Tier 2** – Companies with material client holdings and identifiable long-term sustainability or corporate governance issues with the opportunity of feasible engagement, which we consider can be meaningfully pursued with average levels of time and effort, with the expectation of approximately three interactions per year.

**Tier 3** – Companies representing significant client holdings which either a) face a particular identified ESG-related risk which can be addressed with limited, targeted engagement; b) companies with generally lower levels of risk to long-term sustainability or which are in the process of being monitored for implementation of the outcomes of previous engagement work. We typically only set one engagement objective, or follow a limited number of engagement issues, rather than specific engagement objectives and plan one or two interactions per year.

There are many companies with whom we engage that sit outside of our core engagement plan. EOS proactively engages with around 1,000 companies annually, of which approximately 550 are held by FHL. Around 350 of the companies which are not in the core engagement programme are selected as EOS engagement targets by our investment teams based again on the size of our holding, the materiality of the issues and the feasibility of engagement. Although these engagement targets are selected by our investment teams, the output of these engagements are also provided to EOS third-party clients. In 2023, the dedicated engagers such as those in our SDG Engagement strategies engaged with a further 42 companies as part of continuous relationship engagement are reported as part of EOS' reporting. The remainder of reported engagements relate to issues around

EOS proactively engages with around

**1,000** companies annually,  
of which approximately  
**550** are held by  
Federated Hermes Limited.



voting at general meetings or are in reaction to events that cannot be predicted in advance. In addition to the above, non-dedicated engagers in our investment teams also conduct engagements with companies directly. These engagements are not reflected in our overall engagement statistics.

In addition, EOS provides voting recommendations for around 13,000 meetings to both FHL and third-party clients, using engagement insights to inform its rationale where possible. Finally, EOS monitors around 23,000 companies held by FHL and third-party clients. Overall, these processes enable us to provide comprehensive stewardship coverage.

The EOS & Responsibility senior leadership team, consisting of the Head of Responsibility, the Head of Stewardship, the Regional Team Leads, the Head of Policy & Integration, the Head of Client Service & Business Development, the Head of Business Management and the Sustainability Director, review and advise on the design and implementation of our Engagement Plan and engagement programme, in addition to our voting recommendations and screening services. It considers engagement quality, continuity, and coverage in the interests of clients.

**Setting engagement objectives:** We set clear and specific objectives within our company engagements to ensure we achieve positive outcomes. An objective is a specific, measurable change defined at the company – an outcome we are seeking to achieve. Each objective is tracked using milestones. Objectives are regularly reviewed until they are completed – when the company has demonstrably implemented the change requested – or discontinued. Objectives may be discontinued if the objective is no longer relevant, or because the engagement is no longer feasible or material.

**Issues:** An issue is a topic we have raised with a company in engagement but, unlike objectives, we do not precisely define the outcome that we are seeking to achieve. This can be more appropriate if the issue is of lower materiality and so we do not anticipate engaging with the frequency required to pursue an objective. Or perhaps we are still in the process of identifying what type of change we may want to see at a company and so are not yet able to set a precise objective. Issues are frequently used for companies outside our continuous engagement programme, for example those where we typically engage only around the annual shareholder meeting and our voting recommendation.

**Measuring progress – Milestones:** Our four-stage milestone system allows us to track the progress of our engagement, relative to the objectives set for each company. When we set an objective at the start of an engagement, we will also identify recognisable milestones that need to be achieved. Progress against these objectives is assessed regularly and evaluated against the original engagement proposal.

**EOS provides voting recommendations for around 13,000 meetings to both FHL and third-party clients, using engagement insights to inform its rationale where possible.**



Figure 35. EOS' proprietary milestone system



Source: FHL, as at 31 December 2023.

In this example, we have applied human and labour rights, which is one of our Engagement Plan social and ethical themes, and focused on the specific supply chain rights sub-theme to set a tailored objective for a European food and drink company. We asked the firm to demonstrate traceability and effective human rights monitoring of its supply chain and detail below how we would recognise progress along our milestone stages:

- **Milestone 1:** Concerns raised at company on the human rights failures in their supply chain management.
- **Milestone 2:** Company acknowledges that its monitoring system should be enhanced and there are lessons to be learnt from the human rights failure in its supply chain.
- **Milestone 3:** Milestone progress made: company establishes a plan to strengthen the whole supply chain, with a clear commitment to transparency when issues arise, key partner assessments and a strengthened audit process.
- **Milestone 4:** Completion – company demonstrates traceability and effective human rights monitoring of 80% of its supply chain, as well as a structured and well-resourced human rights strategy in place.

Our milestones are specific and measurable, which helps us identify progress towards achieving the objective. An engagement objective can take up to three years to complete, depending on factors that include the nature of the issue and how receptive the company is to engagement. Engagement clinics are held with directors to review and challenge engagement strategy and tactics, to ensure that objectives are appropriate and also that milestone progress correctly reflects reality. In some rare instances, we will discontinue engagements on the basis that our engagement efforts have been met with strong resistance or the matter has dissolved.

**Actions:** These are the interactions that take place between our engagement professionals and the companies or public policy bodies with whom they are engaging. Every call, meeting or correspondence is recorded as an action. Actions can be linked to objectives or issues. We only consider companies to be engaged when we have an individual interaction with the company that relates to an objective or issue.

Our approach to climate change engagement is detailed in our [Climate Action Plan](#).

### Private markets

For our private market strategies, engagements are prioritised according to the exposure of the portfolios. For example, in our Direct Lending strategy, the team engages with the sponsor and management team to remedy any ESG issue that arises during the life of a loan. This engagement is conducted in collaboration with EOS, where appropriate, to ensure that the engagement is outcomes-focused and impactful.

### Real Estate

Our real estate business is an industry leader in responsible asset management. The team has developed their ESG framework with principles, commitments and targets. Following growing awareness in the investment industry, we believe that responsible investors need to go beyond standard KPIs and develop qualitative processes to assess the wider socioeconomic impacts of their investment programmes and occupier engagement.

Over the years, the increasing focus on ESG has demanded fresh thinking and new ways of working. The real estate team has been monitoring the sustainability performance of its directly managed assets since 2006 and has annual targets which are monitored and reported against in our public Real Estate ESG report. The team has also created a range of dedicated tools and procedures that cover all aspects of our real-estate operations. Our ESG programme integrates the following procedures and tools:

- Minimum sustainability requirements for refurbishments and developments set out in our internal Design Innovation Standards and Responsible Property Management Refurbishment Guide. These include requirements that construction contractors comply with sustainability guidelines, environmental site-selection requirements, environmental site-development requirements, resilient building design and orientation and minimum requirements on pollution, sustainable materials, waste, energy, water and biodiversity.
- Dedicated ESG guidelines for our directly managed assets, covering the following ESG matters: water efficiency requirements, energy efficiency requirements, energy generation from on-site renewable sources, waste management plans at sites and occupier health and wellbeing requirements.
- Strategic and operational sustainability benchmarking of our real-estate funds.
- Active data management systems for utilities and waste.
- Ongoing monitoring of performance with continuous feedback between property managers, investment managers and sustainability experts.
- Stringent risk and safety requirements and supporting tools.
- Community and occupier engagement tools and programmes.

These tools enable us to assess, monitor and manage social and environmental risks and opportunities in the real-estate portfolio, and therefore informs the objectives of our engagement.

As part of our Real Estate ESG programme, we have been assessing what positive impact investment would mean for each step of our investment process. Our 'impactful intent' approach aims to deepen our ESG practice by intentionally seeking a defined positive environmental or social outcome in a particular place or market as a core focus of our responsible investment strategy, in addition to strong risk-adjusted financial returns. This involves using a purposeful framework to focus our real-estate operations on three specific impactful investment themes. For each of these investment themes, we are committing to activities with measurable environmental, economic and societal outcomes, which ultimately support specific SDG targets. Our impactful investment themes are:

- Meaningful placemaking that creates civic pride;
- Healthy, engaged and productive communities that drive desirable social and environmental outcomes; and
- Climate and resource efficiency and achieving a just transition to a low-carbon, circular economy in order to help prevent further adverse climate change and resource scarcity.



At the heart of our approach is our commitment to creating a 'meaningful city' – or a place that people want to live and work in, and which foster a sense of belonging among inhabitants. Because most of our investment is concentrated in densely populated urban areas, it is inevitable that the way we manage these developments will have a deep, long-lasting effect on the cities and the people that live in them.

Under Principle 4, we describe our real estate team's commitment to net zero and pathway to achieving these goals.

### Infrastructure

Every investment professional in the infrastructure team has responsibility for asset management, albeit with certain professionals being primarily focussed on this area. The asset management team for each investment is responsible for the ongoing monitoring of the investment including annual strategic reviews, the semi-annual valuation process and investor reporting, and engagement at the portfolio company-level, for example through Board representation on operating or holding companies, as applicable.

Our principal asset management purpose is to generate long-term, sustainable and mandate compliant returns for our investors. We have a mature framework in place which creates the environment to achieve this purpose. Below is an infographic version of this approach.

Post initial acquisition, annual strategic reviews, undertaken in Q1 each year, provide a status update of each investment, investment performance to date, key valuation metrics and outlook, and key risks and opportunities, informing our strategy at asset and at portfolio-level. Strategic reviews incorporate an assessment of sustainability risks, opportunities and impacts.

**Strategic reviews incorporate an assessment of sustainability risks, opportunities and impacts.**



Targeted asset and portfolio level objectives are developed in an integrated nature with sustainability, through our detailed Asset Management sustainability guidance document, which is aligned with the EOS stewardship model building blocks. Objectives will either relate to specific financial/commercial areas (where success is often based on having completed the objective), or sustainability, where we apply an EOS-informed milestone approach with the aim of seeking continuous improvement.

Progress against objectives is subject to semi-annual reviews. Day-to-day financial and operational performance is monitored, analysed and then reported through an internal monthly flash report, which is reviewed by the Infrastructure Investment Committee. We produce quarterly reporting, in line with IILPA guidelines, to investors in line with our valuations process. In addition, we hold an AGM to provide a detailed overview of the full-year performance and outlook across the portfolio. We produce annual sustainability reporting that includes performance against sustainability KPIs. Performance against engagement objectives is reported to investors in our quarterly reports.

Figure 36. Infrastructure asset management approach



Source: FHL, as at 31 December 2023.

From a thematic perspective, climate change and emission reductions are currently our number one sustainability engagement priority with infrastructure portfolio companies. The climate crisis, manifested through the increasing frequency of extreme climate events, necessitates a strong and continued focus to reduce business carbon footprint and manage climate risk and opportunity at Board level, which given our strong governance rights and active engagement approach, we are able to influence. The infrastructure team has set an objective for all portfolio companies to put in place Paris-aligned targets (aligned with a pathway that limits temperature increase to 1.5°C) by 2025, in line with the Paris-alignment approach described under Principle 4.

Pollution and waste from operations, supply chains or products are inconsistent with a sustainable business model in infrastructure. Shifting to circular business models and a proactive approach to natural resource conservation and management are central to futureproofing businesses and protecting the environment. This is an important engagement priority for our infrastructure team.

Infrastructure often involves heavy industry and potentially dangerous activity meaning occupational health, safety and wellbeing is always of primary importance. We also encourage active promotion of all facets of physical and mental wellbeing, as drivers of overall health, happiness and productivity.

We promote diversity, equity and inclusion (DE&I) strategies, actions and advocacy covering closing pay gaps, representation of all elements of diversity at all levels of an organisation and the creation of an inclusive workplace. DEI strategies should include relevant targets, dedicated resources, implementation, monitoring, metric reporting and continuous effectiveness assessment and improvement.

We are also continually conscious of the public service nature of infrastructure investments; the need to maintain our social licence to operate in a variety of ways; and the importance of maintaining a reputation as a force for good to both the businesses we invest in and our investors.

## Private equity

We seek to improve and protect the financial value of investments through assessing, monitoring and seeking improvements to material ESG risk areas. Our private equity team takes a risk-based approach to effectively identify, monitor and manage ESG risks, opportunities and impacts identified across its portfolio. For direct co-investments, we receive quarterly reports from the GP that include both financial information and qualitative data. These reports often contain ESG information. In addition to this, we often have a follow up call with the GP where we discuss the reports and any other topics we wish to raise. For fund investments we also receive quarterly reports and are invited to participate in AGMs. In a minority of cases, we are part of the limited partner advisory committee (LPAC) and hence part of the fund's governance structure. Engagement objectives are focused on the assets with higher identified ESG risks.

## How we engage

Our public markets dialogue with investee companies is primarily conducted through in-person meetings, calls, letters or emails, either directly or as part of a collaborative group. The nature and frequency of the dialogue depends on the location of the company, stage of engagement, severity of the issue and willingness of the company to engage. As evidenced by research, effective engagement that delivers value, demands a specific skill set that goes far beyond written activity or interaction with lower-level company representatives. Change is brought about by access at the board level gained by engagement professionals who have industry or professional experience, gravitas and specialist skills at challenging senior decision makers.<sup>50</sup> The majority of our dialogues are conducted with the board of directors (primarily the chair, lead independent director and chairs of board committees), corporate secretary, subject specialists or investor relations. Occasionally the dialogue is with executive teams, although only where we believe the concern justifies their time and attention.

**Figure 37.** Number of companies engaged at board/senior level in public markets

**We have engaged 304 companies at board/senior management level,<sup>51</sup> including:**

Senior management	
CEO	58
Chair	22
Company secretary	75
Executive management team	38
Head of Sustainability	52
Other board director	19
Other company executive	40

Source: FHL, as at 31 December 2023.

We use our own relationships to initiate and progress engagements in the majority of cases, whether this is through the investment teams or EOS, in addition to attending meetings facilitated by intermediaries. Most public-markets engagements are carried out by EOS, who may be joined by relevant portfolio managers or analysts from our investment teams. The investment teams also carry out engagements themselves, although these are only reported if conducted by dedicated engagement staff. The Responsibility Office ensures that our investment teams and EOS work closely together with a joined-up approach.

Making realistic and realisable demands of companies, informed by hands-on experience of business management and strategy setting, is critical to the success of our engagements. With all engagements, we seek to build a strong relationship with the company and are willing to be patient, remaining focused on achieving goals which are directed towards long-term success. Our proprietary systems

<sup>50</sup> FHL, 'New research shows the importance of board', (September 2017).

<sup>51</sup> Individual companies may be engaged at multiple levels of board or senior management.

enable us to track progress against specific objectives and remain outcomes-focused throughout the duration of our engagement with a company. We have invested in the underlying systems in which we capture, measure, manage and then express our stewardship activity and outcomes. Not only can our engagement professionals better capture their progress, momentum, challenges and next steps and general workflow, but our clients are able to absorb the information in ways and through lenses that suit them.

**Geographies:** There are some nuances in how we engage with each market. EOS has developed regional voting guidelines and policies which set out our fundamental expectations of the companies we invest in across a number of important ESG topics. This regional approach reflects the variations in the markets in which the companies we invest in operate. They also inform EOS' Global Voting Guidelines and FHL's Global Voting Policy and Guidelines. Together these guide EOS' voting recommendations and our investment teams' voting decisions for listed equities. EOS has intentionally built a diverse team of experienced and international voting and engagement professionals who have the expertise, language skills and cultural knowledge to work to deliver real beneficial change at companies. Our ability to engage in the local language and understanding of local culture and business practice are critical to the success of our engagement work. Within our team, we have nationals from 16 countries who are fluent in 20 languages.

**Figure 38.** 2023 Engagement activity<sup>52</sup>

Theme	Issues and objectives engaged
Environmental	831
Social and Ethical	698
Governance	721
Strategy, Risk and Communication	335
<b>Total</b>	<b>2,585</b>

Source: FHL, as at 31 December 2023.

