Nikko Asset Management Group Response to the UK Stewardship Code 2020

April 2023

nikko am
Nikko Asset Management

For the reporting period 1st January to 31st December 2022

Foreword

We realise the growing importance of sustainability with every year that passes. We see it in our investments, we hear it from our clients, and we witness it in world events. As the needs of our clients and society evolve, we recognise that the definition of what it means to be responsible stewards of our client's capital also evolves. We have taken proactive and bold steps across our organisation to address these needs, described within this report, and I believe that they speak louder than any words.

2022 marked a notable milestone for Nikko AM Group. My appointment as its first female President was important, not just for us, but for asset management as a whole. Women have historically not been well represented in the finance industry, whether in Japan, Asia or globally. That is now changing, and I am proud that Nikko AM Group is in the vanguard, a testament to my colleagues and predecessors on our board.

Since joining the company in 2014, I have been a vocal advocate for change. I was an early supporter of our diversity and inclusion efforts, which began in 2015 with our Women's Working Group and have championed the importance of having the widest range of talent possible represented in our ranks. For many years, Nikko AM Group has also been energetic in supporting better stewardship and governance, both within and outside the company.

Our Non-Executive Chairman, Yoichiro Iwama, played a key role in promoting the introduction of Japan's version of the Stewardship Code in 2014 as a member of the Panel for Vitalizing Financial Capital Markets. In his current role as member of The Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code he continues to be involved in any subsequent revisions to the Code.

On these solid foundations, we have continued to build our stewardship credentials in 2022. Both our Executive Chairman, Yutaka Nishida, and I have been given specific key performance indicators covering our sustainable investment activities. At the same time, we as a firm have undertaken a major review of our sustainability activities, resulting in the creation of a much-enlarged and centralised Global Sustainable Investment department. This will extend and deepen the reach of sustainability in our everyday investing and Stewardship activities.

We approach stewardship from a different perspective to many European asset managers. It is no less strong in Japan, but emphasises consensus over confrontation, collaboration over individuality. In our efforts, we are therefore trying to unite best practices from across the globe. In doing so, we believe we have an educational role in furthering stewardship, sustainability and diversity amongst both investors and investee companies in Japan and globally.

We believe we have gone a long way to fulfilling that role in the actions we have undertaken during the past year. But, given the pressing need for stewardship – and not least action on climate change – we understand the danger of complacency: we know we can and must do more in future years. Our to-do list includes further growing our Global Sustainable Investment department, advancing our ESG integration and stewardship activities and increasing the number of women in senior roles. They are among my top priorities in my role as President and I hope these will be seen in future reports of this kind.

Stefanie Drews, Group President

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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.

Statement of purpose

"Nikko AM, as an asset management company, acts as a fiduciary on behalf of its clients and is firmly committed to putting its clients' best interests first. It places fiduciary and ESG principles as the highest guiding themes of its corporate values and actions."

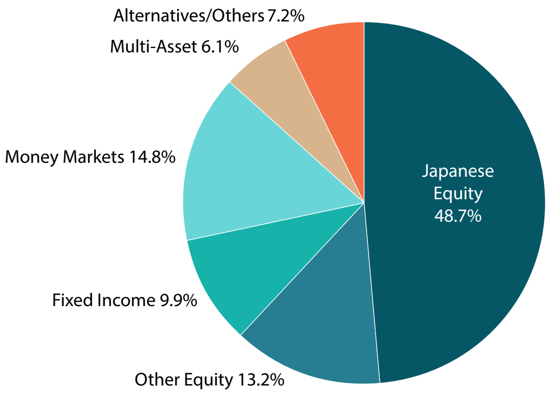
Context

With its origins in Japan, the Nikko Asset Management Group ("Nikko AM Group") is today one of Asia's largest independent asset managers, with $203.9 billion[1] assets under management ("AUM", as at 31 December 2022). Headquartered in Japan, which is home to a large proportion of both our clients and our AUM, we are also represented in the rest of the world, including the UK. We combine a global perspective with our Asian roots to create sophisticated and diverse investment solutions to meet our clients' needs. These needs differ, depending on whether the client is retail or institutional. But for all types, our guiding strategy is to ascertain the purpose for which their assets are being managed and then to steer them towards the outcomes that best meet that purpose. In doing so, we put stewardship at the heart of our activities and the distinctive values that our Japanese heritage brings.

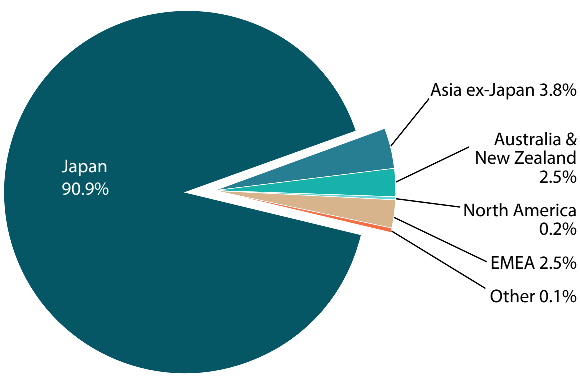
Japanese culture values harmony, both with nature and with other people, putting less emphasis on the individual and more on society than in Western traditions. We have therefore grown up over the past 60 years infused with the belief that we must be good corporate citizens. Our approach to stewardship and engagement has evolved against that background and it informs the way we have addressed our response to the UK Stewardship Code.

A breakdown of our AUM by asset class and client domicile is shown in the following charts.[2]

Assets Under Management by asset class[2]



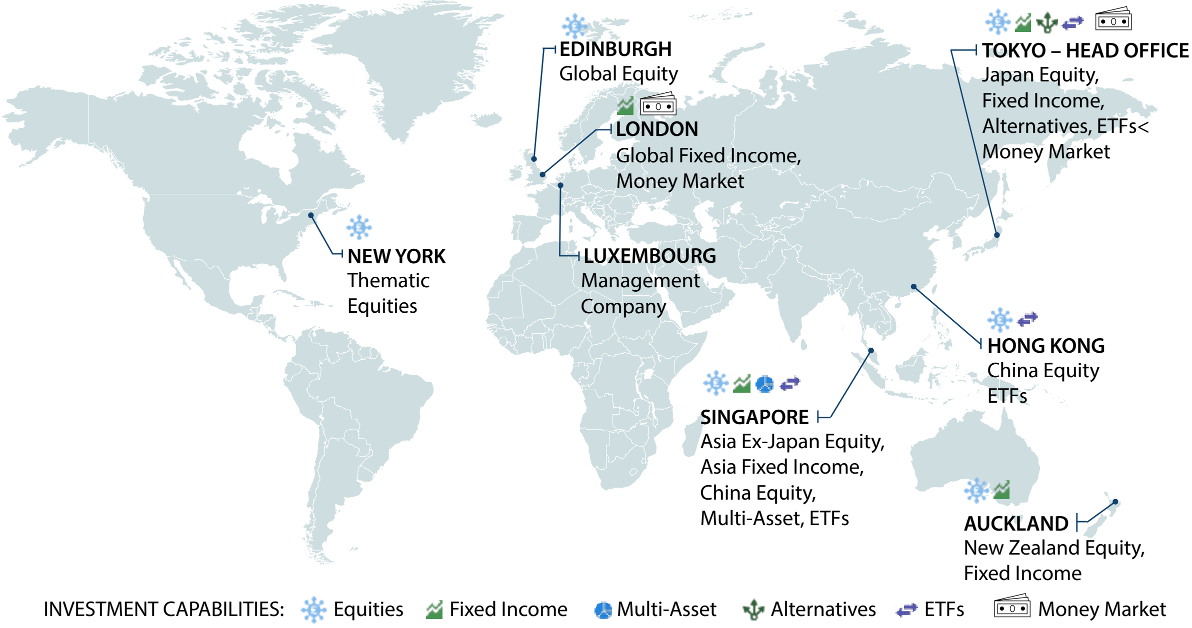
Assets Under Management by client domicile[2]



The Nikko AM Group and its affiliates has a presence in 11 countries, with our in-house investment teams located in seven of our offices in four continents. We have a diverse workforce that includes 30 nationalities working together with the common purpose of protecting and growing the assets of our customers in a way that best meets their long-term investment goals. Together we provide high-conviction asset management from across our global network, as well as across a range of active equity, fixed income and multi-asset strategies, with a complementary range of passive strategies, including some of Asia's largest exchange-traded funds (ETFs).

[1] As of 31 December 2022. Consolidated assets under management and advice of Nikko AM Group, including subsidiaries but excluding minority affiliates and minority joint ventures.
[2] Totals may not sum due to rounding of data at source. 'Multi-Asset' funds are made up of Equity and Fixed Income assets; the stewardship of each of these assets is addressed individually in this report. 'Alternatives' constitutes REITs, Equity Long/Short and Infrastructure funds. Infrastructure represents 0.5% of group AUM and is managed by external managers. These managers are subject to Nikko AM's external manager due diligence process, which includes a review of ESG policies.

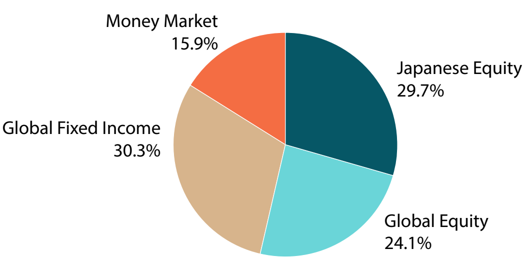
Locations of our offices and investment teams



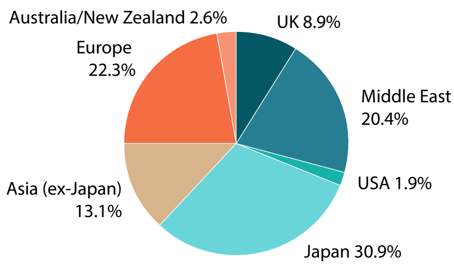
While most of our AUM and clients are based in Asia, our long-term business goal is to offer best-in-class investment solutions for clients worldwide.

We implement cross border delegation arrangements whereby the locally contracted Nikko AM Group office manages business development, supported by local client servicing teams, with portfolio management delegated to the respective regional Nikko AM entity where the relevant investment expertise is based. For example, the AUM of our UK entity, accounting for approximately 8% of the Group total (as at 31 December 2022), represents assets managed on behalf of a range of clients who are accessing the investment capabilities of both our local and global investment teams. A breakdown of the AUM of our UK entity as at 31 December 2022 is provided in the charts below:

Nikko Asset Management Europe Limited:
AUM breakdown by asset class



Nikko Asset Management Europe Limited:
AUM breakdown by client domicile



We believe in a sense of responsibility, stressing stability and harmony. We believe in promoting respect for our environment, for our community and for other people. As active owners we recognise the value of building long-term relationships built on trust and respect for the companies in which we invest to promote better outcomes for our clients, the economy, the environment and society. In doing so, we strive to be better global citizens.

Code of ethics

Below we outline our values in the context of our investment beliefs, culture and engagement and, in the activity section, explain how these enable effective stewardship. These values are encapsulated in our Code of Ethics, which commits us to upholding:

- our fiduciary duty to our clients,
- the integrity of capital markets,
- our responsibilities to environmental conservation, and
- our social responsibility.

The Code of Ethics is reviewed by the Nikko AM Group Board of Directors (more details of the review process are described in Principle 5) and attested to annually by all employees globally. It acknowledges that, as a fiduciary, we owe our clients a duty of loyalty and care. When acting in a fiduciary capacity, all employees must act for the benefit of our clients, placing their interests before the interests of the Group, a third party or their own. Employees must also act with reasonable care and diligence and exercise prudent judgement in the performance of their duties. The code provides guidance and sets standards in a number of specific areas, including our duties to regulators and the public, to upholding the integrity of financial markets, to ethical business practices, fair competition, and personal trading, and also our environmental and social responsibilities.

At the heart of our culture is the belief that, as stewards of our clients' money, we have a duty to provide the right investment solutions to meet their goals. To do this requires us to understand their investment objectives, risk appetite, sustainability ambitions, regulatory and accounting frameworks, as well as the wider social and environmental climate in which we all live.

Environmental, social and governance strategy

We strongly believe that environmental, social and governance (ESG) considerations are inherent to long-term corporate value creation and contribute to the realisation of sustainable economic growth. In the light of this, we view ESG issues as an integral part of our fiduciary duty to clients and endeavour to incorporate ESG principles in all our investment processes.

ESG has been a historical area of focus with our launch of Japan's first socially-responsible investment fund in 1999 and the Global Green Bond Fund with the World Bank in 2010 and forms a part of our wider global growth plans. In 2022, we launched an internal project, driven by our Group President Stefanie Drews, with the aim of establishing an enhanced ESG structure, fully connected across our global offices, that would enable us to deliver leading ESG outcomes for our clients and meet high international standards.

This project culminated in the launch of a Global Sustainable Investment department in August 2022 and the appointment of a Global Head of Sustainable Investment, a newly created role as well as significantly expanded ESG resources across the UK, Japan and Singapore. Further details on the resourcing and governance of this department can be found under Principle 2.

The department is split into five functions:

- **Regional ESG specialists:** these are our ESG "all-rounders" who work closely with the investment teams supporting their ESG integration and stewardship efforts. They also work closely with our other functions, such as client services and product development, to ensure that we deliver the best outcomes for our clients across the entire value chain.
- **Research and integration:** this function, which is still being developed, is responsible for supporting our investment teams and ESG Specialists with subject matter expertise and ensuring we continuously improve our integration efforts. The function will include, for example, an environmental specialist to help us enhance our activities in this area.
- **Stewardship:** this function will support and co-ordinate our firm-wide stewardship efforts. Looking forward, it will aim to continuously improve our stewardship activities, including engagement, proxy voting and ESG research and respective disclosures.
- **Data and reporting:** this function is dedicated to sourcing, storing, validating and disseminating ESG data globally, as well as providing support with ESG data analytics and reporting.
- **ESG regulations:** this function is responsible for identifying, assessing, determining and supporting our approach to ESG regulations and standards globally, with a focus on regulations in EMEA.

Principle 1

The creation of this department, and other organisational developments highlighted in this report, reflect the implementation of our updated ESG strategy and our commitment to meeting high international standards on ESG. Our approach to ESG integration is outlined in more detail under Principle 7. Our policies on ESG, responsible investing and stewardship are available on our website under the following headings: Fiduciary and ESG Principles, Commitment to Responsible Investment, Position Statement on Climate Change, Task Force on Climate-Related Financial Disclosures, Sustainability Report, Engagement and Stewardship Strategy, and Stewardship Activities Report and Self-assessment.

As part of our commitment to meeting international standards, we are continually improving many of our existing frameworks, policies and disclosures. For example, and as outlined below, in 2022 we developed and disclosed our 2030 net zero target under the Net Zero Asset Managers Initiative. Further initiatives that we are involved with are expanded upon throughout this report, with a list of key initiatives provided under Principle 4.

Culture

Our diverse, inclusive and collaborative culture is a key competitive advantage and supports our ability to generate differentiated insights. Our staff members come from a rich diversity of backgrounds, with language capabilities covering all the main Asian and European languages.

Our team meetings encourage widespread participation, drawing on the collective intellect, experience and cultural and gender diversity of our teams and each individual's experience to question the market consensus. Combined with common values based on mutual respect, our teams are well-composed to meet the challenge of investing in diverse and fast-moving global and regional markets. These principles of respect for diversity and the rights of our fellow workers are set out in our Code of Ethics.

Our investment teams have autonomy to implement their own investment philosophies and processes in the markets and asset classes in which they specialise. To support these them, we are making investments in both our investment and stewardship teams and, as mentioned above, developing and building the resources we devote to ESG. This is discussed in more detail under Principle 2.

Our diverse, inclusive and collaborative culture is a key competitive advantage and supports our ability to generate differentiated insights

Engagement

Engagement is a key factor in the stewardship of our clients' assets. We find that constructive dialogue with our investee companies helps foster their long-term value and sustainable growth characteristics, improving both returns for clients and managements' accountability to society and the environment. This requires in-depth knowledge of the companies and the environment in which they operate, as well as wider considerations of sustainability consistent with our investment management strategies. Our long experience in these areas means that the approach to engagement we adopt sometimes needs to be adapted to cultural differences in different parts of the world. We discuss engagement further under Principles 9, 10, 11 and 12.

Activity

Policies and position statements

In line with our commitment to continuous improvement, during 2022 we took steps to ensure that our investment approaches, strategy and culture continue to foster effective stewardship. Detailed updates to policies and position statements can be found under Principles 2 and 5.

A key update relates to our membership of the Net Zero Asset Managers Initiative. Following our successful application in 2021 to join the Initiative, we drafted and submitted our initial disclosures covering:

- our initial commitment on the proportion of assets to be managed in line with net zero (43%)[3];
- our interim 2030 targets for emission reduction (50% reduction in carbon footprint for assets covered by the Initiative); and
- the methodology underlying our commitment.

We will continue to progress towards our net zero commitments and link them to wider projects, such as our reporting under the Task Force on Climate-Related Disclosures (TCFD), as appropriate.

As part of the project to implement the EU's Sustainable Finance Disclosure Regulation, new frameworks and processes were established and documented to ensure the alignment of our portfolios with regulatory requirements and to make relevant disclosures. Additionally, relevant policies were reviewed to ensure that key ESG requirements, such as the integration of sustainability risk, were covered. We continued to invest in people, technology and ESG data-extraction and integration capabilities to ensure that we are able to provide strong solutions to our clients. This is described in more detail under Principle 2.

Staff diversity and inclusion

We set up our first Diversity and Inclusion (D&I) Working Group (the Women's Working Group) in 2015 and we currently have four D&I working groups supported by the Corporate Sustainability department—Women's, LGBTQ, Disabilities, and Racial Equality—where employees plan initiatives and events to promote diversity. For instance, our working group for people with disabilities helps to provide a better working environment for such employees. It also works to enhance employees' understanding of each other's needs and encourages cross-departmental co-operation.

We have a Diversity and Inclusion Policy, underlining the firm's commitment to embracing diversity and creating a work environment free from discrimination and harassment. In it we state that Nikko AM Group embraces and encourages individual differences amongst staff and has a zero-tolerance policy towards discrimination of any kind. These principles apply, amongst other things, to our practices and policies on recruitment and selection, compensation and benefits, professional development and training, promotions, transfers, social and recreational programmes, redundancies and terminations.

It aims to ensure that:

- all staff treat each other with respect;
- teamwork and participation are inclusive, allowing all groups and perspectives to be represented;
- a healthy work/life balance is promoted and encouraged through flexible work schedules;
- both we and our employees contribute to our communities and develop programmes that support them.

Support for our Diversity and Inclusion initiatives comes from the highest levels of the organisation, with particular focus from Stefanie Drews, Nikko AM Group Director and President. Ms. Drews has been a champion of diversity and sustainability issues within the company since joining the company in 2014 as Head of Institutional Marketing and Proposition and has been an internal campaigner on matters of equality as she has moved through the ranks of the organisation.

Nikko AM Group embraces and encourages individual differences amongst staff and has a zero-tolerance policy towards discrimination of any kind

In terms of staff diversity, we recognise that we can do better. Currently, women make up 38% of our total staff and occupy 20% of our management positions. We are actively trying to raise the numbers and are a signatory to the "30 by 2030" initiative, committing the firm to ensuring that at least 30% of all our managerial positions are occupied by women in 2030. We are also a member of the 30% Club Japan Investor Group, which aims to have 30% of all board seats of TOPIX 100 companies occupied by women by 2030. Our current female Group Board representation is 30%. We give staff in Japan at least two years' time off to look after children – which may be extended to three in special circumstances – after which they are welcomed back at the same level as when they left. We are long-time supporters of the Women's Empowerment Principles, established by the UN Global Compact and the United Nations Entity for Gender Equality and the Empowerment of Women.

[3] 43% of total groupwide AUM by 50% by 2030, compared to levels as of 31 December 2019.

Linked to this, in 2022 we rolled out regional action plans to achieve our goal of raising the percentage of female managers to 30% by 2030. Within Japan, we have the following list of initiatives underway:

- **Recruitment:** we have adopted a number of aims and policies to increase the number of women at Nikko AM Group through, for instance, ensuring that all job candidates are interviewed by at least one female interviewer.
- **Working environment:** we have introduced more flexible working arrangements and further improved both maternity and paternity leave.
- **Talent development:** we are providing more mentoring and leadership guidance to help advance employees' careers.
- **Raising awareness and culture building:** we are promoting gender balance by taking measures to increase awareness at all levels of the business.

These activities are not confined to our Japanese offices. Each of our regions has developed its own set of initiatives to support this global aim.

We are also actively seeking to create more welcoming working conditions for LGBTQ employees. We are an official member of LGBT Finance, an organisation set up by financial institutions in Japan to support LGBTQ individuals. This initiative enjoys very visible grass-roots support from our employees and very engaged sponsorship from our senior management. In 2022, for the fourth year running, Nikko AM Group was awarded a gold award in the Pride Index, created by Work With Pride, a non-profit-making organisation that helps companies and other organisations adopt and promote LGBTQ-related diversity and inclusion initiatives.

Additionally, in 2022, Nikko AM Group became the first Japanese asset manager to join the LGBT Great initiative (receiving a Bronze award). LGBT Great is an alliance of various types of organisations in the financial services industry, with a shared vision to make it a trusted place for LGBTQ talent, clients and investors.

In 2022, we conducted our first-ever global employee survey on racial equality. This was led by the Global Racial Equality Group and the Corporate Sustainability department. We received 587 responses in total and held follow-up educational sessions for employees globally. As a result of the survey, we are now looking into focused training options for our staff.

Lastly, we conducted several employee education seminars on supporting people with disabilities, including a series of sign language lessons. As a firm, we continue to sponsor the Japan Wheelchair Rugby Team.

Social outreach

We realise how important it is to nurture future talent in this industry, so we participate in the UK-based initiative Future Asset. This tries to make the fund management industry relevant and interesting for young people, especially women.

Several of our Global Equities team are mentors and judges in Future Asset's annual Growing Future Assets Competition, where teams of girls make an investment pitch to win prizes for themselves and their school. There were more than 80 teams entered in 2022 and each had to prepare an investment report on a company by answering questions about the industry, the company and how to value it. The teams then summarised their case in a short video, where they were able to use their creative skills in video production to pitch their investment idea. From these entrants, the field was narrowed down to a final pitch to a live panel of judges.

We hope our participation in Future Asset will help Scottish girls to leave school understanding that investment is relevant to everyone, can have a positive impact, and offers fulfilling career opportunities. We were encouraged that, in 2022, following her participation in the competition a few years before, one of the girls from the initiative worked as an intern at Nikko AM Group.

We are also one of the first firms to sign up as a member firm of the UK-based initiative Progress Together. This is the first body of its kind to promote socio-economic diversity and progression in the UK financial services sector, particularly at a senior level. As a member firm, Nikko AM Group has committed itself to start collecting employee data and sharing that data (anonymised) with Progress Together to ensure they can strengthen their benchmarking capability. We are also supporting the organisation through senior level sponsorship, sharing our experiences, and using our influence to push for change across the sector. We look forward to what can be achieved from our partnership in 2023 and beyond.

Investments

Our main instrument for translating our investment beliefs, strategy and culture into effective stewardship is our investment teams. They have different approaches and different opportunities to exercise stewardship, which are described below and in the rest of this report.

Equity

The rights of an equity shareholder, particularly in terms of voting and accessibility to companies, allow us to implement our investment beliefs and carry out our stewardship responsibilities in many ways other than making an investment decision. These are discussed further throughout the report, with our engagement and voting activity covered in particular under Principles 9, 10, 11 and 12.

One way stewardship has influenced our actions is the discussions our investment teams have been having with clients and prospects regarding their own priorities and obligations. The looming spectre of climate change is a concern for many and is one of the topics we have in the front of our minds, not only during internal deliberations in respect of our own net zero ambitions and targets, but also in our engagements with investee companies and increasingly in our voting deliberations. We are investing in tools that enhance our ability to report on greenhouse gas emissions and fulfil the evolving regulatory requirements that our clients face (for example in respect of TCFD obligations under the Taskforce on Climate-Related Financial Disclosures).

An example of one of our proactive initiatives on the environmental front during 2022 was when our Global Equity team contacted investee companies to ensure they understood our obligations as signatories of the Net Zero Asset Managers initiative and other climate-related commitments, as well as the expectations of our clients (further detail on this is provided under Principle 4). Meanwhile, following increasing interest expressed by a number of clients invested in our Global Equity strategy about the "social" element of ESG, the team is in the process of collating diversity, equity and inclusion metrics on investee companies.

Fixed income

Fixed income is an area where it can be more difficult to have a direct influence on the direction of investee companies. A bondholder lacks the voting rights that accompany equity ownership, however bond holders may choose to not participate in new issues or divest holdings of a company as a way to express displeasure at corporate behaviour. It is also important to engage with management to encourage positive changes where we as stewards see areas of improvement for a company.

Our teams have been active in extending our stewardship activities in a number of fixed income areas during the year which are discussed further throughout the report.

Our Global Fixed Income team for example, engages with clients on ESG and broader stewardship questions and has intensified its engagement with bond issuers. During 2022 the team continued to develop their proprietary ESG monitoring tools. It is increasingly taking ESG considerations into account at a bond selection level, regardless of whether these considerations are explicitly outlined in investment mandates. The team's rationale is that it wants to avoid situations where the market moves in favour of issuers with superior ESG scores, causing client portfolios to be left holding underperforming bonds. As a result, if there is a choice of issuance that would fulfil a specific need in terms of duration positioning and risk profile, the team will opt for the higher ESG scoring bond. Our other fixed income teams have their own analytical tools to integrate ESG factors effectively into their investment decisions.

Our main instrument for translating our investment beliefs, strategy and culture into effective stewardship is our investment teams

Our Asia Fixed Income team, for example, made significant improvements to its ESG monitoring system during 2021, formalising the process by which ESG risks and opportunities recorded during the issuer analysis process are factored into the outcome of our proprietary Internal Credit Rating. The team has continued to embed this process into its operations during 2022 and has added a further model to better understand the ESG risk of sovereign bonds. In 2022 more focus has also been placed on dedicated ESG engagements with Asian bond issuers. This is explained more fully under Principle 7.

Outcome

We believe this year's report reflects a number of major advances in our culture of stewardship. Evidence of our progress will be found in subsequent sections, but perhaps the most important has been the establishment of our Global Sustainable Investment department as the culmination of a project to redefine our organisational strategy in relation to ESG issues. Along with the appointment of a Global Head of Sustainable Investment at a senior level, reporting directly into our Group President and Chief Investment Officer, this for the first time brings all our stewardship and ESG resources under one umbrella and significantly expands the resources we commit to stewardship. The department is already influencing how we integrate ESG into investment decisions. Its creation is concrete proof of how we are embedding stewardship values in everything we do. Further detail on these developments is provided in our response to Principle 2.

Beyond that, we believe we have been more effective than ever in intervening at companies where we have identified ESG failings. These interventions have been both on our account and collectively with other investors. Evidence of our success will be found in the case studies later in the report.

We have not stood still in pushing forward the stewardship agenda more widely either. We have extended our commitments to industry initiatives such as the Net Zero Asset Managers initiative, the TCFD and Climate Action 100+. In all cases, we have been increasingly active in participating in industry initiatives and conferences on major issues, often stewardship related. Further information on these will be found in our responses to Principles 4, 7 and 10. The disclosures that we make as a result of these commitments are driven by, and in turn help to drive, underlying organisational change, such as the formation of the new Global Sustainable Investment department, revamped governance, enhanced analytical capabilities and more focused engagement initiatives.

