

# Responsible investing update

September 2022

This update summarises MLC Asset Management Services Limited's (MSL) environmental, social and governance (ESG) approach and provides examples of recent ESG-related activities in client portfolios.

## What is responsible investing?

There is broad agreement across the asset management community that ESG factors can materially impact investee companies' operational and financial performance, and thus investor returns. 'Responsible investing' is the shorthand for integrating the assessment of ESG factors into the investment process.

Drawing from extensive industry as well as academic evidence, responsible investing recognises companies that:

- ✓ act with an environmental duty of care
- ✓ have the support of communities in which they operate, and
- ✓ have transparent and robust governance processes and standards,

are more likely to deliver sustainable long-term investment returns than those that fall short on these grounds.

Intuitively too, responsible investing makes sense. If, for example, a company doesn't take into account physical risks such as risks arising from pollution (E), does not properly manage its human capital by underpaying workers (S), or has weak oversight of key management functions (G), it will likely experience adverse economic consequences at some point, which in turn will negatively impact its value.

Owing to all of this, we believe ESG factors matter when making investment decisions.

## Examples of ESG factors include:

 <p><b>Environmental</b></p> <ul style="list-style-type: none"> <li>• Climate change</li> <li>• Water supply</li> <li>• Energy use</li> <li>• Pollution</li> <li>• Biodiversity</li> </ul>	 <p><b>Social</b></p> <ul style="list-style-type: none"> <li>• Human rights</li> <li>• Supply chains</li> <li>• Health and safety</li> <li>• Indigenous rights</li> <li>• Modern slavery</li> </ul>	 <p><b>Governance</b></p> <ul style="list-style-type: none"> <li>• Board independence</li> <li>• Remuneration</li> <li>• Bribery and corruption</li> <li>• Shareholder rights</li> <li>• Human capital management</li> </ul>
---	--	---

## How does MSL consider ESG factors?

MSL uses the services of many specialist investment managers to select individual investments for clients' portfolios.

We expect active investment managers to consider all material factors, including ESG, that may impact investment performance. Rather than second-guessing our investment managers, and prescribing what they should do, we believe they are best placed to scrutinise ESG factors across all investments they consider.

Some of the ways in which ESG risks can be managed include:

- avoiding an investment, or reducing the position size
- engagement with the company or using proxy voting rights to influence positive change, or
- as a last resort, divestment or exclusion.

As part of our responsible investment practice, we work closely with MLC Investments Limited, the Responsible Entity that determines how proxy voting is conducted for our portfolios, to vote on AGM resolutions. Primarily via our managers, we also actively engage with companies with a view to improving

companies' performance on ESG issues, which in turn is expected to enhance and protect the long-term value of clients' portfolios.

## How does MSL monitor its managers' ESG incorporation?

As part of MSL's ongoing manager reviews, our investment managers' processes for assessing ESG factors are actively monitored to ensure alignment with MSL's **Responsible Investment Policy**. Assessments are done through regular face-to-face interactions as well as by reviews of managers' quarterly ESG reports.

We also undertake annual reviews of each manager's ESG policies and expect evidence of incorporation of ESG factors into their processes. A manager's ESG underperformance can contribute to its termination.

## ESG activity

The following section highlights some of our investment managers' ESG perspectives and activities in MLC portfolios during the 1st half of 2022.

### Environmental



#### Energy efficiency in data centres

As part of its engagement with an Australian listed company, one of our managers met with the investor relations team of the company to discuss energy efficiency in data centres.

A key purpose for the engagement was to better understand the company's efforts towards lower Power Usage Effectiveness (PUE) ratios (energy efficiency) given the energy intensive nature of operations.

This particular company's PUE levels are around 1.4x, which are industry leading. This is underpinned by high quality equipment, the use of artificial intelligence and advanced engineering and serves as a competitive advantage.

The company also discussed a few of their social initiatives which the largest clients are attracted to because of alignment to their own ESG initiatives.

## Environmental continued



### Fashion industry needs to do more and quickly to reduce its carbon emissions

In June one of our managers co-Heads of Research travelled to Copenhagen for the 2022 Global Fashion Summit, a two-day forum for the discussion of the global apparel industry's most pressing sustainability challenges. These are not insignificant; the industry is estimated to be responsible for between 4% to 10% of annual global emissions.