We engaged with 549 individual investee companies, some of which were engaged on one or more themes.

**Figure 39.** Engagement by region in 2023

Region	Companies engaged	Issues and objectives engaged
Australia & New Zealand	23	87
Developed Asia	63	290
Emerging & Developing Markets	81	362
Europe	117	516
North America	234	1,178
United Kingdom	31	152
<b>Total</b>	<b>549</b>	<b>2,585</b>

Source: FHL, as at 31 December 2023.

**Equity vs. Credit:** Both equity and bond holders have a shared interest in sustainable growth, increasing enterprise value and the long-term health of companies. EOS' breadth of engagement allows us to engage with companies on behalf of equity and bondholders. We believe that engaging simultaneously on equity and credit creates a common long-term voice, increases access and influence and shared resourcing to pool the priorities of like-minded investors. In a two-part paper over 2018-19, we explained why we believe the shared interests of bondholders and shareholders provide incentives to jointly engage companies – and generate positive outcomes by doing so.

Where there are rare conflicts such as when a company is failing, and its very survival is in doubt, the interests of bond and shareholders can diverge as they compete over what remains for investors. We have established a Stewardship Conflicts of Interest Policy to follow in such rare situations, as described under Principle 3. If a potential conflict of interest is identified, the issue is escalated first to a line manager and then to the escalation group if the conflict cannot be resolved. If a potential conflict materialises, the joint equity-credit engagement is restricted to those objectives that are not affected.

As shareholders and creditors are both financial stakeholders, they share a common basis to engage in constructive dialogue with companies. However, as creditors serve as a recurring source of cash to a company, they have a different kind of influence. This influence varies even within fixed income. For example, for smaller companies in leveraged finance or direct lending, the disintermediation of capital is spread over a smaller investor base. This means these investors may have greater influence versus any individual investor in a large-cap name. When engaging as bondholders, we may be able to use other routes to the company such as the Chief Financial Officer or treasury department, or as part of bond roadshows, which are typically more frequent than equity issuance. Also, we may encourage companies to issue green and sustainability-labelled bonds to encourage clearer sustainability frameworks and reporting, and, in cases where companies issue such bonds, we may engage on the validity of any sustainability claims made. Moreover, we are seeing an increasing number of leveraged buyout deals being funded with green and sustainable bonds, and, in such cases, we may engage with private equity sponsors.

Engaging on derivatives in credit portfolios is done in the same way as we engage with equities and bonds; we engage with the underlying issuer. Engaging on sovereign bonds poses a particular challenge, as there is often a shortage of relevant data and little accessibility. However, we use what data we do have to assess ESG risks and their potential impact on the sovereign's ability and willingness to meet financial obligations. Momentum is building across the investment industry to improve the availability of data and engagement within this asset class.

<sup>52</sup> We engaged with 578 individual companies, some of which were engaged on one or more themes.

<sup>53</sup> FHL, 'We can all get along', (September 2018); FHL, 'We can all get along: Part II', (June 2019).



## Tencent



**Tencent Holdings Ltd. engages in the provision of value-added services and online advertising services. This includes online and mobile games, applications across various internet and mobile platforms, display- and performance-based advertisements, and software development to name a few.**

Given the company's business model is centred around digital-based services with a varied and wide-ranging customer base, we engaged to ensure the company had sufficient policies and principles in place that would safeguard consumers and guide the ethical use of artificial intelligence (AI).

### Our engagement

We first began engagement in January 2019, when we met with the company and encouraged it to disclose its consideration of business ethics, including AI ethics, in its next ESG report. Over the course of 2020, we engaged in a deeper discussion on data privacy. Although security by design and privacy by design are principles highlighted by the company in its disclosure, we recommended a more elaborate description of the process, citing reports of inappropriate surveillance of WeChat accounts registered to foreign users.<sup>54</sup>

In May 2023, we engaged the company in response to a Sustainalytics report alleging a breach of UN Global Compact Principle Two<sup>55</sup> related to content moderation and

sharing of user data with the Chinese government. We also raised concerns with the company's low score on Ranking Digital Rights, an NGO that benchmarks the world's largest tech companies on digital rights issues. We further encouraged the company to add a commitment to user consent to its privacy policies and terms and conditions and shared specific suggestions on making these documents easier to read and understand for its users.

### Engagement outcomes

In 2023, the company released and executed its AI Data Security Management Policy, which mandates key principles for all aspects of AI data handling, including data minimisation, legal compliance, and data categorisation. The policy mandates that all businesses strictly adhere to the principles, and is guided by the four principles of availability, reliability, comprehensibility, and controllability.

EOS was subsequently notified that the company's Sustainalytics ESG risk rating was upgraded from "Medium Risk" to "Low Risk." The upgrade acknowledged the company's progress in establishing a Personal Information Protection and Data Compliance Management Taskforce; collecting user data for only stated purposes and notifying users of any substantial policy changes or data breaches; and conducting Privacy Impact Assessments of products and services regularly. The full case study is available on our website.

<sup>54</sup> The Citizen Lab, 'We Chat, They Watch: How International Users Unwittingly Build up WeChat's Chinese Censorship Apparatus' (May 2020).

<sup>55</sup> Principle Two of the UN Global Compact is Human Rights. Businesses should make sure that they are not complicit in human right abuses.

Within private markets, our real estate team has an extensive community and occupier engagement programme across our retail and office assets that focuses on governance, skills, safety, health and wellbeing. Retail and office assets represent, on average, about 50-60% of our direct investment, depending on the fund. We aim to positively impact the health and wellbeing of our occupiers and local communities by establishing a constructive dialogue through a range of activities carried out during the life cycle of real estate assets, including: development and refurbishment; asset management; actively managing wellbeing initiatives; targeting greater occupier engagement; wellbeing and comfort; as well as:

- **Attaining wellbeing certification:** in 2023, we continued to maintain our BREEAM in-use coverage. This certification adds value to our assets demonstrating that they are run in a sustainable manner, ensuring that occupiers benefit from reduced utility costs from occupying space in an efficient building and showcasing environmental improvements over time for an asset. In total, we obtained 42 BREEAM in-use certifications and 7 Fitwel certificates. Additionally, three NABERS pioneer projects were delivered, demonstrating the potential for energy efficiency of new builds with 11/12 Wellington Place becoming the first 5-star certification outside London.
- **Participating or supporting initiatives that promote wellbeing among occupiers and communities:** we have addressed sustainable transport, healthy living among occupiers and community health, and have implemented measures in line with the UK Modern Slavery Act through our activities and supply chain.
- The team have also engaged with all occupiers during lease negotiations, with the intention of including sustainability clauses in all lease agreements.

We have continued to focus on reducing the carbon footprint and energy use of our real estate portfolios in 2023 and increase the energy efficiency of our assets.

We have progressed our work on social value by analysing local needs at a range of different assets and identify where targeted improvements could be made. Furthermore, we manage our community engagement programme through our property managers and have established a stakeholder engagement plan, which provides support to our property managers, sets minimum requirements, and facilitates additional community engagement activities. Moving forward, the Real Estate ESG team will place an increased emphasis on occupier engagement.

It is naturally more challenging to engage with occupiers within the industrial and retail sectors, given the type of leases and structure of their activities. The full repairing and insuring (FRI) lease structure common in these types of assets offers the occupiers complete autonomy in how they manage and maintain the building and carry out procurement activities. This means that obtaining data and encouraging sustainable procurement choices can be challenging. In our indirect funds, the managing partners engage with the occupiers.

Meaningful cities provide a well-functioning backdrop that allows citizens to participate freely in social, economic, leisure and community-based activities. Cities designed around such holistic principles create a virtuous cycle, benefiting individuals,

communities, businesses, and local and regional government authorities, while helping to preserve natural capital and ensuring the historic continuity of built environments. In turn, meaningful cities can likely sustain higher economic growth by attracting and retaining talent and capital, which provides a better return on capital for investors: a true win-win.

**For our direct lending and real estate debt teams,** the key is to identify both current and potential meaningful ESG risks before investing. Due to the difficulty of divesting these illiquid investments at par prior to maturity, it is important to manage the downside ex ante. Because of a lack of market benchmarks, the teams often use more qualitative information – often gained through dialogue with the borrower – as well as information contained in the due diligence packs. The teams collaborate with EOS, where appropriate, to ensure that their engagement is outcomes focused and impactful.

Following the completion of an investment in the Direct Lending funds, ESG risks – like all credit risks – are monitored. Should an ESG issue arise during the life of the investment, the Direct Lending team will seek to engage with the sponsor and management of the borrower to rectify or improve the ESG issue.

We include information requirements in all of our real estate debt loan documentation to ensure that the borrower passes on the relevant ESG information to us, which we use to monitor ESG in our investments. Many of our real estate debt loans support assets where a wider impact is delivered, such as refurbishments and regeneration. These factors are a strong consideration before investments are made, as are risks posed by ESG factors. As with our direct lending investments, the key is to identify risks that may impact on a borrower's ability to repay their loan. We also intend to engage with the borrower where additional ESG issues arise during the life of the loan.





**For our infrastructure team**, superior investment performance, for the benefit of all stakeholders, begins with best-in-class governance, where transparency of information, clear lines of responsibility, accountability and appropriate management of conflicts are paramount.

We encourage the integration by management teams of sustainability considerations into companies' governance structures, strategies and risk registers in the belief this will have a catalysing and disproportionate positive impact on a company's long-term sustainability.

As an active investor, we engage directly with companies, at all levels, on a range of issues whilst maintaining an appropriate level of executive accountability. We set engagement priorities annually in an integrated approach with wider non-sustainability objectives. Priorities are guided by the use of the EOS stewardship model. This provides the framework on which asset teams will develop priority areas, focusing on the parts of the model deemed most material to the particular asset. Progress against engagement priorities is reviewed twice annually.

**In private equity**, for a small proportion of our assets where the team have some control and/or the ability to influence company decisions directly, we seek to work closely with investee companies to monitor, challenge and improve ESG performance. We engage with the lead GP and management team on a regular cadence (quarterly or yearly, depending on the severity of the risk) to monitor the risk and engage on potential outcomes. Engagement objectives are focused on the assets with higher identified ESG risks.

However, in almost all cases our team has limited control and/or ability to influence decisions directly (whether for direct or indirect co-investments). In these instances, the team will work closely with the lead GPs to assess, monitor, and seek to

improve ESG performance of the underlying investee companies. Where we believe there are significant ESG risks we will ask the lead GP to address these. Whilst we have no formal rights in this situation and the assets are illiquid, we seek to leverage on our relationship with the GP to have a constructive discussion. The GP would then typically engage with the company management. We only invest with active GPs who are very closely involved with the investee companies and in regular contact, and as set out under Principle 7 ESG considerations are factored into the GP selection process.

## Outcomes of engagement in 2023

### Public markets

Through stewardship activities, led by EOS, we engaged with 549 of our public markets' holdings in 2023, covering 2,585 identified objectives or issues. We made progress on 54% of all objectives related to our holdings, which equated to 81% of our equity and credit AUM (the same as we reported in 2022).<sup>56</sup>

**Figure 40.** Fund level engagement coverage for pooled equity funds during 2023<sup>57</sup>

Fund name	% AUM Engaged in 2023
Federated Hermes Absolute Return Credit Fund	78%
Federated Hermes Asia Ex-Japan Equity Fund	82%
Federated Hermes Biodiversity Equity Fund	76%
Federated Hermes China Equity Fund	51%
Federated Hermes Climate Change High Yield Credit Fund	77%
Federated Hermes Emerging Asia Equity Fund	30%
Federated Hermes Emerging Markets Debt Fund	8%
Federated Hermes Global Emerging Markets Equity Fund	78%
Federated Hermes Global Emerging Markets ex-China Equity Fund	74%
Federated Hermes Global Emerging Markets SMID Equity Fund	56%
Federated Hermes Global Equity ESG Fund	88%
Federated Hermes Global High Yield Credit Fund	80%
Federated Hermes Global Small Cap Equity Fund	78%
Federated Hermes Impact Opportunities Equity Fund	75%
Federated Hermes Multi-Strategy Credit Fund	79%
Federated Hermes SDG Engagement Equity Fund	100%
Federated Hermes SDG Engagement High Yield Credit Fund <sup>58</sup>	100%
Federated Hermes Sustainable Global Equity Fund	92%
Federated Hermes Unconstrained Credit Fund	78%
Federated Hermes US High Yield Credit Fund	36%
Federated Hermes US SMID Equity Fund	75%

Source: FHL, as at 31 December 2023. To note, the Federated Hermes Sustainable Global Investment Grade Credit Fund is excluded from this chart as it was launched during 2023 and therefore, has insufficient engagement data.

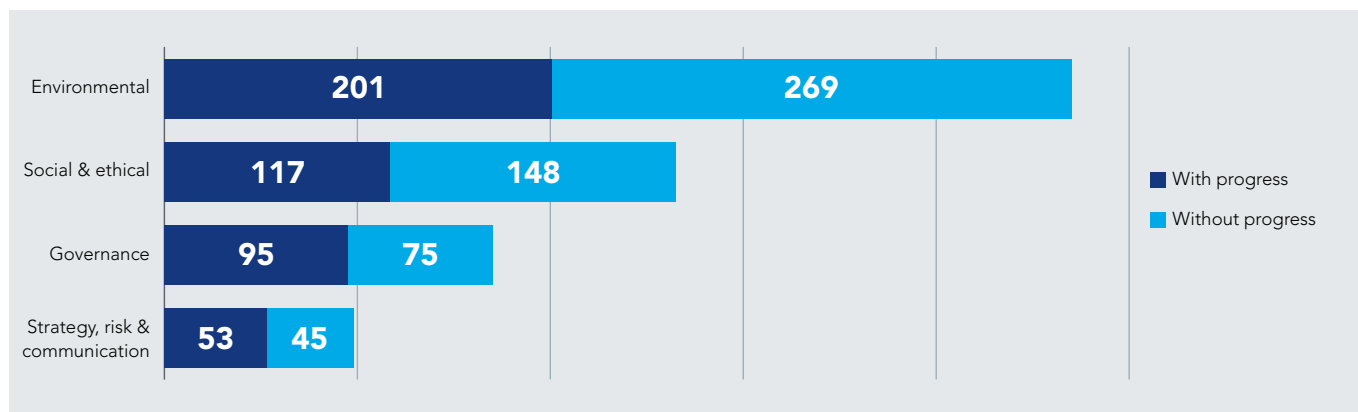
<sup>56</sup> Our AUM here includes equities, warrants and bonds, as well as single name credit default swaps that give the firm long exposure to the underlying instrument and its associated company. Other derivatives, cash, index and government instruments are excluded.

<sup>57</sup> This table covers those funds which were launched prior to 2023 and for which data for the whole year is therefore available.

<sup>58</sup> 4% of the portfolio was not engaged due to an investment decision to remove one of the holdings from the portfolio.



Figure 41. Progress made on our engagement objectives by theme in 2023



Source: FHL, as at 31 December 2023.

We publish case studies throughout the year on our website to demonstrate the approach we take and the outcomes of our engagement. EOS case studies are fact checked by the engagement companies and published on the [EOS Insights website page](#).

🔍 CASE STUDY

## Delta Electronics

**Delta Electronics, Inc. is a Taiwanese company providing power and thermal management solutions, with a mission statement “to provide innovative, clean and energy-efficient solutions for a better tomorrow.” As an energy-saving solutions provider with core competencies in power electronics and automation, Delta’s products are integral to many renewable energy and energy-saving technologies.**

Delta Electronics was one of the first 100 companies globally to commit to the Science Based Targets initiative (SBTi) and to achieve validation of its Paris-aligned targets. In order to help achieve its ambitions, the company established an internal carbon pricing (ICP) mechanism in 2021. This mechanism involves attributing a cost of 300 US dollars per tonne of carbon emitted by each business division, thereby incentivising emissions reductions and also raising funds to support emissions reductions elsewhere in the business. While we welcomed this development, we said to the company on a call in November 2021 that we expected to see a more comprehensive explanation of how the mechanism worked and is implemented.