We face different challenges to asset managers that have a European or North American heritage. Japanese culture values stewardship, but often approaches it from a different perspective than Western societies. As we have grown over the last 60 years from an organisation focused on the domestic Japanese market into a global asset manager, we have brought with us these Asian traditions of stewardship which are themselves evolving as they meet Western practice. This process is challenging us to review and enhance our approach to stewardship.

We believe this year's report reflects a number of major advances in Nikko AM Group's culture of stewardship

One of the key forces driving change at Nikko AM Group is feedback from clients. We take feedback from our retail and institutional clients very seriously. As we describe in detail under Principle 6 and other sections of this report, they help guide how we manage their assets and the type of assets we use. We know that many clients are interested in returns to be won in a principled and sustainable way. As we describe later on, this can result in us adjusting our approach or launching products that better suit our clients' requirements. This, we believe, is a key part of stewardship, while also helping to improving the long-term returns for clients and bringing sustainable benefits to the economy, the environment and society. While recognising that we can do more, the feedback we receive and our client retention suggests that we are being effective in serving the best interests of our clients and beneficiaries.

We believe our activities, particularly those undertaken during 2022 described in this and other sections of the report, reflect our commitment to fiduciary duty and our effectiveness in embedding stewardship values across the organisation. In particular, we continue to bring an ever-greater focus on environmental and societal outcomes, while recognising that there are opportunities for further development. This process of evolution involves long-term initiatives and a commitment to continuous improvement – values that are consistent with our Japanese heritage – but which are being increasingly honed by experience and the need to comply with the highest international standards.

Principle 2

Signatories' governance, resources and incentives support stewardship.

Activity

We regard fiduciary and ESG principles as paramount guides in fulfilling our duties as stewards of our clients' assets. In implementing these principles, corporate governance is critical. Our fiduciary and stewardship responsibilities are overseen by the Nikko AM Group Board of Directors, including Non-Executive Director and Chairman, Yoichiro Iwama, our Director and Executive Chairman, Yutaka Nishida, and Director and Group President, Stefanie Drews. Our commitment to gender diversity is reflected by the composition of our Group Board, where three out of ten members are female, while our commitment to independence is ensured by having 60% of the Group Board as outside directors.

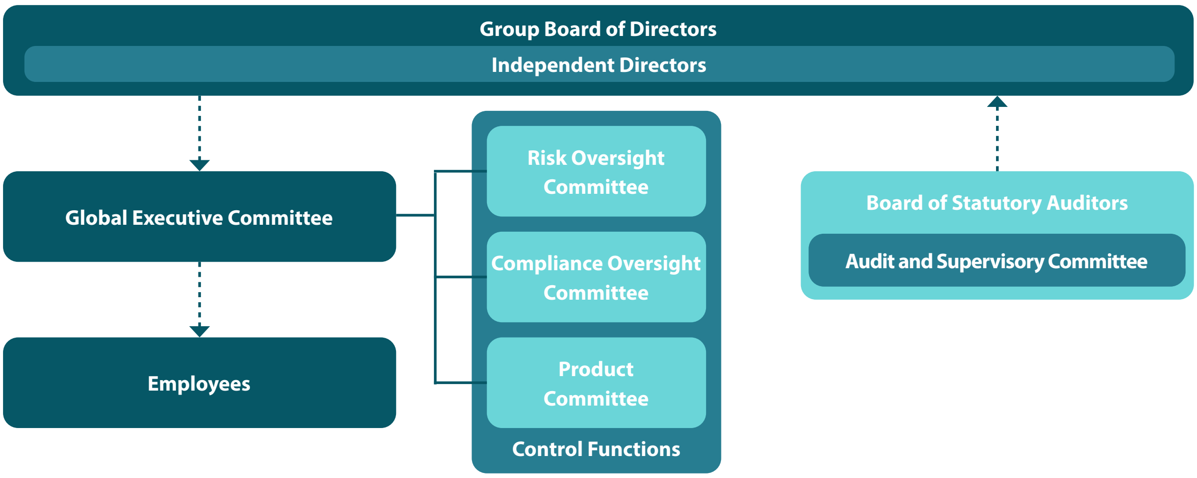
The Nikko AM Group Board delegates responsibility for day-to-day decision-making to our Global Executive Committee (GEC), comprising members of the senior management team, whose details can be found under the leadership section of our website. The chart below shows a simplified representation of our group governance structure.

Yoichiro Iwama
Outside Director and Chairman of the Board of Directors

Stefanie Drews
Group President

Yutaka Nishida
Executive Chairman

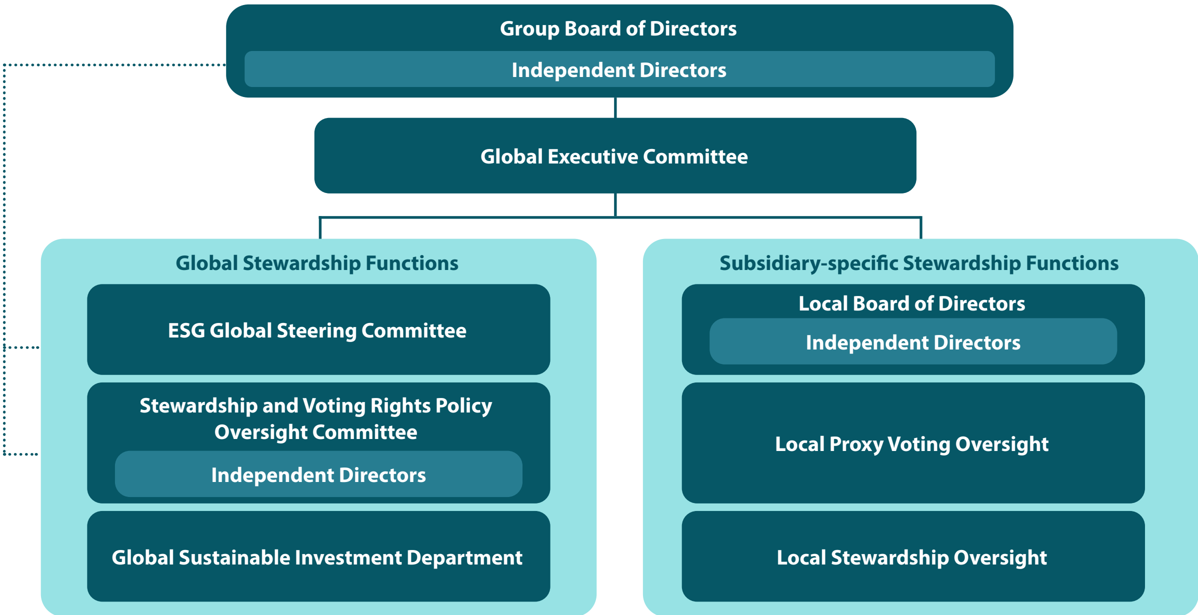
NAM Group Governance



Nikko AM Group's supervisory and governance structure includes an audit and supervisory committee. The role of the committee is to strengthen oversight and enhance our corporate governance framework.

Principle 2

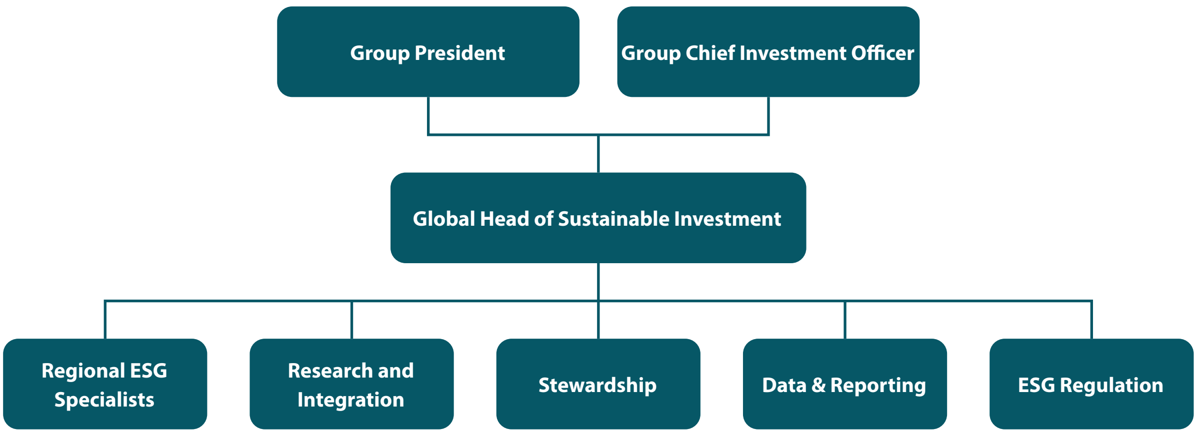
Stewardship Governance Structure



Governance of stewardship activities operates at both the global and local subsidiary level. The overall oversight of our ESG activities is the responsibility of the ESG Global Steering Committee. It oversees the integration of ESG within investment teams, sets policy and develops strategy, makes external disclosures and recommends ESG-related initiatives and participation in external bodies. The ESG Global Steering Committee is governed by the GEC but, in addition, reports directly to the Group Board. It is chaired by the Global Head of Investment and members are the heads of our investment teams worldwide, who are in charge of stewardship implementation in their individual investment processes (including ESG integration, company engagement and proxy voting, where applicable). It is further supported by the Sustainable Investment department who provides dedicated expertise and administrative support. As well as its monitoring and guidance activities, the Steering Committee drives our implementation of the United Nations-supported Principles for Responsible Investment (PRI).

As outlined under Principle 1, in 2022 we undertook a project to create a new ESG framework to support our existing global ESG community. The functions and objectives of this team were outlined in Principle 1, while its governance is illustrated in the chart below. It has significantly expanded our ESG resources and added new ESG roles in EMEA, Singapore and Japan, as well as bringing under its wing our existing Japan Sustainable Investment department (formally Active Ownership Group). We have made Singapore our Sustainable Investment Centre of Excellence, given the city-state's advantages in terms of talent, its time zone sitting between Japan and Europe, and its language capabilities. We will further build and develop our team of ESG specialists during 2023. For more on ESG integration, see Principles 7, 9 and 10.

Global Sustainable Investment Department Governance Structure



Principle 2

As part of the new structure, a Global Head of Sustainable Investment, Natalia Rajewska, was appointed at a senior level, based in Singapore. She reports directly to Group President Stefanie Drews and Chief Investment Officer Hiroshi Yoh to ensure that ESG matters have appropriate senior leadership oversight. The underlying functions of the team report directly to the Global Head of Sustainable Investment.

The core priorities of the Global Head of Sustainable Investment centre around shaping our sustainable investment strategy, building Nikko AM Group's Global Sustainable Investment department and working closely with investment teams and other business functions in all the regions to strengthen the firm's ESG capabilities and provide insight on broader ESG topics.

This mission is supported by senior leadership, with both Ms Drews and Mr Nishida having specific key performance indicators (KPIs) to improve the group's ESG for the last financial year. One result has been the close involvement of senior management in devising and introducing our new Global Sustainable Investment team structure.

Further details on subsidiary level governance and department biographies are described in the sections below.

Our commitment to stewardship

We believe our actions over the past few years demonstrate our readiness to put principle into practice, starting at the top of the firm. Our Non-Executive Director and Chairman, Mr Iwama, has a wealth of experience in the Japanese asset management industry, particularly in developing stewardship policy in Japan. As a previous Chair of the Council of Experts on Japan's Stewardship Code (a body created by the Japanese Financial Services Authority), Mr Iwama played a leading role in introducing the concept of stewardship to the Japanese asset management industry. He was then heavily involved in bringing in the Code as Chairman of the Japan Investment Advisers Association from 2010 to 2017, both in its original form in February 2014 and in later revisions in May 2017 and in May 2021. He has played a crucial role in improving stewardship in the Japanese asset management industry and corporate governance at investee companies. During 2022, Mr Iwama also served as a member of the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code, which made recommendations about revising the two corporate codes. Under Mr Iwama's supervision of the Group Board, we continue to strive for the highest standards of governance and stewardship.

Our Group President, Stefanie Drews, is herself a vocal champion of sustainability and diversity issues, both within the organisation and publicly. During her years with the company, she has worked at fostering a culture based on recognising talent and merit. She is also keen to boost the number of women in senior roles. By the end of December 2022, the number of women in managerial roles had reached 20% and was as high as 30% at Group Board level, putting us on track to achieve our goal of 30% of managerial positions by 2030. However, we see this as only an interim goal on the way to parity.

Principle 2

Subsidiary-level governance

Each Nikko AM Group subsidiary has an independent executive team led by a regional head who reports to the Group President and is responsible for formulating and executing targets and plans decided by the Group Board and GEC in line with local regulations and customs. Each regional office is required to present its ESG implementation activities regularly to its respective board. The global and local stewardship framework is illustrated in the chart above. There are differences in detail as to how these processes operate at subsidiary level. To illustrate these variations, we outline two regional examples below.

Stewardship oversight of Japanese investment functions

Our Japanese operations represent more than half the business, so we devote a great deal of resources to their governance and stewardship. The Stewardship and Voting Rights Policy Oversight Committee monitors and supervises our engagement with Japanese investee companies and proxy voting, ensuring that both remain in line with our fiduciary and ESG principles and truly meet the interests of investors.

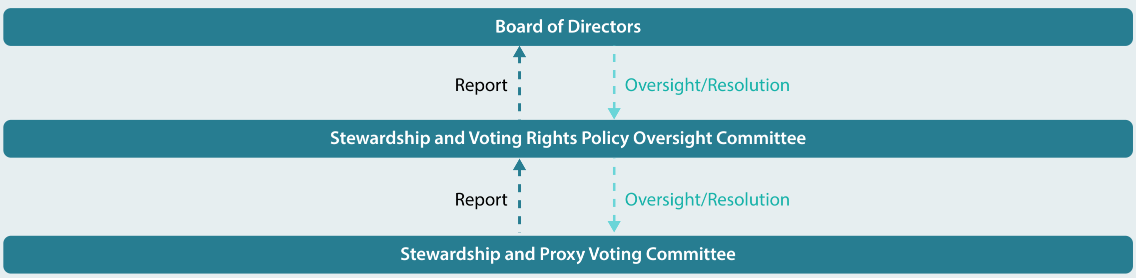
The committee was launched in 2016 as a way of enhancing the transparency of our stewardship activities and strengthening our governance. Four out of the committee's seven members are from outside the Nikko AM Group, making it highly independent. Its decisions carry weight, as it reports directly to the Group Board on matters such as the governance of our stewardship activities and conflicts of interest, ensuring, for example, that proxy votes are used in line with our Conflict of Interest Control Policy. For more on this committee, see Principle 12.

Directly answering to the Oversight Committee is the Stewardship and Proxy Voting Committee, which is responsible for formulating stewardship policy, providing guidance on stewardship activities and is also responsible for updating our Group Proxy Voting Policy, addendums to which can be applied at the subsidiary level in line with local customs and the requirements of the respective investment teams.

Our Japan Sustainable Investment department (previously known as the Active Ownership Group or "AOG") that reports into the Stewardship and Proxy Voting Committee, was set up in 2017 to enhance the firm's ability to: firstly, make judgements on how to exercise voting rights and implement stewardship activities in our Japanese portfolios; and, secondly, conduct engagements with Japanese companies not already covered by sector analysts in actively-managed portfolios. As a result, even stocks which are held only in passive portfolios are now subject to engagement.

The analysts in the Japan Sustainable Investment department are responsible for conducting the risk assessments we use to filter out from our investment universe companies at high risk of governance failings. They also provide the Japan-based investment teams with other relevant ESG-related information derived from their research and engagements. Department analysts engage with large and mid-sized firms specifically on ESG issues. The department was fully incorporated under the Global Sustainable Investment department in early 2023, when they also increased the breadth of their scope to cover all asset classes managed by our Japanese investment teams. It is headed by our seasoned specialists, Masahiko Komatsu and Kiyoshi Noda, whose background and experience are described further below. Further detail about the departments activities is provided under Principle 7.

Oversight of proxy voting at our Japanese entity



Principle 2

Stewardship oversight of UK investment functions

Our UK entity is responsible for stewardship activities in the UK and Europe in collaboration with the Global Sustainable Investment department. Given the significant number of ESG regulatory developments in the EU and an increasing focus on ESG and stewardship in the UK, we introduced new local governance in 2022 for ESG regulations and standards, as well as stewardship.

Our review and adoption process for ESG regulations and standards now works in three layers. The initial stage involves a dedicated team scanning the horizon for ESG requirements that might affect the group. Any that are highlighted are then reviewed and assessed by a dedicated working group comprising key business functions. Lastly, requirements, impact assessments and recommendations are presented to a newly-formed board committee dedicated to ESG and stewardship.

Reporting on stewardship activities in Europe has been further formalised with defined KPIs and summaries of engagements presented to the newly-formed board committee referred to above. Our aim is to continuously improve the quality of our engagements through rigorous challenge and oversight by key business stakeholders.

Stewardship resources

Seniority, experience, qualifications, training and diversity

It is our global network of more than 200 investment professionals, with their wide breadth of experience, who are at the forefront of our stewardship activities, aided by our Global Sustainable Investment department. As an organisation we are committed to sustainable and responsible investing and our portfolio managers, analysts and governance specialists all share in this commitment. They apply this philosophy by implementing stewardship in their day-to-day activities and practising active ownership.

They are compensated using a methodology that is intended to align their interests and motivation with the outcomes of client portfolios. Annual evaluations are based on quantitative measures such as the long-term returns of client portfolios (for example, weighted portfolio returns for investment staff, or performance of securities recommended for analysts), but also the qualitative aspects of individual as well as group performance (for example, quality of analysis and contributions to the team).

In recent years, all employees are encouraged to include corporate sustainability goals in their annual performance objectives. This has given staff the opportunity to think about how they can practise sustainability in their roles. We view this goal-setting exercise as part of a multi-year process of weaving sustainability into our culture. Further information on these matters can be found in our annual Sustainability Report, which can be downloaded from the Sustainability Insights section of our website.

We have a strong emphasis on internal training as stewardship is the responsibility of our entire workforce, and therefore all employees have an annual training plan that includes topics such as conflicts of interest, personal trading and our code of ethics. Investment employees across the firm's global network undertake responsible investment training via an online course offered by the PRI Academy as part of our continuing focus on implementing the PRI's six Principles for Responsible Investment. The training concentrates on how ESG issues affect business and investment decision-making through the use of financial modelling and in-depth case studies.

Our long commitment to ESG is reflected in the fact that we launched Japan's first socially-responsible investment fund as long ago as 1999. We now practise deep and direct ESG integration across the firm, where every investment team and department integrates ESG directly into their work. We have a number of systems, platforms and forums that allow our global investment teams to share research analysis on events and issues, especially those that may not always be covered in the media. During the year we have invested in people, technology and ESG data extraction and integration capabilities to ensure that we are able to provide the level of service required to meet the needs of our clients. This investment has ranged from ESG-specific resources, training in stewardship themes and client communications, through to the means to engage and monitor company engagements on a larger scale.

An example of the training that was provided during 2022 is the dedicated sessions that were held with investment teams across the globe to inform them of the background and reporting requirements under the revised UK Stewardship Code. This included presentation materials in Japanese to discuss examples of best practice. We believe that these sessions have had a meaningful impact on our reporting for this submission.

Systems, analysis and service providers

Institutional Shareholder Services (ISS) is used to execute our proxy voting, which we consider a key activity in fulfilling our stewardship responsibilities. ISS also provides research and customised voting recommendations based on our voting and responsible investment policies, although the ultimate decision on how we vote is taken in-house. Our interaction with ISS is discussed in more detail under our responses to Principles 8 and 12.

As part of the creation of our Global Sustainable Investment department in 2022, we established a centralised ESG data team (shown in the Global Sustainable Investment department governance structure chart earlier) to help provide consistency, accuracy and improve the coverage of our ESG data, as well as expanding our analytics capabilities. In 2022, we hired Zishan Cheema as our first specialised ESG data analyst, sitting under the Head of Strategic Analytics and Data and Global ESG Data & Reporting Lead, to begin this process. This strengthening of the team goes hand in hand with plans to expand our external ESG data sources, for example, through the acquisition of advanced climate analytics tools.

The ESG data team now works with a variety of stakeholders across the firm. The team has focused on analysing and integrating data sets we acquire from our primary ESG data provider for use by investment and client reporting teams. This has included enhancing our ability to identify and assess climate-related risks and opportunities (linking to our work on the Task Force on Climate-Related Financial Disclosures, which is explained in more detail under Principle 7). The team also works on a variety of regulatory reports, plays a key function in providing data to prove our compliance with the EU's Sustainable Finance Disclosure Regulation, and has been charged with developing leading ESG data capabilities to meet our evolving needs.

Data from external service providers are used as one input in our investment decision-making process to supplement our proprietary analyses. We use a wide range of data from a combination of public disclosures (issuers' annual and sustainability reports etc.) for the purpose of research, as well as through direct engagement and communication with companies and external ESG analysts and data providers, such as MSCI ESG, Sustainalytics, Good Bankers, ISS and Bloomberg.

Having access to multiple sources of data can be useful in allowing us to cross-check our assumptions. However, we recognise that third-party data providers have shortcomings, including a lack of consistency arising from differences in methodology, therefore in our active strategies, we treat these data as supplementary to our proprietary research, as further outlined in Principle 8.

Below are biographies of key members of the Global Sustainable Investment department:

Natalia Rajewska, Global Head of Sustainable Investment

Ms Rajewska joined Nikko AM Group in 2021 from ING Bank in Singapore. She started in sustainability consulting in 2013 and has worked over the years in sustainable investment and finance in banking and asset management. She had been involved in sustainable development and social change since 2008. At ING she rose to VP covering APAC clients, having originated and structured some of the market leading and world's first sustainable finance instruments. Prior to ING, Ms. Rajewska worked at Aviva Investors as an ESG analyst. She has also worked at Corporate Citizenship, a sustainability consultancy, and at an impact investment foundation in Singapore.

Deborah Loke, ESG Analyst

Ms Loke has had previous roles at UOB Asset Management and Maitri Asset Management, where she was an ESG investment analyst covering the Asia Ex-Japan region, supporting the investment teams in ESG analysis, stock picking, and stewardship activities. She joined Nikko AM Group in 2022.

Yukari Kaito, ESG Specialist, Sustainable Investment, Japan

Ms Kaito joined the Nikko AM Group Investment Support & Planning department as an ESG Specialist in December 2018. Prior to joining Nikko AM Group, she was a specialist in the global corporate responsibility team of a listed company in Japan, working on enhancing corporate value by implementing ESG throughout the organisation and increasing corporate ESG disclosure. Prior to this, she worked for more than five years as an ESG analyst, most notably as a principal analyst overseeing ESG research on over 1,800 companies, providing advice on proxy voting and engaging with boards on behalf of clients.

Masahiko Komatsu, Acting Co-Head, Sustainable Investment, Japan

Mr Komatsu is based in Tokyo and co-leads the Stewardship function in the Global Sustainable Investment department with a particular focus on ESG integration. He joined Nikko AM Group in April 2021 and led the Japan Sustainable Investment department. Prior to joining Nikko AM Group, he worked for four asset management companies, including Prudential, Schroders and Polar Capital, mainly as a Japanese equity analyst. He has contributed to corporate governance improvements at Japanese listed companies, including playing a leading role in collaborative engagement with foreign institutional investors. He holds an MBA from Waseda Business School and is also a chartered member of the Securities Analysts Association of Japan.

Kiyoshi Noda, Acting Co-Head, Sustainable Investment, Japan

Mr Noda joined Nikko AM Group in August 2022 as an analyst in the Japan Sustainable Investment department focusing on ESG research, proxy voting and company engagements. Prior to joining Nikko AM Group, he worked as a fund manager for nearly 20 years and changed roles to lead the responsible investment section at MU Investment Company. He holds a BA in Economics from Keio University and is a chartered member of the Security Analysts Association of Japan.

Ken Kajiyama, Senior Stewardship Specialist, Sustainable Investment, Japan

Mr Kajiyama joined Nikko Securities Investment Trust & Management, one of Nikko AM Group's predecessor firms, in April 1993. After serving as a fund manager for five years, he took on the role of equity research analyst, where the sectors he covered included steel, non-ferrous metals, trading companies, marine transportation and pulp & paper. In 2018, he joined the Japan Sustainable Investment department as a proxy voting and engagement specialist, a role which he served concurrently with that of equity analyst. Since 2019, he has served as a dedicated proxy voting and engagement specialist. He holds a BA in commerce from Chuo University and is a chartered member of the Security Analysts Association of Japan.

Kozue Saito, Stewardship Specialist, Sustainable Investment, Japan

Ms Saito joined Nikko AM Group in 2007 as a fixed income analyst. In 2011, she changed roles to become a value style analyst on the Value Strategy Fund Management team. Since 2018, she has served concurrently as a proxy voting and engagement specialist in the Japan Sustainable Investment department, focusing on ESG research, proxy voting and company engagements. Prior to joining Nikko AM Group, she was a corporate credit risk analyst at Gibraltar Life Insurance Company, where she started her career in 2003. Her credit background gives a unique perspective to her bottom-up company analysis. Saito holds a BA in Law from Aoyama Gakuin University. She is also a chartered member of the Security Analysts Association of Japan.

Hiroki Wakita, Stewardship Specialist, Sustainable Investment, Japan

Mr Wakita joined Nikko AM Group in 2017 as an analyst in the Japan Sustainable Investment department, focusing on ESG research, proxy voting and company engagements. Prior to joining Nikko AM Group, he worked as a Japanese equity analyst at Citigroup Securities. He began his career at Mizuho Securities in 2009, first working in sales of Japanese equities to institutional investors and later on initial public offerings. He holds a BA in Economics from Tokyo University and is a chartered member of the Security Analysts Association of Japan.

Taro Egami, ESG Integration Specialist, Sustainable Investment, Japan

Mr Egami joined Nikko AM Group in March 2023 as an ESG Integration Specialist in the Japan Sustainable Investment department. Prior to joining Nikko AM Group, he performed investment analysis, shareholder engagement and firmwide ESG integration at a Singapore-based engagement fund. He began his career at the Investment Banking Division of Citigroup Global Markets Japan Inc., working on domestic and cross-border Mergers and Acquisitions as well as transaction financing. He holds a Bachelor of Agriculture from Kyoto University, majored in Environmental Economics. He is a certified member analyst of the Securities Analysts Association of Japan.

Amisha Patel, ESG Specialist

Ms Patel is based in London. She joined Nikko AM Group in 2014, having previously held roles at Wellington Asset Management and GAM. She supports our UK-based investment teams with their implementation of ESG policies and initiatives, stewardship activities and company engagements on pertinent ESG issues.

Harry Wilson, ESG Regulatory Lead, EMEA

Mr Wilson joined Nikko AM Group in 2022 from Alpha Financial Markets Consulting, where he led client projects in ESG and regulatory risk and compliance. Prior to Alpha, Mr Wilson held roles at Capgemini and Aon Hewitt. He is responsible for identifying, assessing and developing Nikko AM Group's responses to UK and European ESG regulations.

Aria Goudarzi, Head of Strategic Analytics and Data and Global ESG Data & Reporting Lead

Mr Goudarzi joined Nikko AM Group in 2014 from Macquarie Investment Management and has played a significant role in building our performance and data solutions capabilities, running teams in Europe and globally. He is responsible for working with the Global Head of Sustainable Investment in creating the firm's global ESG data strategy, as well as enhancing reporting capabilities.

