SARASIN
& PARTNERS

Our ownership discipline[1]

June 2019

Introduction

Once we have bought a stake in a company on behalf of our clients, our clients become owners of that company. Ownership confers important rights to select the company's leadership, approve major transactions, the auditor, and senior executives' pay amongst other things. But ownership also entails responsibilities to exercise these rights with due care and consideration.

The collective failure of asset owners and managers to properly monitor and hold executives to account is widely viewed as a weakness with capital markets[2] . In the end, the passive approach to ownership risks making all of us worse off if capital is allocated inappropriately, executives are not held to account and short-term results are prioritised over long-term productive investment.

Against this backdrop, Sarasin & Partners' stewardship philosophy has at its heart an ownership mindset. We stay close to our clients' companies not just to ensure we can monitor developments and the persistence of long-term value drivers, but also so we can effectively scrutinise and hold management to account for their performance.

Like most asset managers, we have a clear set of guidelines that govern our purchase and sale of company shares (our buy and sell disciplines). This document sets out how we act on a day-to-day basis as an owner on behalf of our clients: our ownership discipline[3]

It is worth emphasising that our ability to implement our ownership responsibilities varies by jurisdiction due to differences in legal frameworks, culture and market practice. We cannot commit to having the same access to, or influence over, company leadership everywhere we invest. Also, we are inevitably limited by the challenge of diffuse ownership, which means that in most cases our clients' holdings represent a small percentage of the total issued share capital. Finally, engagement can be very resource intensive, which means we inevitably have to prioritise those we believe to be most urgent and impactful. Notwithstanding these constraints, we believe it is important to use responsibly governance powers bestowed on us.

We endeavour to implement our "Ownership discipline" as effectively as possible for all our clients' companies. We believe we can – and do – make a difference as owners.

[1] This document should be read alongside our "Global Equity Investment & Ownership Philosophy and Process" and our "Principles for engaged company ownership", which details our goal to protect and enhance our clients' capital; and our commitment to take a long-term and constructive approach to our clients' companies, but equally our promise to challenge poor or damaging behavior.

[2] See for instance, the UK government commissioned Kay Review 2012.

[3] This paper focuses on how we pursue engagements as a shareholder, but we also pursue dialogues with companies where we hold debt instruments. In some cases the two are combined. The key difference, of course, is that creditors do not have a vote at company meetings. But they can exert influence in many of the other ways outlined here.

Responsibility for ownership rests with every member of the team

Importantly, our ownership discipline is not solely the responsibility of our stewardship team, or any particular individual to implement. Each and every member of our asset management team takes on this responsibility. The stewardship team offers support, advice and challenge for engagements, particularly in instances where problems have been identified and we embark on a programme of escalation. Our integrated approach is designed to bring together different skill sets to ensure we adopt an holistic and ultimately successful engagement strategy.

Early ownership

The decision to acquire shares in a company is taken on the back of in-depth scrutiny and early communication with company management. We will have established a strong long-term investment case, having taken account of environmental, social and governance considerations. We will have identified any areas for early engagement where we would be keen to see the company take action. An obvious area for initial dialogue with a company is where their practices or policies fall foul of our corporate governance and voting guidance.

Broader issues could relate to capital allocation, regulatory risk, labour treatment, harmful environmental impacts, etc.

Following the purchase of the company's shares, we write to the company's leadership – and ideally the Chair or Senior Independent Director (SID) of the board where this is possible – to introduce ourselves, outline the basis for our investment thesis and set out the identified areas for engagement. The engagement will normally be led by the responsible analyst and / or portfolio manager alongside a member of the stewardship team, with regular feedback to the broader team.

Ongoing monitoring

Each company is monitored by a dedicated analyst, supported by the wider team. In addition to the engagement topics identified and initiated on purchase of the company's shares, we keep abreast of company news and any new areas for dialogue that emerge. The lead analyst and stewardship team review shareholder meeting votes, and keep abreast of areas we vote against the board. Where material we will endeavour to engage with the board on matters of concern prior to a vote against, and communicate what we wish to see change. If we believe our voting policy produces a perverse outcome, we will over-ride it, recording our rationale. In this way, our voting is an integral part of our ongoing monitoring as well as our engagements.