The company’s 2021 ESG report, published in August 2022, explained that internally generated funds from the ICP mechanism are directed to energy and resource management, development of renewable electricity and renewable energy technology and low-carbon innovations. However, we felt that the company needed to provide more information on how the mechanism operates in order for investors to have confidence that it is effective. We explained this on a call in May 2023 and the company indicated that it would look to provide greater detail in its upcoming ESG report.



Delta Electronics’ 2022 ESG report, published in August 2023, contained significant new information on how its ICP mechanism helps it to achieve its climate ambitions. It quantified funds raised by the mechanism (120 million US dollars in 2022) and explained that the carbon fee charged by the mechanism is regarded as one of the costs in monthly financial management reports and is related to key performance indicators of business group heads. The report also highlights that one use of the mechanism is to help fund a transition to electric vehicles, in line with Delta Electronics’ commitment to using only zero-emission company vehicles by 2030.

We will continue to engage with Delta Electronics on the implementation of its net zero strategy, managing risks in its supply chain and its approach to biodiversity.

 CASE STUDY

## SDG Engagement Equity Strategy – Glanbia



**Once again, this global sports nutrition and food ingredients company was among the team's most engaged holdings during 2023 with seven engagement actions in the year and over 40 since inception of the strategy at the beginning of 2018.**

The team's engagement focus with Glanbia has for some time been directed towards its upstream dairy supply chain and their ability to work with their suppliers to reduce emissions in this part of their value chain – these emissions represent c.90% of their total emissions footprint.

The company set Science Based Targets in 2021 which include a 31% absolute reduction in scope 1 and 2 greenhouse gas (GHG) emissions by 2030 as well as a 25% reduction in scope 3 GHG emissions from purchased goods and services of 25% per tonne of dairy product produced. The team have continued to engage with Glanbia on this topic as well as engaging with the wider industry given the need for all parties in the value chain to move in lock-step in order for progress to be realised. To this end, the team's lead engager was invited to speak at the International Dairy Federation Global Summit in October 2023. The team took this opportunity to emphasise how the pace of emissions reduction technology adoption needs to accelerate and public commitments and transparency around progress towards such targets needs to be provided across the value chain. This presentation was well received and pleasingly Glanbia were able to confirm to the team that they have mapped 100% of their supplier farms and have developed a roadmap with their suppliers to realise the necessary reductions in emissions.

 CASE STUDY

## SDG Engagement Equity Strategy – Techtronic Industries

**This Hong Kong listed power tools company was the strategy's most engaged holding during 2023, clocking up nine engagement actions.**

The team's engagement focus in the early years of the strategy was focused on the company's cobalt supply chain. The company responded positively and swiftly to this engagement and established a detailed and granular cobalt sourcing policy and process. As a result, the engagement focus has pivoted towards the company's wider production processes and their ability to expand their remanufactured product offering.

In 2023, the company was the subject of allegations of forced labour within its protective gloves supply chain which reached the attention of US Congress during the summer. The company was able to confirm to the team that both the company and its primary customer had investigated these allegations immediately. The company visited its supplier factories and tested the cotton in its products in order to identify the region of origination. Both the company and their principal customer reached the conclusion that the products which were the cause of the allegations were most likely counterfeit products. Nonetheless, the focus on this aspect of its supply chain has triggered the company to adopt a more prudent approach and it has in turn changed its supplier and shifted production out of China.



On the topic of product circularity, their approach to enabling one battery to be used across multiple products in a range avoids unnecessary product obsolescence and waste generation. Nonetheless, with tens of millions of their products and batteries being sold, the team's estimate (based on figures in their 2022 ARA<sup>59</sup>) of 500-600k batteries recycled and products remanufactured per annum is a small percentage of that total. Positively, the vast majority of the battery packs on their tools are already recyclable and the company has confirmed that they expect the size of the remanufactured business to continue growing. Further engagement on this theme is expected through 2024 as the company also looks to establish targets for its scope 3 emissions.

<sup>59</sup> Techtronics Industries, 'Annual Report 2022'.

In some instances, we will discontinue engagements on the basis that our efforts have been met with strong resistance, or the matter is no longer relevant. The following are reasons an objective may be discontinued:

- **Company unresponsive:** the company has not been responsive to our engagement, and we do not believe it worthwhile to dedicate further stewardship resource, having considered the effort required to achieve change, the probability of achieving change and the materiality of the issue.
- **Company disagreed:** the company has expressed its disagreement with our engagement proposals, and we do not believe it worthwhile to dedicate further stewardship resource, having considered the effort required to achieve change, the probability of achieving change and the materiality of the issue.
- **No longer relevant/material:** the original objective is no longer considered sufficiently material or relevant. This could be due to a change in the company's business profile (such as divestment of a business unit of concern) or if engagement reveals that the original concern is of lower materiality than originally anticipated.
- **Restarted as new objective/issue:** engagement reveals that the original objective should be materially changed – for example, split into two separate and related objectives or combined with another objective.

Providing explanations for scenarios where engagement has stalled – that is, in instances where engagement is moving slowly, or a company refuses to make changes – is more challenging because we conduct the majority of our engagements behind closed doors. We are mindful of the relationships we have built with companies, as well as our future engagements with them. For these reasons, we provide anonymised case study examples.



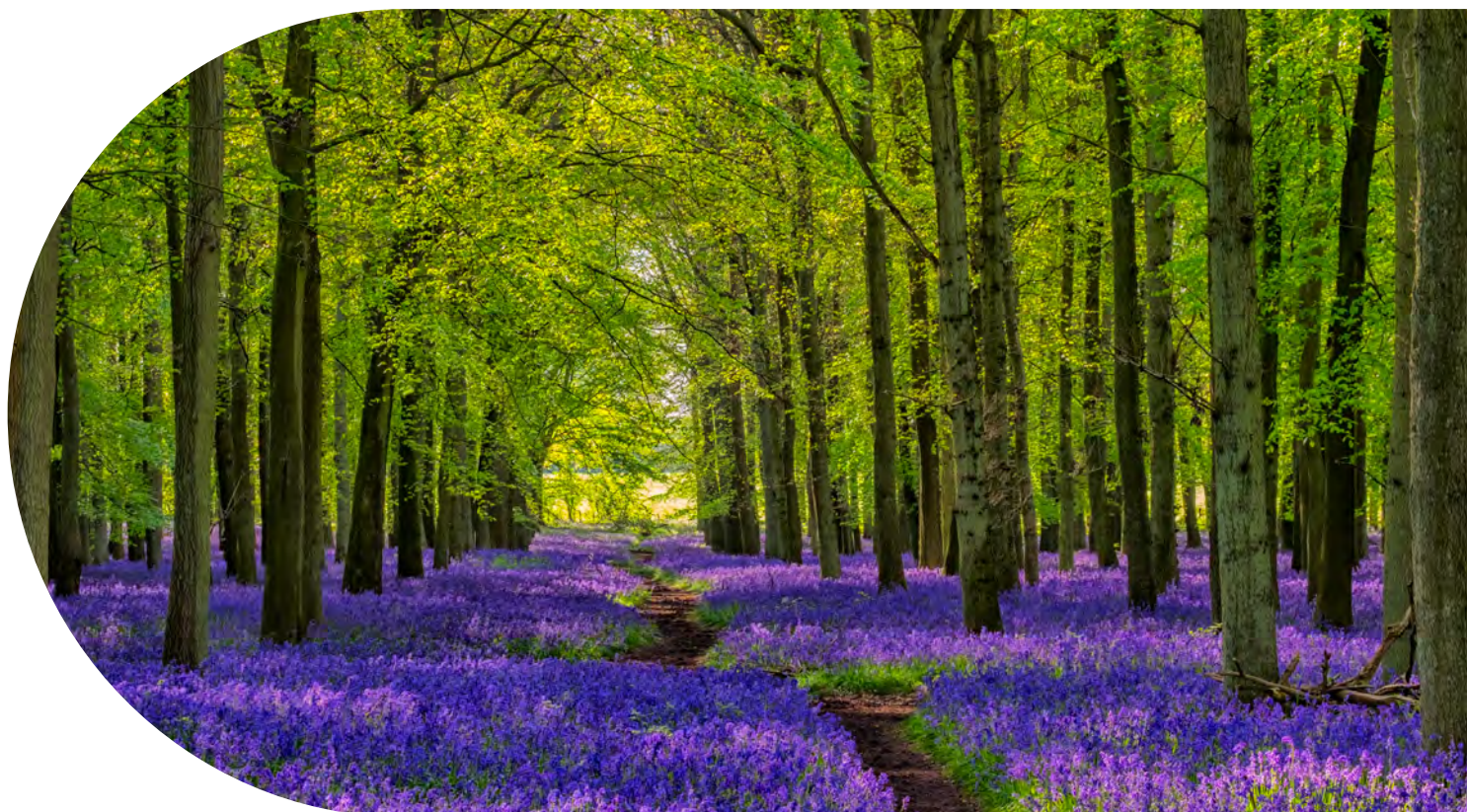
#### CASE STUDY:

### Discontinued objective, auditor rotation



We engaged with a company in the aftermath of a safety scandal. We made several recommendations to improve governance including auditor rotation. The company has used the same auditor since 1934. We believe audit independence and audit quality is at risk when the same assurance provider is maintained for too long, and the safety scandal constituted a material oversight that should have been subject to greater auditor scrutiny. We recommended auditor rotation during the 2020, 2021, and 2022 annual meetings.

Ahead of the 2023 annual meeting, the company shared that it has close to zero appetite for auditor rotation. The company said it is the only US firm that uses a complex form of programme accounting and believes the practical impact of auditor rotation would be unnecessarily costly. In 2023, we explained in a letter to the board that EOS recommended votes against the ratification of the auditor and the audit committee chair, consistent with our policy to oppose auditors that have been in place for more than 20 years. However, as there has been no indication of positive momentum on this issue, we have discontinued our engagement.





## Private markets

### Real Estate

Our real estate team publishes an annual ESG report, which publicly discloses environmental and social outcomes for our real estate funds. Through our placemaking activities, we have created significant social and economic growth in a number of our real estate construction projects. This has been achieved through generating construction jobs, apprenticeships and local supply chain spending. As we expand our reporting to cover the eight social hubs identified for real estate placemaking initiatives, we have developed a comparative framework which enables us to clearly measure and analyse the positive impact that investment has on social infrastructure. This work will focus on different types of operational assets within our portfolio in a range of locations. We have continued to work with Social Value Portal to develop our understanding of the social capital generated by our placemaking schemes in Leeds and Manchester.

**Figure 42.** Real Estate 2023 GRESB scores

Fund	Star Rating		GRESB Rating		Peer Ranking	
	2022	2023	2022	2023	2022	2023
BTPS Direct Real Estate Portfolio	4	4	85	85	1	1
BTPS Developments	4	4	89	96	5	3
Federated Hermes Property Unit Trust (FHPUT)	3	2	77	75	15	53
Hermes Central London (HCLLP)	5	4	88	85	3	4
Metro Property Unit Trust (MetroPUT)	2	3	72	76	5	3
Centre:MK	5	5	90	92	1	1
Hestia (UK residential)	4	5	85	89	3	2
Paradise	3	4	75	82	7	6
Paradise Developments	3	4	82	92	7	5
NOMA	2	3	71	76	9	9
NOMA Developments	5	5	99	100	2	1
Wellington Place	5	5	90	92	1	1
Wellington Place Developments	5	5	99	100	1	1
Silverstone Park	2	2	67	69	5	3
Silverstone Park Developments	2	2	67	84	5	9
Milton Park	2	2	68	71	4	5
Milton Park Developments	2	4	81	92	8	5

Source: FHL, as at 31 December 2023.

**GRESB:** GRESB – the global real-estate sustainability benchmark for real assets – is an investor-driven global sustainability benchmark and reporting framework for listed property companies, private property funds, developers and investors that invest directly in real estate.

The assessment is shaped by what investors and the industry consider to be material issues in the sustainability performance of real estate investments. Scoring covers seven areas: management, policy and disclosure, risks and opportunities, monitoring and environmental management systems, performance indicators, building certifications and stakeholder engagement.

The real estate team continued to support the GRESB benchmark in 2023, submitting 11 funds for assessment. The progress that FHL has made in its drive towards ESG integration into fund delivery was recognised with maximum scores achieved for the management section in both standing investments and developments.

Whilst the majority of funds maintained or increased their performance scores, two funds experienced a slight drop in score due to increased utility use and waste production, the cause of which has been determined to be the Covid-19 lockdown data (2021) being compared to a higher occupancy years data (2022) and the two funds having high levels of exposure to retail occupiers, particularly in the food and beverage sector.

All funds outperformed their peer groups demonstrating that the above issues are industry wide. The emphasis placed on developing highly sustainable assets was recognised with Wellington Place and NOMA developments achieving maximum points and first in their peer groups.

## The success of our real estate ESG approach can be seen in the certifications that our properties receive.

In the overall ratings, our standing investments Centre:MK, Hestia, NOMA, and Wellington Place all achieved a 5-star rating, whilst for developments, BTPS, NOMA and Wellington Place also achieved a 5-star rating. The recognition further exemplifies our commitment to creating community-engaged spaces and our ongoing pursuit achieving net zero.

The success of our real estate ESG approach can also be seen in the certifications that our properties receive. We have maintained our certifications in 2023 with 19 recertification submissions made in the last 12 months. The recertification demonstrates the sustainable credentials of an asset and exhibits the progress assets are making in supporting the environment and society in which they are positioned.

Information on our wellbeing certifications can be found earlier in this section.



### Promoting Social Inclusion in Leeds

**Wellington Place in Leeds has been transformed into one of the UK’s most successful city-centre regeneration projects.**

From educational partnerships focused on social mobility to a year-round programme of participatory events, the development is bringing people together in meaningful ways.

Since 2018, we have collaborated with the Ahead Partnership to engage students from across Leeds that face barriers, disadvantage and under-representation.

We aim to show students the varied career opportunities available at Wellington Place, showcasing the innovative environment and encouraging them to start thinking about their own future careers.

The schools we work with have been specially selected to achieve maximum social impact, with a higher than national average percentage of students eligible for free school meals, and/or a high percentage of students with English as an additional language. Feedback from students who took part in our 2022 Wellington Place events programme was:

- **100%** said it improved their understanding of different careers
- **82%** said it helped them think about their own career goals
- **98%** said it increased their confidence Assessing Social and Local Economic Value

### Assessing the local economic value

In partnership with Social Value Portal, we assessed the social value contribution being generated at Wellington Place between 2019-2022 to help create a baseline and inform future strategy. Our research showed that during this time, the development had:

- created over 1,500 jobs facilitated nearly 600 volunteering hours
- provided nearly 270 apprenticeship weeks
- generated over £5,000 in charity donations
- planted 2,000 trees in Leeds

This contributed towards an estimated social value of £339,370 and a local economic value of £44,172,288. These figures reflect the benefits Wellington Place delivers to society and environment beyond regulatory compliance and business-as-usual activity.



### Engaging purposefully with our occupiers

Source: Milton Parkl

**At Milton Park, a science and technology park in Oxfordshire, The Greener Workplace Forum is engaging the development’s 250+ occupiers on a range of sustainability topics.**

The Forum enables businesses operating in Milton Park to work collaboratively – sharing best practice, innovation and sustainability challenges – with the aim of reducing emissions and waste, increasing recycling, enhancing biodiversity and making a positive impact on local communities and the environment. The group’s achievements to date include a shift in single-occupancy private car use towards more sustainable modes of travel, with cycling up 4% in 2022 and bus use doubling in the last two years. Collaborative lobbying has also led to improvements to local cycling infrastructure and bus services, as well as the purchase and installation of a polystyrene compactor to improve on-site segregation of waste.