Zishan Cheema, Senior ESG Data Analyst

Mr Cheema joined Nikko AM Group in March 2022. Prior to this he had 16 years' experience in a variety of front office roles, including equity analysis and portfolio management, in both active and passive investment strategies. His most recent experience was working as head of research at a fintech startup focused on ESG analytics for retail investors.

Principle 2

These significantly expanded resources allow even closer collaboration and co-ordination with investment teams and other key business stakeholders, such as sales and sales support staff. Amongst other things, the enlarged department's duties include conducting ESG research and integrating it into our investment processes. This will see ESG analysts embedded in investment teams, supported by integration and thematic specialists. The new department will also be involved in enhancing our ESG data and analytics capabilities and ensuring that we take a proactive approach to capturing and integrating regulatory and market standards in relation to ESG. Our work in expanding our ESG resourcing is not done, however, we will be further expanding the team in 2023.

Outcome

As a group we are committed to active stewardship. Our governance structures and stewardship processes address several areas, including the management of conflicts of interest, engagement in active and passive investment management, our sustainability efforts and information disclosure.

In 2021, we recognised the need to enhance our ESG capabilities as an organisation, including in relation to stewardship. As a result, and as outlined throughout this report, we made significant organisational changes during 2022. Central to them was the establishment of the Global Sustainable Investment department, with resources allocated to ESG research and integration, stewardship, ESG data and reporting capabilities and ESG regulations and standards.

Additional roles were created as part of the new department in 2022 and we expect additional hires in 2023. Ms Rajewska was appointed to manage the department as the new Global Head of Sustainable Investment. The fact that she reports directly to our Group President and Chief Investment Officer is testimony to the importance we give to stewardship and broader ESG activities as an organisation. The department has already improved how we review and integrate ESG factors across our product range and significantly enhanced our ESG data and analytics capabilities.

In Europe, during the year we created and formalised new governance structures relating to our stewardship activities, as well as improving our understanding of, and response to, ESG regulations and standards. Lastly, we further underscored our commitment with specific ESG and stewardship KPIs assigned to both our Group President and our Executive Chairman for the 2022 financial year.

As stewardship needs and expectations are continuously evolving, we will continue to adapt and fine-tune our responsibilities and activities as stewards of our clients' capital. This means ensuring that we have the right resources, governance and incentives in place to support our responsibilities to the economy, the environment and society. We understand that effective stewardship requires continuous improvement, and we aim to critically evaluate our approach and implement meaningful changes wherever and whenever required.

Principle 3

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

Context

We always seek to put the interest of our clients first in all our activities. We aim to identify all actual or potential conflicts of interest and maintain and operate arrangements to minimise the possibility of conflicts giving rise to a material risk of damage to the interests of our clients. We have established a Group Conflict of Interest Control Policy (addendums to which can be applied at the subsidiary level in line with local requirements), which has been designed to prevent us from prejudicing the interests of customers in the conduct of our business and is reviewed at least annually. Potential new conflicts are considered as part of any new business development and/or business process changes.

In addition, group subsidiaries maintain their own conflicts of interest registers which record potential conflicts that have come to light during their activities and the measures taken to resolve them. Each register is regularly reviewed and approved by the relevant subsidiary board of directors. Group subsidiaries may also add local addendums to the group policy, changes to which are reported to the local boards and the Group Board as per the process described under Principle 5.

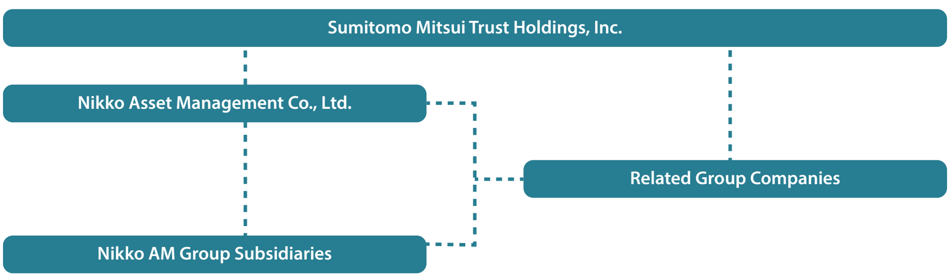
More details about how our conflicts of interest policies operate can be found in the Activity section below. However, in general, when identifying the types of conflict of interest that may arise, we take into account, as a minimum, whether we or any of our directors, managers or employees or a person directly or indirectly linked to the firm:

- is likely to make a financial gain, or avoid a financial loss, at the expense of a client;
- has an interest in the outcome of a service provided to a client or of a transaction carried out on behalf of a client which is distinct from the client's interest in that outcome;
- has a financial or other incentive to favour the interest of one client or group of clients over the interests of another;
- carries on the same business as the client; and/or
- receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monetary or non-monetary benefits, other than the standard commission or fee for that service.

Responsibility for controlling transactions and other conduct likely to give rise to conflicts of interest is managed by our Compliance departments. Together, the group Compliance heads are charged with maintaining the conflicts of interest control framework and periodically verifying its effectiveness, as well as continuously striving to improve it. They are also responsible for communicating all aspects of conflict control to employees through education and training programmes. They are immediately answerable either to the subsidiary board of directors of the relevant subsidiary or, if the incident occurs in Japan, to the Compliance Oversight Committee, part of the Global Executive Committee.

One area where conflicts can arise is as a result of our ownership, where there is potential to treat a related group company more favourably than an unconnected company. Nikko AM Group is ultimately owned by Sumitomo Mitsui Trust Holdings (SMTH), which is a large Japanese conglomerate with interests in, amongst other things, banking, pension administration, real estate, stock transfer, custody services, and asset management. Nikko AM Group itself has subsidiaries in the UK, Luxembourg, the US, Hong Kong, Singapore, New Zealand and has a branch office in Germany and associates in China, Malaysia and Australia. An up-to-date list of related group companies is maintained in the appendix of the Group Conflict of Interest Control Regulations. In addition, the names of related group companies, including two additions in 2022, as well as that of our publicly-listed parent, are kept on a restricted list at local subsidiaries to help prevent any potential conflicts. Other possible conflicts are listed in the table below.

Our Corporate Structure



Activity

Examples of potential conflicts of interest related to stewardship that may arise during the course of business and how we manage them are summarised in the table below.

Conflict	Example	Management
Related group companies	In undertaking business for our clients, our dealings, or other arrangements, with related group companies present possibilities for us to treat our related group companies more favourably than unrelated companies.	We and our related group companies have adopted policies and procedures throughout our businesses to manage conflicts of interests. These policies and procedures are subject to our normal monitoring and review processes.
Fair allocation	The processes involved in the research of securities, execution of trades, allocation of securities forming part of a trade and participation in new issues could result in unfair trade execution or allocation among clients' accounts. Investment and/or trades may be executed in a way that favours one or more clients to the disadvantage of others.	All trades across accounts are pre-allocated and trades that are partially filled are allocated pro-rata. Compliance monitoring is conducted to ensure adherence.
Proxy voting	Where clients permit us to exercise voting rights attached to securities held in their portfolios, the possible conflicts of interest include circumstances where: (i) we manage assets for companies whose management are soliciting proxies and the failure to vote in favour of management resolutions may harm our relationship with the company, (ii) we may have a business relationship with a proponent of a proxy proposal and may manage assets for the proponent, or (iii) any employee may have a personal or outside business interest in the outcome of a particular proxy vote.	Our Proxy Voting Policy is designed to ensure that votes are cast in accordance with the best economic interest of clients.
Outside directorships	Employees who have access to portfolio management or proxy voting activity or directors who hold similar positions with another firm or firms may be able to use their position and information obtained from either firm to obtain financial gain or avoid a loss.	All employees are required to seek Compliance and senior management approval of any outside directorships which they may hold. Any committee members who have oversight of other companies are excluded from agenda items where Nikko AM's stewardship activities involving such companies are discussed.

Principle 3

An area of particular focus for our efforts to control conflicts of interest is voting. We assess our voting conduct every quarter at a regional level and publish an annual summary of our firm-wide voting activity on our website.

An example of our quarterly monitoring is the work of our Stewardship and Voting Rights Policy Oversight Committee, which meets every three months to review votes on individual proposals from investee companies that might trigger a conflict of interest. A regular item on the committee's agenda is reviewing votes involving related group companies and confirming that there is no bias in favour of the related group company. In addition to related group companies, including the parent company, the committee also judges the exercise of voting rights on listed customers, business partners, and financial institutions that sell our products. In doing so, the committee is aided by advice from our proxy voting agency, ISS. Approximately 1,500 resolutions were reviewed by the Stewardship and Voting Rights Policy Oversight Committee during 2022. There were no instances where the committee deemed that there was bias in the way that votes had been cast.

We firmly believe that such reviews of individual votes help us to increase the transparency of our stewardship activities and minimise conflicts of interest when we exercise our voting rights. We believe that having the reasons for our voting decisions reviewed by the independent oversight frameworks, such as those displayed in the Governance of Stewardship Activities structure under Principle 2, helps us manage potential conflicts of interest and facilitates constructive engagement with investee companies. For more on our voting activities, see Principle 12.

As we do every year, we identified new scenarios in 2022 that may cause potential conflicts and these have been incorporated in local policy, as set out in Principle 5. Amongst the amendments to local policy were revised disclosure requirements, including the widening of the definition of outside interests from directorships to any outside business interest which must be reviewed by the Compliance department.

Outcome

No actual conflicts of interest arose during the year that prevented us from performing our stewardship activities in accordance with the best interests of our clients.

We believe that our thorough management of conflicts of interest helps to maintain the trust of both clients and investee companies and allows us to conduct our stewardship activities more effectively. Our everyday stewardship activities, such as proxy voting, are governed by the management framework and supervision functions described above, including our policy for managing conflicts of interest.

Principle 4

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

Activity

As an asset manager, we are reliant on our ability to invest in liquid, transparent and functional markets. Market-wide and systemic risks directly affect the value of the assets that we invest in, therefore, as a fiduciary, one of our key responsibilities is to manage these risks in order to improve outcomes for our clients. As long-term investors, it is in our interest to support and advance initiatives that aim to reduce market-wide and systemic risks and, as responsible stewards, we recognise both the responsibility – and the opportunity – we have in promoting well-functioning, stable markets in the interest of the wider economy, environment and society.

A core part of our philosophy is that our investment professionals are best positioned to identify market-wide and systemic risks through their research and engagements. The natural corollary of this is that they then have the freedom to follow their own high-conviction approaches in dealing with these risks, supported by the infrastructure and resources of the wider organisation.

Our fundamental research is supplemented by external sources which enhance our overall understanding of the investment landscape. External sources include contacts with market-makers and related participants, dialogue with companies, sell-side research, independent research vendors, roadshows, presentations, conferences, and rating agencies.

Research is shared globally through informal information-sharing platforms, as well as more formal regular meetings to discuss views, build synergies, debate and refine ideas. Research notes are recorded and distributed across geographies and asset classes. Our teams also share unique and timely analysis on important macroeconomic and political issues, especially those that may not always be covered in the media. Ad-hoc meetings may also be organised between offices to discuss urgent market news and/or important developments.

Managing portfolio risks

One of the key defences we have against systemic risks is our Group Investment Risk Management department. It operates independently of the investment management division, with a separate reporting line to the Global Executive Committee via the Chief Risk Officer. The department oversees our risk management framework, keeping track of our exposure to a number of risks, including market risk, counterparty risk and liquidity risk, in order to ensure our portfolios are aligned to meet the best interests of our clients.

Group Risk Management Framework

A number of measures, such as scenario analysis and stress testing, are used to monitor exposure and the resilience of our portfolios to market shocks. In addition to these routine measures, ad-hoc stress tests are run in response to developing market risk. These stress tests may cover short – or long-term time horizons and use various macroeconomic and firm-specific assumptions.

The Group's Risk Oversight Committee reviews the firm-wide stress-test and scenario analyses and their impact on the firm's business at its quarterly meetings. Once risks are identified, we have a responsibility as an active manager to mitigate them in order to achieve the best outcomes for our clients. Actions taken will depend on the nature of the risk, the asset class of the strategy and also the style of the individual investment team, but may range from a review of portfolio holdings to ensure their suitability for the given market environment to a rotation into other instruments. During periods of market upheaval, we might also increase liquidity in our portfolios, either by increasing cash balances or by switching into more liquid instruments. This might be to provide a buffer to market volatility or to give us the ability to deploy cash when buying opportunities emerge, or both. We must also remain alert to the need to ensure that liquidity is sufficient to meet client redemptions.

Managing emerging and systemic risks

Emerging systemic risks and their impact on companies or industries are discussed at regular investment meetings. Financial markets faced a number of challenges in 2022 – geopolitical tensions such as the ongoing Russia-Ukraine conflict and Sino-US policy differences, global inflationary trends, quantitative tightening and increases to interest rates, as well as the ever-present hazards of climate change, to name just a few. The impact of each challenge varies depending on the nature of the asset class and the make-up of each individual portfolio. As a result, the way that our teams respond to these challenges, varies in order to try and position portfolios to ensure the best outcomes. In our passive portfolios for example, our operations team rebalances portfolios frequently to ensure a low tracking error versus the respective benchmark and aims to keep transaction costs to a minimum. How we have identified and addressed risks across our active strategies are described in the examples that follow.

Another example is in fixed income, where we hold monthly meetings to review the foreign exchange and interest rate outlook, as well as quarterly "horizon-scanning" meetings which consider long-term market issues without being distracted by the immediate focus of products or issuers. These meetings are led by our Global Fixed Income team and the purpose is to address fundamental challenges to the smooth functioning of global fixed income markets and what we can do to mitigate those challenges for our clients.

The Group's Risk Oversight Committee reviews the firm-wide stress-test and scenario analyses and their impact on the firm's business at its quarterly meetings

To aid the analysis that feeds into the regular meetings, the Global Fixed Income team uses a portfolio dashboard to help monitor market and systemic risk from a quant level to give an understanding of the range of risks from a number of angles, including regions, countries, maturity buckets, capital structures, currency, ratings and sectors, as well as the concentration of risks and portfolio limits. This process provides a high-level picture of global fixed income and currency markets, with each region and traded currency being assessed against macroeconomic, microeconomic, technical and valuation factors, helping us to navigate the current environment for global risk.

This scoring process provides the investment team with a gauge of the risk and risk appetite in the market, while also providing a one-month forward-looking view. The portfolio managers meet regularly to discuss information and research on the current condition of fixed income markets. The regional scorecards provide background for these discussions, along with our currency and interest rate views, helping to determine whether any changes are needed to be debated at our investment strategy meetings.

Once we have undertaken our analysis from a regional perspective, the team will then perform a country analysis. Amongst the many factors we look at, close attention is paid to central banks' policy stances, governments' fiscal positions, financial stability, and domestic and geopolitical developments. Each country is scored and the investment team's views are subsequently checked against market consensus and central bank projections to gauge the extent of risk in the market.

Principle 4

HOME

Below we show an example scorecard from January 2022, when the investment team was debating threats from inflation, growing labour shortages and an increasing inclination by the US Federal Reserve to raise rates and reverse quantitative easing, as well as growing geopolitical risk around the Ukraine crisis. The colour coding – red for "risk off", green for "risk on" and a spectrum in between – provides a visual indication of how risks were being viewed across core and periphery currency markets by the team at the time.

Fixed income risk scorecard

	Qualitative								Quantitative					
	Duration (1 Min to 5 Max)				FX (1 Min to 5 Max)				FX (over) Under			Duration		
	Median Team View	Quant	T-1	Δ	Median Team View	Quant	T-1M	Δ	FX (over) Under	RSI(30)	FX Rank	10yr Bond over (Under)	RSI(30)	Factor Rank
USD	2.0	2.0	2.0	0.00	4.0	1.0	4.5	-0.5	-5.7%	46.70	14	0.69%	51.6	10
AUD	2.0	1.0	2.0	0.00	3.0	3.0	3.0	0.0	5.6%	45.00	8	1.68%	50.0	13
NZD	2.0	2.0	3.5	-1.50	3.0	4.0	3.0	0.0	6.5%	36.80	6	1.01%	53.4	11
GBP	2.0	3.0	3.0	-1.00	3.0	5.0	3.0	0.0	10.1%	55.20	3	0.28%	45.8	8
CAD	2.0	5.0	2.0	0.00	3.5	4.0	3.0	0.5	9.2%	48.90	4	-0.64%	46.7	1
SEK	2.5	1.0	2.5	0.00	3.0	5.0	3.0	0.0	13.4%	45.30	2	2.09%	45.9	14
CHF	3.0	4.0	3.0	0.00	2.0	3.0	2.0	0.0	5.5%	46.70	9	0.00%	0.0	6
NOK	3.0	3.0	3.0	0.00	3.0	4.0	4.0	-1.0	6.6%	44.80	5	0.16%	49.7	7
EUR – Core	2.0	5.0	3.0	-1.00	2.0	3.0	2.0	0.0	6.1%	45.30	7	-0.46%	46.4	2
EUR – Periphery	4.0		4.0	0.00										
JPY	3.0	5.0	3.0	0.00	2.0	2.0	2.0	0.0	3.8%	46.56	10	-0.42%	47.3	3
EM	**2.8**	**3.3**	**2.8**	**-0.08**	**2.8**	**2.5**	**2.9**	**-0.1**						
MYR	2.5	3.0	2.5	0.00	2.5	1.0	2.5	0.0	-5.0%	45.86	13	0.45%	54.2	9
MXN	3.0	4.0	3.0	0.00	3.0	2.0	3.0	0.0	3.1%	50.63	11	-0.24%	72.1	4
PLN	2.5	4.0	2.5	0.00	2.5	5.0	2.5	0.0	18.2%	43.87		-0.01%	54.9	5
SGD	2.5	2.0	2.5	0.00	3.0	2.0	3.0	0.0	2.2%	47.93	12	1.61%	44.3	12
CNY	3.0		3.0	0.00	3.0		3.0	0.0						
ILS	3.0		3.0	0.00	3.0		3.0	0.0						

This risk analysis helped guide the team in positioning bond portfolios to meet the threats they faced. For example, as interest rates rose in major economies throughout the year, portfolios were adjusted to reduce their sensitivity to those rises and thus limit price depreciation. Similarly, the team actively traded currencies based on both near and longer-term views of expected strengths and weaknesses in order to limit downside risk and attempt to profit from opportunistic positioning where possible.

Systemic risks come in many forms and require many different methods to deal with them. An example of a geopolitical risk is shown by the case study below and examples of climate-related risks are illustrated later in this section:

Case study: Anticipating the shock to markets of the forced de-listing of Chinese companies from US stock exchanges (fixed income)

Issue: The Asian Fixed Income team identified the potential for widespread de-listing by Chinese companies from US stock exchanges as a market-wide risk in December 2020, following passage of the US Holding Foreign Companies Accountable Act. This required foreign companies to comply with audits by the US Public Accounting Oversight Board (PCAOB). Under the legislation, non-compliance for three consecutive years would result in forced delisting from US stock exchanges.

While the law would apply to all companies from any country, it was aimed at Chinese companies listed in the US. The US regulator identified more than 100 Chinese companies that were at risk of trading prohibitions for not complying with audit requirements. The lack of transparency at Chinese companies has long been a concern amongst investors, but Beijing has until recently resisted the calls for more disclosures on grounds of national security.

Finally, in August 2022, China agreed to allow US officials to inspect the audit work done on Chinese listed companies. The PCAOB inspectors and investigators have since been able to review the audits done on companies based in both mainland China and Hong Kong. They have said that they will release a report on their findings in the first half of this year.

Action: Shortly after these risks came to light, the team assessed the possible impact to companies of a forced de-listing, as well as the impact on our portfolios. In terms of companies, the team came to the following conclusions:

- Companies' access to capital markets would be impaired and could even mean them losing an important source of funding.
- De-listing could disrupt the market and affect the trading liquidity of the secondary market.

When assessing the possible impact to our universe, the effect was seen as being much smaller, with only a few companies likely to be hit. In terms of credit ratings, there were expected to be no immediate rating downgrades as the regulator had allowed a three-year grace period for Chinese companies to comply with the legislation.

Internally, the team placed the companies affected on "underweight", although several cross-market factors were also in play, then and later. As well as the threat of forced de-listing, there were wider Sino-US tensions, increased pressure from China's domestic market regulatory crackdown and the drag on the economy caused by China's zero-Covid policy. As a result, the Chinese tech sector, potentially a major victim of the US legislation, was both volatile and underperforming in 2022.

Outcome: Despite the concessions made by Beijing, the risk of forced de-listing remains. The full findings of the PCAOB will be reported soon and stringent enforcement against any companies that fail the audit review is expected from US regulators.

However, there are reasons to be cautiously optimistic. Recent media reports suggest that there have been positive steps on both sides. Moreover, the team believes that most of the companies at risk of forced de-listing have taken the necessary mitigating and/or pre-emptive measures to limit the impact. Some of the measures taken include:

- Several state-owned enterprises have already delisted from US exchanges in anticipation of not being able to meet the disclosure requirements on national security grounds.
- Some companies are seeking secondary listings on the Shanghai and Hong Kong stock exchanges in order to maintain their quoted status.

We believe that many companies have been working hard to achieve full compliance as they value their US listing. In the meantime, we continue to monitor developments and, from a credit perspective, we are sticking with companies that have strong balance sheets and limited reliance on overseas markets.

Climate change

We recognise climate change as one of the greatest challenges the global community faces. It is a prime example of a market-wide, systemic risk and one which we consider it is our fiduciary duty to address in managing our clients' assets. We adopt a two-pronged approach to climate risk:

1. **Collaboration with other stakeholders:** We work with other stakeholders to help develop solutions and support global initiatives to address the issue, such as the UN's Paris Agreement to limit carbon emissions and the UN's Sustainable Development Goals. We are involved in Asia with other fund managers seeking to collaborate to address the issue of climate change, of which more details can be found under Principle 10. We are signatories to, and participants in, many environmental initiatives, both globally and locally. Our commitments under the Net Zero Asset Managers initiative, as detailed under Principle 1, is one example and our implementation of the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), as detailed under Principle 7, is another. Other collective initiatives in which we are involved are described towards the end of this section.

2. **Addressing climate-related portfolio risks:** We see climate-related factors as both a key ESG risk and a potential opportunity for the companies in which we invest. Climate change is therefore factored into the investment processes of our teams across asset classes to ensure our investments are aligned to properly address both the risks and the opportunities. For example, for our Asia Ex-Japan equity and fixed income, we apply an investment risk management process to the monitoring of greenhouse gas emissions primarily for discretionary accounts. This process is performed by the Investment Risk department, which monitors the carbon emission of each portfolio against its applicable benchmark on a monthly basis based on agreed measurements and thresholds. Should a portfolio exceed its threshold, the Investment Risk department alerts the portfolio manager who subsequently evaluates the holdings. We do not exclude any company purely based on high carbon emissions but rather we evaluate the company's plans for the transition to net zero. For companies that have credible transition plans, they will be placed on a "white list" which allows the portfolios to hold that company despite its current emissions level. Should the portfolio manager be unable to justify that a company has a credible transition plan, they will either trim the holdings to bring the portfolio's carbon emissions down to below its threshold level or divest.

Case study: Monitoring portfolio climate change risks and opportunities (equity)

Activity: In addition to engaging with individual companies on their ESG commitments, the Global Equity team also engages across portfolios to establish a two-way channel of communication with investee companies.

In 2022, the team contacted companies held in our Global Equity strategy. There were several specific objectives of this project:

- to ensure that investee companies understood our commitment to supporting the transition to a low carbon future, as well as our stewardship priorities and those of clients;
- to ensure that the companies were aware of the team's obligations and expectations as signatories of initiatives such as Climate Action 100+ and the Net Zero Asset Managers initiative;
- to ensure the team had a baseline understanding of the strategies being employed by each of the investee companies to guarantee that they continued to generate stakeholder value and sustain revenue streams through the transition to a lower carbon environment (e.g. adoption of Science Based Targets or other commitments already or likely to be adopted);
- to verify the Scope 1, 2 and 3 greenhouse gas emissions (i.e. direct and indirect emissions and those from connected parties, such as suppliers) reported by our primary third-party ESG data vendor and any associated reduction targets;
- to establish whether management had performed assessments of the physical and transition risks associated with climate change and/or the effect of any carbon pricing, if it were to be introduced.

Outcome: The team received good responses from a number of investee companies as a result of this engagement. As expected, some are further along this journey than others, due in part to their wide dispersion, both by geography and sector. Overall, the portfolios have a significantly lower carbon footprint than their wider benchmarks. To a degree, this is because the team tends to underweight traditional oil and gas companies, which it does not think represent good long-term investments for clients. Given the importance of climate change, this is an issue the team will continue to raise with investee companies in the years to come, both in order to keep track of their progress and to encourage greater disclosure and best practice where we believe our influence as owners can encourage positive change.

Our investment approach focuses on ESG integration. We therefore continually strive to recognise and understand the risks and opportunities of climate change in our clients' portfolios, as well as improving our methodologies for assessing them. This includes appreciating the scientific implications of global warming and the structural changes likely to affect the business environment of the investee companies we analyse. For an illustration of how this operates in practice in our Japanese Equity portfolios, see our case study "ESG factors drive decision to sell major Japanese measuring instrument maker" in our response to Principle 7.

Climate change is an issue that is likely to affect all sectors, albeit on different scales and timelines. Some impacts are direct, such as carbon taxes, while others are indirect, such as the effects on ecosystems and biodiversity. Beyond known effects, we also acknowledge that systemic changes may arise from the increased instability of physical systems as global temperatures rise. Below we list some of the impacts we consider:

- the regulatory and operating environment, which influences the degree of adaptation and vulnerability of companies to climate change;
- the physical impact on business activities, which will differ between industries and locations;
- the social pressures on stakeholders, which may influence consumers' product selection and supply-chain management.

To assess these impacts, we use climate-related research tools and analyses, such as carbon footprinting, shadow pricing and by identifying our exposure to assets considered to be at higher risk of being "stranded" by the move towards a low-carbon economy. More detail on our approach to climate change can be found in our Position Statement on Climate Change, our TCFD Report and the content and case studies under Principles 7 and 10. Further, in 2022 we have started to use and analyse climate-related ESG data and apply them to our portfolio holdings. Further details, and an account of the challenges we face, can be found under Principle 8.

As a firm, we have been certified as carbon neutral since 2019 by Carbon Footprint Ltd, a UK-based consultant. We use the consultant for carbon assessments and offsets: it purchases carbon credits and retires them on our behalf to balance our emissions.

Collaboration to promote well-functioning markets

An important way in which we promote well-functioning financial markets is through our participation in industry bodies and forums, which help us to identify and address market and systemic risks and ensure that our processes, policies and procedures remain relevant.

We participate actively in forums and events, publish thought leadership articles and engage with a wide range of stakeholders, including clients, members of the investment management industry, policy makers and civil society.

An important way in which we promote well-functioning financial markets is through our participation in industry bodies and forums

Each of our subsidiaries is a member of the applicable local regulatory and industry bodies, for example the Investment Association in the UK. Members of our UK subsidiary have joined the IA's peer-to-peer knowledge sharing forums such as the Net Zero Forum, the SFDR Implementation Forum and the TCFD Implementation Forum. Some of the members of the Nikko AM Group take an active role in these bodies. For instance:

- Yoichiro Iwama, the Non-Executive Director and Chairman of our Group Board, continued to serve as a member of The Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Japan's Corporate Governance Code. The Council was established for the purpose of monitoring the use and adoption of Japan's Stewardship Code, launched in February 2014, and Japan's Corporate Governance Code, which came into force in June 2015, as well as further improving corporate governance of all listed companies in Japan.
- Eleanor Seet, the Chief Executive Officer of our Singapore subsidiary, is Deputy Chair of the Executive Committee of the Investment Management Association of Singapore (IMAS), a representative body of investment managers spearheading the development of the industry in Singapore. She also chairs the Conference Organising Committee of IMAS, which organises networking events such as the IMAS-Bloomberg Investment Conference 2022, of which more details are provided in the case study below.
- Also in Singapore, Kenneth Lim, our Joint Global Head of Operations is a member of the Environmental Risk Management Working Group, which was formed to help develop the Monetary Authority of Singapore's MAS Guidelines on Environmental Risk Management for Asset Managers.