While fashion may have stepped up its sustainability efforts in recent years, to date these measures have had only limited impact – the current trajectory of carbon emissions is not aligned with the goals of the Paris agreement, with the gap likely to widen in the years ahead. In Copenhagen, the manager was left in little doubt that the industry understands it must do more and do it more quickly. The manager was also impressed by some of the genuinely innovative work going on to try and turn that understanding into

action. For now, however, this isn't happening at the scale required. For that to happen, more systemic change is required. At the heart of this is the need for greater collaboration between brands, competitors and value chain stakeholders, while pressure is also growing for the industry to embrace a more circular model which minimises waste, maximises resource efficiency and extends the life of textiles already in existence.

Bringing together clothing brands, supply chain operators, non-governmental organisations (NGOs), charities and a host of other stakeholders, the event was an opportunity for our manager to build further on its existing understanding of fashion's sustainability landscape and how its evolution might not only impact the companies in which the manager invests today but how it could also shape the opportunities of tomorrow.



### Protecting biodiversity in accordance with forestry regulations

One of our fixed income managers highlighted an engagement during the period with a global tyre manufacturer. The company had been subject to allegations that they were complicit in and covered up industrial-scale deforestation of over 2,500 hectares of rainforest in the run-up to the launch of their flagship 'eco-friendly' sustainable natural rubber joint venture project in Indonesia. The company noted that it fully respects and complies with all prevailing Indonesian laws with proper forestry permitting.

During the engagement, the company detailed the numerous environmental and social safeguards it undertook to protect biodiversity in accordance with forestry regulations.

In addition to the detailed actions that the company took in relation to this project, the company has published commitments for sustainable natural rubber since 2016 with regular assessments of the various participants in its supply chain.

The company was also one of the founding members of the Global Platform for Sustainable Natural Rubber, which includes tyre manufacturers, rubber suppliers and processors, vehicle producers, smallholders of rubber and NGOs. The company has engaged with 100% of its rubber suppliers and performs regular assessments on its supply chain. Finally, the company has had a zero deforestation-commitment for years.

## Social



### Workplace diversity and inclusion

One of our managers highlighted a specific engagement with one of its holdings, being a multinational industrial company that manufactures industrial tools and equipment.

A key topic for the meeting with the company was the discussion regarding the company's business ethics practices, a field where they have strong policies and very detailed disclosures. Nevertheless, allegedly the company has had practices where equipment was sold to or used by the Russian military. A practice that should not be possible shows signs that procedures have not been followed. A detailed investigation is taking place internally to address the incident thoroughly and

prevent anything similar from happening again.

The manager also engaged with the same company on workforce diversity and inclusion (D&I), discussing attracting and retaining women to the workforce. The company has a target of 30% women by 2030, but due to a somewhat decentralised organisation, it is challenging to have the same increase across different divisions. The company tries to combat this by having D&I programs fitted to different divisions and markets, where local legislation applies. Additionally, the company offers more flexible working hours, female focus on engineering in local communities, and having meetings to share initiatives to develop and attract D&I across divisions.

## Governance



### Making proxy votes<sup>1</sup> count

For Australian companies, MSL works closely with MLC Investments Limited (MLCI), the Responsible Entity that determines how proxy voting is conducted for portfolios we manage. The process is designed to protect and enhance the investment value of our portfolios' share investments, recognising the strong link between good corporate governance and investment value. MLCI applies the Financial Service Council (FSC) Standard and Guidelines on proxy

voting to its operational processes where applicable.

Refer to MLCI's **Proxy Voting Policy** for more details, including a summary of proxy voting records.

For global shares, we currently outsource proxy voting to our international investment managers as we believe they are best placed to vote on matters pertaining to international companies held in their portfolios.

1. Governance is an important component of ESG, as it's the governance of companies that ultimately determines the ethos of management and how robustly environmental and social risks are managed. Shareholder voting is a means by which shareholders can influence a company's operations, its corporate governance and activities of social responsibility. Proxy voting is where a vote is cast on behalf of a shareholder.