## Infrastructure

At a number of our portfolio companies, our roles at board and committee level have enabled us to successfully collaborate and influence sustainability strategy and go on to approve matters related to the strategy's implementation.

Owing to our engagement approach and nature of the asset class, we have a significant number of day-to-day engagements. We choose to monitor number and quality of engagements on a sample basis, using a single quarter of the

year. For 2022 we recorded engagements for Q4. In Q4 2022, we recorded 50 sustainability-related engagements. Of these, 44% were direct engagements with investee company management teams. The other engagements were mainly with co-shareholders, Board Committees and industry associations. In terms of theme, 42% of engagements were related to climate change, 21% focused on health, safety and wellbeing and 13% on diversity and inclusion. At time of finalising this report, Q4 2023 statistics were in the process of being compiled.



### INFRASTRUCTURE CASE STUDY

## Scandlines

**The global ferry industry – both passenger and freight – has seen a steady rise in demand over the last few years.<sup>60</sup> However, any efforts to expand capacity also present a conundrum as companies across the maritime transport industry seek to reduce their carbon footprint.**

In 2021, Nordic ferry group Scandlines – which is co-owned by FHL – was looking to increase the size of its fleet by acquiring second-hand tonnage ships. But the group was unable to source vessels with the right specifications or environmental profile. Scandlines operates one of the world's largest diesel-electric hybrid fleets and launched its first hybrid ferry in 2013.<sup>61</sup>

The group embarked on an innovative solution and two years on it is completing the construction of one of the world's first electric freight ferries. The new ferry (PR24) will produce zero direct emissions and is due to begin operating on the busy sea corridor between Puttgarden in Germany and Rødby in Denmark in H2 2024.

PR24 requires 25% less energy to operate relative to the company's existing fleet on the route. It boasts the world's largest battery bank to date and can be recharged in 12 minutes. With a capacity of 66 freight units, PR24 will boost the current capacity on the route by up to 23%, helping to meet the rising demand for freight services.

### Climate-neutral shipping

The construction of the vessel marks a turning point for the shipping industry, paving the way for climate-neutral shipping. "This development is proof that even larger ships can sail completely without greenhouse gas and air pollutant emissions today," says Sönke Diesener, a shipping expert at the German Nature and Biodiversity Conservation Union.

Scandlines and the Cemre shipyard in Turkey – which was contracted to build the vessel – drew on cutting-edge technology to help overcome some of the complexities that accompany such an ambitious project.



### FHL's role

Federated Hermes, as one of three shareholders in the business, worked closely with the Scandlines executive team to ratify and test the investment case for PR24.

Scandlines is a key holding within the infrastructure portfolio and the team at Federated Hermes was committed to ensuring the needs of investors remained at the core of the decision to build the vessel. Collectively both shareholders and leadership worked together to ensure the project was in keeping with the company's overall strategic objectives and sustainability goals.

FHL seeks to lead the industry in the application of sustainable investment principles to the management of infrastructure assets.

As the shareholder member of the now superseded ESG working group, FHL provided key input into the development of Scandlines' first public-facing sustainability report in 2021. Published annually, the document is in line with the industry's highest global reporting standards and marked a significant step forward for the shipping group's long-term sustainability agenda.

Subsequently, FHL played a key role in establishing a full Safety and Sustainability Committee, including drafting the terms of reference, and which it now chairs. Alongside the annual report, the committee provides oversight of and input into Scandlines' broader sustainability strategy and initiatives.

<sup>60</sup> Oxford Economics, 'Economic impact of the global ferry industry' (October 2021).

<sup>61</sup> Scandlines, 'A fleet of hybrid ferries'.

Our infrastructure team also participated in the GRESB assessment on behalf of a selection of their portfolio companies. Every company in which we hold a controlling stake, together with the utility businesses and Eurostar, in which we are a significant minority (and whose co-shareholders also support GRESB), participated in the 2022 assessment. The results of the 2022 assessment were issued in 2023. The majority of companies improved their scores against 2021. Results are published in the infrastructure annual sustainability report for investors, in addition to the UN PRI scores.

## Private Equity

Our private equity team is currently developing an outcome-seeking engagement strategy and engagement presently occurs on an ad-hoc basis.



### PRIVATE EQUITY CASE STUDY

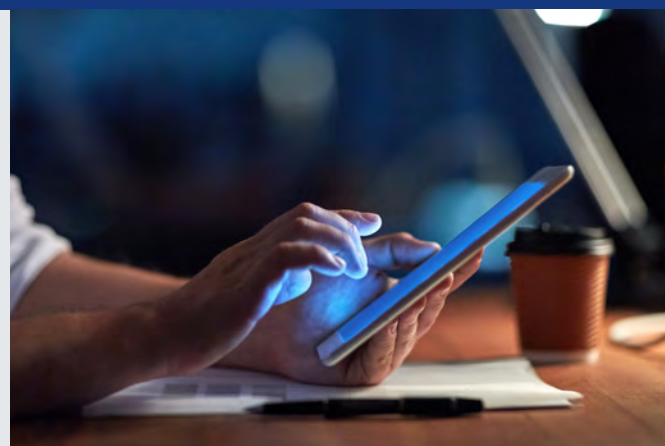
#### Paysend – 2023 update

**Paysend, a private equity portfolio company, is a payments company digitising and lowering the cost of remittances. The company has a global footprint with relevant exposure to the CEE and CIS regions, including Russia at the time of investment.**

The company is addressing SDG 10 directly by reducing the transaction costs of migrant remittances to less than 3%, however its business model has inherent money laundering and conflict financing risks mitigated by company best practices (as per investment due diligence).

The Russian invasion of the Ukraine exacerbated the latent money laundering and conflict financing risk. The investment team engaged with the company and the GP immediately in Q1 2022 to address the company's response to the situation. The company was then flagged further in our internal committees for ESG and quarterly performance.

Management of Paysend reacted swiftly to the crisis and was able to leverage on its best practice experience and rapidly enhanced anti-money laundering and Know Your Customer policies to address the rapidly changing landscape and expanded its sanctions list reviews. Their already strongly tech-enabled model switched to a 24/7 updated compliance product scanning each transaction in line with daily updating sanctions. In addition, it was also decided to forego the fees of any money transfers into and out of Ukraine in order to support the local population, which has led to increased volumes in the region. Lastly, all transfers from and to Russia were turned off and the company has divested their Russian subsidiaries.



The team had daily engagement and monitoring meetings at the outset of the conflict, which turned into weekly and monthly meetings as it came through that all risks were being effectively managed by the company and no breaches were reported. Since then, the company has moved onwards to more strategic growth initiatives focusing on Latin America and the United States and expanding their strong technical partnership with Visa and Mastercard.

In 2023, the company has undertaken a further financing round with new investors Mastercard and UVN (a LatAm television network) leading the round. FHL has also committed to the round and has been actively engaged in discussing terms, alignment and overall round dynamics with the company and investors. Post completion, the team has been granted a 6-month board observer position for increased information rights and oversight.

## Principle 10

Signatories, where necessary, participate in collaborative engagement to influence issuers.

We see value in both direct and collaborative engagement, and it is the combination of both which helps us to influence issuers and borrowers and to carry out effective stewardship. Where there are shared objectives – in particular the promotion of long-term sustainable value – we use both formal fora and other more informal links to work collaboratively with other investors on a global basis. Such interactions can be ad hoc or ongoing. Crucially, the primary concept of EOS' stewardship service is to provide a mechanism for like-minded asset owners to pool their resources and, in so doing, create a stronger and more effective stewardship voice. We consider initiatives on the basis of factors including effectiveness, feasibility, alignment, benefits to the end user and reputation. Any collaboration is done in line with applicable rules on antitrust, conflicts of interest and acting in concert. Indeed, each party will exercise unilateral decision-making principles in deciding how to act while engaging in any collaboration. As described under Principle 4, we contribute to policy discussions both directly and in collaborative fora and initiatives. We are a member of a number of industry bodies and initiatives around the world, through which we conduct collaborative engagement both on thematic issues and with specific issuers.

### Our collaborative engagements

#### Public markets

We collaborate with other investors in our engagement with companies when this may be beneficial for the engagement and could influence the actions and governance of investee companies. We seek collaboration where interests are aligned, and the objectives are based on material issues. Any collaboration is carried out in line with applicable laws and regulations relating to issues such as antitrust, conflicts of interest and acting in concert.

In order to succeed in the long run, we believe that companies will need to effectively manage relationships with key stakeholders. They also need to be mindful of their impact on the environment and their role in both the communities in which they operate and society as a whole – something that grants them their licence to operate. As a result, we are interested in and seek (if necessary) to influence a company's management of these wider risks, where they have been raised. While we do not generally communicate directly with stakeholders, we will feed back their concerns – once verified – to company management through our position as shareholders. We believe we have a duty to use our influence to improve the behaviour of the companies in which we invest; in turn, this should benefit society as a whole. Our stewardship activities may also include discussions with

relevant stakeholders of investee companies, such as industry bodies, policymakers, regulators, customer groups, employee groups and civil society organisations. All of our activities are supplemented by our belief in transparency, and our public reporting may be of value to relevant stakeholders.

We list here examples of how we have collaborated with other investors to engage with issuers in 2023:

- **Investor Initiative on Hazardous Chemicals:** In 2023, EOS joined the Investor Initiative on Hazardous Chemicals (IIHC), as one of 50 signatories representing more than US\$10tn in assets under management or advice.<sup>62</sup> The IIHC was formed primarily to encourage manufacturers through engagement to increase their transparency on hazardous chemicals and cease producing forever chemicals such as PFAS (per- and polyfluoroalkyl substances).

The IIHC builds on action from 2022 when collaboratively EOS wrote to over 50 companies regarding their involvement in the manufacture of hazardous chemicals.<sup>63,64</sup> The companies were targeted based on their ChemScore, a system administered by ChemSec that ranks the world's 50 largest chemical producers on their work to reduce their hazardous chemical footprint.<sup>65</sup>

We are asking companies to improve their transparency around the chemicals they produce globally, including by disclosing any action taken to improve their ChemScore rankings. We also want them to set and disclose a time-bound commitment to phase out PFAS from production. In 2023 and in conjunction with IIHC signatories, we engaged with companies including Sika, Solvay, and Umicore on their ChemScores, focusing on increased transparency, and eliminating PFAS and hazardous chemicals where possible.

- **Investors and Indigenous Peoples Working Group:** In 2022, EOS signed the Investor Statement on Line 3, Oil Sands, and Free, Prior and Informed Consent (FPIC), calling on six US and five Canadian banks to increase protections for Indigenous Peoples' rights within their oil and gas financing. During 2023, we have increased our engagement with financial services companies on Indigenous Peoples' rights, in particular through the steering committee of the Investors and Indigenous Peoples Working Group (IIPWG), of which EOS is a member.

In 2023, we notably participated in a panel discussion called "Indigenous-Defined FPIC: Best Practices for Investment and Corporate Governance", hosted by IIPWG. The panel discussed the core values and protocols that Indigenous Peoples require in a Free, Prior and Informed Consent (FPIC) policy, and how shareholders can move the

<sup>62</sup> ChemSec, 'Investors launch initiative to tackle chemical pollution crisis' (February 2023).

<sup>63</sup> ChemSec, 'Investors with \$8 trillion call for phase-out of dangerous "forever chemicals"' (November 2022).

<sup>64</sup> The Guardian, 'Investors pressure top firms to halt production of toxic "forever chemicals"' (January 2023).

<sup>65</sup> ChemSec, 'ChemScore'.



extractives industry and financial institutions to fully integrate Indigenous Peoples' rights risk screening and FPIC due diligence. The panel brought together a range of Indigenous and investment expertise to debate common questions about FPIC and its integration into corporate practice. Through discussion, resource sharing and breakout sessions, participants gained a better understanding of Indigenous-defined FPIC requirements.

In 2024, we will continue to engage with companies on Indigenous Peoples' rights. We will encourage further implementation of FPIC through formal agreements with Indigenous Peoples, stronger safeguards within financing policies, and representation of Indigenous Peoples at all business levels. We will explore new ways to compare company performance in this area and benchmark companies relative to their peers. Finally, we will continue to support Indigenous Peoples' rights in relevant public policy forums and encourage company alignment with existing third-party guidelines such as UNDRIP. More detail on our engagement approach to indigenous rights can be found in our Q3 Public Engagement Report.

### Private Markets

As well as to collectively finance a loan, our private debt teams may collaborate with other lenders to influence borrowers as part of the engagement process. As described under Principle 9, we would typically do this at a point at which we are in the strongest position, i.e. when we have been mandated to provide the financing and we are negotiating the loan documentation. In particular, as our direct lending team has a co-lending programme with four major European banks, we often work with the relevant co-lending bank to influence the borrower. For example, during 2023, we worked with one of our co-lending banks to negotiate the terms of a loan with a manufacturer of glass and plastic-ware used in laboratory analysis, processing and the storage of hazardous or valuable substances, whereby the interest rate of the loan will decrease as the company reaches targets across three sustainability targets including reductions in greenhouse gas emissions and the reduction in employee accident rates, while the interest rate will increase if the borrower fails to meet the targets.

We work with the other investors within our real estate joint ventures at both the ownership and asset-management levels. The boards of our joint ventures have representatives from both investors. We work together with investors within the decision-making framework of the Partnership Agreement. Each vehicle has an appointment with a FHL company (including MEPC, a fully owned subsidiary) for one or more of the investment management, development management and/or asset management of the asset. The appointed team reports to the board and is responsible for the day-to-day running of the asset, engaging with both owners within the joint venture to suggest and progress initiatives. It is at this level that our ESG approach strongly influences the delivery of the asset and property management services.

Our infrastructure team invests directly in assets as a minority (and sometimes majority) shareholder with proportionate governance rights, typically a board seat. Collaborative engagement with portfolio company management teams and co-shareholders is part of our day-to-day interactions, as described under Principle 9. A case study is included in the following section.

In private equity, as described under Principles 2, 7 and 9, as a minority investor we interact with the lead GPs of our direct co-investments and fund investments. Due to the nature of the asset class, other collaborative activities with other investors are limited and usually relate to informal discussions around governance or fees.

Any collaboration is done in line with applicable rules on antitrust, conflicts of interest and acting in concert. Indeed, each party will exercise unilateral decision-making principles in deciding how to act while engaging in any collaboration. More information on our advocacy and collaborative engagement on thematic issues and public policy through industry initiatives is available under Principle 4.



## The outcomes of our collaborative engagement

We monitor the progress of our collaborative engagements with specific issuers in the same way we monitor our direct engagements. We do not categorise our engagements with specific issuers into either collaborative or individual/staff engagements. The outcomes of our collaborative engagements are therefore included in our reporting under Principle 9 of our broader engagement outcomes. However, here we provide some case studies as an example of how we collaborate with others in our engagement with issuers. As noted above, more information on our collaboration on thematic issues and public policy is available under Principle 4.

Each quarter, EOS publishes a Public Engagement Report which details its collaborative work on public policy and best practice over that period. These are publicly available on the EOS library page of the website.



### CASE STUDY

#### Asian Corporate Governance Association (ACGA)



**At Samsung Electronics, direct dialogue with the board is not generally available to investors, as is the case at other companies in the South Korean market. We have been engaging at executive level on the benefits for both parties of a regular dialogue between board members and investors.**

We raised our initial concerns about the lack of communication during a meeting with senior executives in Seoul in 2015. The company acknowledged it was important for investors to have access to independent directors in 2016. The following year, we requested a clear plan for increasing communication between investors and independent directors.