Nikko AM Group staff helped organise and participated in a number of conferences and panel discussions during the year, being keynote speakers in several. For instance,

Nikkei Gender Gap Conference/Bloomberg Women's Buy-side Network Panel: Our Group President, Stefanie Drews, participated in a panel discussion entitled "Companies of choice and diversity: The forefront of female career development and male childcare leave" at the Nikkei Gender Gap Conference, quotes of which have been published in the Financial Times. She also told her career story, addressing inclusive culture and successful diversity and inclusion initiatives, at the Bloomberg Women's Buyside Network Panel, and she was profiled in the January issue of the Japanese women's magazine President Woman.

Organising Committee of the Investment Management Association of Singapore: As chairman of the Investment Management Association of Singapore (IMAS) Conference Organising Committee, Eleanor Seet helped shape the conference format, agenda, and provided guidance to the IMAS Secretariat in arranging the IMAS-Bloomberg Investment Conference 2022. The IMAS-Bloomberg Investment Conference 2022 attracted over 800 participants from 25 different countries interested in learning to be better stewards of capital and drivers of new standards and approaches that blend profit with purpose, while adapting to Asia's economic landscape. The 2022 conference theme was "Stewarding Capital Towards New Horizons: Investing for a Greener Future".

Impower Edge: Sustainable Innovation: Davina Goodall-Smith, Chief Operating Officer of our UK subsidiary, was a member of this panel discussing the availability and use of sustainable data, associated risks and how to avoid greenwashing, as well as different regulatory approaches and the implications for managing a global business. She highlighted the importance of integrating ESG and sustainability throughout the entire operating model, starting with the asset manager itself, through investment, and onwards to regulatory and client reporting. She also elaborated Nikko AM Group's approach to labelling under the EU's Sustainable Finance Disclosure Regulation (SFDR), emphasising that integrity is key and that labels should truly reflect existing investment processes.

Principle 4

The European Sustainable Finance Conference of the Association for Financial Markets in Europe: Cyril Lustac, Conducting Officer in our Luxembourg subsidiary, participated in this panel discussion looking at how investments could be made sustainable even if they did not meet the definitions set out by the taxonomy of the EU's action plan on financing sustainable growth. He reminded the panel and the audience that the EU's taxonomy allowed asset managers to develop their own sustainable investment processes. Although the EU taxonomy should be seen as the gold standard, it was not the only approach and was probably not well adapted to investee companies beyond the EU. He pointed out that the EU taxonomy could sometimes be too stringent in its quantitative demands, given the availability and quality of data. However, it could be used to identify both best practice and the key elements that any sustainable investment process should have.

Pension & Investment Conference: Johnny Russell, portfolio manager in our Global Equities team, gave the keynote speech in Japan on "Stakeholder Capitalism – What is it and Why Should Investors Care?". He focused on how stakeholder capitalism pertains to asset management. With the pendulum swinging from shareholder capitalism to stakeholder capitalism, investors are using ESG and the "three P's" – planet, people and profits – to help shape a better and more sustainable tomorrow. It is important for asset managers and owners to recognise the seismic change towards stakeholder capitalism that is taking place. For asset managers "there is a huge opportunity to add value for their clients with a deeper understanding of the changes within business and how client capital is making an impact. There is a lot the investment community can do". A subsequent Q&A session allowed the audience to discuss further the different definitions of stakeholder capitalism in different geographies, such as Japan and Europe.

ESG World Forum/InvestOps/CDO BFSI Exchange: Aria Goudarzi, our new Head of Strategic Analytics and Data and Global ESG Data and Reporting Lead, was part of multiple panels discussing how to support sustainable growth using ESG data as a strategic measure to drive profitability, efficiency and risk avoidance and how to successfully acquire, store and provide ESG data to meet rising ESG data expectations and enable more informed investment decisions. He also gave a keynote speech on "Creating an ESG Data Strategy to Support Strategic Decision Making", outlining the approach taken to create our groupwide ESG data strategy and why it was important to get as much information as possible from all key stakeholders, including the investment teams, multiple vendors and ESG regulation specialists.

In addition to our attendance at events, we also publish or contribute to thought leadership material and white papers. For example, Davina Goodall-Smith contributed to the white paper "Embracing Digital Innovation: How the buy-side is utilising data and technology to integrate ESG and optimise business growth in 2023" published by S&P Global. This paper covered the findings of a 2022 survey of the heads of investment operations and similar staff at buy-side firms across Europe to find out about challenges they faced and how they were responding.

Other initiatives we support, participate in or are signatories to include:

- The Asian Utilities Engagement Programme of the Asia Investment Group on Climate Change (further details can be found under Principle 10 and the case study there),
- CDP (carbon, forests, water),
- Climate Action 100+ (further details can be found under Principle 10),
- Global Investor Statement to Governments on the Climate Crisis,
- International Corporate Governance Network,
- Net Zero Asset Managers initiative (further details can be found under Principle 1),
- Principles for Responsible Investment,
- Task Force on Climate-related Financial Disclosures,
- The Investor Agenda,
- Women's Empowerment Principles.

Principle 4

Outcome

Overall, we believe both our processes and our actions demonstrate that we have remained effective in identifying and addressing market-wide and systemic risks during the year, ranging from the ongoing Russia-Ukraine conflict and the surge in inflation to forced labour and the perennial threat of climate change. We believe our case studies show that our investment teams have been both responsive and creative in reacting to these risks during 2022.

In addressing these risks, our guiding principle has been – as always – to put our clients first. This means our immediate reaction has been to position clients' portfolios to ensure the best outcomes for them. We are a small player in a large investment market but, by ensuring our clients' assets are directed responsibly, we can play our part in ensuring that capital is directed intelligently and ethically in support of well-functioning markets and a greener future.

And this is a multi-way process. While our first duty is to clients and their portfolios, we have not been slow to remind and educate company managements about the big threats they face. This may be market risks, such as those affecting Danish mortgages, or it may be ESG risks, such as exposure to companies with material climate change risks. In this latter category too falls our Global Equity team's initiative to poll companies on their carbon reduction strategies, approaches to wider ESG initiatives and to inform them of our policies. All this activity supports policy-makers and regulators in their work of maintaining smooth-functioning and responsibly-run markets.

On a wider front, one of the more useful ways of identifying new systemic risks and dealing with existing ones is to debate them with other industry participants. We have thoroughly involved ourselves in a wide range of industry initiatives, addressing a multitude of new threats and opportunities, from ESG investment developments and tightened regulation to improving data and encouraging more use of digital technology to tackle ESG threats.

One area where it is less easy to judge progress in the short run is climate change. This is due to the long-term nature of the risks that this poses and uncertainty around evolving policy developments and technological innovations. We will continue to enhance our strategies and methods to monitor and calculate the climate effects of our investment strategies, while developing approaches that minimise global warming. In doing so, we will continue to engage with other stakeholders in our effort to promote well-functioning markets.

Principle 5

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

Activity

Risk governance and oversight

At a group level, responsibilities for our risk governance and oversight are split according to the "three lines of defence" model:

- **First line of defence:** Front office business units and individuals identify and manage risks in their business function that could threaten the achievement of their objectives. They accept risks within assigned limits of risk exposure and are responsible and accountable for identifying, assessing and controlling the risks of their operations.
- **Second line of defence:** The support functions, such as Risk Management and Compliance, assess and oversee risk at the firm level, developing and maintaining risk frameworks, including firmwide policies. Each of these support functions, in close relationship with the front office business units, ensures that the risks of the business have been appropriately identified and managed.
- **Third line of defence:** The Internal Audit function provides independent and objective confirmation of the design and effectiveness of internal controls, i.e. it independently assesses the effectiveness of the processes created in the first and second lines of defence and provides assurance for these processes.

Policy & procedure review

All of our policies and processes, including our stewardship policies, are subject at least annually to a review and assurance process to ensure that they remain appropriate and effective. The review process varies depending on the substance of the policy, but in principle it is as follows: creation and drafting (for new policies), revision by the applicable department, and, if relevant, review by the appropriate committee, then review by either the subsidiary board, in the case of local policies, or the Global Executive Committee and Group Board, in the case of global policy.

The key policies that are applied to stewardship activities are listed below, with any changes made during 2022 detailed in the Outcome section. (We have not detailed policies less directly related to stewardship, but they follow the same review process described above.)

- Group Code of Ethics and Business Conduct
- Group Diversity and Inclusion Policy
- Group Commitment to Responsible Investing
- Group Conflict of Interest Control Regulations
- Group Engagement and Stewardship Strategy
- Group Proxy Voting Policy
- Group Best Execution Policy
- Group Trading Policy
- Group Environmental Policy
- Regulations on Engagement and Compliance Regarding Fiduciary/ESG Principles

Internal and external assurance

In terms of audit and assurance, we have a number of internal checks and balances provided by, for instance, oversight committees that include independent non-executive directors, as well as our Compliance department. Our policy is to audit each division every two years, with a follow-up to ensure implementation of any corrective action identified as a result of the audit. There were no substantial internal audit issues raised during 2022.

Various stewardship activities are audited by outside bodies. At the most basic level, they include our external financial auditors, who audit our annual accounts, but we are also assessed by a number of other independent auditors. For instance, under SSAE18 (for the US) and ISAE3402 (for the rest of the world), independent auditors assess our control procedures and their effectiveness, service delivery, information security and controls over data privacy. No substantial matters were raised during the 2022 external and independent audit.

As signatories of the UN-backed Principles for Responsible Investment (PRI), we gain further external assurance through our regular assessment by that organisation. This covers a range of stewardship-related activities, including our responsible investment policy, coverage and objectives, conflicts of interest policy, governance and human resources, performance management and rewards, personal development and training, collaboration and promotion of responsible investment. The PRI assessment is designed to provide us with feedback to support our understanding and development of responsible investment, which we subsequently process and integrate into our activities where applicable.

Principle 5

Our collaboration with industry organisations ensures that we stay up to date on the range of issues that are important to investors and the wider market and keeps our policies and processes up to date. As well as the PRI, these organisations include the regulatory and collaborative investment initiatives that our subsidiaries are members of, as set out in Principles 4 and 10, respectively.

Ensuring reporting is fair, balanced and understandable

All external material, including regular reports to clients, our annual sustainability reports and stewardship reporting to meet the requirements of local codes, is produced locally and reviewed by the local Compliance department. However, the ultimate judges of whether our reporting is fair, balanced and understandable are our clients, with whom we work closely. For instance, we have had relationships spanning decades with many of our institutional clients. Reporting has therefore evolved over time, not only in line with market norms – including an increased emphasis on ESG – but also as a result of our knowledge of clients' specific requirements. Further detail on how we communicate with clients and the process with which they assess our reporting is included under Principle 6.

Stewardship reporting required under other codes, such as those for Japan, are produced and reviewed by the relevant group companies.

Review and sign off process for our reporting under the UK Stewardship Code

To produce this report, we have brought together a number of internal teams from across the firm, including our Global Sustainable Investment department, ESG specialists, Compliance, Operations, global investment and members of our Client Services teams. We have used both internal and external resources to make it as informative and accessible as possible. It has been reviewed by our local stewardship governance, as well as being reviewed and approved by the UK and Group Boards and signed off by our Group President, Stefanie Drews.

Our collaboration with industry organisations ensures that we stay up to date on the range of issues that are important to investors and the wider market and keeps our policies and processes up to date

Principle 5

HOME

Outcome

We believe our combination of internal checks and balances, external assurance and audits and our widespread involvement in industry and regulatory bodies ensures that our policies, procedures and processes are subject to continuous and rigorous review. To be effective, such review has to result in action to ensure that our policies, procedures and processes are kept up to date and effective. Keeping that in mind, we made a number of changes to key policies that apply to stewardship activities as a result of our review and assurance processes during the year:

- A number of group policies, including the ESG Global Steering Committee Charter, Global Trading Policy and Global Best Execution Policy, have undergone changes relating to their internal structure, making reference to the internal Management Regulations and accordingly referring to applicable changes in policy owners and subsidiaries.
- Group Conflict of Interest Control Regulations – we amended the appendix of related group companies to reflect recent changes.
- Group Conflict of Interest Control Regulations – subsidiaries may add local policies and addendums to the Group policy, with changes to local versions during 2022 listed below:
  - The UK based Compliance department added several new potential conflict scenarios under a number of headings: broker/counterparty selection, fair allocation and participation in investment opportunities, proxy voting and related-party transactions and close personal relationships. Other changes included amendments to execution controls and allocation procedures, as well as a general tightening of disclosure requirements.
  - The Luxembourg-based Compliance department amended the local policy to ensure that there were references to key ESG themes, such as the integration of sustainability risk. The amendment included consideration of the potential conflicts of interest that could give rise to greenwashing or the mis-selling or misrepresentation of investment strategies.
- Group Engagement and Stewardship Strategy – this global strategy was developed during 2021 and reviewed and approved by the ESG Steering Committee in 2022. The strategy formalises our engagement and stewardship activities, ensures unity across regions and allows us to share with the market our global engagement commitments.
- Updates to our Standards for Exercising Voting Rights on Japanese Stocks came into effect in 2022, strengthening our criteria for the selection of directors. Specifically, the ratio for independent outside directors was increased, the absence of gender diversity on boards was agreed as a possible trigger to vote against members' re-election (to be applied in 2023), and the standards for the independence of outside directors were clarified and reinforced. Additionally, insufficient measures to manage and address climate change and sustainability were added as issues that could trigger votes against directors.

Changes because of reviews of policies less directly related to stewardship that took place during 2022 included a change to the compliance and risk management regulations. We amended the definition of compliance risk to clarify that conduct risk is included in Nikko AM Group's definition of compliance and to emphasise the importance of the handling of conduct risk under the existing risk framework.

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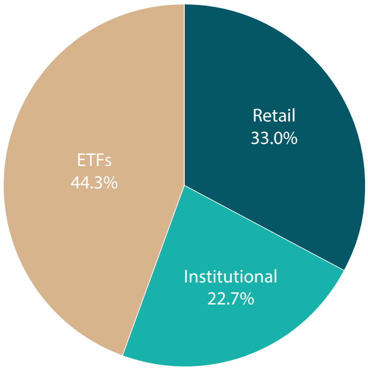
Principle 6

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

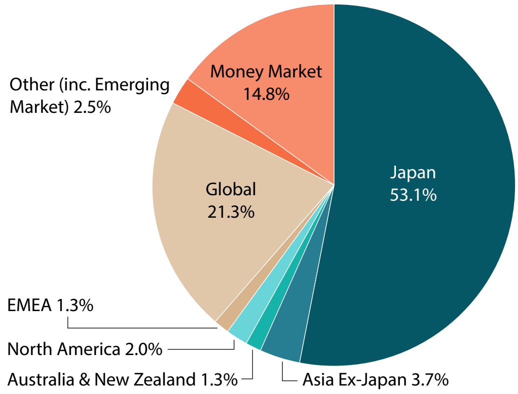
Context

A breakdown of our AUM (as at 31 December 2022) by asset class and client domicile is shown under Principle 1. Below we further present AUM by client segment[4] and AUM by geography of the managed holdings.

AUM by client segment



AUM by geography of asset class



Keeping in touch with clients is a basic duty of any asset manager and is a vital part of good stewardship. However, different clients have different requirements. The largest segment of our client base is in Japan, mainly investing in equities. Where we have retail clients, access to our products is through collective investment schemes via third-party distributors and we have to adopt a different approach when talking to this segment as opposed to our institutional investors. The former require easy-to-digest material that is clear, brief and well presented. The latter expect more direct, sometimes more technical and customised communication, with the amount and timing determined by our contractual relationships.

[4] The ETFs relate to a number of funds replicating equity benchmarks. Owing to the structure of these vehicles, it is not possible for us to know the underlying ownership of the funds and therefore we are unable to classify them as owned by either institutional or retail investors.

Principle 6

Investment time horizons

Whether they are retail or institutional, we believe most of our clients are best served taking a medium – to long-term view of their investments. We are not dogmatic about what this means in reality, but broadly view this as a holding period of three to five years for medium-term investing and ten years or more for long-term. For retail investors, we would argue this fits their need for long-term savings and best allows them to ride out the fluctuations in financial markets, thus maximising the value they can obtain from investing in securities. The same considerations apply to the majority of our institutional strategies, which are typically aimed at pension funds, insurance companies, banks, and sovereign wealth funds, which have long-term horizons. Of course, this overarching philosophy must be tempered by circumstances: political and economic events may require us to curtail our typical holding periods to reduce risks for clients. In contrast, as part of our TCFD project, referred to under Principle 7, we look to align time horizons for the consideration of climate-related risks and opportunities to longer-term scenarios, in particular as these relate to 2030 and 2050 net zero commitments. As displayed in Principle 1, nearly 15% of our groupwide AUM at the end of December 2022 was held in cash equivalents or money market funds, which typically have a shorter holding period of up to one year.

These perspectives are reflected in our communications with clients, which tend to focus on trying to explain long-term economic and market trends, including demographic shifts and the fate of globalisation in a less open world. They are reflected too in our policy of integrating climate change and other ESG considerations into the investment processes.

We believe that this combined range of products and strategies aligns well with the needs of our clients.

Activity

Accountability to our clients is at the heart of our fiduciary principles and communication is therefore crucial. For all clients, this means providing easy-to-understand materials that explain our investment approach, product risk characteristics and fees, as well as tools that help them understand their investments and the risks involved. As is stated in the Context section above, a large segment of our AUM is managed for retail investors via intermediaries and, in terms of geographic location, the majority of our clients are based in Japan. We have therefore focused on our communication with Japanese investors in the Retail investors section below.

The COVID-19 pandemic changed the way we communicate with our clients. We assembled the infrastructure needed to handle events remotely during the pandemic by setting up digital seminars and training sessions. This enabled us to provide customer support without in-person meetings. We were also able to help distributors in their efforts to service their retail customers by supplying them with information quickly, accurately and concisely through a wide range of media. As a result of our active promotion of remote seminars and training sessions, we have built up a hybrid communications strategy, using both traditional in-person and online approaches, that is both robust in the face of widespread disruption and allows greater flexibility and breadth of content in our interactions with clients.

Retail investors

We run a large number of mutual funds which are sold through banks and other distributors to retail as well as institutional investors in Japan. We therefore put a great deal of effort into timely, understandable and accessible communications with Japanese retail investors. As we do not sell directly to them, our communications efforts are primarily directed at our distributors: banks, brokers and, increasingly, internet-based groups.

We provide a wide range of information to distributors and Japanese retail buyers of investment funds, not only concerning the specific funds in question but also related to broader themes, such as the economy and markets. Our aim with our communications aimed at retail investors is to ensure they understand what is happening with their own investments and the reasons, while fostering a deeper understanding of markets and investment trends.

Realising that there are wide differences in the level of financial sophistication amongst our retail investors, we tailor our communications to the differing audiences within the group. Thus we provide videos on our website aimed at both distributors and end investors. For example, we might support a particular fund with:

- videos aimed at first-time viewers to promote the fund;
- videos that explain the concept of the fund in more detail;
- regular videos and other materials that keep the clients up to date with performance and underlying factors that affect the fund.

We also put a great deal of effort into webinars, online educational courses and training for distributors and end investors, an effort we have stepped up since the onset of the pandemic. Under our Nikko AM Fund Academy brand, we provide what we deem to be essential fund-related knowledge and information for our retail investors and distributors, and also for non-customers.

Principle 6

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Regular information material produced under the Nikko AM Fund Academy brand

Item	Frequency
Rakuyomi (easy five-minute briefing)	Twice weekly
Koyomi (quick soundbites)	Monthly
Gokuyomi (deep dive)	Ad-hoc (four released in 2022)
Market 5 Minutes	Monthly
Weekly Market	Weekly
Date Watch (compilation of major index performance and market trends)	Weekly
Follow-up memo (commentary from our chief strategist, Naoki Kamiyama, on major market events)	Ad-hoc (five released in 2022)
Global REIT Weekly	Weekly
Monthly Market	Monthly
Japan In Motion	Quarterly
Nikko AM Newsletter	Ad-hoc (three released in 2022)
China Insight	Ad-hoc (12 released in 2022)
Kamiyama Reports (market update reports by our chief strategist)	Ad-hoc (16 released in 2022)
Kamiyama Seconds! (quick updates by our chief strategist)	Ad-hoc (50 released in 2022)
Why should we invest?	Ad-hoc (one released in 2022)
What Nikko AM wants you to know about money management	Ad-hoc (one released in 2022)
Global Foresight	Quarterly

Seeking retail client views

This is not just about us talking and our clients listening. We take the views of our distributors seriously as they are in frequent contact with their clients and are therefore a key conduit in passing retail investors' views back to us. This feedback is an important guide for us, both in the material we provide for distributors and in the design of new products. There are several ways in which we seek the views of both distributors and, in some cases, retail investors directly.

A significant amount of effort in the Tokyo-based retail business is spent on an extensive programme of seminars conducted by around 50 dedicated personnel. These seminars are planned and organised for individual branches for audiences of roughly 200 distributors at a time. Such seminars can be divided into:

- on-site seminars for retail investors, where a distributor invites its customers to one of its branches, and
- study sessions for sales representatives of distributors.

In both cases, speakers from Nikko AM Group visit the financial institution to give presentations which last typically for about 60 minutes.

In the 2022 calendar year, we have held seminars both online and in person. The content of these seminars and investor feedback was successively reported to relevant managers by the in-house customer relationship management system, enabling them to both stay abreast of recent developments and changes in investors' and distributors' views.

We organise annual events under the umbrella of the Nikko AM Product Strategy Academy targeting the product planning teams of our distributors. In addition to providing information on existing products, we also present ideas for new products that are expected to meet future investor needs. These are valuable opportunities for open communication with our distributors, enabling us to receive candid views directly from the teams responsible for fund marketing. For instance, we poll participants after the many presentations on new product ideas. Those that receive strong support in these votes are often then realised in new fund launches. Our most recent Product Strategy Academy was in November 2022, with over 130 participants from 84 financial institutions from across Japan attending in person.

To gather all this feedback, our staff in Tokyo regularly contact distributors' headquarters and local branches. This information is then added to views gathered directly from retail investors who have contacted our call centre team and is shared with relevant Nikko AM Group staff via the customer relationship management system. In addition, there is an internal process so that particularly important comments, particularly any strong views of our distributors, are brought to the attention of senior sales managers without delay.

While we cannot know directly what our retail clients feel about our retail communications efforts, we regularly receive favourable endorsement from third parties. For instance, in 2022:

- **For the fourth year in a row, we were placed first in the annual mutual fund company satisfaction survey conducted by Rating and Investment Information, Japan's largest rating agency.**
- **We were similarly ranked number one for the fourth year in last year's branding survey by Nikkin, the Japanese news agency.**
- **We were also placed first in the latest asset manager branding survey by MaDo, a major financial publication in Japan.**

We believe the results of these surveys represent a weighty vote of confidence from intermediaries and commentators in the quality of our customer support, as well as how and what we communicate to the market.

Dealing with bad news

Perhaps the acid test of client communication is how well an asset manager talks clients through difficult markets and portfolio losses. As it happened, 2022 turned out to be a year of headwinds for some of our thematic funds focused on innovation that had attracted a great deal of assets in previous years but significantly underperformed in 2022. Not surprisingly, this was a source of disappointment for many of our distributors and their end investors.

We were quickly aware of investors' dissatisfaction through our contacts with both the local branches and the headquarters of our distributors, as well as directly from our call centre team. This triggered urgent discussions within our sales and sales support teams as to how to respond and enhance our information disclosures to calm the anxieties of investors.

Guided by the feedback we received, we substantially increased the production of ad-hoc "spot reports" addressing the points of concern coming from our distributors and investors. These reports were circulated to our distributors and posted on our website, ensuring that we responded quickly to our investors' feedback. During the whole year, we produced 50 such spot reports for our seven innovation funds. To put that into context, in a normal year, we would typically create only one ad-hoc report per fund, which emphasises just how importantly we regarded the concerns of both investors and distributors.

Institutional investors

It is our policy as a group to tailor the frequency and method of communication with institutional clients to meet their specific requirements. These are typically discussed and agreed as part of negotiations when the investment management agreement is set up, but the heart of our communications with institutional clients is our direct discussions. Our sales directors and client services teams work with clients to confirm the required content and timing of all regular client reports. In addition, we schedule investment reviews at least annually, and can arrange ad hoc meetings as required by the client.

Outside of a client's regular performance reviews, we take a proactive approach to ensuring clients are kept up to date with important information affecting their portfolios, including any changes to their mandates or significant market events which may affect performance.

Regular meetings with our institutional clients are a two-way process. As well as the normal discussions and reports on performance, we provide explanations of a wide range of investment-related topics in answer to client queries.

With most of our institutional clients, we hold dedicated meetings once a year, although we may report on proxy voting, company engagement and other stewardship activities more frequently as clients require. Before these meetings, we typically submit information on a range of topics. Information may include our stewardship policy, implementation framework, company engagements and their effect, and third-party assessments of our ESG integration and stewardship activities (for example, the latest Principles for Responsible Investment assessment). To meet clients' requirements, we are also able to provide reports on carbon intensity and other carbon-related disclosures, ESG scores and related information, for the companies in which we invest. Further information on our engagement policy with investee companies is available under Principle 9.

We typically explain our voting decisions in some detail, including how we dealt with specific proposals and, in particular, where we voted against management proposals. We also discuss occasions where views within the firm differed and how internal consensus was reached. Further information on our proxy voting policy and how we voted can be found under Principle 12. How we cast our proxy votes and the number of company engagements we undertook during the year are disclosed on our website.

In addition, we hold regular corporate sustainability meetings with clients, typically on an annual basis, to report on our broader sustainability initiatives that encompass not only investments but also other activities at the corporate level. Such discussions often involve an exchange of ideas as to what asset managers and asset owners can and should do to fulfil their fiduciary responsibilities and contribute to the betterment of society.

We are always keen to understand the investment and stewardship principles our clients wish us to adopt when managing their assets and, in return, we explain the firm's policies and approach to implementation. Should there be any misalignment between the two views, we try to reconcile the differences with the aid of the Stewardship and Proxy Voting Committee's secretariat or other relevant specialists. Our aim is to be flexible when making any necessary amendments to the policy. For instance, when required by equity clients, we will adopt their policies on proxy voting or engagements. For segregated mandates, where possible, we are happy to implement client-supplied lists of investments to be restricted or excluded and will tailor our investment approach to meet their specific requirements.

Case study: Aligning an investment portfolio to meet the client's ESG preferences (equity)

Issue: An insurance company client with a segregated Japanese investment portfolio wanted to raise the classification of its mandate with us under the EU's Sustainable Finance Disclosure Regulation (SFDR), which is aimed at improving ESG disclosures by asset managers. Specifically, the client wanted to move the portfolio from the lower classification provided by Article 6, which does not require sustainability as an ultimate aim, to one complying with Article 8. This higher "light-green" classification requires the portfolio to promote environmental and/or social characteristics, while following good governance practices.

