

ESG integration at Aberdeen Asset Management

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Vermont Pension Investment Committee

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Aberdeen Asset Management

- Global asset manager, serving clients around the world
- Started in 1983
- AUM: £301.4 billion (US\$402.9 billion) as at 30 Jun 16
- Broad range of investment capabilities: equities, fixed income, property and alternatives
- Global presence: 38 offices in 25 countries

Investment philosophy

Fundamental

- Bottom up, conviction investors
- Long term investors

Disciplined

- Investment process is the same within asset classes

Active (Engagement + proxy voting)

- Understand all the unique risks and opportunities (short and longer term)
- Not taken by surprise
- Know best way to engage and potentially make investment better



Stewardship

- Key to our investment philosophy – part of being fundamental, disciplined and active
- Taking care of the capital that investors entrust to us to invest on their behalf
- How do we do this? As bottom up, conviction investors, who invest for the longer term, we:
 - Understand the risks/opportunities of investments before, during and post investment
 - Engage our holdings on their risks/opportunities – aim to help make them better investments
 - Engage our clients on our conversations with holdings – ensure clients are part of dialogue



ESG

Holistic risk assessment – examining all the risks and opportunities of an asset

- Concerned with material risks (financial, environmental, social and governance related)
- Focuses on how a company/investment manages those key risks
- Holistic risk assessment

A deep dive into the issues and management techniques for ESG related issues, through:

- Identification of risks
- Prioritisation of risks
- Target Setting/KPIs for risk mitigation
- Remuneration
- Strategy/Culture/Opportunity Set



ESG

So, ESG is:

- A part of our Stewardship philosophy
- Is 'baked into' our equity investment process
- Also fully integrated into our processes for fixed income, property and alternatives
- Helps mitigate the downside risk

By integrating ESG into our investment decisions, we are able to:

- Better price
 - Understand the true price of an asset and act accordingly
- Better size
 - Allocate the most appropriate weighting of an asset within a portfolio
- Better engage
 - Know the best way to engage a group
 - Know what to push for/encourage the group to improve

How ESG is integrated into our equity process

Quality/Q rating (1 - 5):

- Ease of the business to understand
- Balance sheet strength
- Corporate governance
- Holistic risk/opportunity set (financial + ESG considerations)
- How the group will treat a minority shareholder

Value/V rating (1 - 5):

- How the asset is priced in the market – cheap or expensive?
- Pricing as compared against its own historical price as well as vs its peers

How ESG is integrated into our equity process (continued)

- ESG/RI analyst is on our regional equity teams
- Corporate Governance specialist on each equity team
- ESG is part of the team conversations on holdings
 - Not a box ticking exercise – risks are different for each investment
 - Not a top down or topical approach
 - We weigh all risks/opportunities together – not considered in silo
- Material ESG issues can impact Q/V ratings
- Companies must score a 1, 2, or 3 for both Q and V to be included in portfolios

Examples of ESG considerations

1. Global Retailer of Sporting Goods

- Problem: Supply chain issue – caused reputational damage – share price suffered
- Investment: our Q and V ratings were being impacted
- Our action: engage the company and encourage improvement
 - Have a rep at Board level accountable for supply chain
 - Tie supply chain performance to exec remuneration
 - Create a human rights policy; set standards for suppliers
 - Have a third party audit the supply chain/ETI
 - Report fully on risk and mitigation techniques
- The result:
 - Group mitigated supply chain risk
 - Mitigation of reputational damage
 - Boosted share price
- Investment: holding remained in portfolio

Examples of ESG considerations

2. Mining group

- Problem: relations with labour unions – caused reputational damage – caused costly stoppages with mining operations – loss of competitive advantage
- Investment: our Q and V ratings were being impacted
- Our action: engage the company, help identify specific issues and push for improvement
 - Identify scale to which group was impacted by poor relationship with unions
 - Put remedial action in place: opening up communication with unions
 - Improve source of problem – treatment of workers, pay, better health and safety programmes – making workers part of the solution
 - Put oversight on Board and link performance to exec remuneration
 - Report fully on risk, mitigation techniques and outcomes
- The result:
 - Group mitigated risk with unions/work force
 - Boosted competitive advantage – reflected in share price
- Investment: holding remained in portfolio

Examples of ESG considerations

3. Integrated oil and gas company / mining group

- Problem: negative impact from climate change (GHG emissions, carbon trading, stranded assets)
- Investment: our Q and V ratings could be impacted
- Our action: engage the company, prioritise the risks, and suggest mitigation plan
 - Ascertain the relative impact to the group (% of business)
 - Create a KPI for reducing GHG emissions; raise understanding of carbon trading schemes
 - Push for greater transparency on carbon emissions data and how mitigation fits with overall group strategy
 - Encourage the use of newer technologies for exploration, extraction, and refining
 - Report on assets likely to be stranded longer term due to changes in legislation
- The result:
 - Reduction of GHG emissions in the context of group properties
 - Mitigation of reputational damage
 - Increase competitive advantage
- Investment: holdings remained in portfolio

Examples of ESG considerations

4. Telcoms group

- Problem: bribery and corruption – reputational damage – competitive disadvantage
- Investment: our Q and V ratings are being impacted
- Our action: engage the company, analyse the extent of the problem and encourage improvement
 - Have a rep at Board level accountable for bribery and corruption
 - Tie adherence to group code/policy to exec remuneration
 - Put whistle-blower procedures in place and report on non-compliance
 - Increase transparency on method of mitigation and on risk management platform
- The result:
 - Still in engagement
 - To date, not much progress made
- Investment: Q and V can be lowered to reflect risk

Summary

- Engagement is an ongoing process
- Change doesn't happen over night
- A risk is a risk, no matter how it is categorized

- We believe in doing our homework and understanding everything there is to know about an investment
- By doing this, we minimize the chance of being surprised by a negative event

- ESG is integrated into our investment process
- Good stewardship is part of our investment philosophy



Q&A



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