In 2018, EOS recommended voting against the election of the chair due to, amongst other reasons, a lack of access to non-executive directors. We met with the chair in April 2019 as part of the ACGA. He felt that the new

independent non-executive directors (INEDs) had improved discussion and debate, but that the company could still benefit from an INED with global experience.

#### Outcomes and next steps

In Q4 2021, Samsung agreed to organise an engagement between the board chair and a group of investors and members of ACGA. In Q2 2022, we reinforced our request for regular engagement with the chair.

The company said that the chair valued the engagement and assured us that a framework had now been established for an annual collective engagement between the chair and members of ACGA. This is a significant step forward and enables regular engagement between the board and investors on various material topics such as corporate governance, capital allocation and climate change. The latest of these annual collaborative engagements with Samsung was in January 2024.

 CASE STUDY

## LyondellBasell – 2023 update



**We have engaged with the multinational chemical major, LyondellBasell Industries NV (LyondellBasell), on climate change since 2017. As part of CA100+, a collaborative engagement of more than 370 investors and their representatives seeking greenhouse gas emissions reductions from the world's largest emitters, we co-lead the engagement with the company.**

After LyondellBasell published its first sustainability disclosures and CDP reports in 2017, we engaged with the company to set more ambitious climate targets. With the support of other CA100+ investors and their representatives, we met the CEO and senior management in Q2 2021 to discuss the company's progress towards disclosing sustainability targets, including its planned science-based targets and a net-zero ambition.

In order to accelerate progress, as the CA100+ lead for the company, we used a legal mechanism to propose a discussion on climate change at the company's 2021 annual meeting. EOS led contributions by a group of eight institutional investors who questioned climate progress leading to over 45 minutes of shareholder-board discussion on the company's climate change strategy. During the meeting the company indicated its willingness to make further commitments.

In Q3 2021, we welcomed the company's release of its climate strategy, setting a Scopes 1 and 2 net-zero ambition for its global operations by 2050; a 30% absolute reduction of Scopes 1 and 2 emissions by 2030; and a goal to source a minimum of 50% of its electricity from renewable energy by 2030. In addition to its climate goals, LyondellBasell prioritised actions in its 2020 sustainability report to help eliminate plastic waste from the environment including waterways and oceans and to advance a circular economy.

It has also set out a pathway towards achieving its 2030 target and we encouraged LyondellBasell to collaborate with industry peers with the aim of developing a science-based sector-wide Scope 3 approach. In late 2022, LyondellBasell announced that it would increase its 2030 greenhouse gas emissions reduction target for Scopes 1 and 2 emissions to 42%, relative to a 2020 baseline. It also said it would establish a 2030 Scope 3 greenhouse gas emissions reduction target of 30%, relative to a 2020 baseline, and in accordance with guidelines from the Science Based Targets initiative (SBTi). It will submit its climate goals to the SBTi to be validated against SBTi guidance.

In July 2023, we spoke to the audit committee chair, the chief accounting officer and the chief sustainability officer, giving an overview of our expectations regarding climate-aligned accounts and audit.

The company said that it had initiated an ESG dashboard to track progress at the board level, with the external auditor providing limited assurance. We reiterated the expectations for climate-aligned accounts and audit that we had set out in an earlier letter. We provided examples drawn from the company's 2022 financial statement and emphasised the need for clear disclosure of assumptions, consistency across reporting, and evidence that the auditor had assessed climate in the context of critical audit matters.

The chair said that he would raise these matters with management, adding that our engagement on this topic was well timed. He agreed to a further dialogue on the topic in 2024.

## Principle 11

### Signatories, where necessary, escalate stewardship activities to influence issuers

Any voting recommendation or other intensification or alternative stewardship approach is carried out in line with applicable rules on antitrust, conflicts of interest and acting in concert. Indeed, each party will exercise unilateral decision-making principles in deciding how to vote. Our engagements across all asset classes are outcomes focused, although the nature of stewardship approach varies depending on both the rights available and the specific context.

#### Public markets

The companies identified for the core engagement programme at the beginning of each year are assigned an engagement intensity tier, although this is subject to change throughout the year, as individual company circumstances change.

We escalate the intensity of an engagement activity over time, depending on the nature of the challenges each company faces and the attitude of the board towards our dialogue. Generally, our engagement activity becomes more active where we believe that engagement will lead to an increase in or prevent/limit a decrease in the value of a company over the long-term.

Engagements on some objectives may involve only a small number of meetings, although others are more complex and will entail multiple meetings with management and board members over several years. Such activity often requires persistence. Our long-term and diverse perspective enables us to persist with the more difficult and time-consuming engagements to bring about changes in either strategy, financial structure, operational or risk management or governance, including in relation to ESG risks. Any change we encourage a board or management team to make will be with the intent of improving a company's long-term performance.

While we can be robust in our dealings with companies, the aim is to deliver value for clients, not to seek headlines which could undermine the trust that we believe should otherwise exist between a company and its owners. As a result, we generally prefer to conduct engagement privately, rather than taking a public route when seeking change at companies, although (as described earlier under Principle 7) details of all engagement meetings conducted by our stewardship team

are shared across investment teams and with EOS' third-party clients. In our experience, working constructively with boards and management in private is the most effective way to achieve positive change, as it allows us to build trusted relationships with companies, which results in more open and frank discussions.

However, on the occasions that we are not able to achieve success by our usual methods of conversations behind closed doors, we may intensify or adapt our engagement approach, for example by choosing to speak publicly at the company's annual general meeting (AGM) to garner additional investor support and add further pressure. When doing so, we would normally notify a company in advance. We may also vote against (or EOS may recommend voting services clients vote against) a resolution or management/the board at a company's AGM – we consider this choice carefully as we only want to use this technique if our usual engagement has consistently stalled, and we are not confident that the company is taking any action to address our concerns. We disclose a number of these instances under Principle 12. Given the assets we represent, such action sends a strong signal to the company and can help progress our dialogue.

Similarly, we have demonstrated a willingness to use the full range of rights that we have at our disposal, including the tabling of resolutions at shareholder meetings when necessary or collaborating with others to co-file shareholder resolutions (as described under Principle 12). We prioritise issues for escalation for the most material issues and companies, typically with our Tier 1 engagement companies, our most intense dialogues. Using the stewardship techniques described can be a time consuming, and sometimes costly, process. As mentioned above, through the EOS annual survey, we have seen that a consistent majority of clients say engaging for impact and outcomes is a priority.

EOS uses the following engagement tools to adapt engagement over time to the needs of the situation in the interests of clients. The graphic demonstrates how different tools are selected as the scope or intensity of the engagement increases in tandem with pressure for change at the company.

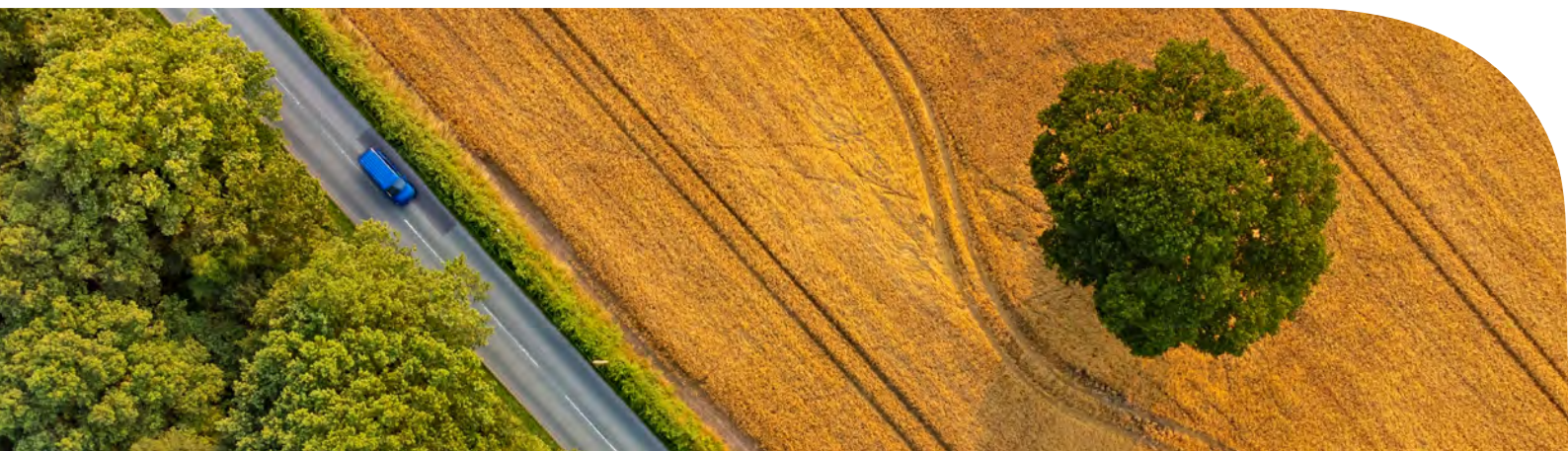
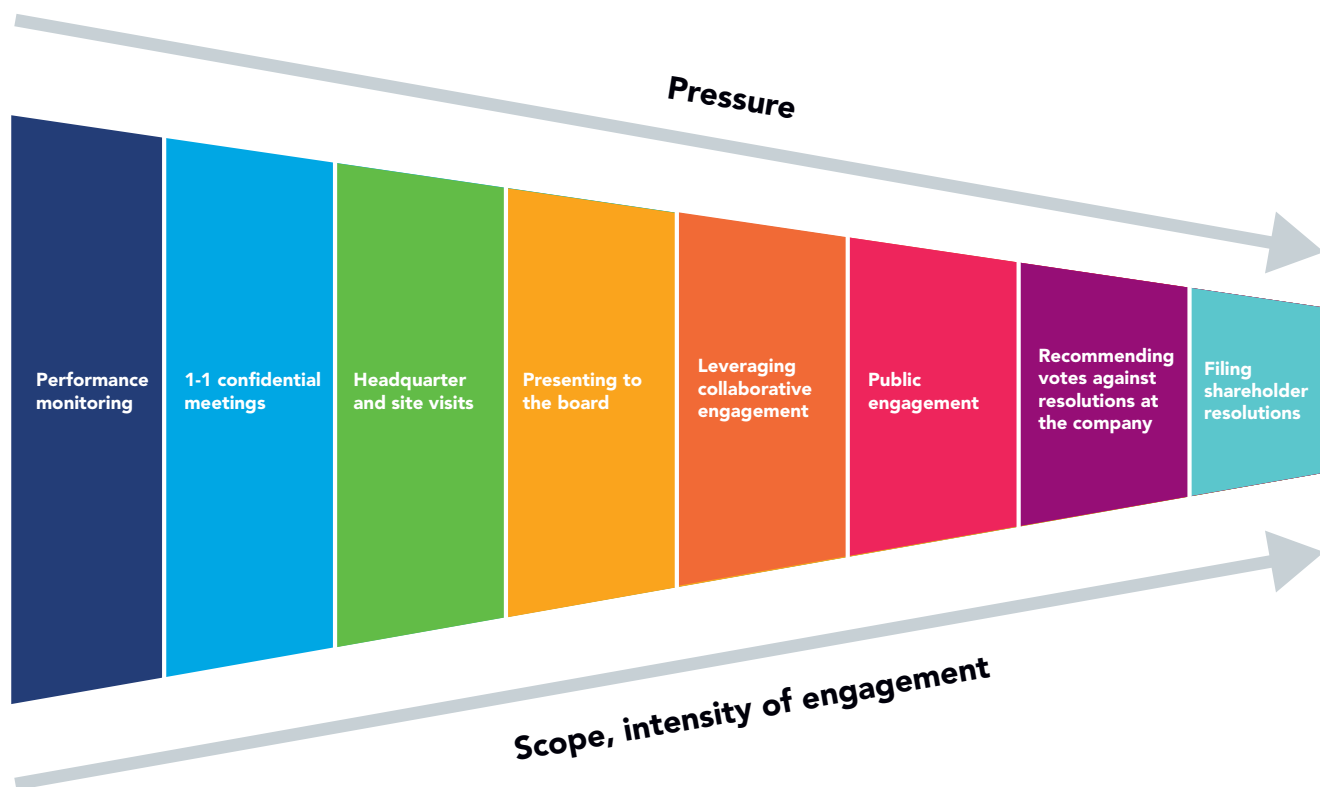


Figure 43. Engagement tools employed by EOS



Source: FHL, as at 31 December 2023.

If our usual private engagement approach has not been successful and EOS decides it is appropriate to change stewardship strategy, relevant portfolio managers are notified about it as soon as possible, to allow this to be factored into their investment decision-making process. Companies that consider changing their practices show a willingness to engage and listen to shareholders. This indicates the potential for positive change, which may enhance the investment case. On the other hand, a red flag is raised when a company is not willing to engage with its investor base or is resistant to change even after a change in approach, such as intensification of engagement. If a company is unwilling to make changes in relation to material ESG or strategic issues, this may be an indication that it is less likely to create sustainable wealth over the long-term.

Adapting engagement on debt has many similarities to equity, including the use of collaborative engagement, formal letters to the company and public statements. There are, however, some differences. Companies have a recurring presence in the debt capital markets, which gives our public credit teams additional pressure points to influence corporate behaviour. Where a company has been unresponsive to our engagement efforts, we may also contact the banks involved in a new issuance.

For our engagement-focused funds, we may also withdraw our capital where we deem the engagement has failed, for example, where the company’s actions contradict the outcome our engagement has been seeking. However, this is a last resort and only used after allowing sufficient time for the situation to improve.

Our case studies provide detailed insights into how our engagement changes over time and can lead to change and completion of our objectives. In addition to the case study below, there are further examples of how we have used voting and shareholder resolutions as a technique, and the breakdown of why we have voted against proposals during 2023, under Principle 12.



 CASE STUDY

## Lonza Group



**Lonza Group is a Swiss multinational manufacturing company for the pharmaceutical, biotechnology and nutrition sectors.**

### Engagement

Audit quality and integrity is at risk when the same assurance provider is maintained for long periods. In line with international good practice, we wish to see mandatory rotation of the audit firm after 20 years' tenure, with an open and competitive re-tender process at the interim point of 10 years. Supporting this is EU regulation which requires an absolute maximum auditor tenure of 20 years (although this does not strictly apply to Lonza, domiciled in Switzerland).

Ahead of the 2021 AGM, we contacted Lonza to raise concerns regarding the fact that it had the same auditor since at least 1999 when it was independently listed. Accordingly, we recommended a vote against the re-election of its auditor at the 2021 AGM. We contacted the company again ahead of the 2022 AGM to reiterate our concerns. However, the company did not provide any reassurance that this would be addressed so we escalated our engagement by recommending both a vote against the re-election of the audit firm and the audit committee members too.