Outcome: After about eight months of discussions between the client, our investment team, the Japan Sustainable Investment department and our global ESG staff, we reached agreement on an Article 8 proposal. This was reviewed by the client's responsible investment specialists and modified as required in line with their feedback. Having been agreed with the client, the changes required to upgrade the portfolio were then agreed by our internal Product Committee and implemented in July 2022.

Case study: The Danish mortgage bond market – an example of end-client and broker engagement (fixed income)

As part of our 2022 submission, the Global Fixed Income team outlined the role of Nikko AM Group as a bridge between Japanese investors and the Danish mortgage bond market. The case for investing in the market includes its depth of issuance, liquidity, and quality in terms of being predominantly AAA-rated. These attributes mean it offers a valuable diversification and income stream compared to domestic Japanese bonds.

Initial positions in the market were taken by Nikko AM Group clients as long ago as 2016, at which time our holdings were enhanced by beneficial hedging, but those benefits have since been gradually eroded. And while the market has generally proved to be robust and resilient in both favourable and difficult market conditions, it experienced falls in 2022 in line with most other bond markets on the back of increasing fears of tightening monetary policy in Europe. As bond prices fell, concerns grew that some Japanese clients would become forced sellers of their positions, owing to the structures and rules of their funds, notably if the market price fell below the original purchase price of the bonds. Our London-based investment team worked extensively with investors to provide the background to the prevailing market conditions and, in particular, to demonstrate that price movements were not out of line with other markets. Moreover, concerns about much higher inflation and much tighter monetary policy in Denmark seemed overdone and, with the peak of the rate cycle nearing, domestic investors were confident that the market would find a good level and recover.

A key aspect of a significant number of direct client meetings over this period was to support clients who wanted to disinvest in a way that helped them avoid selling at the lowest prices. Client sales did occur, but were largely executed in recovering markets. Moreover, clients were able to make decisions from a position that embraced the fundamental arguments in favour of the market, even if the changing cost of hedging might have altered its attractiveness from a Japanese perspective.

Outcome: Our intervention during this market volatility often strengthened our client relationships, as we formed a key bridge between investors on the one hand and brokers and issuers on the other. The increased communication did not halt outflows, but allowed them to be well managed and probably lower than they might otherwise have been, as some investors took stock of their positions before the market stabilised.

Our role as a bridge was two-way, with domestic brokers keen to understand the changing sentiment amongst overseas holders. This ongoing dialogue with brokers and issuers helped ensure flows were well managed and did not overwhelm or surprise local players. Indeed, some did not even realise the extent of overseas sales.

Principle 6

Case study: Helping pension fund clients prepare to sign Japan's Stewardship Code (equity)

Issue: We manage Japan equity portfolios for several corporate pension funds which were considering signing Japan's Stewardship Code. Being a signatory of the Code ourselves,[5] we were able to organise meetings with specialists from our Japan Sustainable Investment department who are well versed in the Code's principles and well able to provide relevant materials. These discussions often expanded from an explanation of the basic concepts of the Code into a wider debate about its key points, the merits and demerits of accepting the Code for asset owners, and broad trends relating to stewardship activities.

Outcome: This process helped our clients deepen their understanding of the Code and related initiatives. One client requested further help in drafting its own policy to enable it to fulfil its responsibility as an asset owner under the Code. We drew up a list of items to monitor and proposed a stewardship structure that would allow it to perform its duty towards its plan participants. On the back of the assistance we provided, the fund was able to publicly announce its commitment to the Code. This was an encouraging example of sharing best practice. We will continue to encourage our investee companies to benefit from our knowledge of the practical application of stewardship, just as we will continue to be educated by their experiences.

Case study: Incorporating client feedback into our company engagements (equity)

Issue: An example of how we use feedback from clients to adjust our interactions with investee companies emerged from recent discussions with a Japanese public pension fund whose Japan equities portfolio we manage. The client indicated that, while it was pleased with the frequency and content of our company engagements, the management framework for how we engage could be enhanced. This observation was based on extensive experience as well as peer analysis by the client of all its investment managers.

Outcome: This feedback prompted us to enhance our internal engagement platform, covering the Japan Sustainable Investment department, research analysts and portfolio managers – so that we could strengthen collaboration within the investment division. We also enhanced our milestone management approach for company engagement in order to more closely track the progress and effects of our activities.

In future, our focus will be on selecting issues or areas that require improvement at investee companies. Progress towards targeted goals will be closely watched and further steps laid out according to the stage a specific engagement has reached. Monthly reviews of outstanding issues and the status of engagement will be conducted by specialists from the Japan Sustainable Investment department and shared with research analysts and portfolio managers. A more detailed analysis of the engagement plans and progress to date by the company will be performed at least on an annual basis, following which engagement goals may be upgraded, materially revised or scrapped.

In terms of this particular Japanese pension fund client, we relayed to it our enhancement plans and gave our assurance that they should go a long way to meeting the request for enhanced engagement. Nonetheless, we will continue our discussions with the client with a view to further improving the quality of our stewardship activities.

[5] https://en.nikkoam.com/stewardship-code

Principle 6

These discussions help to confirm that we and our institutional clients understand each other and that their views are accurately shared with all the relevant people in the firm, particularly the investment teams. In order to maintain close communication with our institutional clients, we focus on face-to-face interaction via online and/or offline meetings although we also use other methods of communication. Our client-facing personnel spare no effort in seeking detailed feedback, confirming whether explanations given at meetings are sufficient and generally ensuring that clients' expectations and requirements have been met.

Our Compliance department provides an independent check on whether investment portfolios are adhering to clients' investment policies and the relevant guidelines. Where necessary, it will discuss its review findings and any operational issues that need to be addressed with the investment teams, local management and head office.

Our non-Japanese investment teams maintain an active dialogue with our Japanese clients via our Tokyo-based Client Service team. We supply monthly investment positioning and performance reports, as well as market outlook updates. The Client Service team offers the first response to client requests about their portfolios and many of these are subsequently fed through to the teams on the ground for a further response. Portfolio managers typically visit Japan on a regular basis and, in addition to updating clients on their portfolios during investor meetings, they will also offer educational workshops. For example, our Global Fixed Income team offers seminars on European markets and the Danish mortgage bond market to clients and prospective clients. Some clients have also sent their representatives to London as a means of learning about the market and its day-to-day workings. These contacts strengthen our dialogue with clients and our understanding of their needs.

Outcome

Given that our largest client base is in the intermediary segment, it is harder for us than some other asset managers to assess the effectiveness of our communications with the retail market. However, we take comfort in the high rankings we regularly receive in the three most influential independent industry surveys in Japan, described above. These third-party endorsements of our retail communications provide testimony to our success in getting our message across to retail clients.

We increasingly use retail client feedback to shape and drive our communications , for example by addressing specific points of concern in the reports that we produce. Both our distributor network and our call centre team are essential in garnering, understanding and making use of this feedback.

In terms of institutional clients, we make it a regular point at our client meetings to ask whether clients feel that they still understand the investment strategy we adopt for them and whether it continues to meet their needs. Beyond that, we are constantly seeking clients' comments on the scope and quality of the services we provide, as well as their degree of satisfaction with our investment results. This can be through separate feedback sessions or during the course of our regular communication with clients – portfolio and operational review meetings conducted by our Client Service teams are another important feedback point. Some of our institutional clients formally evaluate their third-party managers, such as ourselves, and assign scores. We always value such feedback from clients as it enables us to more objectively evaluate the effectiveness of the service we provide and highlight areas where we can improve.

We are very ready to make changes to the strategies we employ based on client views, for instance, by strengthening our ESG integration or using additional investment techniques (e.g. derivatives) to better meet clients' needs. As outlined in the case study above ("Incorporating client feedback into our company engagements"), such feedback was instrumental in prompting us to enhance our internal engagement platform to both consolidate and better manage our engagement activities. By the same token, we constantly strive to enhance the regular reporting of our investment or stewardship activities to meet clients' demands.

There were only very rare instances during the year when there were breaches of clients' investment policies. Breaches sometimes occurred when, for instance, the attributes of securities in mandates had not been properly reflected or updated in the order management system, which resulted in erroneous purchases of securities, or there were changes due to external factors outside of our control, such as market movements. There were also a few instances of deviation from the client proxy voting guidelines caused by the conflict between our guidelines and those of the client. In all such instances, we immediately addressed the situation by clarifying the cause, taking the necessary remedial steps, and implementing preventative measures. We also provided a full explanation to our clients, in line with regulatory requirements and best practice and, if necessary, made additional efforts to eliminate any future ambiguity in the interpretation of clients' investment and proxy voting policies.

HOME

Principle 7

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

Context

As we stated under Principle 1, we strongly believe that stewardship, including fiduciary and ESG considerations, are inherent to long-term corporate value creation and contribute to the realisation of sustainable economic growth. We therefore see ESG issues as an integral part of our fiduciary duty to clients and incorporate ESG principles in all our investment processes.

We do not adopt a one-size-fits-all approach to integration. The main responsibility for implementing our fiduciary duties falls on our investment teams and they are given a remit to act in the best interests of our clients within the global and local governance frameworks provided by the Group. This means that our ESG integration and engagement processes are bespoke to each investment team, ensuring each chooses the methods most appropriate and effective for them. Where appropriate to the asset class, investment strategy and client requirements, certain investment teams may maintain specific ESG policies and procedures pertaining to their investment philosophy and process.

Allowing for asset class and regional differences, our Global ESG Steering Committee via the Global Sustainable Investment department is responsible for monitoring and improving the investment teams' implementation of stewardship principles. Whilst the local approaches may differ, this global process ensures there is consistency across the firm. We believe that it results in a structure that enables us to serve the best interests of our clients.

ESG issues are rarely the only consideration when making investment decisions, but an understanding of these issues informs the investment process and gives our investment teams a more rounded view of companies. In applying ESG policies and procedures to their particular circumstances, our investment teams consider a number of factors, including (but not limited to) the environment, climate change, human rights and labour standards, talent management, product safety, diversity, board structure and independence, alignment of remuneration, transparency of ownership and control, and accounting. An acceptable ESG standard is never the sole determinant for investment, however, where materially negative ESG issues are identified and we do not believe that corrective measures will be taken, the relevant investment team will take appropriate action which may include excluding the company from investment consideration. For existing holdings, an indication of material deterioration in ESG factors may lead to a rating downgrade and subsequent sale from the portfolio.

This is not a one-off exercise but rather a process of continuous assessment. ESG considerations are applied before investing, while holding an investment and before selling. In addition to our own policies and considerations, certain issues may be given priority because of feedback from our institutional clients, either at the inception of a mandate or as the mandate evolves over time. We also maintain an active dialogue with our service providers, making clear to them our ESG priorities. For example, during our annual review with ISS, who provide us with analysis for proxy voting resolutions, we share any updates to our responsible investment and voting policies. The service level agreement with ISS defines the relationship at a group level, but each subsidiary works directly with ISS to tailor its local platform to accommodate any criteria required, including those relating to ESG.

Since the creation of the ESG data team in 2022, we have focused on improving the availability, as well as the quality, of the data being used by investment teams. A primary focus has been to ensure that our data are accurate, timely and consistent across all investments covered. One important service provider which we currently use for the provision of ESG data analysis is MSCI. As part of an internal project, which is continuing, we have had several calls, teach-ins and email discussions with MSCI to ensure we both understand and know how to use the data it supplies. The results of these sessions then feed into discussions between the ESG data team and the investment teams to decide how to use the data in practice.

We also engage with MSCI when we see errors and try to resolve them in a timely manner. We go into more detail about this under Principle 8. In addition to liaising with MSCI, the ESG data team contacts our portfolio companies to verify the data being supplied by third parties, and to encourage climate-related disclosure and target setting in line with the Science Based Targets initiative (SBTi), which is further discussed later in this report. We would view success here as being confirmation that the ESG data used in our analysis and client reporting accords with what we are receiving on the ground from companies.

Further information on how we interact with and hold to account our service providers can be found in our responses to Principles 8 and 12.

Climate change

Amongst the most important ESG issues, we recognise climate change as the greatest the global community faces. We therefore consider it a fiduciary principle that we must address when managing our clients' assets. We reinforced our commitment to this principle and outlined our approach to climate change in 2019, when we published our Position Statement on Climate Change. In 2022, we reinforced this with a project to widen and deepen our implementation of the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD), as outlined further below.

The current position statement contains the four building-blocks of our approach:

1. enhance in-house analytical capabilities;
2. collaborate with the investment community;
3. conduct active stewardship; and
4. report on our activities.

While these are the outlines of our approach, we do not seek to regulate how each investment team puts principle into practice in their own investment processes. However, in all cases we do believe that active dialogue and exercising voting rights on climate change, where appropriate, can lead to positive outcomes for investee companies, our clients and our firm. We participate in relevant collaborative corporate engagement activities, such as the Climate Action 100+, to communicate our expectations to investee companies (see Principle 10 for more on our collaborative engagement activities).

We generally do not apply blanket exclusions of investments based on climate change factors unless directed by our clients. We prefer active engagement and the exercise of voting rights, which we see as more effective in upholding ESG and stewardship standards, whether it be for our clients, for the broader economy or for the environment. We believe that exclusions based on formulaic filters to determine climate risks can be inflexible at times and in some cases might fail to capture the future potential of companies to respond to the transition to a low-carbon economy.

We believe that thorough research and vigorous debate within the teams, as well as direct engagement with companies to get a first-hand appreciation of the issues, are still the best ways to evaluate ESG factors and judge their impact on investment outcomes. We also recognise that climate-related impacts are complex and uncertain, so we need to keep abreast of scientific findings and information, and how regulators and stakeholders are responding to them.

While we take account of our own climate change principles in our portfolios, we also work with clients to provide low-carbon investment solutions aligned with their specific investment beliefs. For example, our Global Green Bond Fund is a low-carbon collective investment that invests in securities that finance climate change mitigation and adaptation projects, ensuring the highest level of transparency for investors who want to avoid "greenwashing". Launched in 2010, the strategy invests in bonds issued by AAA-rated sovereign issuers, "supranational" bodies, such as the Asian Development Bank and European Investment Bank, and agencies, such as the US Federal National Mortgage Association (Fannie Mae). We also have a Hydrogen Fund managed by our Global Equity team, which enables our clients to participate in the financing of the green hydrogen economy and the transition away from fossil fuels.

As a signatory of the TCFD and in line with its recommendations, we encourage our investee companies to take the following steps:

- identify material climate change risks and opportunities in a range of scenarios (including where the global temperature rise is kept below 2°C) over appropriate time horizons;
- integrate material climate change risks and opportunities into their overall business strategy and risk management;
- disclose the management policies and processes they have designed to meet the goals – and resulting performance – that emerge from the above activities.

We recognise the need to continually enhance and improve our efforts in relation to climate change and in 2022, we took a further step by initiating a global project to assess and enhance our response to the recommendations of the TCFD, which includes purchase of advanced climate analytics data. The outcomes of this work will be published in our next version of the TCFD report in 2023.

Activity

The investment teams in our actively-managed strategies identify attractive stocks through in-depth bottom-up research, based on their own philosophy and approach. ESG factors and the risks and opportunities they present for the stock or bond are integrated into this process, providing additional considerations to be taken into account in stock selection.

ESG factors are thus rooted in our investment philosophies and processes and not treated as being part of a separate exercise. We strongly believe that attention to ESG factors is a part of good investment discipline – core to any business and inherent to its long-term value creation, while contributing to the realisation of wider sustainable economic growth. Given this view, we endeavour to incorporate ESG considerations across all asset classes and geographies.

Having said that, different asset classes have different dynamics, with varied geographies and industry sectors adding to the complexity. Each of our investment teams is therefore allowed to view ESG implementation through its own lens, leading to diverse approaches across the organisation. Whatever the approach, we strive to apply all ESG policies to the highest standard, continually seeking improvement and innovation.

ESG risk analysis is integrated into the investment research function rather than outsourced to a separate team. Each investment team is responsible for the assessment of risks that may affect the success and long-term sustainability of holdings in the portfolio. Our detailed process – including stress-testing investment candidates, stock selection and portfolio construction – also helps to ensure that the whole investment team is engaged in managing ESG risks.

ESG specialists support the investment teams as part of our aim of having all investment professionals integrate ESG into their investment processes to the fullest extent. They also build relationships with various ESG-focused organisations and regularly share information with the ESG Global Steering Committee on developments, such as ESG-related legal changes in countries around the world. The Global ESG Global Steering Committee reports to the Group Board and in our UK subsidiary, the regional investment teams are required to present their ESG implementation activities to the local Board.

The table below gives a brief overview of the approach taken to ESG integration as applied across the various asset types and geographies that we manage.

Asset class	How we integrate ESG and stewardship responsibilities into the investment process
Japanese Equities	• ESG is integrated into all investment decisions in these portfolios through the use of a selection process based on "Creating Shared Value" (CSV) evaluations. CSV evaluations come from the work of Harvard University Professor Michael Porter, which found that the creation of social value leads to economic value. • We have used our own CSV evaluations as part of our investment process since 2013. They currently comprise 12 factors grouped into three categories – ESG, competitiveness and financial strength. See our case study: "ESG factors drive decision to sell major Japanese measuring instrument maker" for an example of how we integrate this assessment into our management of Japanese equities. • Engaging constructively with company management in relation to our key themes: **E:** Action for a Decarbonised Society, **S:** Human Capital and Productivity, **G:** Effective Governance. • Exercising voting rights, including voting against director appointments where the firm faces serious risks related to climate change or sustainability issues, where management initiatives to address them are deemed insufficient and where the situation is not deemed to be improving. • Proxy voting is executed in the interests of our clients in line with our proxy voting guidelines. See Principle 9 for more on our approach to engagement.

Asset class	How we integrate ESG and stewardship responsibilities into the investment process
Global Equities	• ESG analysis is undertaken by each portfolio manager and fully integrated into the stock-picking process to ensure we can robustly evaluate the materiality of each factor and its potential impact in the future. • Our four-pillar "Future Quality" analysis includes in-depth evaluations of ESG factors to determine their effect on the company's risks and returns. • Research includes an analysis of a company's corporate governance, social practices, the environmental sustainability of its products or services and its capacity to fund its growth and ESG commitments. • Our investment team engages with investee companies to help promote better ESG practices if we believe there is room for standards to improve. This includes ESG controversies identified by the Global Equity team. • MSCI validates our ESG analysis through its ESG Fund Ratings service by scoring our global equity portfolio, which is rated AAA as at the end of December 2022.[6] • Proxy voting is executed in the interests of our clients in line with our proxy voting guidelines.
Asia Ex-Japan Equities and China Equities	• ESG analysis is incorporated into company research, security selection and portfolio construction. Our ESG "Materiality Map" focuses on the material issues and opportunities for each of the companies we cover, based on ESG factors from the Sustainability Accounting Standards Board (SASB) and MSCI. • As part of our in-house proprietary ESG scoring methodology, individual companies are scored on ESG pillars, alongside fundamental analysis which is aggregated to provide a company-level score. ESG-focused research is also used to identify areas for company engagement and improvement. (For how this applies in practice, see our case study: "Improving ESG disclosures at a large Singaporean agribusiness").
New Zealand Equities	• The team seeks to understand how industry and company ESG factors may impact investments and ultimately client portfolios. • ESG factors are considered as one aspect of the overall analysis to build a picture of the risks and opportunities faced by a company. • Portfolio companies with low ESG scores are targeted for engagement in an effort to lift the bar in weak areas or where improvement would be beneficial to stakeholders. • We are also proactive in finding and addressing wider issues affecting New Zealand companies, such as modern slavery (see our case study: "Taking a stance against modern slavery in New Zealand" below for more detail). As part of this effort, we have launched the Nikko AM Freedom Fund, which donates all the fees and returns to the charitable organisation, Tearfund. Tearfund works through partnerships in some of the poorest parts of the world. Together with these partners, it offers an end-to-end response to the issue of human trafficking and slavery, tackling poverty and injustice through sustainable development. • Proxy voting is executed in the interests of our clients in line with our proxy voting guidelines.
Global Fixed Income	• The majority of fixed income assets managed by the investment team are in AAA-rated bonds. Particularly in the case of corporate credit, ESG factors are considered to the extent that they are deemed material to the investment case and in line with our Japanese clients' risk appetite and perspectives on ESG investing. • In relation to our holdings in sovereign entities and major banks, we maintain an active dialogue on ESG themes as a means of building our insight and market intelligence.

[6] MSCI ESG Fund Ratings are designed to measure the environmental, social and governance (ESG) characteristics of a fund's underlying holdings, making it possible to rank or screen mutual funds and ETFs on a AAA to CCC ratings scale.

Principle 7

Asset class	How we integrate ESG and stewardship responsibilities into the investment process
Asia Fixed Income	• Our ESG Materiality Map is applied to the company using ESG factors based on the Sustainability Accounting Standards Board and MSCI, but adapted to reflect conditions in Asia. • ESG analysis is incorporated into all company research and portfolio construction. ESG-focused research is also used to identify areas for issuer engagement. • In 2022, we embarked on a project to improve how we assess sovereign bond issuers' exposure to, and management of, ESG risk factors. To that end, we reviewed existing market practice, guidance, and available data, involving a close collaboration between our Asian Fixed Income and Global Sustainable Investment department. We have now developed a proprietary ESG sovereign rating model using public data from sources such as the World Bank, the United Nations, and EDGAR (the European Commission Emissions Database for Global Atmospheric Research). • We have selected 20 indicators that broadly cover all three areas of E, S, and G. These include: greenhouse gas emissions (per capita and proportional to GDP), an index of human development and a measure of government effectiveness. Implemented in 2022, the new model has since been deployed as an ESG element in our sovereign credit model and has already added substantially to the quality of our investment analysis.
New Zealand Fixed Income	• The team seeks to understand how industry and company ESG factors may affect investments and, ultimately, client portfolios. • ESG factors are incorporated into the due diligence process to provide an overall picture of the risks and opportunities faced by issuers. • The team engages with portfolio companies with low ESG scores in an effort to seek improvements that would be beneficial to stakeholders.
Multi Asset	• ESG integration is conducted from both a top-down and bottom-up perspective: – The bottom-up approach relies on our teams of ESG Specialists and research analysts, whose processes form part of the fundamental research process. – The top-down approach entails the use of norms-based screening methods to identify companies that breach ESG safeguards such as the United Nations Global Compact (UNGC) Principles, or OECD Guidelines. • For existing holdings, where a company is involved in controversy, or is identified to have breached a social safeguard, further due diligence is conducted before concluding if the position should be sold from the portfolio.
Money Market	• ESG and stewardship considerations are considered as part of the issuer selection process to the extent that they are deemed material to the investment case and in line with our clients' risk appetites.

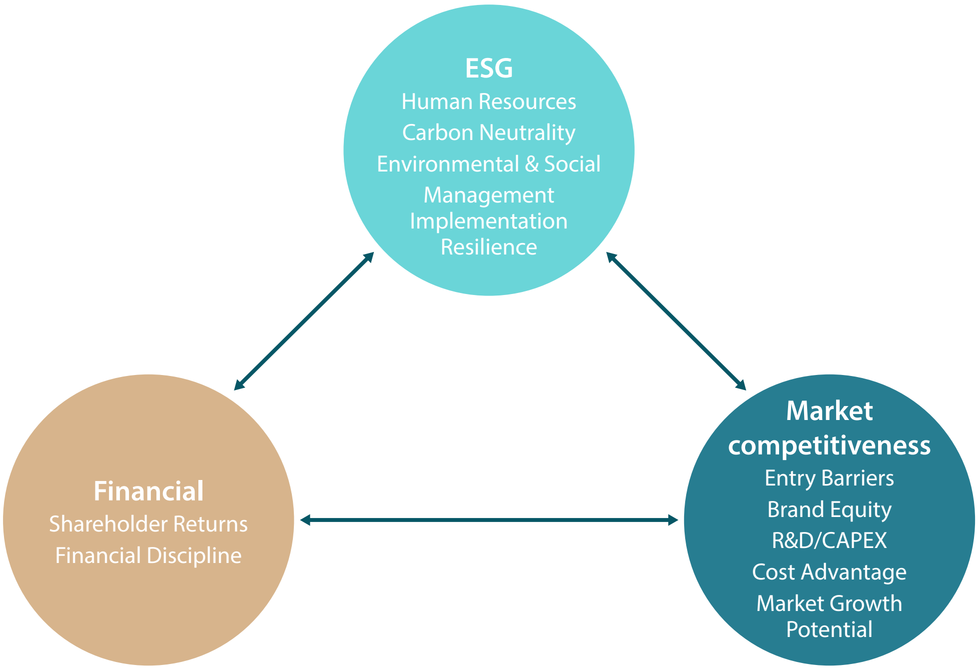
Some examples of how we integrate ESG in our portfolios is shown in the case studies that follow:

Case study: ESG factors drive decision to sell major Japanese measuring instrument maker (equity)

This company is a major manufacturer of analytical and measuring instruments. It provides advanced analytical technology to industries that need to measure air, water and other environmental pollution. As the global market leader in automotive engine emissions measurement equipment, its instruments were used to expose Volkswagen's emissions fraud. However, the Japanese Equity team's concerns started to grow that the automotive measuring equipment business would lose money in 2022 as car manufacturers increasingly shift to electric vehicles. There was a clear risk that the automotive measuring equipment business would shrink as a result of growing transition risk, i.e. as economies move towards a low-carbon environment.

Issue: We have used our proprietary Creating Shared Value (CSV) evaluations based on the work of Harvard University Professor Michael Porter as part of our Japanese Equity investment process since 2013 to determine whether a stock is at a premium, neutral or at a discount relative to the sector. These evaluations incorporate 12 factors such as diversity, management ability to execute, contribution to the environment and society, and threats to business continuity together with an evaluation of financial strength and returns to shareholders grouped into three categories: competitiveness, ESG, and financial strength.

Our sector analysts cut our proprietary Creating Shared Value score in September 2021 from 20 to 13 (out of a possible 24), largely on the back of the risks facing automotive instrumentation.



This followed a decision by MSCI to reduce its ESG rating from A to BBB in August 2020, mainly due to the company's controversial sourcing and labour management policies. We continued to monitor the company through 2022, although there were no further changes to the CSV score or MSCI ESG rating.

Outcome: It turned out that the semiconductor-related market was strong in 2022, with income from measuring equipment for semiconductors boosting profits and more than offsetting automotive measuring equipment, which remained in the red, as in the previous year. Despite the overall increase in profits, the share price valuation fell. Our analyst believed that there was little room for any upward re-rating due to the climate-related risks in the business and the automotive market. As a result of this evaluation and the fundamentals of the stock, our fund manager sold all the shares during 2022.

Framework for aligning Nikko AM Group funds to SFDR categories

There have been a significant number of regulatory developments in the European Union in relation to environmental, social and governance issues, notably the Sustainable Finance Disclosure Regulation (SFDR). This has coincided with rising investor demand for products that integrate material ESG factors from both a valuation and wider environmental/social impact perspective.

To address both of these points, in 2022 we put in place a global framework to allow products to be elevated to a higher SFDR categorisation. The framework consists of minimum ESG criteria that must be integrated into the investment process in order for a product to achieve a certain SFDR status. They include, for example, negative screens or exclusions, positive screens (screening for companies that have enhanced ESG characteristics) and portfolio-level targets, such as lower greenhouse gas emissions.

All candidates for a change in SFDR categorisation have to pass through an internal process, including their initial adaptation by the investment team and ESG specialists to include the requisite ESG characteristics, followed by internal approvals, to ensure that the minimum criteria have been met.

The framework got underway in late 2022 with two funds moving through the process. Further products are expected to pass through in 2023. This is a further example of how we look to integrate ESG across our portfolios.