We monitor company public statements, sell-side and ESG research, proxy guidance, general media as well as information provided by regulatory and non-governmental entities. We look for independent third-party perspectives on significant developments; and we actively seek exchanges with civil society or government bodies that have company or sector-specific campaigns. As a responsible owner, we believe it is important to monitor public perceptions and reactions to our clients' companies.

Early ownership actions

- Investment case identifies areas for engagement
- Initial introductory letter to Chair/SID setting out the basis for our investment and any areas of concern (introducing likely votes against the board)

Ongoing monitoring

- Look to wider sources of information beyond sell-side notes, including non-governmental and governmental analysis
- Embedding our voting decisions into company monitoring
- Seek direct discussions with civil society and government where pertinent

Addressing problems

Our investment process will tend to screen out companies with major concerns. But inevitably problems arise from time to time. This may pertain to a change in leadership; a shift in strategy; a damaging revelation around misconduct; or an external event that leaves our clients' company vulnerable in some way. Every situation will be assessed on its own merits, but the critical point is that we approach such matters as an engaged owner, not a passive bystander. We will consider whether we can play a constructive role to either support or challenge the company in its response. In certain cases we may decide to sell the company's shares (see below on our sell discipline).

In the event that we decide to proceed with an engagement, the lead analyst, portfolio manager(s) and stewardship team work together to set out an engagement plan.

These plans are sufficiently high level to permit flexibility as events unfold and new information is revealed. They are important to ensure we maintain clarity around the desired outcome of the engagement, and how we believe this will benefit our clients.

In the first instance, exchanges are normally undertaken privately in writing and through calls and/or face-to-face meetings. Alongside exchanges with the Chief Executive/Chief Financial Officer, we seek direct exchanges with the company chair, lead independent director, or other non-executive and independent board members if we feel this would be more effective. Early information gathering may take place through Investor Relations. We consider whether to work alone or alongside other shareholders at all stages.

We are guided by our responsible long-term ownership mindset. We would not, for instance, encourage a management team to look for a 'quick fix', or to shift blame or costs in a way that leaves the underlying problem unresolved or harms others unfairly. Such a course would run contrary to our philosophy that companies that act responsibly are more likely to deliver sustainable returns.

Of course, the team's assessment of any situation will necessitate judgements, and there will be cases where the appropriate course of action is uncertain. We are also realistic about our ability to effect change and may limit our intervention to setting out our perspective as a concerned shareholder to the board (see below on "Knowing when not to engage").

Addressing problems

- Draw up an engagement plan, with clear objectives and based on an assessment of likely impact
- Initiate a direct dialogue through correspondence and/or meetings with identified directors where possible

Escalation procedure

If our effort to persuade a company through private exchanges to take a particular course of action falls of deaf ears, we may escalate our engagement. We will do this if we believe that a more determined and potentially public approach is necessary, likely to have an impact, in line with local regulatory rules and ultimately helpful to our clients' interests.

There is a range of options open to shareholders to apply greater pressure on boards, including:

Voting against directors. A central pillar of good governance is that individual directors can be held personally accountable for shareholder outcomes. We therefore use our votes thoughtfully, and do not automatically vote for directors. We communicate with proxy advisory agencies to ensure they are aware of long-term shareholder concerns. The power of the vote varies by jurisdiction, but is not limited to the legal rights it conveys. Heavy votes against individual directors (in some cases more than a 10% vote against) can be influential through the reputational impact it has, and the signal it sends. Also, it is important to understand the board dynamic to identify those who might be sympathetic to our cause and take a differentiated approach reflecting this.