### Outcomes

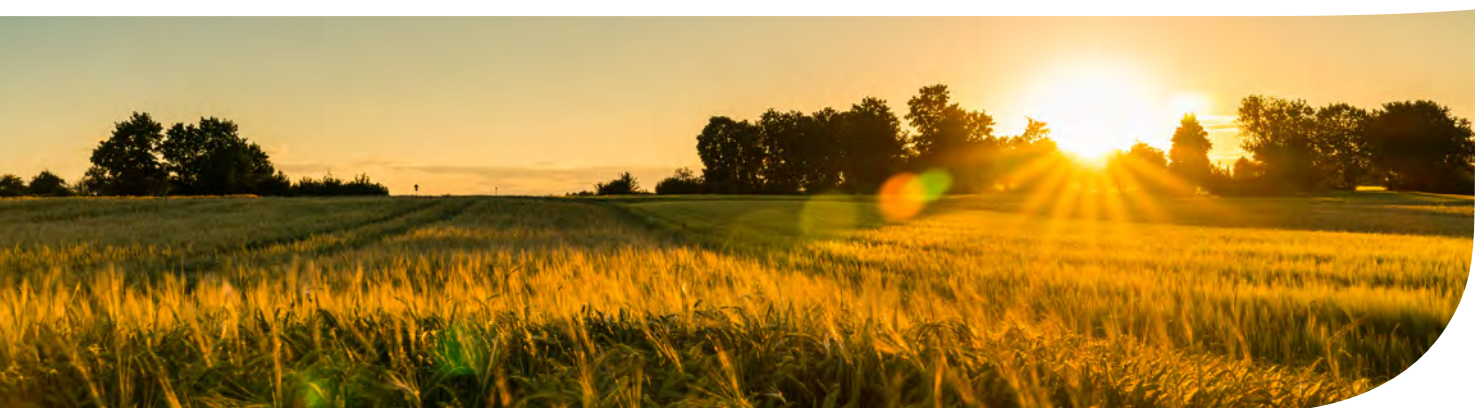
We were pleased to see that for its 2023 AGM, Lonza was seeking shareholder approval for the election of a new audit firm, and we contacted the company to share our appreciation for this.

## Private markets

For most of our private markets' teams, a lack of liquidity means that it is not easy to divest or decrease exposure to investments. As a result, investments in this space are considered to be long-term relationships, and it is for the investment team to conduct appropriate due diligence prior to investing to ensure that the firm and its shareholders are willing to work with us to drive positive change. At this point, positive behavioural changes in relation to ESG risks can be included as a requirement in the documentation to ensure progress. However, it is not always possible to envisage all ESG risks that could arise during the life of the investment. In these situations, our private debt and real estate teams would engage with the appropriate stakeholders such as the borrower or the occupier, potentially with the help of EOS, to escalate and resolve any issues through dialogue. Our Direct Lending team may also involve the private equity shareholder. There can be additional instances during the life of a loan when we have an ability to influence the company's behaviours. This is primarily when the borrower needs to amend the terms of the loan. As described under Principle 12, while we have enforcement rights when a borrower breaches the agreed terms or defaults on a loan, we use these rights only as a last resort. In the first instance, we seek to negotiate a positive outcome for all parties involved, although we will always act in our investors' best interests in line with our fiduciary duty.

As a direct investor in portfolio companies, our infrastructure team escalates from asset management (operational) level, to committee, then board, then shareholder level discussions to the extent needed. As an example, over the last two years we have escalated engagement on sustainability with Eurostar. Although we view Eurostar as a climate solution, supporting green travel across Europe, we prioritised engagement to ensure the appropriate governance and resource is in place in order to further the green agenda, particularly around emissions reduction target setting. Having started with asset management discussions, we promoted the escalation of this to executive and board level through collaborative discussions with co-shareholders. A Head of Sustainability was appointed in 2023 and a Sustainability Steering Committee established on which we have representation. In 2023, the Committee approved Eurostar's first emission reduction targets.

Due the nature of the asset class and our position as a co-investor, our private equity team aims to identify ESG risks at the point of investment due to the difficulties faced in escalating activities during the investment hold.



## Principle 12

Signatories actively exercise their rights and responsibilities.

### Our rights and responsibilities as an investor

As we set out under Principle 1, we believe that the purpose of investment is to create wealth sustainably over the long-term, and that investors must behave in a way that is consistent with solving the world's problems rather than compounding them. Intertwined with this is the belief that, consistent with client objectives and applicable requirements, investors must be responsible stewards of capital in order to contribute to positive outcomes for our clients and beneficiaries, as well as society and the environment.

Throughout this report, we have sought to demonstrate how we have responded through active stewardship across all of our products and asset classes. Investor rights are themselves an asset, and we view the exercise of these rights as part of our fiduciary duty and a responsibility of effective stewardship.

For listed equities, our voting and engagement are co-integrated as part of our overarching approach to stewardship. As such, our voting decisions – as well as EOS' recommendations to third-party clients on voting decisions – are informed by the insights and experience of engagement with the investee company. We may attend the AGMs of investee companies or arrange for representation at the AGMs by the EOS team. This can include asking questions or making statements to the board. We may also file or co-file shareholder resolutions. The exercise of all such rights is based on an evaluation of materiality and an analysis of costs and value. EOS engagement professionals go through a training and onboarding process which involves shadowing more experienced colleagues to ensure they sufficiently understand the voting policies and how shareholder rights differ according to the markets involved. Senior engagement professionals dedicate time to handling escalated votes and discuss market developments. We set out in more detail how we have exercised our shareholder rights for listed equities, including voting rights, in the following section.

For our fixed income products, the rights we hold vary between the type of assets we invest in and even between individual investments. We seek to achieve mutually beneficial outcomes while protecting our clients' interests, in line with our fiduciary duty. For our Credit team, documentation is a governance factor, and the quality of the documentation can be used to determine how a company's management thinks about its stakeholders. As part of the investment process, we therefore see both the covenants and the quality of bond and loan documentation as indicators of governance strength or weakness.

As investment managers, we use the rights granted to us by our real estate client mandates to improve the value of the assets in our portfolios in line with our fiduciary duty. The rights and responsibilities we hold vary between mandates and depend on the level of client involvement in the decision-making process. Our investment strategies reflect market conditions and consider material ESG factors. Our asset management activities seek to improve the assets – by improving their ESG profiles and through tenant engagement – and thereby deliver positive social and environmental outcomes, which benefit our clients and their end beneficiaries.

Our infrastructure team invests directly in assets as a minority (and sometimes majority) shareholder with proportionate governance rights. Shareholder rights, including reserved matters and the right to board representation, enable downside protection and strategic influence over value-impacting topics, in both cases including sustainability/ESG considerations. Our expectation is to have at least one board member at each portfolio company. We also have representation at various committees, including chairing two sustainability committees at Cadent Gas and Scandlines. Information rights are essential to ongoing monitoring and management and should cover all information needed by us for our day-to-day asset management, valuation and investor reporting.

Due to the nature of the asset class and holding the position of co-investors, direct investments are very limited for our private equity team and our formal investor rights tend to be focused on information rights and minority protection rights. Lead GPs have significantly more rights than we typically do as a minority co-investor. They are able to make decisions that impact the company, such as deciding on company strategy. Whilst we do not have contracted expectations around how they use such rights; we select managers based on their previous experience and demonstrated capabilities in managing such rights appropriately.



## Listed equities: voting approach

We, as shareholders, are granted a wide range of rights which both offer us a level of protection and enable us to fulfil our stewardship responsibilities effectively. In particular, we consider the vote as part of the asset and accept that we have a responsibility to exercise this right in a considered fashion.

### Our voting policies

EOS' Global Voting Guidelines act as a policy to inform EOS' voting recommendations to our investment teams, as well as to EOS clients who request to receive EOS' voting recommendation service. FHL's Global Voting Policy and Guidelines, which are aligned with EOS' Global Voting Guidelines, inform the voting decisions made by our investment teams. Our Guidelines are informed by a hierarchy of external and internally developed global and regional best practice guidelines. The most important of these are our EOS-developed regional voting guidelines and Corporate Governance Principles, which are available on our website. In 2023, we successfully completed our transition from market-level Corporate Governance Principles to an approach centred on three regional Public Vote Guidelines, with the overall goal being to provide companies and clients with a clearer structure for our disclosures. The three regional groupings are 1) UK, Europe and Australia, 2) North America and 3) Asia and Global Emerging Markets (AsiaGEMs). Alongside this, we updated our regional vote policies across 28 global markets. While our previous regional Corporate Governance Principles focused on the high-level principles that guided our vote policies across 28 global markets, our Public Vote Guidelines place a stronger emphasis on the policies themselves, which more directly inform the voting recommendations we issue to our clients. EOS also published a set of Global Corporate Governance Principles to provide more information on what EOS considers to be governance best practices, not limited to issues with direct vote policy implications.

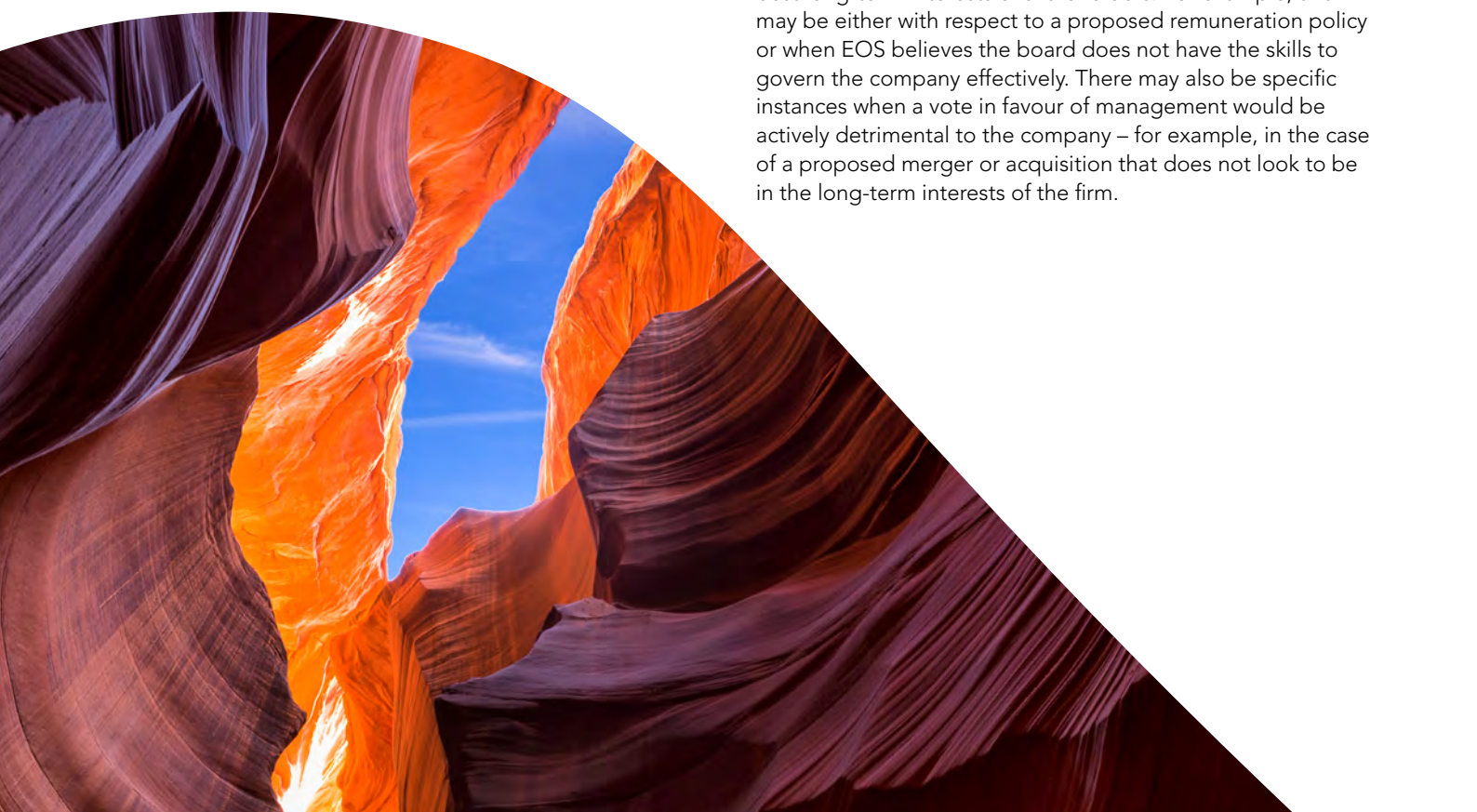
Some of the updates made to our voting policies in 2023 included: harmonising director independence expectations across AsiaGEMS markets; increased focus on below board-level gender diversity in the UK, European and Australian market; and the implementation of a focused policy on auditor tenure and fees in North America.

The policy development cycle for our voting guidelines runs annually, in conjunction with the policy review process at ISS, which informs its benchmark research. EOS considers changes made at ISS in view of resolution-level data for past voting seasons in order to consider what additional changes are warranted. This includes integrating feedback from clients and evolving best practice in each market. EOS' Engagement Plan provides further input and identifies thematic priorities for engagement. This can often be boosted by enhanced vigilance and, potentially, escalation through our voting recommendations. EOS completes its major policy changes before the main voting season in each market. Once changes are applied, the policy is monitored to ensure it is having the desired effect and is adjusted further, where appropriate.

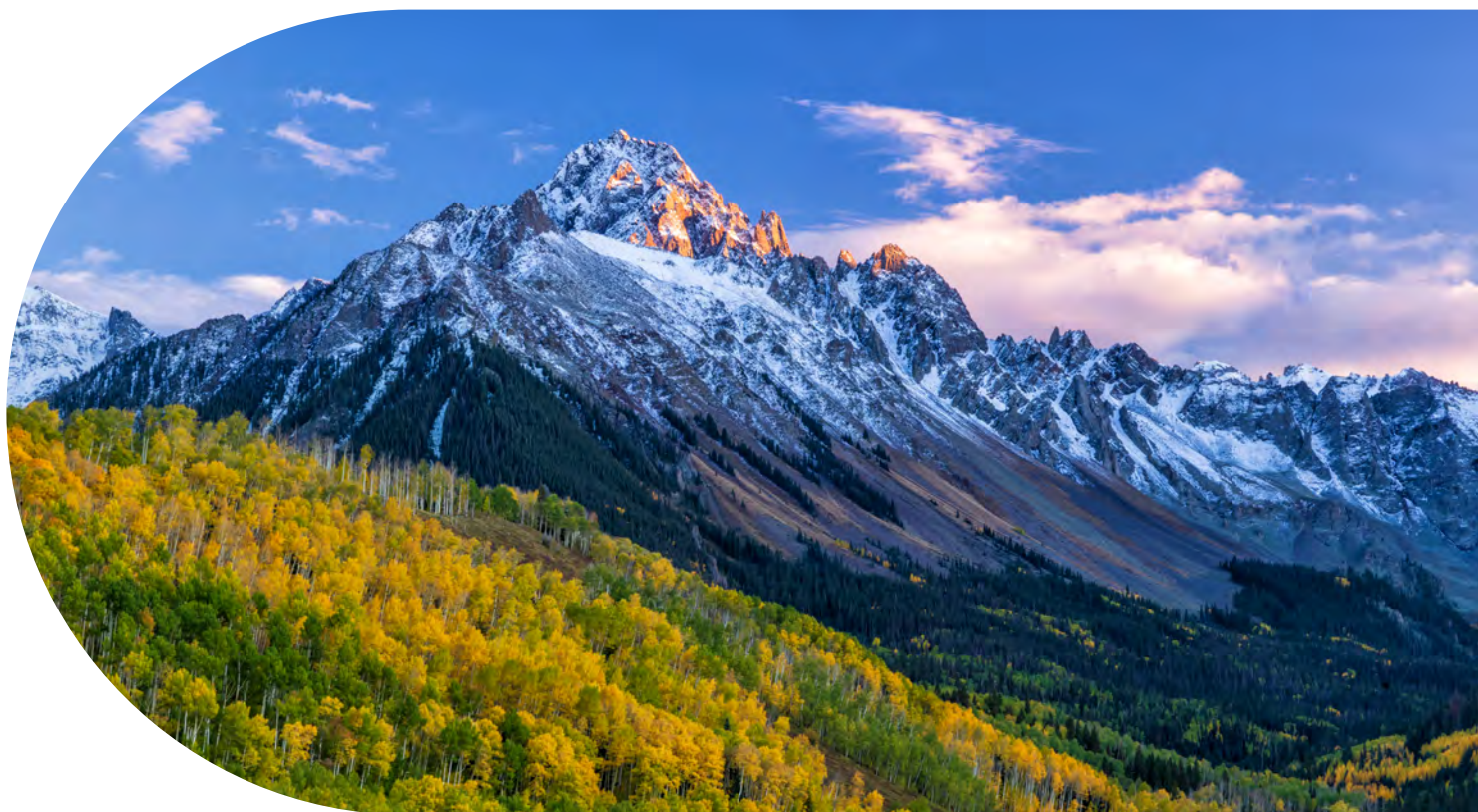
### Voting decisions

Voting rights are exercised with a view to achieving best practice standards of corporate governance and equity stewardship and with the aim to support the delivery of long-term value in our funds. Ultimately our investment teams make all voting decisions, based on EOS recommendations. EOS engagers, who are well versed in the voting policies, make recommendations to our investment teams based on our voting guidelines, as well as any further information that they receive through their research, engagement and specialist knowledge of the company.