## Modern slavery

*Modern slavery describes situations where offenders use coercion, threats or deception to exploit victims and undermine their freedom. Practices that constitute modern slavery can include human trafficking, slavery, servitude, forced labour, debt bondage, forced marriage and child labour.*

### The intersection of renewable energy generation and modern slavery

One of our listed property managers observed that an emerging issue they've seen this year with several Real Estate Investment Trusts (REITs) has been the intersection of renewable energy generation and modern slavery. As an increasing number of REITs commit to net zero carbon targets and renewable electricity generation targets, solar panel supply is very important.

However, our manager noted that a study by the Helena Kennedy Centre at Sheffield Hallam University in 2021 found that a significant proportion of the world's solar panels are manufactured with forced labour in the Xinjiang Region of China, meaning this increase in solar generation has led to an increased risk of sourcing solar panels that have been made with forced labour. In order to avoid this, several companies are making a deliberate move towards more expensive solar panel manufacturers that are able to show that their supply chains are free of forced labour.

Source: MLC Asset Management Services Limited. As our investment managers are constantly reviewing and making changes to their holdings, these investments may no longer be included in the portfolio.

MSL's Responsible Investment Policy is available at [mlcam.com.au/responsible-investment-policy](https://mlcam.com.au/responsible-investment-policy).

For MLC MySuper, MSL is also required to adhere to the NULIS Responsible Investment Policy available at [mlc.com.au/nulis-nominees-responsible-investment-policy](https://mlc.com.au/nulis-nominees-responsible-investment-policy).

## Important information

The information in this communication is for MLC Asset Management Services Limited only. You should assess or seek information on the responsible investing policy or equivalent environmental, social and governance policy for any other entity, including another Insignia Financial Group entity or one of its partner investment managers, and whether it is appropriate for your needs, financial situation and investment objectives.

This communication is provided by MLC Investments Limited (ABN 30 002 641 661 AFSL 230705) as Responsible Entity of the MLC Investment Trusts and MLC MasterKey Unit Trust, Navigator Australia Limited (ABN 45 006 302 987, AFSL 236466) as Responsible Entity of the Pre Select funds, and NULIS Nominees (Australia) Limited (ABN 80 008 515 633, AFSL 236465) as trustee of Plum Super, MLC MasterKey Fundamentals Super and Pension, and MLC MasterKey Business Super products which are a part of the MLC Super Fund (ABN 70 732 426 024) (together 'MLC'). MLC Asset Management Services Limited (ABN 38 055 638 474, AFSL 230687) ('MSL', 'we', or 'our') is the Principal Investment Advisor to MLC Investments Limited and the Portfolio Manager to NULIS Nominees (Australia) Limited. MLC Investments Limited, Navigator Australia Limited, NULIS Nominees (Australia) Limited and MLC Asset Management Services Limited are part of the Insignia Financial group of companies (comprising Insignia Financial Ltd ABN 49 100 103 722 and its related bodies corporate) ('Insignia Financial Group').

This communication may constitute general advice. It has been prepared without taking account of an investor's objectives, financial situation or needs and because of that an investor should, before acting on the advice, consider the appropriateness of the advice having regard to their personal objectives, financial situation and needs. No member of the Insignia Financial Group guarantees or otherwise accepts any liability in respect of any financial product referred to in this communication.

You should obtain a Product Disclosure Statement (PDS) and target market determination (TMD) relating to any financial products mentioned in this communication issued by MLC Investments Limited, Navigator Australia Limited or NULIS Nominees (Australia) Limited, and consider it before making any decision about the product. A copy of the PDS is available upon request by phoning the MLC call centre on 132 652 or on MLC's website at [mlc.com.au](https://mlc.com.au).

Any projection or other forward-looking statement ('Projection') in this document is provided for information purposes only. No representation is made as to the accuracy or reasonableness of any such Projection or that it will be met. Actual events may vary materially. Any opinions expressed in this communication constitute our judgement at the time of issue and are subject to change. We believe that the information contained in this communication is correct and that any estimates, opinions, conclusions or recommendations are reasonably held or made as at the time of compilation. However, no warranty is made as to their accuracy or reliability (which may change without notice) or other information contained in this communication.

This communication is directed to and prepared for Australian residents only.

The investment strategies are current as at the date this communication was prepared, but are subject to change. Investment strategies are regularly added or removed at any time.

We may use the services of any member of the Insignia Financial Group where it makes good business sense to do so and will benefit customers. Amounts paid for these services are always negotiated on an arm's length basis.