Case study: Taking a stance against modern slavery in New Zealand

Issue: Unfortunately, slavery in New Zealand, and globally, is much more widespread than is generally acknowledged or understood. In the light of this, in April 2022, the New Zealand government launched a consultation on planned legislation addressing slavery and worker exploitation. As proposed, the legislation would create due diligence and disclosure obligations for a large number of companies operating in the country, with additional responsibilities for larger organizations. This will affect a big part of our portfolio and investible universe.

Activity: Our New Zealand office decided to get ahead of the issue by engaging an ex-detective who is now a consultant helping private and public companies map their exposure risk to modern slavery, as well as uncovering and addressing slavery and people trafficking in their supply chains. He has provided training and information to our analysts, equipping them to better interrogate company managements and boards about the issue and help them with ways to deal with it. Typically, this involves looking closely at contractors and sub-contractors.

Outcome: By working with companies, raising awareness and facing into the problem rather than ignoring it, we hope to see more change, both legislatively and practically, at companies and their supply chains, here and abroad. On the back of our training and information sessions, we have since regularly discussed the modern slavery environment in New Zealand with managements, especially those in riskier industries like agriculture and construction. These insights are generally well received. In one instance, as a direct response of our engagement, a listed healthcare provider has shared the information we provided to help inform their own teams of the scope of the modern slavery risk assessment process.

Outcome

Further demonstrations of the practical outcomes of our integration of stewardship – and particularly ESG considerations – into our investment activities is through some examples. We have therefore included additional case studies in this section.

Case study: Moving an energy-intensive company in the right direction (fixed income)

PT Indika Energy TBK[7] is an Indonesian-based company whose primary businesses are coal production, engineering, construction services and power generation.

Issue: Indika's substantial coal mining operations mean that the company is likely to face increased stranded asset risk as thermal coal demand declines and decarbonisation initiatives gather pace, both regionally and globally. The company is aware of the threat and has publicly announced its sustainability strategy, committing itself to reaching net-zero carbon by 2050, with an interim target in 2025. In achieving this aim, it plans to:

- increase non-coal revenue streams to at least 50%;
- reduce its greenhouse gas footprint;
- divest coal-related and high-carbon assets; and
- increase investments in non-coal and renewable energy and nature-based business solutions.

Engagement: We believed it was important to engage with the company to further understand its long-term transition strategy and encourage its execution, which would help to mitigate the risk from stranded assets. Our engagements were primarily through one-to-one meetings, group investor meetings and web calls.

Multiple contacts with the company's senior management and investor relations team were made through the course of 2022. These sought to both clarify with management the company's sustainable business strategy and track the progress of its implementation.

Outcome: Indika has been actively executing its business strategy during 2022. Alongside commitments to invest in renewable and nature-based businesses, the company also undertook several tangible initiatives to build its low-carbon business streams. These have included establishing:

- A joint venture with Foxconn, the Taiwanese electronic products group, to manufacture electric commercial vehicles.
- A business based on a forest area in East and Central Kalimantan amounting to more than 160,000 hectares for:
  - making wood pellets for use in biomass energy generation;
  - creating carbon offsets that are available for the group or for sale; and
  - manufacturing high-value agro-forestry products.
- A joint venture to develop a solar photovoltaic panels business; and
- A joint venture to build electric motorcycles, with an aspiration to become a leading brand and create the necessary charging and other infrastructure, which is currently minimal in Indonesia.

We estimate that over 50% of the company's investments and capex will be directed towards non-coal segments, with a strong focus on green businesses.

In addition, Indika has announced the disposal of certain coal-related assets, selling both its holding in PT Petrosea, a mining engineering business, and in PT Mitrabahtera Segara Sejati, a coal shipping company. ESG-related initiatives have also included expanding greenhouse gas reporting to cover the more extensive Scope 2 and Scope 3 emissions and developing a roadmap for the company's journey towards reaching net-zero carbon.

Our assessment is that Indika has been taking very concrete steps to move away from its coal business and view the company's ESG profile as improving. We will continue to engage with Indika and monitor its progress in delivering its strategy in accordance with its interim and long-term targets.

[7] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Case study: Improving ESG disclosures at a large Singaporean agribusiness (equity)

We aim to identify companies where ESG factors are improving, as there is then scope for an uplift in valuation once the improvements become evident to the market. An example is the history of our investment in Wilmar International, a Singapore-based agribusiness which is held within our Asia Ex-Japan Equity portfolios.

Wilmar International[8] is an integrated agribusiness encompassing the entire value chain of agricultural commodities. Its operations span cultivation, processing and distribution of agriproducts, ranging from food to industrial chemicals, such as oleochemicals and biodiesels.

Issue: As a leading palm oil plantation owner, refiner and distributor, the company operates in a highly controversial sector. It faces a number of material ESG issues, including carbon emissions, land conservation and labour practices. The diagram below illustrates the investment team's ESG Materiality Map for the company.

ESG Materiality Map									
Environmental Pillar (50%)				Social Pillar (30%)			Governance Pillar (20%)		
Climate Change	Nature Capital	Pollution & Waste Management	Environmental Opportunities	Human Capital	Product Liability	Social Opportunities	Corporate Governance	Corporate Behaviour	Governance Opportunities
Emissions & Energy Management	Water	Toxic Emissions & Waste	Clean Tech	Labour Management & Development	Product Safety & Quality	Access to Basic Services (Food, Healthcare, Finance, Power, Communications, Education)	Beneficial Ownership Assessment (Individual, SOE or Capital Market)		Ownership & Management Change
Product Emissions Footprint	Land	Packaging Material & Waste	Green Building	Equal Opportunities	Customer Welfare		Treatment of Minorities	Business Ethics	Minority interest Alignment
Financing Envionmental Impact	Biodiversity	Electronic Waste	Renewables	Health & Safety	Privacy & Data Security	Opportunities in Health & Wellbeing	Board	Anti-Competitive Practices	Principal-Agency Alignment
Climate Change Vulnerability	Resource Management			Supply Chain Management	Responsible Investment	Community Development	Pay	Corruption & Instability	
					Financial System Instability		Accounting Practices	Past Transactions	
								Transparency & Disclosure	

Primary Risks	Issues which can put a company out of business
Secondary Risks	Issues which can have a material impact on shareholder return
Opportunities	Issues which can lead to a material enhancement in shareholder returns

Engagement: We have been engaging with the company directly since 2018 and also previously as a member of the investor working group on sustainable palm oil set up by the UN-backed Principles for Responsible Investment (this collaboration has now concluded). In the intervening years, we have seen big improvements in the company's engagement with ESG. These have included addressing deforestation, winning certification from the Roundtable on Sustainable Palm Oil (a stakeholder industry group), ensuring traceability in its supply chain and aiding development in the communities from which its labour is sourced. We have also witnessed a substantial improvement in the company's attempts to improve food safety and nutrition practices, which we had previously highlighted as an area where there was an opportunity to improve sustainability.

Through 2022, we have continued to engage with Wilmar to better understand the company's ESG disclosures, while tracking developments in the three ESG areas and push it to improve the information it provides.

Further developments noted through 2022 were in three main areas:

1. **Environment:** The company agreed to provide more data about its emissions ahead of its goal to become carbon neutral by 2030. It has committed itself to providing more definitive ESG data and targets in its 2023 Sustainability Report. The company has also agreed to put more effort into reducing methane emissions and improving methane disclosures.
2. **Social:** The company continued to play an important role in ensuring food security during Covid lockdowns last year in China. In another context, it has invested in areas like education and housing for Indonesian farmers struggling with the difficulties they faced over Covid. More details will be announced in the forthcoming Sustainability Report.

   We encouraged Wilmar to be more public in highlighting its social contribution, given its big role as a supplier of consumer goods in China and the under-appreciation of Wilmar's contribution in recent years towards the betterment of the farming community.
3. **Governance:** The company continues to maintain a good standard of governance and respect for minority shareholders, while the annual accounts are more transparent.

We believe Wilmar has made progress with its ESG development during the year and has been receptive to our feedback in our engagements with the company.

[8] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 8

Signatories monitor and hold to account service providers.

Activity

A number of outside service providers help us in the stewardship of the assets we manage. These include MSCI, Bloomberg, ISS, Good Bankers and IR Japan for ESG information and analysis. We also have regular meetings with external ESG analysts to improve our understanding of how they engage with companies and to enhance the quality of the research we receive. The quality and depth of reports and insights are considered, as well as the effectiveness of the vendor in providing us with the necessary insights to fulfil our stewardship obligations on behalf of our clients.

Although there is value in the data provided by our third-party providers, we mostly treat it as supplemental to our own analyses, particularly for our active strategies, and believe any enhancement depends on how the information is incorporated into the investment process. A large portion of our AUM are in Japanese and Asia Ex-Japan equities, as well as fixed income assets where coverage by third-party providers is still evolving. We find that there are data gaps and delays while, at times, we disagree with the analyses or ratings even when they are available. We therefore do not rely exclusively on these services. Additionally, we conduct all engagement with investee companies ourselves and the decisions on how we vote proxies are ultimately made internally.

When engaging with any external service provider, we undertake an initial due diligence analysis, after which the provider is subject to ongoing monitoring and due diligence. Each department that owns the relationship with the applicable external service provider undertakes an annual review of the cost, effectiveness and usage of the services received. Vendors are also subject to anti-money-laundering and adverse media screening checks. Monitoring includes maintaining appropriate levels of regular contact and may include regular performance assessment. The areas covered in the initial due diligence are illustrated in the diagram below.

During 2022, we have expanded the template used for the due diligence questionnaire in the UK subsidiary, with additional questions on ESG and modern slavery. The level of scrutiny depends on the type of vendor and follows a risk-based approach.

How we monitor service providers

- Internal control system
- Information security system
- Management stability, industry standing, corporate culture, organisational structure
- Public accreditations, licences, certifications by private certification bodies
- Quality, technical capabilities, environmental friendliness and track record in consigned business or similar business and reputation thereof
- Outsourcing fees and payment conditions
- Emergency measures, Business Continuity Managment (BCM), Business Continuity Plans (BCP)

Principle 8

An example of a service provider we use extensively for our stewardship activities is ISS with whom we share our proxy voting policies and who we use to carry out proxy voting on our behalf. For the majority of resolutions, upon receipt of advisory research and voting recommendations from ISS, the portfolio manager or analyst responsible for the security in question looks at the report and conducts further research where any issues have been flagged.

ISS has benchmark policy guidelines which are regularly updated. It is part of our annual review process to combine the review of these guidelines with the annual review of our own proxy voting policy. We then liaise with ISS if its guidelines do not match our expectations. Our interaction with ISS and our voting process is further detailed in our response to Principle 12.

Case study: Voting against management and a service provider's recommendation (equity)

This relates to a packaged foods company held in one of our equity strategies.

Issue: In September 2022 a shareholder resolution was proposed at the annual meeting of shareholders to request that the company adopt a policy that the chairman be an independent director. In this instance ISS recommended a vote against this proposal for a number of reasons – the company had established governance guidelines and there were no concerns regarding board or committee independence, or the company's governance practices at that time. Also, the company had outperformed peers in its sector on both a short – and long-term basis under the current leadership structure and so there were no concerns regarding either the company's performance or the independent oversight of management on the part of the board.

Activity and outcome: We voted in favour of the shareholder proposal for an independent chairman and against ISS's recommendation on this occasion. Our basis for the decision was that we believed (in line with our proxy voting policy) that separating the roles of CEO and chairman is best industry practice and helps to ensure that company decisions are made in the best interests of shareholders. The resolution failed to pass with an approval rating of 41.75%. We will continue to vote in a similar vein in order to use our influence as shareholders to encourage best practice.

HOME

Monitoring our main ESG data vendor

Since the creation of our new, global, ESG data team in early 2022 (see Principle 7 for more on this), we have focused on improving both the availability and quality of ESG data being used by investment teams. Our primary focus has been to ensure that our data are accurate, timely and consistent across all investments covered by us. As we rely on a large data vendor for a significant portion of our data, we have engaged with it on a regular basis to improve the accuracy and usability of the data. Since April 2022, we have raised 31 issues with it to address underlying issues. The types of issues raised have fallen into two categories: 17 have related to general queries regarding overall data sets and 14 have been related to specific data quality issues.

In the general category, we raised issues regarding the consistency of data used in common calculations (such as weighted average carbon intensity). For instance, we noticed that the sales figures and carbon figures could be for different years for some securities, whilst for others they were the same. To address this, we had multiple discussions with our vendor to persuade it to provide consistent data which would allow proper comparability for both investments and potential investments. The process took over two months, but we were able to improve the quality of our analysis as a result.

On specific data, we have found that some of the numbers supplied can be incorrect. In one case we found that the gender pay gap ratio for a company was reported at a high level for a specific holding, whereas we believed the organisation did not disclose this piece of information. After some discussion, our data vendor agreed that it had incorrectly reported the figure and subsequently corrected the field.

Many of these discussions have resulted in inadequate responses. We have therefore escalated the issue with our vendor and agreed that from early 2023 we will be conducting a monthly call to ensure that the data we receive continue to improve and adequately support our investment decision-making and understanding of ESG issues. We have also taken additional steps that should improve the quality of our data:

- We have put in place an override option that allows us to by-pass any data points we feel are inaccurate. The evaluation process will sit with the ESG data team, which is independent of the investment teams, to ensure that we are using publicly-reported data that are timely and accurate.
- We are conducting a large-scale data vendor assessment process to improve our understanding of the data market. We have thus far engaged with 17 ESG data vendors to assess them on coverage, quality and organisational commitments to sustainable goals. This is an ongoing process, but we hope it will result in ensuring we have access to the best data available for integration into all of our ESG-related decisions.
- We are continuing to review and enhance our vendor due diligence oversight process, including in areas such as ESG and sustainability.

Outcome

The expectations of regulators and our clients grow all the time, for example, in complying with the requirements of the Sustainable Finance Disclosure Regulation or the Task Force on Climate-Related Financial Disclosures, as well as more detailed reporting of proxy voting. This in turn raises our expectations of the service providers we use to provide the data that ensures we can meet these requirements.

Although we have made significant progress during 2022 in our ability to collate and process ESG data, we are far from content with the depth and quality of some of the information we are processing. In some instances, we have found that the information published is dated or inaccurate; in others, coverage is so poor as to make reporting effectively meaningless and, in yet others, the methodologies and assumptions used to draw conclusions are not clearly defined.

In such instances where data fail to meet our minimum standards, we feed our concerns back to the relevant service provider as part of our day-to-day operations, although this does not always result in records being updated at source.

As mentioned in the Activity section, we are working hard to gain a better understanding of the data market in order to ensure that we are sourcing the most appropriate data to fulfil both our regulatory and our client obligations. In the meantime, we continue to use our knowledge of the companies in which we invest to correct erroneous data to ensure that our investment theses and reports are as up to date as possible.

HOME

Principle 9

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

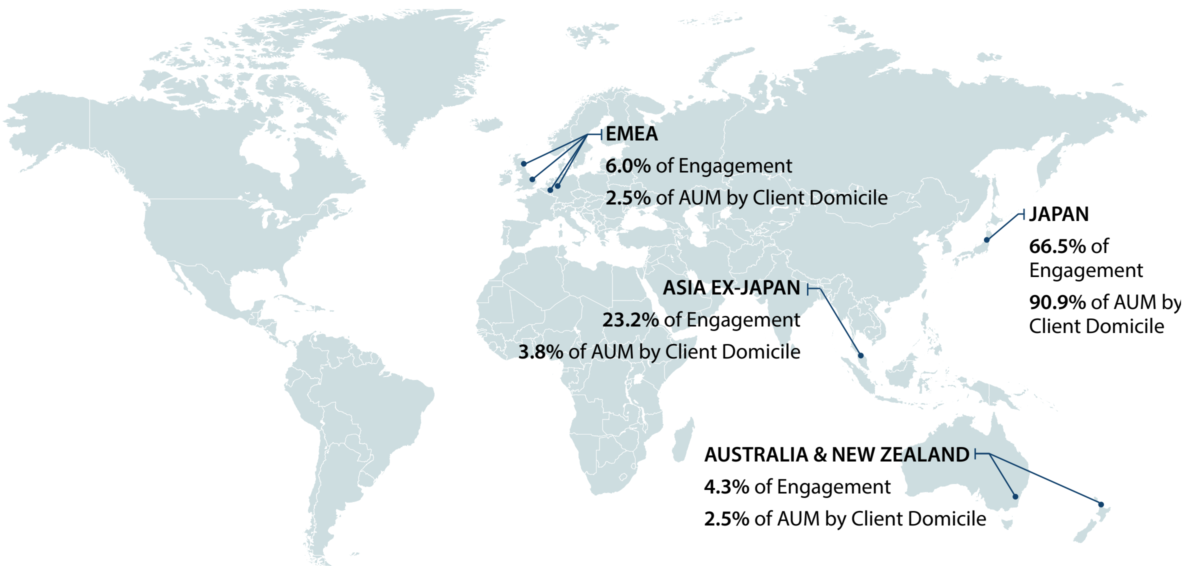
Activity

As a leading asset manager, we recognise that engagement and stewardship are part and parcel of our fiduciary duty. Active engagement with our companies is built into our investment processes and plays an integral role in fulfilling our commitments as a good steward of the capital that our clients have entrusted us with. Our strategy as outlined here should be read in conjunction with our Global Engagement Strategy, Commitment to Responsible Investing and the Group Proxy Voting Policy.

While the general approach outlined here applies to all discretionary accounts, it will be adapted to circumstances. For example, Japanese culture may approach engagement from a different perspective than Western societies, since public engagement to influence change is viewed as discordant and can have negative impacts on relationships built up over many years. Furthermore, as displayed in the pie charts under Principle 6, since a significant portion of our Japanese equity AUM is held in passive portfolios, this limits our influence since we do not have the same ability to divest these assets, however our Japan Sustainable Investment department is actively working to influence positive change at target companies on core ESG themes even where they are held only in passive portfolios. This is a multi-year project.

The map below gives the proportion of the firm's total ESG engagements[9] undertaken across our different regions. We compare this to the relevant proportion of total AUM in different client domiciles. The charts that follow provide a further breakdown of ESG engagement by theme and investment team respectively.

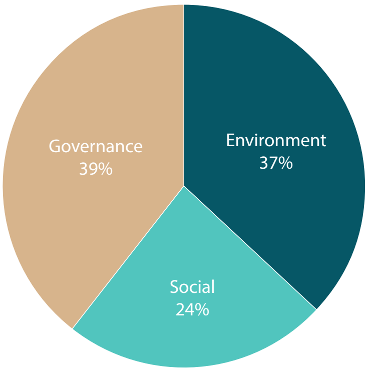
ESG engagement compared to AUM by client domicile



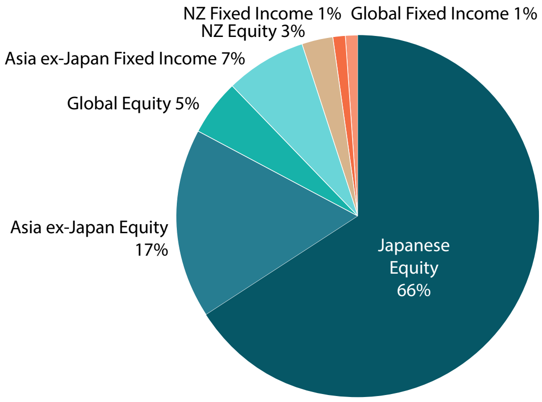
[9]The total number of engagements (as at 31 December 2022) is greater than those reflected here. For example, the Japan Sustainable Investment department in 2022, working with the Equity Fund Management department, met 1,116 firms a total of 3,404 times.

Principle 9

ESG engagement by theme



ESG engagement by investment team

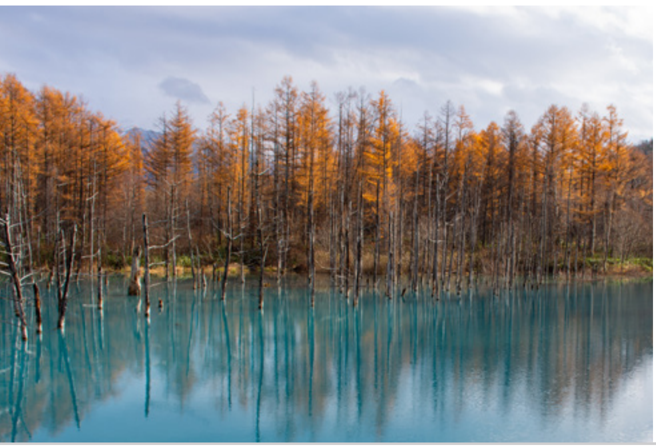


Engagement objectives

We engage with our investee companies on their strategy, operations and financial decisions, as well as their performance and management with respect to material environmental, social and governance issues. The purpose of our engagements is to help them attain and sustain high returns and create value, while becoming and remaining good corporate citizens. In carrying out our purpose, we seek to understand managements' stance and strategy on material issues, monitor their performance on these issues and set milestones, where appropriate, and shape corporate behaviour and influence positive change by encouraging policies such as enhanced ESG disclosure and performance in line with best ESG practice.

Our discussions with managements often seek the rationale for their decisions and policies and, where appropriate, commitments to address any issues raised. Three overarching principles guide our engagements:

- Materiality: our engagements are driven by material factors, including ESG factors;
- Intentionality: we establish clear objectives and expectations for our engagements;
- Effectiveness: we engage in a constructive, positive and pragmatic manner.



Engagement methods and execution

Our engagement methods vary, based on the needs of the situation. These methods include:

- one-to-one company dialogues, including on-site visits,
- management calls and roadshows,
- written communications,
- collaborative engagements.

In some parts of Asia, one-to-one engagements are often the most constructive and culturally appropriate way to build trust, on the basis that confidentiality can bring better results than open confrontation. Mindful of these important regional nuances and our commitment to constructive, positive and pragmatic engagements, we carefully select our engagement methods, whilst being committed to supporting collaborative engagements where appropriate. For more on collaboration, see Principle 10.

Regardless of the method of engagement, we always seek to have a dialogue with the key decision makers, including founders, chief executives, chief financial officers, and executive directors, where appropriate, as well as others whose duties include sustainability and investor relations. If these more consensual approaches fail to achieve our desired ends, or there are more serious failings by a company, we may escalate the matter. This could involve collaboration with other investors. These approaches are discussed in more detail under Principles 11 and 10 respectively.

As discussed under Principles 1, 2, 6 and 7, ESG is integrated into our investment process, with investment teams engaging with our companies on relevant ESG issues both before and during the period of investment. Our regional ESG specialists are also beginning to perform more thematic engagements (for example, in relation to our responsibilities under the Net Zero Asset Managers initiative and Climate Action 100+), however the analysts and portfolio managers in our investment teams are ultimately responsible for assessing the ESG risks and opportunities that inform portfolio buy and sell decisions and engaging with the companies they cover.

Principle 9

Several key issues decide how we prioritise companies for engagement, which can differ by region and asset class. The factors that may be considered for prioritisation are:

- the size of holding and/or our influence,
- a poor ESG score or the scope for improvement,
- the nature of the issue and/or the severity of the breach,
- materiality,
- a voting event,
- our ESG thematic priorities,
- the client's priorities,
- the company's openness to dialogue.

The results of our engagements supplement our investment analysis, risk management frameworks and, consequently, our investment decisions. Our principal objective, however, is to seek commitments from company managements that they will address any material concerns raised by investment and Global Sustainable Investment department as a result of our engagement.

Engagement by asset class

The type of engagement undertaken depends in part on the asset class in question, as well as its geographic location. Below we outline the approach adopted in the main asset classes we manage.

Japan Equity

Our Japanese equity investment teams have a deep understanding of local markets and the intricacies of Japanese corporate culture, which helps us develop relationships with the companies in which we invest. Sources of information extend beyond written forms, such as financial statements, sell-side research and local news flow, with managers placing an emphasis on direct contact with company management, including site visits. Our local presence in Tokyo, where we are one of the largest asset managers in Japan and where the market generally tends to be under-researched by non-domestic peers, helps facilitate dialogue with companies. Over the years, we have been able to establish strong local relationships, providing us with unique insights, investment opportunities that might have otherwise been overlooked and the ability to undertake unusually far-reaching stewardship.

Since August 2021, a key focus of the Japan Sustainable Investment department has been to work with portfolio managers and analysts in our research teams to engage with large and mid-sized firms specifically on ESG issues. The priorities when deciding which firms to engage with are based on several stewardship considerations, including, amongst other things, ESG (on which see more below), corporate earnings, asset efficiency and shareholder return. After each engagement, a report is created to track progress and is shared internally. Feedback is also provided to active investment portfolio managers. Some illustrations of how we engage with our Japanese portfolio companies can be found in our case studies below.

Principle 9

In March 2021, the Japan Sustainable Investment department established three ESG priorities (published on our website as Nikko AM's Key ESG Themes) for engagement with our Japanese equity investments, which we believe will contribute to better investment returns in the medium – to long-term. They are listed below with the background to each one:

Environment – Action for a decarbonised society: The shift toward a decarbonised society is creating growth opportunities for companies with environmentally-friendly technologies. At the same time, decarbonisation and other such changes put companies at risk of potential cost rises, while their brand power may be damaged if they fail to take sufficient action. This is making decarbonisation increasingly important as a driving force behind future corporate value. We use our engagement to urge firms to address these changes, for example by allocating business resources to related fields and preparing for the associated risks. Our analyses of companies' actions in this area are pivotal to our assessments of their corporate value.

Social – Human capital and productivity: The way companies use human capital is clearly important for their medium – to long-term earnings and corporate value, and it will become increasingly crucial as populations age further and birth rates continue to fall. Following the Covid-19 pandemic, reconsiderations of working styles and the need for flexible responses to similar environmental changes have also driven improvements in corporate sustainability. Deepening our engagement and analyses with companies, with a focus on personnel strategies and systems, as well as labour productivity, is another way in which we are helping to enhance corporate value.

Governance – Effective governance: Thanks in part to the Corporate Governance Code, Japanese companies have made great strides in developing their governance frameworks. We continue to urge companies to increase their corporate value even further through sustained development and enhancement of their governance frameworks. Our engagement covers the appropriateness of their long-term vision and management strategies, their ability to put these plans into practice, and the effectiveness of their oversight and advisory functions.

In 2022, the Japan Sustainable Investment department established an engagement platform for information sharing to enable the wider Equity Fund Management department to carry out engagement in a systematic and effective manner. The department identified over 100 companies that could enhance their value by resolving certain material issues. To ensure that action follows this analysis, we are setting up a milestone management system to monitor progress towards the resolution of these issues. The aim is to form a common purpose within the department, while encouraging and co-ordinating collaboration between fund managers and sector analysts.

Global Equity

When appropriate, our Global Equity team engages with investee companies to help us understand how their ESG opportunities and risks are being managed. These meetings can occur at any point in the investment process – from initial research, through to portfolio inclusion and beyond. These discussions provide us with an opportunity to develop our knowledge of each business and industry, and to take a view on the quality of management teams and their strategies, including on ESG issues. We also engage to promote better ESG practices if we believe there is room for standards to improve, for example by encouraging enhanced ESG disclosure and performance in line with best ESG practice. More on how we engage with our investee companies can be found in our case studies below.

Global Fixed Income

In our Global Fixed Income portfolios, most of our AUM are in sovereign or other AAA bonds and money market instruments. We also hold small shares of issuance by major banks and some leading corporates. We maintain an active dialogue with issuers and see this as a means of building our insight and market intelligence. We have had a number of engagements during 2022 with finance ministries and municipalities in relation to their green bond issuance programmes. For example, we spoke to a number of Canadian and New Zealand issuers about the growing importance of biodiversity to the wider market as well as our own clients. We also spoke of the growing importance of the "S" in ESG and the concept of a just transition to a zero-carbon society. We will continue this dialogue. .