While it is difficult to provide a general description, EOS will typically recommend a vote against management when it considers that a vote with management would not serve the best long-term interests of shareholders. For example, this may be either with respect to a proposed remuneration policy or when EOS believes the board does not have the skills to govern the company effectively. There may also be specific instances when a vote in favour of management would be actively detrimental to the company – for example, in the case of a proposed merger or acquisition that does not look to be in the long-term interests of the firm.







EOS uses ISS to provide research on all the companies for which it provides voting recommendations, which comes to over 13,000 meetings a year. The recommendations that our investment teams and EOS third-party clients receive are, in the first instance, based on ISS's research using our voting guidelines. This is then overlaid with our intelligent voting approach.

EOS has a value-add and cost-effective mix of automated and manual voting recommendations, which focuses resources on key topics and companies with significant holdings and/or contentious issues or ongoing engagement objectives. Engagers add insight and value to a specific subset of these meetings – those on EOS' watchlist – by considering the voting recommendation approach in light of the specific company context and the engagement. A shortlist of high priority equity holdings are added to the EOS watchlist each year, based on size of holding and insight into the potential level of complexity of vote. EOS recommendations are applied to FHL's remaining equity holdings and if the investment teams disagree with the proposed recommendation, then EOS will manually review the recommendation. EOS endeavours to engage around the vote with all companies on the watchlist for which it is considering recommending a vote against – this comprises 807 companies, including around 320 in the core engagement programme. EOS will also discuss such cases with the relevant portfolio manager. We receive research from ISS, but also have access to our own information on our electronic platform, which captures meeting notes and documentation relevant to the company's engagement history and objectives.

EOS will also engage to identify any further relevant information that might inform the voting recommendation and has regular conversations with our investment teams about the reasons for their views on particular votes. We will

vote 'for, by exception' to our voting policy when we judge that we will further the engagement and likely achieve beneficial change by doing so.

Votes are escalated when especially important for the company or particularly complex, or when a disagreement or potential conflict of interest arises with the recommendation received from EOS. For our investment teams, the voting recommendation provided by EOS will inform their assessment, but they will make their final judgement independently. On the rare occasion that there are disagreements between investment teams and/or EOS on the appropriate voting recommendation or decision, the matter is logged and escalated for consensus to be reached at the director level. We expect votes cast by our investment teams to be consistent with the voting recommendations we provide to our stewardship clients, who request to receive voting recommendations. In such cases, the rationale for divergence will be documented. As described under Principle 3, we have escalation processes in place when there are different views between EOS and our investment teams, or when conflicts of interest arise in the course of fulfilling our commitment to acting as good stewards of those companies in which we invest.

Clients with segregated mandates have the option to carry out the voting themselves, or to benefit from the voting recommendations and decisions of the relevant investment team, based on EOS' recommendations. Underlying clients of our pooled funds are not able to override the investment team's vote or to vote their share separately.

### **Securities lending**

We do not, as a matter of course, participate in securities lending transactions. We endorse best practice principles, such as the Securities Lending Code of Best Practice issued by the ICGN.

### Listed equities: 2023 voting

#### Our 2023 voting records and rationale

Our voting records are published online in arrears. This ensures that we are transparently accountable, but that our dialogue with companies around voting issues is not compromised. The records include all voting decisions of FHL. These records relate to the voting decisions of the FHL teams on behalf of FHL funds and clients. Information on the voting recommendations made by EOS to EOS voting service clients can be found in the EOS Stewardship Report. Company meetings where we have recommended voting in line with management on all resolutions are condensed. In 2023, we cast votes at 784 meetings involving 8,852 resolutions.

Figure 44. Global 2023 voting statistics

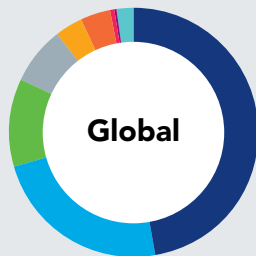


- Total meetings voted in favour **36.6%**
- Meetings where voted against (or voted against AND abstained) **55.9%**
- Meetings where abstained **0.3%**
- Meetings where voted with management by exception **7.3%**

Source: FHL, as at 31 December 2023.

**Votes against the board:** We provide the rationale behind our decision when we have voted against management on one or more resolutions. We seek to be supportive of boards and to recommend votes in favour of proposals unless there is a good reason not to do so. This is in accordance with our voting policies and global or regional governance standards. We will vote against management if, by doing so, we are striving to protect long-term shareholder interests.

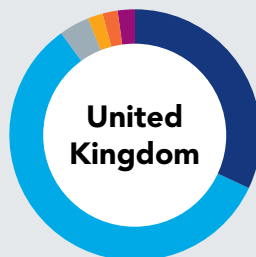
Figure 45. Breakdown of votes against by region



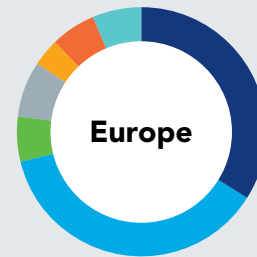
- Board structure **47.5%**
- Remuneration **23.3%**
- Shareholder resolution **11.4%**
- Capital structure and dividends **7.4%**
- Amend Articles **3.7%**
- Audit and Accounts **3.9%**
- Investment/MandA **0.6%**
- Poison Pill/Anti-Takeover Device **0.1%**
- Other **2.2%**



- Board structure **75.0%**
- Remuneration **8.7%**
- Shareholder resolution **4.6%**
- Capital structure and dividends **1.5%**
- Amend Articles **2.6%**
- Audit and Accounts **7.7%**



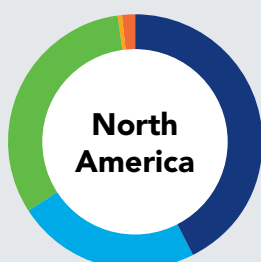
- Board structure **32.0%**
- Remuneration **58.0%**
- Capital structure and dividends **4.0%**
- Amend Articles **2.0%**
- Audit and Accounts **2.0%**
- Poison Pill/Anti-Takeover Device **2.0%**



- Board structure **34.1%**
- Remuneration **37.1%**
- Shareholder resolution **5.9%**
- Capital structure and dividends **7.3%**
- Amend Articles **3.4%**
- Audit and Accounts **5.9%**
- Other **6.3%**



Board structure	48.1%
Remuneration	17.5%
Shareholder resolution	2.0%
Capital structure and dividends	16.4%
Amend Articles	7.2%
Audit and Accounts	3.6%
Investment/MandA	1.8%
Other	3.4%



Board structure	42.6%
Remuneration	23.4%
Shareholder resolution	32.0%
Amend Articles	0.6%
Audit and Accounts	1.4%



Board structure	30.8%
Remuneration	53.8%
Shareholder resolution	3.8%
Capital structure and dividends	7.7%
Audit and Accounts	3.8%

Source: FHL, as at 31 December 2023.

**Votes not in line with our policy:** We retain the ability to vote differently to that indicated by our high-level policy when warranted. This is on the basis of particular company circumstances or engagement insights, to best serve the interests of long-term shareholders. If EOS engagers are considering whether to recommend a vote that is not in line with our policy, this will generally be escalated to a more senior team member or otherwise follow an established and agreed precedent that was earlier escalated. In these cases, engagers record in our Engagement Management System that they have consulted a senior engager. When a potential conflict is identified, the matter is escalated in line with our Conflicts of Interest policy, following the process outlined earlier under Principle 3.

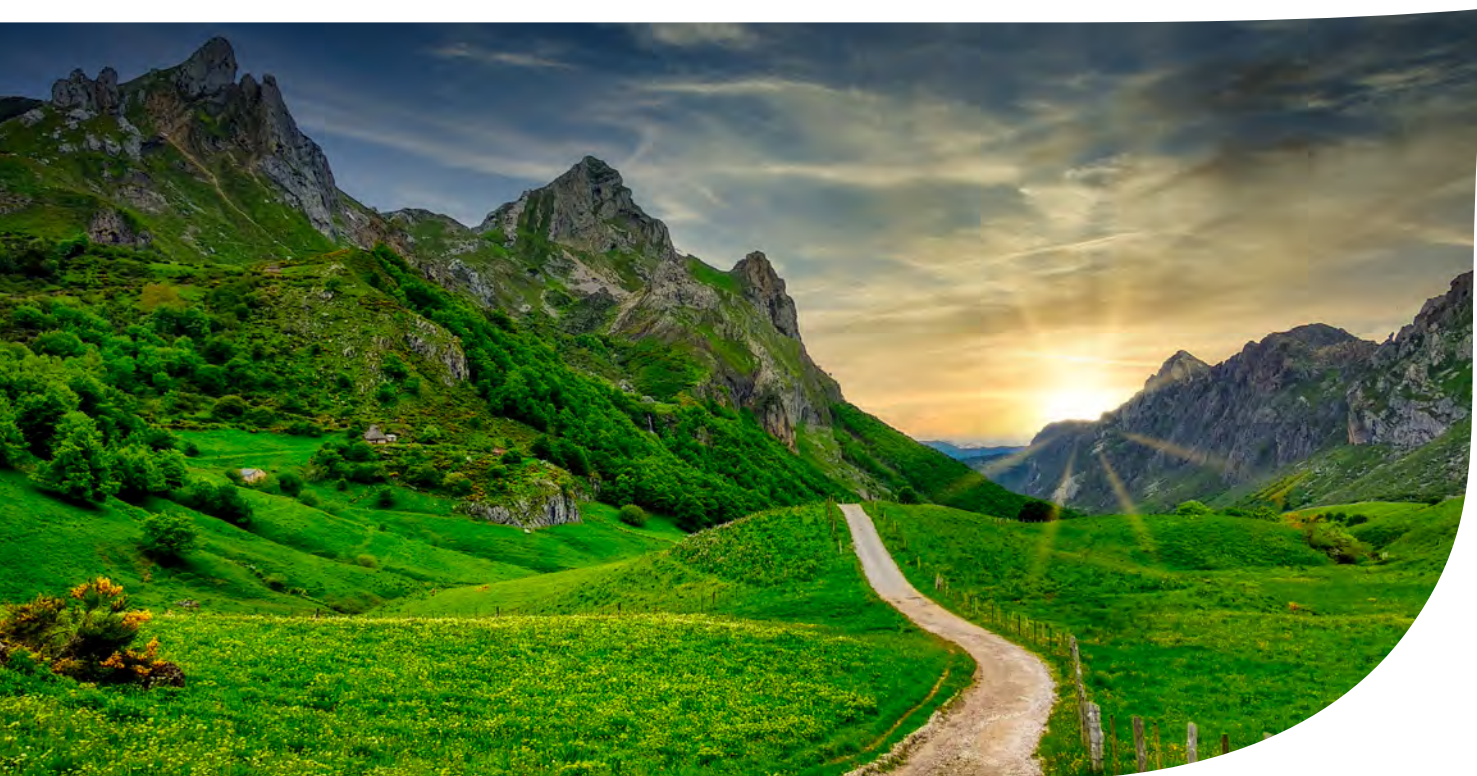
On occasion, our policy may suggest a vote against management, but engagement insight suggests otherwise – for example, a company may have committed to making a change, with a view to implementing this the following year leading us to vote for, by exception to our policy. These instances are highlighted in our voting disclosures and are within the scope of our overall voting policy.

- At life science supplier **Thermo Fisher**, we voted for the governance committee chair, by exception to our policy. Although we had concerns on the approach to board gender diversity, we considered the company’s progress in achieving 45% overall board diversity and the most recent appointment of a female director. We have board diversity expectations of a minimum of 30% gender diversity and a minimum of 40% overall diversity.
- At mining and metals company **BHP Group**, we voted for the election of a director, by exception to our policy in 2023. The company is flagged on the Global Coal Exit List for thermal coal production due to inadequate management of climate-related risks. However, BHP has announced plans to divest its thermal coal assets by 2030, in line with the Paris Agreement commitments to fully exit coal.
- At health company, **Dabur India**, we voted for the nomination of a committee member, by exception to our policy. Although board gender diversity is below our expectations, a new female director was appointed to the board during 2023 and the nomination committee member was an independent director.

**Shareholder resolutions:** We support the selective use of shareholder resolutions, as they can be a useful tool for communicating investor concerns and priorities, asserting shareholder rights or supplementing or escalating direct engagement with companies. We consider such resolutions on a case-by-case basis and encourage boards to engage with serious, committed long-term shareholders like ourselves. When considering whether or not to support resolutions, we consider factors which help to ensure that the proposal promotes the interests of long-term shareholders. These include what the company is already doing or has committed to do, the nature and motivations of the filers (if known) and what potential impacts – positive and negative – the proposal could have on the company if implemented. When boards interact in an active and engaged way with shareholders on issues that affect the long-term value of companies, we see less need to file or support shareholder resolutions.

In our experience, shareholder proposals can facilitate a dialogue with issuers, and we welcome these opportunities, where appropriate, whether we vote in favour of the resolution itself or not. We expect boards to address the issues raised by shareholder proposals, which receive significant support, or where they are material to the company. In addition, we view any failure to implement a shareholder proposal that has received majority support as a clear indication that the board of directors is not fulfilling its obligations to the owners of the company.

When we vote in favour of a shareholder resolution and there is no management recommendation, this is classed as a vote against management in our disclosures. This is to ensure that we do not under-report conflicts, although in some instances it may not be voting against what management would have wanted.



We also initiate shareholder proposals in markets where it is relevant to do so and have done so in Germany, the UK and the US, either as lead filer or as co-filer alongside other investors. Consistent with our intelligent voting approach, this typically forms part of a wider engagement with the company and is used as a tool for leverage in EOS' dialogue with management.

Examples from 2023 shareholder meeting season include:

In **North America**, total shareholder proposals jumped to a new record with social issues such as responsible tax, human and digital rights, and diversity, equity and inclusion (DEI), seeing the biggest increase.

- At US pharmacy retailer **CVS** we supported a shareholder proposal seeking a third-party assessment of CVS's adherence, above and beyond legal compliance, to its stated commitment to workers' freedom of association and collective bargaining rights. We also supported a shareholder proposal calling for paid sick leave benefits for all employees, for a second consecutive proxy season. We believe it is good business practice to offer paid sick leave to all employees, and this would be in line with the company's purpose, "to help people on their path to better health". These received 25.9% and 25.6% support respectively.
- Several 2023 shareholder proposals appeared supportive of DEI on the surface but were designed to derail DEI momentum. For example, we opposed the proposal asking for a civil rights and non-discrimination audit at **Apple**, as it appeared the proponent's objectives were in direct opposition to the civil rights audit proposal we had supported in 2022, and which the company was now conducting. This proposal received 1.4% support. Similarly, at **Amazon** we voted to oppose the proposal calling for an analysis of costs associated with DEI programmes at the company, due to questionable filer intent in opposing a scale-up of diversity and inclusion efforts, and lack of alignment with long-term shareholder value. This received 1.5% support.