Filing shareholder resolutions/proposing directors. Shareholders often have powers to file shareholder resolutions, including proposing independent directors for the board. This can be an effective tool to ensure the board has the right leadership, or to press a board to undertake a particular action they are otherwise resisting. Even where the shareholder proposals are not ultimately passed, if sufficient support is gandered this sends a strong signal to the board that it needs to act.

Voting against the auditor and/or annual report and accounts. Shareholders often have a binding vote on the auditor's appointment (and even non-binding votes can be powerful). This is because the auditor play a critical role in protecting investors from misleading reporting of performance and capital strength. This vote (and any associated engagement with the auditor) can be influential since by pressing an auditor to be tougher this can force management to reveal information they might otherwise wish to conceal. Similarly, a vote against an annual report and accounts sends a strong signal that shareholders' lack faith in what is being reported.

Submitting formal complaints to regulators. Where a breach has occurred, for instance inadequate shareholder disclosure or poor treatment of a stakeholder, then a complaint to the relevant regulator may be an appropriate tool to drive change.

Public statements. Depending on the situation, a public statement by one or more shareholders challenging a company's actions or directors can help to draw broader market scrutiny and prove effective in generating a response.

Litigation. While there are frequently high hurdles to overcome in any legal action, in extreme cases it may be appropriate to consider legal action against directors – or supporting someone else in their legal action – for failures to uphold, for instance, their fiduciary duties. The threat of legal action can also prove influential.

None of the actions should be taken lightly. At every stage we ensure proper internal debate and challenge, weighing up the benefits and costs, and where appropriate we seek legal guidance. Our effectiveness depends on building our reputation for accurate analysis, our commitment to long-term sustainable returns, and our integrity, so we need to move forward with any engagement carefully. But, as already highlighted, we believe investors have a responsibility to speak out against poor behavior, and we do not avoid confrontation at all costs. Where appropriate we seek partnership with other shareholders, and/or civil society actors. We routinely review our investment thesis to ensure our holding remains appropriate.

Escalation

- In the event that our initial engagement fails to progress, we assess whether or not to escalate
- If we proceed, we update the engagement plan with specific and iterative escalation measures; and potential outreach to partners
- We ensure necessary internal communication, review and legal checks

Knowing when not to engage, or when to stop

Just as we are committed to fulfill our clients' ownership responsibilities, it is just as important to know our limits to effect change, either alone or as part of a broader group. There will inevitably be cases where our ability to drive change will be remote. Likewise, there will be cases where we fail to achieve our objective. In these instances, beyond clearly setting out our concerns to the board, we will deploy our efforts elsewhere. We will also carefully review our conviction in the investment case, to determine whether or not we should continue to hold the company's shares.

Our sell discipline

Sometimes, our experience with an engagement will be a material driver for a decision to sell the investment. Even where an engagement is progressing well, however, we may decide to sell the shares where new information comes to light that causes us to reassess the investment case, or the share price rises to unsustainable levels.

The long-term nature of some engagements always needs to be balanced with the need to take quick sale decisions. The portfolio manager retains the final decision about whether or not to sell a company's shares, and will take this decision with a clear understanding of any ongoing dialogue and expectations over progress. The rationale will be detailed in any final sell note.

Stopping engagement

- In the event that we decide not to engage/abandon an engagement, we record the reasons for this decision
- A review of our investment case is undertaken, taking account of the abandoned engagement

Sell discipline

- The sell decision is undertaken by the portfolio manager(s) taking into account any ongoing engagement
- In the event that the portfolio manager(s) decides to sell a company's shares during an engagement process, the team will coordinate to ensure appropriate communication to the company, and other partners or entities involved
- A sell note will detail the rationale for the sale, including how the engagement experience was taken into account

Important note: We do not need to be 'taken inside'

We operate in public markets and all of our interactions are governed by local laws and regulations that seek to ensure a level playing field for all investors. We are clear that we do not normally wish to receive any material non-public information. In the rare case where we are in receipt of 'inside' information, we have policies to ensure we abide by the required procedures to prevent the spread of this information or any associated trading.

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