We recognise our position as a "gateway investor" for Japanese investors in the Danish mortgage bond market. We therefore believe it is important to regularly engage with the Danish mortgage banks in respect of their lending practices, securitisation methods and issuer programmes. See Principle 6 for a case study on our engagements in this area during 2022.

Principle 9

With respect to corporate credit, our Global Fixed Income portfolio managers and research analysts engage with the companies in which we invest. These discussions cover the firms' corporate earnings and financial strategies, as well as other non-financial information, including their management policies, business strategies and material ESG matters, as part of an assessment of corporate value that ultimately informs our investment decisions.

Where we have identified company-specific or systemic risks, we may raise these concerns through meetings, site visits, conference calls or correspondence in order to gain assurance that risks are being managed. We prioritise engagements based on our holding, the bond issue in question and our exposure. The level of engagement depends on the asset class and the geographic region. Given our relatively small exposure to corporate bonds and emerging markets, we are realistic about the practical limits to our influence and we avoid situations where we might end up in corporate actions which would tie-up disproportionate resources and time. We illustrate how we engage with bond issuers in our case studies below.

Outcome

The best way to describe our engagements in the past 12 months and their outcomes is by a series of examples and case studies.

Case study: Decarbonising executive compensation at a Japanese oil group (equity)

This company is a major Japanese oil wholesaler held in our Japanese equity portfolios.

Issue: Given the carbon intensity of its business, the company urgently needed a strategy to address climate change.

Engagement: In April 2022, we met one of the company's executives and exchanged views on the company's efforts to decarbonise its businesses. Our focus was executive compensation, where we pointed out that financial incentives should include an assessment of progress in meeting the needs of a decarbonised society, which the company had highlighted was a priority management issue. Currently, executive compensation is performance-linked, mainly based on achieving operating income and net income targets in a single year. These are, in turn, mainly dependent on previous investment in fossil fuels and on current commodity prices.

The director responded that the executive compensation system was a key area for review in a new medium-term management plan to be announced in the autumn. He added that our views were helpful as the company debated how to improve its approach to executive compensation.

Outcome: In November, the company announced its new medium-term management plan, which included a new target of cutting revenue from the fossil fuel business to below 50% by 2030. It also announced that its greenhouse gas reduction target would be linked to executive compensation.

Case study: Improving independent oversight at an insurance company (equity)

This is a major Japanese insurance company held in our Japanese Equity portfolios.

Issue: We opened a conversation with the company after a change in our policies on outside directors and auditors to improve independent company oversight. These changes were part of a revision of our criteria for exercising voting rights made in February 2022 to include new guidelines on the maximum tenure of outside directors and auditors. This stated that we no longer considered outside directors to be independent once they have been in office for more than 12 years and that we would then vote against their re-election.

Activity: We started discussions with the company in January 2022, informing it of the forthcoming changes to our criteria and the rationale. We asked that it publish its policy on the maximum tenure of both outside directors and outside auditors. The company promised to consider our representations.

Outcome: The company has since revised its basic governance policy. It has established a new policy that, in principle, the maximum tenure of outside directors should be 10 years and the maximum tenure of outside auditors should be 3 terms or 12 years. This change satisfies our new criteria for exercising voting rights in favour of boards.

Case study: Successfully pushing a chemical company to be greener and more diverse (equity)

This is a Japanese chemical company we hold in our Japanese Equity portfolios.

Issue: A major restructuring offered us the opportunity to revisit the company's strategy on growth, decarbonisation and board diversity.

Engagement: The company announced in 2021 that it was planning to deconsolidate its cement business through a joint venture with another company. The reorganisation prompted us to seek information on how the company's growth strategy would change as a result, and on any new decarbonisation strategy and targets at the cement business.

We met the president of the company and requested the disclosure of the cement business decarbonisation strategy, decarbonisation targets and the company's new business strategy in the wake of the establishment of the cement business joint venture. In addition, we raised the issue of the absence of female directors and made clear our expectation that this would be rectified.

Outcome: In 2022, the company announced a new 2030 target to reduce greenhouse gas emissions to less than 50% of their 2013 level. It also said that it planned to move to a business structure centred on specialty chemicals, which have a lower energy burden and are less susceptible to market conditions than the existing businesses. On the question of diversity, a woman was successfully elected to fill a place for an outside director at the company's 2022 annual general meeting of shareholders.

We appreciate the progress the company is making and believe pressure from our engagement helped push it in the right direction. Nonetheless, we will continue to engage the company on all ESG fronts to ensure that forward momentum is maintained.

Case study: Controversial sourcing policies at an IT company (equity)

Hexagon[10] is a global provider of design, measurement and visualisation technologies held in our Global Equity portfolios.

Issue: MSCI had given it a low ESG score compared to rival companies on account of its sourcing policies and the lack of traceability of its raw materials.

Engagement: We discussed the issue in early 2021 with the Head of Investor Relations and Sustainability. Since then, the company has published its first annual sustainability report. This states that appropriate sourcing policies are now in place, with close to 50% of suppliers being covered by a new audit scheme introduced in 2020. Its Conflict Minerals Policy commits it to identifying products that may include minerals from countries where there is fighting – so-called "conflict minerals" – and extends its policy to suppliers, where possible. It is also enjoined to take reasonable efforts to avoid the use of raw materials that directly or indirectly finance armed groups which violate human rights. Amongst other things, Hexagon is also implementing a sustainability programme, a supplier qualification process and encouraging suppliers to adopt guidance from the OECD on responsible supply chains.

Following the company's response to our engagement, we left our investment recommendation unchanged, with no change to our Future Quality thesis. We said, however, that we would continue to engage with management on procurement as part of our regular interaction with portfolio companies. We particularly wanted to focus on the degree of progress by the company in auditing suppliers.

Outcome: Hexagon has since shown steady improvement. In August 2021, MSCI upgraded its "controversial sourcing" score for the company to close to the industry average. MSCI also gave it a top score on its commitment to avoiding controversial materials. In May 2022, we followed up on our initial engagement with a number of questions to gauge progress. We were pleased to see that, despite Covid restrictions, Hexagon had carried out 24% of planned supplier audits and was on track to meet its target of 100% of direct suppliers audited by the end of 2023. Based on the numbers to date, Hexagon has seen the level of non-compliance per supplier remain stable, while controversial sourcing has ceased to be a key issue in a more recent report from MSCI.

[10] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 9

Case study: Following-up on our efforts to improve environmental commitments at a US building products group (equity)

Carlisle Companies[11] is a US building products group held in our Global Equity portfolios.

Issue: Carlisle has been divesting non-core segments of its business and allocating capital to higher-return products that aim to help meet customers' environmental and energy requirements. As part of this strategy, it sold its Carlisle Brake & Friction brakes division and bought Henry, a rival building products company.

We believe this new direction for the group should benefit all stakeholders and lead to strong share price appreciation in time. It also makes sense from an ESG perspective, as buildings account for about 28% of greenhouse gas emissions globally and Carlisle's products help reduce heat and energy loss. Management has started to improve its ESG and sustainability communications, notably in its recently-published sustainability report.

Engagement: We engaged with management towards the end of 2021 and highlighted a number of ESG improvements the company could make. Given its strengths in staff relations and climate-related products, we believed these steps would improve the perception of the company. Specifically, our recommendations were:

- sign up to the UN Global Compact;
- disclose the gender pay gap as it already does for the gender make-up of the board;
- sign up to the Science Based Targets initiative, a collaboration between CDP (formerly the Carbon Disclosure Project), the United Nations Global Compact, the World Resources Institute and the World Wide Fund for Nature, once it can measure its Scope 3 emissions (those from suppliers and the like).

We followed up this engagement in June 2022 when we met the Head of Investor Relations and the Vice President of Sustainability. It was evident that Carlisle had progressed on its ESG journey – the company had committed itself to adopting Science Based Targets, with a 2030 goal of reducing Scope 1 and 2 emissions (those produced directly and indirectly by the company) by 70% and an ambition to set further targets for 2050, including those that fall under Scope 3.

We reiterated our previous recommendations and discussed disclosure requirements from European investors in relation to the EU's Sustainable Finance Disclosure Regulation. The Vice President of Sustainability responded that our requests would be explored further.

Outcome: Despite the progress, it remains clear that further developments are needed for the company to reach net zero. Carlisle is partnering with universities and technology leaders to develop what will be required. Creating bio-based products, likely involving carbon sequestration, is a possibility, while it is also discussing how its products could be recycled or reused once they are no longer needed, so-called "end-of-life circularity".

We remain long-term investors and will continue to put pressure on the company to adopt best practice during 2023 and beyond. However, bearing in mind our position as relatively small shareholders, we are cognisant of the limitations of our influence.

[11] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Case study: Keeping the heat on an Indian steel maker to be more green (fixed income)

In our Asia Fixed Income portfolios, we hold bonds issued by JSW Steel, an Indian-based integrated steel manufacturing company that ranks among the largest steel producers in the country.

Issue: The company's production processes involve high energy consumption and large emissions of greenhouse gases and waste products. We wanted to understand the company's decarbonisation strategy and track its execution and progress.

Engagement: We have engaged with the company several times during the year, both via ad hoc calls or through more formal meetings. During these discussions, the company has identified 17 priority ESG areas to be addressed and has set some specific sustainability targets, including:

- to reduce Scope 1 (direct) and Scope 2 (indirect) CO_2 emissions by 42% from 2005 levels by 2030;
- to reduce energy consumption by 19% from 2005 levels by 2030;
- to achieve carbon neutrality at JSW Steel Coated Products by 2030.

Outcome: The company is clearly trying to make progress, although there is still a way to go yet. For instance, greenhouse gas emissions and energy consumption showed a small uptick in 2022 after new plant was commissioned at its Dolvi works on India's west coast. However, both have been brought down again this year through a combination of measures, including an increase in green energy consumption.

This is evidence of the seriousness of the company's commitment to systematically increase the share of renewable power used in production. It has entered into solar and wind power purchase agreements through its JSW Energy offshoot. The plan is to ultimately develop renewable power capacity of 958 MW, of which 225 MW of solar power was commissioned in April 2022. The balance will come on stream in phases. The company has not yet specified a target for renewable power, but India as a country is set to meet 50% of its energy needs from renewable sources by 2030.

JSW Steel has also committed itself to using more steel scrap as it shifts from carbon-intensive blast furnaces to potentially "greener" electric arc furnaces (EAF), and to use more low – and medium-grade iron ore. As part of its steel scrap commitment, the company has entered into a 50-50 joint venture with National Steel Holdings, a New Zealand metal recycling group, to set up scrap shredding plants using industry-leading machinery. Its plans should be boosted by the Indian government's vehicle scrappage policy, which aims to phase out polluting vehicles over time. This should help the development of an "ecosystem" of steel scrap collection and recycling, for which JSW's environment-friendly EAF-based steel production should be well placed.

On the debit side, while the company discloses data on Scope 3 emissions (from suppliers and the like), it has no specific targets for reductions, nor has it established a firm-wide net-zero target and roadmap. And while the company's MSCI ESG Rating was upgraded from CCC to B in December 2021, it admits that it remains on the low end of the rating band. It has been making efforts to improve the score, including appointing an independent auditor and increasing the number of female board members. We will continue in our engagements to press the case for further action on ESG priorities.

Case study: Probing the green commitment of one of Asia's biggest banks (fixed income)

DBS Bank[12] is Singapore's leading multinational banking and financial services corporation and one of the largest banks in Asia. We hold its bonds in our Asia Fixed Income portfolios.

Issue: As a leading Asian financial services provider, the bank services a wide clientele. As a result, any commitment to ESG will have an extensive influence on society in Asia. We also expect it to provide an example to other banks.

Engagement: We have been directly engaging with the bank over the years, both on an individual basis and as part of a group of investors. In 2022, DBS released its targets for sector-specific decarbonisation to achieve overall net zero by 2050. Targeted sectors include power, oil and gas, automotive, aviation, shipping, steel, and real estate. We have highlighted our concerns about the bank's ability to reach its targets and sought a deeper understanding of the rationale and thinking behind them so that we could have a better appreciation of its commitment.

Outcome: During a meeting in 2022, DBS addressed our concerns. It said its favoured approach was to stand alongside clients in their shift to net zero rather than simply avoiding clients where there were ESG concerns. In such cases, it argued, there would always be someone else ready to fill the gap and so there was unlikely to be any positive change. This gave us confidence that DBS has a long-term commitment to sustainability and that we can expect further steps to be taken.

[12] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 10

Signatories, where necessary, participate in collaborative engagement to influence issuers.

HOME

Activity

We believe that in some instances where one-to-one company engagements deliver insufficient progress, collaborative initiatives with like-minded investors can increase shareholders' influence on companies' corporate behaviour and ESG performance. Whilst we are seeing increasing investor collaboration efforts across many regions, this engagement method is still in relatively uncharted territory in some parts of the world. For example, in parts of Asia, one-to-one engagements can be viewed as more constructive and culturally appropriate to build trust. In Japan (which accounts for the majority of our equity assets under management) we are mindful about how we are involved in collaborative engagements due to local regulations concerning joint and large shareholdings, whereby severe sanctions may be imposed if reporting requirements have not been met. We therefore participate in such engagements only after taking into careful consideration any potential ramifications.

Our involvement in collaborative engagements, often working with other stakeholders such as industry partners and academics, allows us to deepen our understanding of particular ESG topics, issuers' ESG performance and industry best practice. To date, most of our engagements have been restricted to a single asset class as there has been limited cross-over of equity and fixed income holdings and our engagements are typically conducted by asset-specific portfolio managers and analysts. However, in some regions we are exploring ways in which we could engage in a way that covers both equity and fixed income holdings if the need arose, for instance, where we have holdings of different asset classes in the same company.

Our regional investment offices select the most suitable and effective methods for their collaborative engagement. Generally speaking however, we use the following criteria to determine whether to join common cause with other shareholders:

- whether the initiative is consistent with the particular issues we want raised and our responsible investment policy;
- whether the initiative is likely to be successful, taking account of, for instance, past results and other participants in the initiative;
- whether the cost, time and effort involved is commensurate with the anticipated effect; and
- whether the organisation sponsoring the initiative is one with which we want to be associated.

Outcome

In 2022, we participated in multiple collaborative engagements (across initiatives such as CA100+and AIGCC), as shown in the example case studies below. However, despite our best intentions, it has not always been possible for us to join collaborative engagements. For example, during 2022 we made enquiries about participating in collaborative engagements for two companies held within our Global Equity strategy. We were advised by the regional co-ordinators of the initiative in question that they either already had sufficient participation in engagements or were only accepting applications from "large shareholders". Our requests for each of the two companies therefore did not meet qualifying criteria for participation and so our team proceeded to contact them independently to ascertain information on their climate ambitions.

Case study: Sparking awareness of ESG at Indonesia's biggest power company (fixed income)

In 2022, Nikko AM Group joined the Asian Utilities Engagement Programme (AUEP) of the Asia Investment Group on Climate Change (AIGCC), an industry body trying to raise awareness among investors about global warming. An example of our collaboration with the AIGCC under this engagement programme concerned Perusahaan Listrik Negara[13] (PLN), the only vertically-integrated electricity utility in Indonesia, whose bonds we own in our Asia Fixed Income portfolios. The state-owned company is the dominant power generation, transmission and distribution provider in the country, accounting for more than 70% of electricity power production. PLN is also the sole buyer for Indonesia's independent power producers.

Issue: With a total installed capacity of around 45.9GW, close to 90% of PLN's production is powered by thermal sources, exposing PLN to high risk in the transition to zero carbon. Not surprisingly, the company scores poorly among APAC utilities for both absolute and relative carbon emissions. In addition, PLN's governance continues to lag global peers. The Indonesian government appoints half the directors of the board, severely limiting its independence.

In the light of these environmental and governance issues, the AUEP is aiming to engage with the board and senior management to secure several commitments:

1. To strengthen the governance framework to ensure the board's accountability and oversight for climate change risks and opportunities. Specifically, to clarify the role and responsibility of the Sustainability Committee in the implementation of PLN's decarbonisation strategies.
2. To draft action plans to reduce greenhouse gas emissions in line with the Paris Agreement of the UN's 2015 Climate Change Conference. This covers decarbonisation strategies, requiring a timetable to phase out coal-based emissions in less-developed economies at the latest by 2040, with similar commitments for natural gas.
3. To provide enhanced corporate disclosure in line with the final recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD).
4. To outline the physical risks the company faces from climate change and what strategies it is adopting to mitigate these risks.
5. To engage with public policy makers and other stakeholders to support cost-effective policy measures to mitigate climate-related risks and facilitate low carbon investments in line with achieving net zero emissions by 2050 or sooner.

Activity: In September 2022, we participated in our first collaborative engagement call together with other members of the AIGCC who are engaging PLN as part of the AUEP. The call was held with PLN's climate change team. The team presented five possible routes that the company's decarbonisation pathways might follow. Based on the accelerated scenario, it outlined in more detail the company's roadmap to net zero by 2060, which would see its emissions peak in 2030, in line with Indonesia's national target. As part of these plans, the company has committed itself to building no new coal-, oil-, or unabated gas-based power plants after 2030, making hydropower the dominant energy source in its renewables mix.

From PLN's perspective, four key issues need to be unlocked for the company to accelerate its net zero emissions target. These are:

- ensuring supportive electricity pricing;
- maintaining favourable finance channels;
- deploying new technologies, such as carbon capture, utilisation and storage, and hydrogen power, in large scale in Indonesia;
- increasing support from public policy, such as incentives for electric vehicle adoption.

Outcome: We will continue our collaborative engagements with PLN through the AIGCC and actively monitor its compliance with decarbonisation strategies over the short-, medium-, and long-term, notably the timetable to phase out coal-based emissions in line with 1.5°C temperature scenarios.

[13] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 10

Case study: Setting concrete targets at India's biggest cement company (equity)

Last year, we participated in a collaborative engagement group organised by CA100+, an investor-led initiative aimed at getting the world's largest greenhouse gas emitters to reduce emissions. The target was UltraTech Cement,[14] India's biggest cement company.

Issue: UltraTech operates in a hard-to-abate sector in a country whose electricity supplies are dominated by coal-fired power. As a result, its carbon intensity is one of the highest, both in Asia and amongst its peers. Over the years, there has been little material improvement in the company's carbon intensity and it had yet to announce a strategy to move towards a lower carbon future.

In 2021, the company's high emissions had caused us to sell the shares held in our Asia Ex-Japan Equity regional portfolios, where emission intensity benchmarks are relatively tight. However, we continued to hold them in our Indian equity portfolios, where benchmark emission intensities are relatively high and where UltraTech is part of the index. Having already engaged the company directly ourselves with little noticeable effect, we believed the company represented an important target for a collaborative effort by CA100+.

Engagement: In our previous direct engagements with UltraTech, our focus had been on getting the company to improve its current carbon emissions. The focus of our collaborative engagement was more on strategy and, specifically, that set by the Disclosure Framework Indicators established by CA100+. As a result, our priority targets for UltraTech in 2022 and 2023 are:

- to reduce greenhouse gas emissions in the years to 2025 on a clearly-defined path (Indicator 4);
- to lay out a decarbonisation strategy that explains how it intends to meet its medium – and long-term greenhouse gas reduction targets (Indicator 5);
- to make a commitment to aligning its capital expenditure plans with its long-term greenhouse gas reduction target, or to phase out planned expenditure in unabated carbon-intensive assets or products (Indicator 6);
- to introduce an executive remuneration scheme that includes climate change performance elements (Indicator 8.2);
- to acknowledge that it has responsibility for helping achieve a just transition to a net zero economy (Indicator 9); and
- to make a commitment to implementing the recommendations of the TCFD (Indicator 10).

Outcome: We were encouraged by the latest CA100+ investor group meeting, noting that UltraTech had been receptive to what participants had to say and had since incorporated some recommendations in its latest sustainability report, including:

- adopting TCFD disclosures and conducting physical and transition risk analyses;
- having its carbon targets verified by the UN-backed Science Based Targets initiative, with the aim of reducing greenhouse gas emissions by 27% by 2022 – in line with the global target of cutting climate warming to 2°C; and
- committing itself to net zero carbon by 2050.

We will continue to engage UltraTech, both directly and collaboratively, and monitor the company's progress in delivering its transition strategy in accordance with its interim and long-term targets.

[14] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 11

Signatories, where necessary, escalate stewardship activities to influence issuers.

Activity

Where we engage with companies to shape corporate behaviour and influence positive change, we may escalate the discussions. The escalation methods vary, but broadly comprise:

- additional meetings and engagement, including meetings with more senior management, where appropriate;
- collaborative engagements, where like-minded shareholders jointly seek change from a company;
- voting at general meetings and/or supporting shareholder resolutions (in our equity holdings);
- reducing or divesting our holdings.

Our investment teams have the discretion to escalate in the most appropriate way, given the nature of the issue. Some might want to follow up, others divest.

When an incident raises concerns about the ESG performance of a portfolio company, we may take a dual approach. On the one hand, we put the company through our evaluation frameworks to determine whether we should continue to hold it in the portfolio. On the other, we may engage with company management to urge change. (See our case studies for examples of this engagement.) In some cases, we may join with other investors to escalate the issue. A good example is Climate Action 100+ (CA100+), a collective engagement group referred to under Principle 10.

Escalation timelines may differ, depending on the region and the issue in question. While many engagements touch on topics that are inherently long term and require time for improvement, some issues need to be reviewed quickly. These considerations are taken into account when we select the method of escalation.

Our engagement, escalation and voting decisions are fed back into our investment analysis, providing more information on which to base our investment decisions. Depending on the severity of the issue and the broader context (for example, the outcome of previous engagements), we may reduce our holdings or divest where we have the discretion and where such an outcome would be in the best interests of our clients.

With our Japanese Equity holdings, the initial assessment will be made by our analysts in the Japan Sustainable Investment department, who are responsible for proxy voting and engagement. An analyst will work with the relevant portfolio manager and sector analyst to engage with the company according to priorities based on the gravity of the issue, the company's response and the weight of the holding in the portfolio. They will open a dialogue with management with the initial aim of trying to avoid any loss of shareholder value.

If no improvement is observable and it is determined that there is a high likelihood of long-term damage to the company, the analyst may remove the stock from the investment universe. Any such evaluation will be made independently of any investment decision by the portfolio manager. In addition, when governance issues are revealed by this evaluation process, we will in principle seek to express our opinion through our proxy voting activity.

Our investment teams have the discretion to escalate in the most appropriate way, given the nature of the issue. Some might want to follow up, others divest

Principle 11

Outcome

As we have suggested under earlier principles, our general policy in our Asian businesses is to rely, where possible, on one-to-one engagements. Particularly in Japan, escalation involving a group of investors is rare, given the complications associated with large and joint shareholdings and the cultural aversion to public challenge or conflict. Having said that, we are not afraid to be robust with companies where we think there are failings, both in financial performance and stewardship. And we will escalate where we think that we can improve the outcome for our investors. The case studies that follow give a flavour of how we escalate issues when they occur. Other examples can be found throughout this document.

Case study: Mettle lacking in the governance of a substantial Japanese steel group (equity)

The company is a big Japanese steelmaker owned by our Japanese Equity portfolios.

Issue: We had concerns about the independence of the company's oversight and its capital policy. The entire board consisted of directors from the parent company. Meanwhile, approximately ¥70 billion in cash, equivalent to 35% of total assets, was deposited with or lent to the parent. This cash was not used for business activities and continues to be a drag on return on equity.

Action: We raised questions over the independence of the board and the inefficiency of the capital structure, asking what plans there were for the future use of the cash. The company's response was that the board composition helped maintain management stability, while it was retaining flexible reserves in cash to support sustainable growth. We replied that we considered that there was room for improvement and requested that it take action on both issues.

Outcome: The company has continued to show no commitment to raising the number of genuinely independent directors on its board, nor has it outlined plans to improve its balance sheet and make more effective use of the cash, such as earmarking strategic investments. As our minimum requirements had not been fulfilled and we did not expect any improvement in the short term, we sold the shares.

Case study: Tackling quality issues at an electronics company (equity)

The company is one of the world's leading manufacturers and sellers of electrical and electronic products and systems.

Issue: Immediately after the annual general meeting in June 2021, the company announced an investigation into its quality control practices. Given that there had been no mention of this material information at the immediately preceding meeting, the timing of the announcement suggested a weak governance system.

Engagement: We held a meeting with directors in July. We pointed out that this was just the latest of several similar incidents. Each time, a recurrence prevention plan had been drawn up and an internal control system put in place, but measures to address the root causes, such as changing employee awareness and corporate culture, were neglected. Management recognition of the seriousness of the problem needed to be improved, while appropriate action was not being taken to communicate and disclose information. We requested that the company take prompt action to rectify these failings to prevent a recurrence of the quality control problems.

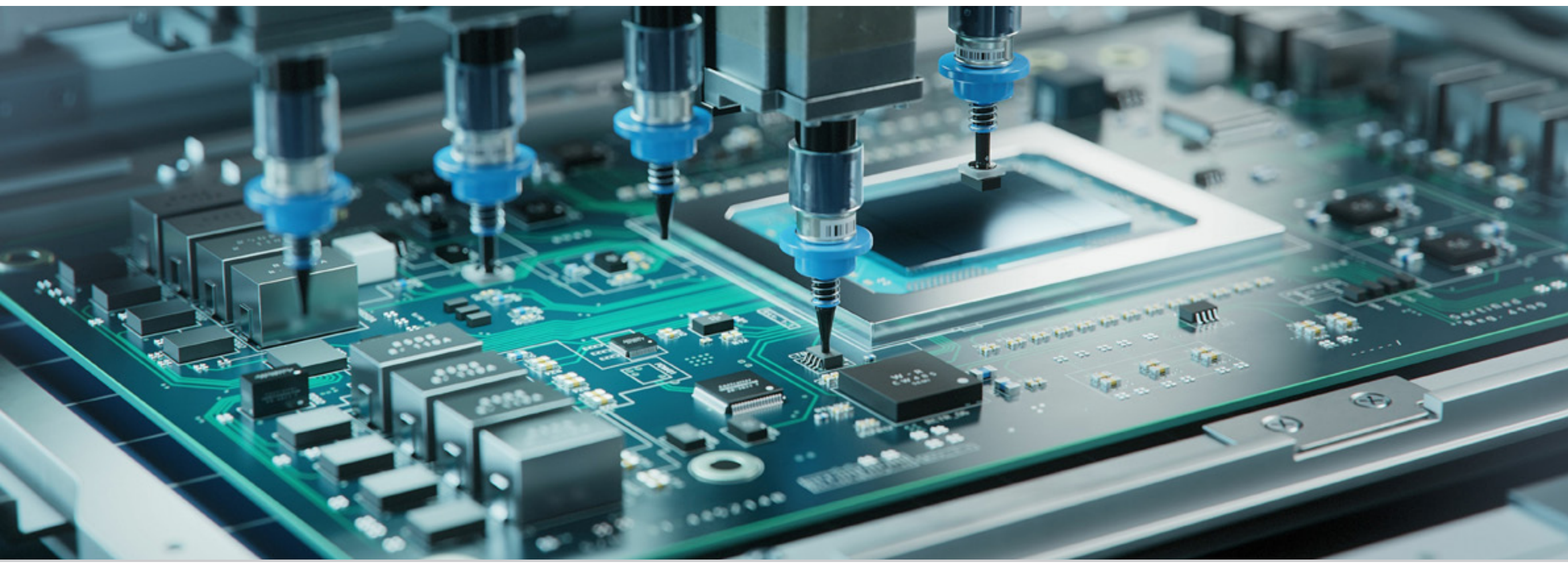
The company's interim report published in December 2021 found both quality and inspection problems in some cases. However, it took around a month for the report to be published, delaying remedial action and suggesting a lack of crisis awareness.