In **developed Asia** and **emerging markets**, we saw an uptick in the number of climate-related shareholder resolutions, with investors seeking more robust transition plans from banks and utilities. For example, at trading house **Mitsubishi Corp**, we supported the proposals calling for the company to align its emissions reduction targets with the Paris Agreement, and to evaluate the consistency of its new capital expenditure with its net zero by 2050 commitment. These received 20% and 12% support respectively.

**Other notable votes:** There are other instances when votes are notable due to the outcome of the resolution, the level of dissent or the subject matter of the vote. The shareholder resolutions described above are examples of this, as are the following examples:

- At car manufacturer **Toyota**, the first shareholder proposal in almost 20 years asked for improved reporting of the company's climate-related lobbying activities. We met the company several times to discuss the proposal, which we ultimately supported. The proposal received 15% support, which was significant given that Toyota's shareholder base includes many strategic shareholders and group companies, which were unlikely to vote for a resolution that was not management-approved.
- At commercial bank **UniCredit**, the proposed remuneration policy attracted considerable coverage. Following extensive engagement with the company and internal discussion, we supported the pay proposals, by exception to our policy. We considered various mitigating factors, which led to a finely balanced decision to support. These included the fact that the package is structured so that total pay is the same at target as in the current policy, the introduction of higher minimum shareholding requirements, and because performance targets under the variable pay are materially more stretching. This received 69% support.

## The proportion of shares voted and votes withheld

We aim to vote either in favour or against a resolution and only to abstain in exceptional circumstances, such as when our vote is conflicted, a resolution is to be withdrawn or there is insufficient information upon which to base a decision. We voted 100% of all votable shares.<sup>66</sup> There are a very small minority of meetings where we may not successfully execute votes. In 2023, this included meetings where Powers of Attorney were missing or late, as well as instances of share-blocking, where we chose not to vote in order to avoid the risk to trading. There was also an operational oversight leading to a no vote instruction being placed on ballots.

## Monitoring our shares and voting rights

As highlighted previously, EOS' approach is to focus engagement resource on the meetings of greatest interest and materiality to our investment teams and third-party stewardship clients. Each year we compile a list of the highest-priority companies where we want to ensure that our engagers are manually reviewing each agenda item for any vote that comes up. These are known as watchlist companies and are comprised of our engagement programme firms, companies of particular interest/sensitivity or those where our investment teams or EOS third-party clients represent significant holdings (in absolute terms or as a percentage of the company's voting rights). The voting watchlist represents a majority of EOS' AUA by value. EOS uses ISS to identify the meetings for which we have voting rights. EOS ensures that these accounts are suitably set up for voting.

## Monitoring service providers

We use the services of ISS to provide research on all companies for which EOS makes voting recommendations. EOS leverages and builds on ISS research and infrastructure (including the ISS ProxyExchange platform) and seeks to add value primarily by selectively escalating the most important or difficult voting recommendations (based on the materiality of holdings and the nature of the issues under consideration), engaging with companies and operating voting policies and approaches that more closely align to our views than ISS's benchmark policy.

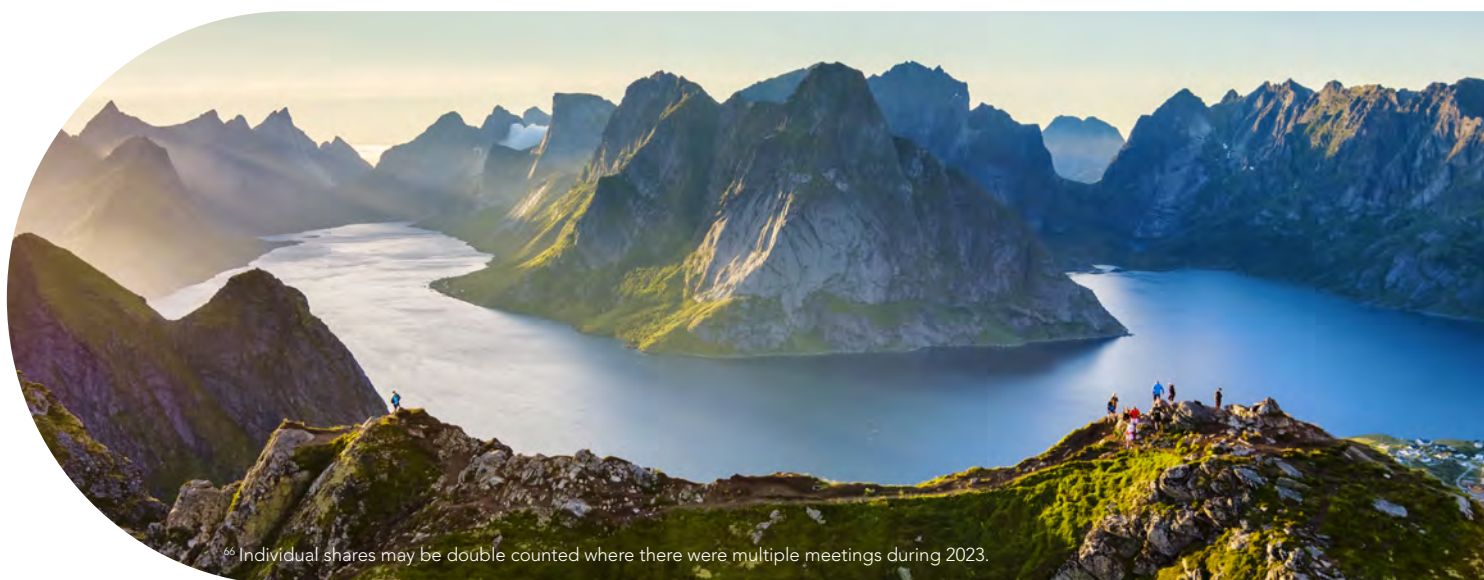
The recommendations that our investment teams and EOS third-party clients receive are, in the first instance, based on ISS' research using our voting guidelines. This is then overlaid with our intelligent voting approach. Engagers are deployed to add insight and value to a specific subset of these meetings – those on EOS' watchlist – by considering the voting recommendations approach in light of the specific company context and the engagement. As described earlier, our equity holdings are added to the EOS watchlist at the beginning of each year. As a result, the majority of the voting recommendations made to our investment teams are manual. ISS services are monitored by EOS through daily communication, ISS scheduled reports providing oversight of voting performance, regular service meetings, client voting account reconciliation and audit reviews conducted periodically by EOS on automatic voting instructions submitted by ISS across EOS client accounts.

## Fixed income: how we use our investor rights

### Fixed Income

Our real estate debt team does not habitually buy into deals that have already been structured. As a result, we have the opportunity to negotiate transaction documents ourselves. We seek to find mutually beneficial outcomes, while protecting the interests of our clients. Our approach to seeking amendments differs case-by-case, depending on the nature of the amendment. We aim to embody the values captured in the Federated Hermes Pledge in all of our dealings.

Meanwhile, our direct lending loan agreements are bespoke, and negotiated between ourselves and the borrower after we have conducted our due diligence. We construct the loan documentation to align it to the specific borrower and their behaviours, including issues identified in our ESG due diligence. Each loan contract is different, and we may require the borrower to change certain behaviours (including in relation to ESG risks) as part of the conditions of the loan. While we are not able to initiate an amendment of the loan terms once the financing has been provided, key opportunities where we can seek to influence the company's



<sup>66</sup> Individual shares may be double counted where there were multiple meetings during 2023.

behaviour after the contract has been agreed can arise when the borrower seeks our permission to alter the loan terms – for example, because the company wishes to make an acquisition. Outside of these amendment events, we will engage with management or the private equity shareholder to influence behaviours via the resources we have internally.

For credit and structured credit markets, the chance to influence such documentation comes at the time of primary issuance. If the documentation is unfavourable to the interests of creditors, this is a risk factor and we may engage with the company, as well as the originator of the assets and arranging bank for structured credit, to improve it. If we are unable to achieve these changes, they will become a factor in our investment decision and will influence how we choose to allocate our risk.

Within structured credit, an essential part of the due diligence process is to review the prospectus and transaction documents. These govern the noteholders' relationship to the special purpose vehicle (SPV), the assets within and the related counterparties. We pay particular attention to the ability of the SPV to pay interest and the principal on notes under multiple stress scenarios, which includes an assessment of the triggers and covenants in the deal and our enforcement rights over the assets in the collateral pool. We also ensure the transaction complies with all relevant regulation and any appropriate safeguards for future changes to regulations. Once the prospectus and transaction documents have been thoroughly reviewed, we work alongside the issuers, originators, sponsors and/or arranging banks to secure any amendments in the documentation that we feel are necessary to protect our position as a noteholder in the capital structure.

We seek access to information provided in all documentation through engagement with the company, as well as the originator of the assets and arranging bank for structured credit. The more information we have, the less uncertainty there is. This, in turn, may increase our willingness to take on more risk.

## Impairment and enforcement rights

The relevant rights for real estate debt are the control over cash flows within the Borrower structure and enforcement rights, which are available when there is a breach of covenants. We only use enforcement as a last resort – in the first instance, we seek to engage and agree an alternate approach with the party in breach. As we are often the sole lender, we are able to hold these bilateral conversations directly with the recipient of the loan. We continue to manage our loan portfolio with the long-term interests of our clients in mind. Since the interest rate rises, we have had a number of loans mature. Refinancing risk increases in times of rising interest rates, but we are pleased to report that all loans that matured in 2023 were repaid in full and on time.

As each of our direct lending loan agreements is bespoke, our specific rights can vary. If a borrower defaults on a loan – for example, if an interest payment is missed or the borrower fails a covenant test – our Direct Lending team will enter into a negotiation with both the shareholder and the management team of the borrower. We will seek a positive outcome for all parties involved in the negotiation, although we will always act in our investors' interests in line with our fiduciary duty and applicable requirements. We have a right to take security over the shares and other assets of the borrower in such circumstances but will always seek to find other solutions before taking this action.

In a distressed situation, value is impaired and will be redistributed among financial stakeholders. When we invest, we seek to understand the recovery risks associated with the impairment of assets. If a company is in distress, an organised group of bondholders can decide whether to enforce their rights or not, although this is very rare. We want the appropriate right to recovery of a failed business. In some cases, bond documentation is written so that there is a carveout or 'trap door', meaning that the assets that support the bond we are buying can be transferred outside of the restricted group. This would be a disincentive to invest, and we would communicate this to the bank or company. Under certain situations we would not invest, as we would not have what we deem to be appropriate rights under a distressed scenario.

**The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Past performance is not a reliable indicator of future results and targets are not guaranteed. This document is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments.**



## Sustainability and investment glossary

### Active Management

Actively selecting investments based on an investment team's own judgment, research and experience rather than an asset's index weighting. An actively managed fund is not a tracker fund.

### Active Ownership

Actively exercising shareholder rights by voting at meetings and engaging with companies to encourage responsible corporate behaviour.

### Active Share

A measure of the percentage of a fund that is invested differently than its benchmark. It expresses how active the fund manager is.

### Advocacy

Actively seeking to influence change in public policy in the interests of investors and the wider society by engaging with policymakers, regulators and industry bodies on a range of issues. These include: the financial system and investment industry, corporate governance, business purpose, climate change, inequality and inclusion.

### Carbon footprint

A measure of a group, individual or a company's total greenhouse gas emissions.

### Carbon pricing

The economic cost of emitting CO<sub>2</sub> into the atmosphere, either in the form of a fee per unit of emissions or an incentive for reducing emissions.

### COP

An annually held UN conference. The Paris Agreement was negotiated at the 21st conference in 2015.

### Corporate governance

The system of rules, practices and processes by which a company is managed, directed and controlled.

### Corporate responsibility

A company's duty to operate in a manner that does not harm the environment or society, and to take responsibility for its actions and their impact on employees, stakeholders and communities.

### Divestment

A form of negative screening through the process of selling investments that are not aligned with ESG or other objectives.

### Engagement

A purposeful, long-term dialogue between a company and its shareholders that aims to change or influence the way in which a company is run, in order to enhance the value of the company and generate positive environmental and social outcomes.

### ESG

Environmental, social and governance issues, which constitute the three pillars of responsible investing.

### ESG integration

A responsible investing approach which systematically and consequentially integrates financially material ESG factors and engagement insights alongside traditional performance factors in investment analysis and investment decisions.

### ESG leaders

A responsible investing approach which invests in assets with an above-average ESG performance, thereby creating a portfolio with a better ESG performance than the benchmark.

### Exclusions Policy

An investment firm or team's policy to exclude investments from specific sectors, business activities and/or behaviours from their investment universe.

### Exclusions Investing

A responsible investing approach which excludes investments from specific sectors, business activities and/or behaviours from the investment universe.

### Fiduciary duty

Fiduciary duties ensure that those who manage other people's money act in the interests of beneficiaries, rather than serve their own interests.

### Green bond

Debt securities which are used to fund projects with environmental benefits.

### Greenwashing

The act of making a product, service or organisation seem more environmentally friendly than it actually is.

### Impact investing

Investing in order to achieve a measurable, positive impact on the environment or society, in addition to generating financial returns.

### Integrated reporting

Company reporting that integrates both sustainability and financial information in one source.

### Negative screening

An investment approach that excludes some companies or sectors from the investment universe due to their policies, actions, products or services.

### Paris Agreement

An international accord, agreed at COP 21 in Paris in 2015, that aims to keep the rise in global average temperatures below 2°C compared to pre-industrial levels, while pursuing efforts to limit the increase to 1.5°C.

### Principles for Responsible Investment

Developed by investors, the six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a set of possible actions for incorporating ESG issues into investment practices.

### Positive screening

An investment approach that seeks to include companies from the investment universe due to their policies, actions, products or services.

### Proxy voting

A ballot cast by one person on behalf of the others. As many shareholders cannot attend annual and special meetings, companies allow shareholders to cast proxy votes.

### Responsible investing

An investment approach that considers ESG related factors and incorporates engagement and stewardship activities to better manage risk, create positive societal impacts and generate sustainable, long-term financial returns.

### Shareholder activism

A form of public engagement by which investors use their shareholdings to promote change at a company and achieve certain goals.

### Shareholder Rights Directive II

A directive from the European Union that aims to strengthen the position of shareholders and to ensure that decisions are made for the long-term stability of a company.

### Stewardship

A dialogue between shareholders and boards that aims to ensure that the company's management and strategy are effective and aligned with shareholders' interests. A focus on ESG issues helps to mitigate risk and produces positive outcomes for society and the environment.

### Sustainable investing

A long-term, active approach to investing that is efficient and intergenerationally fair to all beneficiaries and stakeholders, combining an analysis of ESG factors and active ownership.

### Stewardship codes

Codes that offer guidance on investor engagement and transparency about how investors should exercise their ownership and governance responsibilities. The first stewardship code was introduced in the UK in 2010 and almost all OECD jurisdictions now have national codes or principles.

### Sustainable Development Goals (SDGs)

Convened by the UN, the Sustainable Development Goals (SDGs) are the blueprint to achieve a better and more sustainable future for all. They address the global challenges we face, including those related to poverty, inequality, climate change, environmental degradation, peace and justice. There are 17 goals, 169 targets, and progress towards these targets are tracked by 232 indicators inherent in the goals.

### UN Global Compact

A global corporate sustainability initiative that calls on companies, investors and other participants to align their strategies and operations with universal principles on human rights, labour, the environment and anti-corruption.

### Voting

Exercising the rights given to equity holders in companies to vote on business matters and director elections during annual and extraordinary general meetings.



**The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Any investments overseas may be affected by currency exchange rates. Past performance is not a reliable indicator of future results and targets are not guaranteed.**

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## Federated Hermes

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Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns and, where possible, to contribute to positive outcomes that benefit the wider world.

## Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by five decades of experience
- **Private markets:** private equity, private credit, real estate, infrastructure and natural capital
- **Stewardship:** corporate engagement, proxy voting, policy advocacy

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