We interviewed management again in February 2022. We learned that reforms to quality, organisational and governance processes had been put in place. Concrete measures included the appointment of an officer from outside the company to take charge of the Quality Reform Promotion Division, the use of external reviews and the adoption of a management approach focused on quality inspection processes. It remains to be seen whether these actions will be sufficient to prevent further incidents. We asked to be kept informed of progress.

Interviews were again conducted in May 2022 to discuss the third report of the internal investigation. Although progress had been made, there were still many items outstanding. We asked a number of questions relating to the organisational culture, including poor communication and lack of crisis awareness. At that stage, it was not possible to judge from the company's answers that the measures it had put in place to prevent recurrence were functioning effectively.

Outcome: At the AGM in June, based on our dialogue with the company and our dissatisfaction with the efforts it had made to date, we voted against management. This included voting against the re-election of the company president, a vote which actually passed with an approval rate of 58.46%. The final investigation report was published in October, with additional preventative measures being announced alongside the existing ones.

Since then, no serious incidents have occurred, and we judge that the company's efforts have been successful, confirming that the governance system is gradually improving. However, we will continue to monitor the company's corporate and organisational culture closely, as reforms such as these will take time to take root.



Case study: An independent oil and gas exploration and production company that failed to live up to our environmental expectations (equity)

This was an independent oil and gas exploration and production company owned by our Asia Ex-Japan Equity team.

Issue: Over the year, as part of enhancing our ESG-integrated investment approach, we have tightened our internal processes when it comes to the monitoring and risk management of our portfolios' greenhouse gas (GHG) emissions intensity. Given that this company operates as an independent oil & gas exploration and production company in ASEAN, which by nature of their carbon intensive operations, produces significant GHG emissions, this triggered our internal risk monitoring controls. Our investment process does not automatically exclude companies with high GHG emissions profile as long as they have a credible transition plan to move away from carbon intensive operations. As such, we conducted further due diligence to find out what, if any, plans the company had.

Engagement: When engaging the company in April 2022, it said it had a strategy to deal with climate-related risk, which included a framework plan to reach net zero by 2050. However, it conceded that it was not practically possible for it to significantly decarbonise in the next five years.

It was clear that the company could not meet three of the commitments we require of companies if they are to demonstrate they have a meaningful interim strategy over the next five years for managing the transition to zero carbon:

- reducing greenhouse gas emissions by half;
- spending at least a fifth of the annual capital expenditure budget on renewable energy;
- reducing oil production revenues to below 30%.

Outcome: From our prior discussion with the company, and further due diligence conducted, we concluded that the company did not satisfy our stricter requirements. Hence, we could not justify holding such a high emitter of greenhouse gases and therefore sold our position. However, we will continue monitoring the company's progress towards their climate-related goals, particularly their net zero by 2050 strategy and implementation of their decarbonisation pathway

Case study: Failures of governance and pedestrian environmental progress at a major Asian property group (fixed income)

This is a large logistics real estate fund manager with global operations. The company went private in 2018, but we own publicly-listed bonds through our Asia Fixed Income portfolios.

Issue: The company owns and develops logistics properties, such as warehouses, but has had minimal "green" building targets, while only a small portion of its portfolio could be regarded as sustainable. As a privately-owned company, it is subject to significantly fewer governance controls and restrictions on related-party transactions and dividends than if it had remained listed. It also faces only minimal reporting requirements and is not, for example, required to report significant transactions.

We saw an urgent need to increase the representation of green developments in the portfolio and to improve disclosures and transparency, especially with regard to significant and related-party transactions.

Engagement: We have engaged with the company on these issues several times over the last two years.

In May 2021, during a call with a group of green bond investors, we voiced our concerns about the proportion of green developments. We pointed out that, at around 13% by number and only 8% by value, it was low and we asked if targets had been set for improvement. The response was that it did not have a specific target. On the same call, we discussed a proposal by the company to limit dividends to shareholders to protect bondholders. We argued that any such limitation would be ineffective, given that the company's private status allowed it to pass cash around the group via inter-company loans.

We followed up these concerns during 2022 with two calls and six emails between May and August pushing for more disclosure, notably on the company's significant inter-company loans and related party transactions over the previous year.

Outcome: The company has only been willing to disclose minimal details, stating more would be published at a later date. We felt that this was not acceptable, given the size, opacity and impact of these transactions, and we sold out of the bonds shortly after. We will continue to monitor the company to see if it improves its disclosure policy and whether we want to invest again.

Principle 12

Signatories actively exercise their rights and responsibilities.

Context

Proxy voting is one of the major elements of our stewardship activity in our equity portfolios and we take great care to ensure that our voting serves the interests of both companies and clients. Where we invest through passive strategies, we strive to incorporate stewardship through the voting of proxies and the engagement process, where appropriate.

In our fixed income investments, we do not have the voting rights that are available to shareholders, however we aim to be active owners of assets by utilising other stewardship tools, such as issuer engagement. We hold a small allocation (approximately 0.5% of our group AUM) in infrastructure investments via sub-advised managers who are subject to an annual ESG evaluation.

We do not currently manage private equity or debt assets.

The Nikko AM Group Proxy Voting Policy establishes our company-wide approach to proxy voting decisions. This policy establishes the principles we use for determining the exercise of voting rights at the group level. Implementation of the group-wide policy is undertaken by our local businesses, with the freedom to interpret the rules to suit local conditions. This gives our regional investment teams the ability to tailor their approach to stewardship according to the attributes of the local market.

As a result, there are some variations in how stewardship activities, including voting, are implemented across the group. For example, our UK entity has a supplemental proxy voting policy that applies to our Global Equity strategy for addressing our environmental and social principles.

The full text of our group Guidelines on Exercising Voting Rights (as well as our supplementary Standards for Exercising Voting Rights on Japanese Stocks) is available here with a summary of the main points listed below.

The group-wide policy underscores our focus on ESG in proxy voting decisions and also covers the following non-exhaustive list of considerations:

- shareholder return,
- the separation of executive and supervisory functions,
- the size and composition of the company's board of directors,
- the auditors,
- executive compensation systems,
- new share issuance, and
- company control and takeover defences.

We are generally opposed to resolutions aimed at preventing change of control. On the other hand, takeover defences may be assessed positively if the acquisition risks are clear and existing shareholder value would not be damaged.

We regularly vote and when doing so take account of groupwide policies and advice from proxy voting advisers, where applicable, as well as other considerations like past engagements and local policy.

Our voting principles are applied after full consideration of a company's circumstances, with each corporate governance principle to which we hold our investees being considered. For the majority of resolutions, upon receipt of advisory research and voting recommendations, the team responsible for the security in question will analyse the report and conduct further research where any issues have been flagged.

We aim to cast our votes on the same resolution consistently across all vehicles that we manage, unless specifically directed not to do so by clients in respect of their own accounts. We consider requests from clients to override a house policy on a case-by-case basis. In a small number of instances, segregated account clients have their own policies, which we apply and may supplement with ours where appropriate. We also have segregated account clients who make and execute their own voting decisions. It is not possible for clients in pooled funds to direct our voting.

Proxy voting is one of the major elements of our stewardship activity in our equity portfolios and we take great care to ensure that our voting serves the interests of both companies and clients

Principle 12

For Japanese Equities (which account for over three quarters of our firmwide equity AUM as at December 2022), our Standards for Exercising Voting Rights on Japanese Stocks establish detailed decision criteria. The Japan Sustainable Investment department is responsible for directing all voting proposals for holdings in both actively-managed and passive portfolios. It decides whether to approve or disapprove after taking into account past engagements with investee companies. Advice from ISS based on our proxy voting guidelines is one of the inputs in the decision-making process, but this advice is used for reference only. The Investment Support and Planning (ISP) team is responsible for exercising voting rights for non-Japanese stocks, where the investments are held via Japan-domiciled feeder funds on behalf of Japanese investors. In some cases, when there are important resolutions, the ISP team takes account of the opinions of the overseas investment management subsidiaries who are closest to the market where the investee company is based. The overseas investment team may also engage with local companies whose securities are held in Tokyo in co-ordination with the ISP team. Execution is outsourced to ISS.

For equity strategies not managed in Japan, ISS may provide analysis of individual proposals and customised proxy voting recommendations based on our proxy voting guidelines, however, the local Nikko AM Group entity makes the ultimate decision on how to exercise these voting rights, which are then executed by ISS.

Voting decisions for all of our group entities are executed by ISS. We use ISS to monitor our share and voting rights via a web-based platform. This shows us the accounts for which ISS votes, sends us notification of upcoming meetings, establishes voting decisions, tracks the status of votes and generates reports on voting activities. A record of all votes cast is also stored by ISS, allowing us to look back at historic voting records to ensure all service standards are being met and all votes are being cast as directed.

Recalling lent stock

We sometimes lend stock in accordance with our internal controls on lending practices. In these instances, we may recall stock from the borrowers in order to vote in line with our proxy voting policies. These are cases where exercising voting rights is more desirable from the perspective of responsible stewardship than earning an income from share lending.

For example, in our Japanese Equity operations, if our voting guidelines signal a governance concern that would result in a vote against management or the re-election of directors, we would recall the stock in order to ensure that we are able to vote and therefore satisfy our stewardship responsibilities.

Activity

A summary of our firmwide voting records is listed in the tables that follow (this information is also provided in our annual Sustainability Report). During the year we analysed 7,274 shareholder meetings and voted on 75,242 resolutions.

We cast votes on all shares where there are no legal, client or technical constraints. Examples of where we may not be able to vote include those where power of attorney has not been granted by a client, or in markets where share blocking is applied. These include bearer shares in the Swiss market, some stocks in the Norwegian and German markets and Egyptian market stocks. Such instances accounted for less than 1% of all resolutions in 2022.

Breakdown of voting records by region, January to December 2022

Region	Number of shareholder meetings	Number of resolutions	Votes for management (number)	Vote for management (%)	Vote against management (number)	Vote against management (%)
APAC ex Japan	2,452	19,498	16,820	86.3%	2,678	13.7%
EMEA	1,124	17,024	15,573	91.5%	1,451	8.5%
Japan	2,399	24,904	21,275	85.4%	3,629	14.6%
Latin America	216	2,003	1,798	89.8%	205	10.2%
North America	1,083	11,813	10,657	90.2%	1,156	9.8%
TOTAL	**7,274**	**75,242**	**66,123**	**87.9%**	**9,119**	**12.1%**

Principle 12

Overall, across all regions, we voted against management in 12% of resolutions. The most common reason for voting against management was in relation to the election of directors. A lack of independence amongst non-executive directors often prompts us to oppose management's wishes in these votes. The case study below, "Pushing governance up the agenda at a major Japanese food company (equity)", and another under Principle 8, "Voting against management and a service provider's recommendation (equity)", illustrate the point. On the latter occasion, we disagreed with ISS's recommendation on a shareholder resolution calling for an independent chair separate from the CEO. On this occasion we did not require engagement with ISS as we understood the rationale for their advice, but we voted against their recommendation and in line with our own internal policy.

Detailed voting records, including reasons for voting against specific proposals, are published on our website for the vast majority of our equity assets, notably [Japanese Equities] and [Global Equities]. For those voting records not publicly disclosed (US, New Zealand and Asia Ex-Japan Equities), our policy is to release the information to clients on request and in line with local customs and regulations.

Fixed income

As previously stated, we are not able to exercise the same level of influence as holders of equities in our fixed income allocations since the instruments we hold do not confer proxy voting rights. Nonetheless, we aim to exercise our stewardship responsibilities through other means, such as by engaging with market participants and ensuring that our product offering is in line with the needs of our clients.

When participating in the primary bond issuance markets, our investment teams review prospectuses and transaction documents (for example offering circulars) for every transaction as part of the due diligence process. Where possible, the investment team engages with issuers and structuring advisers on the terms and conditions of issuances in which we are interested, including providing feedback and, where applicable, seeking amendments to terms and conditions in legal bond documentation. In our experience, issuers accessing the bond market for the first time tend to be more receptive to feedback on legal documentation and contracts. For private companies' bond issuances, we also ask for access to further details provided in trust deeds, such as, for example, financial disclosures. It should be noted, however, that in the Japanese bond market this approach is less easy to adopt for publicly-traded corporate bonds.

Outcome

Although we may not be a widely recognised name in global markets we recognise and appreciate our responsibilities as stewards of our clients' capital. The following are examples of resolutions that we voted on during 2022. We have provided below examples of resolutions that we voted on during 2022. We have not always been able to use our influence to generate the outcomes we would have desired, however we will continue to use the influence that we have to act in what we believe is the best interest of our clients and wider stakeholders and to encourage best practice in investee companies where possible.

As has been already described, our Fixed Income allocations do not confer voting rights and our small stature in most fixed income markets or investment in sovereign issuers can limit our influence, but as described in earlier case studies such as "The Danish mortgage bond market – an example of end-client and broker engagement", "Moving an energy-intensive company in the right direction" and "Keeping the heat on an Indian steel maker to be more green", we aim to use the influence we do have to promote the best outcomes for stakeholders.

Case study: Unease at Amazon[15] on a range of concerns from human rights to political lobbying (equity)

The online retailer was held in our Global Equity portfolios.

Issue: At the AGM in May 2022, a number of proposals were put forward by both management and shareholders. We discuss below the background to some of these votes and explain how we voted and why.

Activity: Executive pay – We voted against a management proposal to ratify the compensation of the new CEO and other so-called "named executive officers" (NEOs). This was driven by a large equity grant to the new CEO and also large time-vested awards that were granted to other NEOs. We believed that these lacked objective performance criteria, exacerbating a misalignment between pay and performance. The vote was passed with an approval rating of just under 56%.

Shareholders' resolutions – We voted for shareholders' resolutions on a number of human rights issues since we felt that investors would benefit from increased transparency and disclosure on how the company was managing these risks:

- The commissioning of a third party report assessing the company's human rights due diligence process. The vote failed, gaining just under 40% of votes in favour.
- Increased reporting on how the company was protecting the rights to freedom of association and collective bargaining following increasing public scrutiny, high staff turnover and injury rates in its domestic warehouse operations and allegations of anti-union activities and sourcing from forced labour. The vote failed, gaining an approval rating of just under 39%.
- The commissioning of a third party study and report on "Rekognition", the company's facial recognition technology, looking at the extent to which it may threaten privacy and civil rights, unfairly target people of colour, the extent to which such technologies may be marketed and sold to authoritarian or repressive foreign governments, and the financial or operational risks associated with these human rights issues. This vote also failed, garnering favourable votes from just over 40% of those cast.

We also supported shareholder resolutions related to working conditions:

- To adopt a policy of including non-management employees as board candidates to help resolve worker grievances. This vote failed, with just under 13% of votes in favour.
- To commission a third party audit of working conditions following reports of unsafe working practices and unfair treatment, including the findings by the US Department of Labor in 2021 relating to serious health and safety issues faced by Amazon warehouse employees. This resolutions failed, gaining an approval rating of just under 44%.

Environment – We voted for a resolution requesting an annual report on plastic packaging pollution, including any company strategies or goals to reduce the use of plastic packaging. Concern over the environmental damage caused by plastics is rising and regulations may come into force in several jurisdictions that would limit the use of single-use plastic packaging. Disclosure in line with the resolution would therefore help shareholders gauge whether the company is appropriately mitigating related risks. The vote failed, but with an approval rating of nearly 49%.

Lobbying – We voted for a proposal requesting disclosure of direct and indirect lobbying payments and policy as we felt that this would help shareholders better assess risks and benefits associated with the company's participation in the public policy process. The vote failed, but won an approval rating of 47%.

Diversity – We supported a resolution requesting a report on the median pay gap at the company by gender and racial breakdown, including information on its policy and goals to reduce compensation disparities based on gender and race. Following lawsuits and fines concerning hiring and pay practices, we believed that such increased disclosure would allow shareholders to better assess the company's management of related risks and benefits. The vote failed with an approval rating of just under 29%.

We do not doubt the power of the retail business or the enduring growth offered by Amazon Web Services. However, the company's premium valuation and our increasing concerns about the company's ability to sustain high returns on capital, caused us to sell our position in Amazon during the second quarter of 2022 therefore will not be taking further action on these resolutions.

[15] Reference to individual stocks is for illustration purpose only and does not guarantee their continued inclusion in any portfolio, nor constitute a recommendation to buy or sell.

Principle 12

Case study: Using our voting power to encourage management into action over under-used cash (equity)

This is a Japanese pharmaceutical company held in our Japanese Equity portfolios.

Issue: The company had no debts and had accrued so much cash on its balance sheet that it exceeded its market capitalisation. The cash did not contribute to the main business and offered low returns. It was also affecting the valuation of the shares as the market had formed a negative view of the company's management of its surplus capital. In the absence of any moves by the company to improve its capital efficiency, a shareholder resolution was proposed that a one-off dividend be paid to return some of the cash to shareholders.

This move prompted the company to announce that it would be more aggressive in acquiring "in-licensed" drugs to support sustainable long-term growth as it has limited research and development capabilities to develop its own drugs. However, it argued that the crowded and intensifying competition for new drugs, combined with the possible need to deal with multiple concurrent opportunities, meant there was a requirement for it to hold sufficient cash to move quickly as and when necessary.

Activity: Despite the arguments of the company, we judged that the proposed additional dividend would be modest in relation to the company's net cash and its investment needs and that it would not cause problems for the company's financial health. We knew that the proposal would be rejected since the parent company held the majority of voting rights. Nonetheless, we recognised that it was important to support efforts to enhance shareholder value and therefore voted for the proposal. As expected, the resolution failed, picking up just under 21% of the votes cast.

Outcome: Despite the vote's failure, it has clearly engendered a more favourable atmosphere for minority shareholders. Capital efficiency was discussed at the board meeting following last year's general meeting of shareholders, further to which a new medium-term management plan – including capital allocations – was announced. We continue to evaluate the progress made by the company and will encourage management to clearly express its intentions through dialogue.

Case study: Voting to improve investment efficiency at an IT group (equity)

This company, a large independent IT solution vendor in Japan, is held in our Japanese Equity portfolios.

Issue: At the AGM in March 2022, a large institutional shareholder proposed the appointment of two additional outside directors to the board. It argued that, instead of reinvesting profits in its core business or returning funds to shareholders, the company had for some time directed investment to areas where synergies with the core business were unclear. It had neglected to allocate capital in a way that contributed to sustainable growth or medium – and long-term corporate value, resulting in a depressed valuation and a return on equity that had fallen to half the level of peers. The investor believed that strengthening the board with two outside directors with experience in finance, accounting and capital allocation would boost independent oversight, help improve capital allocation and enhance corporate value.

Activity: We interviewed the candidates proposed by the shareholder and concluded that they would be a welcome addition to the board and strengthen management oversight. We therefore voted in favour of the shareholder resolution. In the event, the resolution failed, gaining only 39% of the vote.

Outcome: Although the resolution failed to pass, it had positive effects. In August 2022 the company established a Corporate Value Enhancement Committee (CVEC) with the aim of adopting advice and suggestions from stakeholders on how to improve the company's value.

In September, we had a meeting with a company director, telling him why we had voted for the shareholder proposal and against management. Despite the failure, we said it was still our expectation that the management would accept independent outside directors to improve oversight of the company's management.

Subsequently, the activist shareholder which had made the original proposal nominated four independent directors at an extraordinary general meeting in November, two of whom were accepted by the company.

Principle 12

Case study: Promoting healthier governance at a medical equipment company (equity)

AdaptHealth, held in our Global Equity portfolios, provides home medical equipment, medical supplies and related services in the United States.

Issue: When AdaptHealth became a public company following the acquisition of AdaptHealth Holdings by DFB Healthcare Acquisitions in 2019, several charter or bylaw provisions (rules established by the board of directors at the time a company is started that govern how the company is run) were established that fall short of what we consider best governance practice. This including a classified board, which prevents shareholders from holding directors accountable on an annual basis, can entrench management, and can deter takeovers and proxy contests. In our opinion this structure therefore adversely impacts shareholder rights.

Activity: Due to the classified board structure, at the AGM in June 2022 three Directors of the governance committee ran (unopposed) for re-election. Given the board's failure to remove the classified board structure or subject it to a sunset requirement, we withheld our votes in line with our views on board effectiveness (where a director runs unopposed, a vote against the resolution is not possible and he or she only needs one vote to be elected; in such cases, a 'withhold' vote is seen as a public statement of disagreement whereas an abstention could be seen as 'undecided').

Outcome: As expected, the votes passed with withhold rates of 17%, 11% and 21%.

Case study: Pushing governance up the agenda at a major Japanese food company (equity)

Background: The company is a large Japanese food products company with a growing business in North America owned in our Japanese Equity portfolios. We were concerned about the long tenure of the company's outside directors.

Activity: We informed the company that we were planning to introduce new voting guidelines opposing the reappointment of outside directors who had been in office for more than 12 years. This would mean we would vote against one of the company's directors at the next annual meeting of shareholders.

The company asked for a dispensation as it was performing well and increasing shareholder value. Moreover, it argued that the individual in question was a former director of the Bank of Japan and was therefore of sufficient standing to hold the company's chairman to account. It therefore requested that he be allowed to be reappointed.

Outcome: A proposal for the reappointment of the outside director was submitted to the annual general meeting. After carefully considering and debating the case, we ultimately voted against the reappointment as a matter of principle. We also believed that this would act as an example to other companies, demonstrating our strong views in this area.

Result of the resolution: The resolution passed with a vote of 68% in favour.

Case study: Boosting independence on the board of a Japanese electronics group (equity)

Background: This information technology and electronics group is held in our Japanese Equity portfolios. We identified the independence of the board as a clear area for improvement for the company. One outside director was a senior manager at the company's biggest lender, from which outside directors had been accepted for over 20 years.

Action: We have consistently voted against the appointment of this director for at least five years. In the absence of any movement, recently we increased the pressure, telling the company that we could not regard directors appointed from the same major lender for decades to be genuinely independent. We said we needed it to appoint outside directors who could demonstrate guaranteed independence.

Outcome: At the general meeting of shareholders in June 2022, the controversial outside director was not put up for re-election and a more independent outside director was appointed instead. As a result, all of the company's outside directors can now demonstrate genuine independence.

Principle 12

Case study: Shareholder differences at a large Japanese electronics group leads to deadlock (equity)

This is a large Japanese multinational conglomerate with a number of diversified products, including personal computers, consumer electronics, home appliances and medical equipment. It is held in our Japan Equities portfolios.

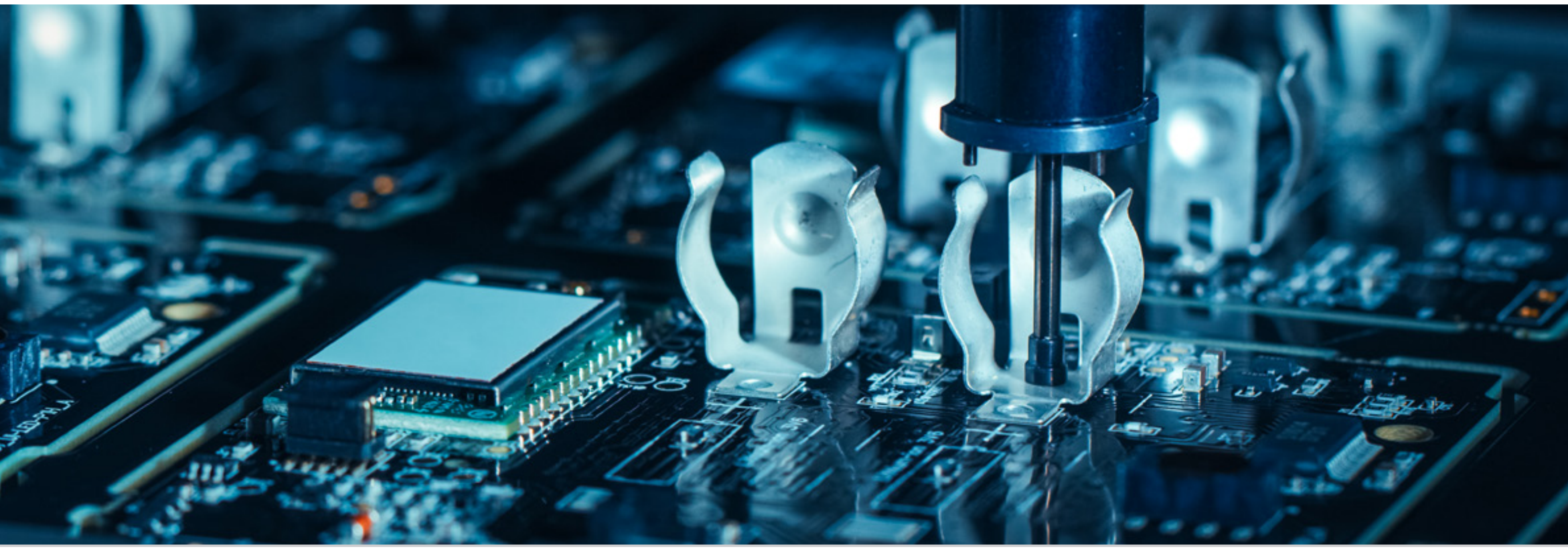
Issue: In November 2021, the company announced plans to split into a number of separate companies through spin-offs. This was followed by discussions about the plans with a variety of stakeholders, including shareholders and the relevant authorities, resulting in further refinement of the proposals.

Activity: At an extraordinary general meeting in March 2022, the company proposed a resolution seeking support for the planned restructuring. We voted in favour of the proposal since we believed that spinning off businesses with different characteristics (e.g. business risks and cycles) would improve management efficiency, reduce information asymmetries, and therefore enhance corporate value. Furthermore, we felt that, by maintaining public listings, the spun-off companies would ensure that current shareholders retained the opportunity to benefit from medium – to long-term corporate value enhancements. This plan was rejected by shareholders, winning approval from holders of just under 40% of the votes.

At the same meeting, shareholders were asked to vote on an alternative plan proposed by a large activist investor the second largest shareholder in the company. It called for the company to continue reviewing alternative options and in particular to engage actively with potential buyers and investors among private equity firms. The position of the company's management was that, while they would not rule out other options, they were best placed to decide the best solution and at that time they remained of the opinion that a strategic restructuring represented the best course of action, arguing that investing a disproportionate amount of time and resources in providing formal due diligence opportunities would be a diversion when they should be focusing on implementation of the strategic reorganisation.

We felt that, were the company to be taken private, the purchase price would be unlikely to be as much as the mid – to long-term value that would be realized if the company were to be restructured into different entities and kept listed. We therefore voted against the shareholder resolution since we felt that it was not in the interests of minority shareholders. This resolution also failed, garnering 44.6% of the votes cast.

Outcome: Since both the company's proposal and the shareholder's proposal were rejected, the management began seeking to go private in order to consolidate divided shareholder opinion. Three months later, at the June 2022 AGM, we opposed the appointment of non-executive directors proposed by the same activist investor whose aim was to realise value for themselves and not necessarily in the interest of wider shareholders by taking the company private. In February 2023, the company received a bid from a Japanese private equity firm. We continue following developments at the company and will use our rights as shareholders to act in what we believe is the best interest of our clients.



Appendix

Appendix – Case study Index*

* Please note that, in some instances, case studies have been anonymised on request of the underlying team to ensure that our engagements remain productive.

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