European SRI Transparency Code

The European SRI Transparency Code (the Code) focuses on SRI funds distributed publicly in Europe and is designed to cover a range of assets classes, such as equity and fixed income.

All information pertaining to the European SRI Transparency Code can be found at the following website: www.eurosif.org. The Code comes with a Guidance Manual for fund managers on how to best use and respond to the Code. The present version of the Code was approved by the Board of Eurosif in February 2018.

REVISION OF THE CODE

In 2017 the Code was updated to better reflect the continuing evolution of the European SRI market. A Working Group was set up to facilitate revision of the Code in line with the latest developments in the industry and in view of the latest work carried out by experts at the European and global level.

Applications to sign up to the Code will now be in line with key elements of the recommendations made by the Task Force on Climate-related Financial Disclosures (TCFD), Article 173 of the French TECV Act and the latest recommendations made by the High-Level Group of Experts on Sustainable Finance (HLEG) in its final report published in January 2018. Questions that are specifically designed to reflect those recommendations/legislation are indicated in the Code with footnotes.

TWO KEY MOTIVATIONS UNDERPIN THIS CODE

1. The opportunity for retail SRI funds to provide clarification to investors and other stakeholders about their SRI approach in an easily accessible and comparable format.
2. Proactive strengthening of self-regulation to contribute to the development and promotion of SRI funds by setting up a common framework for transparency best practices.

GUIDING PRINCIPLE

Signatories to the Code should be open and honest and should disclose accurate, adequate and timely information to enable stakeholders, especially consumers, to understand the ESG policies and practices of the fund.

COMMITMENTS BY SIGNATORIES

- The order and exact wording of the questions should be followed;
- Responses should be informative and clear, and the resources and methodologies used should be described in as much detail and as precisely as possible;
- Funds should report data in the currency that they use for other reporting purposes;
- Reasons preventing the fund from providing all or part of the information to a given question should be clearly stated and, in such cases, signatories should state when they will be able to answer the question;
• Responses should be updated at least on an annual basis and should have a precise publication date;
• Responses to the Code should be easily accessible from the website of the fund and/or of the fund manager. In any case, signatories should make it clear where to find the information required by the Code;
• Signatories are solely responsible for the answers to the questions, and should state this in their response.

**Statement of Commitment**

Sustainable and Responsible Investing is an essential part of the strategic positioning and behaviour of Hermes Investment Management. We have been involved in SRI since 1993 and welcome the European SRI Transparency Code.

This is our second statement of commitment and covers the period October 2018 to October 2019. Our full response to the European SRI Transparency Code can be accessed below and is available in the annual report of the retail funds and on our website.

**Compliance with the Transparency Code**

Hermes Investment Management is committed to transparency and we believe that we are as transparent as possible given the regulatory and competitive environments that exist in the countries in which we operate.

Hermes Investment Management meets the full recommendations of the European SRI Transparency Code without any exceptions.

October 2018

**Eurosif classification of Sustainable and Responsible Investment strategies**

1 Sustainable and responsible investment ("SRI") is a long-term oriented investment approach which integrates ESG factors in the research, analysis and selection process of securities within an investment portfolio. It combines fundamental analysis and engagement with an evaluation of ESG factors in order to better capture long-term returns for investors and to benefit society by influencing the behaviour of companies. Ref. Eurosif 2016
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1. **List of funds covered by the Code**

<table>
<thead>
<tr>
<th>Name of the fund(s): Hermes Global Emerging Markets Equity Fund</th>
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<tbody>
<tr>
<td><strong>Dominant/preferred SRI strategy (Please choose a maximum of 2 strategies)</strong></td>
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</tbody>
</table>
2. General information about the fund management company

2.1. Name of the fund management company that manages the applicant fund(s)

Hermes Fund Managers Limited, 150 Cheapside, London, EC2V 6ET.

www.hermes-investment.com

The fund is not subject to a management delegation.

2.2. What are the company’s track record and principles when it comes to integrating SRI into its processes?

Please provide a hyperlink to any of the company’s sustainable investment webpages.

Our primary purpose is helping beneficiaries retire better by providing world class active investment management and stewardship services. We believe this purpose includes a duty to deliver holistic returns – outcomes for our clients that go far beyond the financial and consider the impact our decisions have on society, the environment and the wider world.

It is this understanding that informs our belief that we have a duty to consider the longer term risk and opportunities when investing. This means extra work in analysing companies; understanding externalities, governance practices, environmental impacts, treatment of workforces and the influence to improve the behaviour of those companies in which we have invested; the operations of the assets that we directly manage, and advocating for systematic improvements to the financial system in which we participate.

Achieving this mission will mean putting the interests of our clients and their ultimate beneficiaries’ front and centre of all that we do. This is a commitment that all Hermes employees are committed to and is embodied in our Pledge of Responsibility.

In the context of our mission as a firm, described above, each of our funds is committed to incorporating ESG considerations into their investment approach in order that portfolio managers are cognisant of the full range of risks and opportunities inherent in any company and are similarly mindful of the impact of a company’s operations on wider society and ultimately are able best able to generate strong and sustainable returns.

In addition our Delivering Holistic Returns document which was authored in January 2018, covers what we do across asset classes and as a responsible investor, owner and firm.

2.3. How does the company formalise its sustainable investment process?

Please provide a link to the sustainable investment policy.

Please provide a link to the voting rights policy.

Please provide a link to the engagement policy.

In line with good corporate governance practice, the Hermes board sets the company’s strategic aims, ensures that the necessary financial and human resources are in place for the company to meet its objectives and reviews and holds management accountable for performance within a framework of prudent and effective controls which enables risk to be assessed and managed. The board also sets the
company’s values and standards and ensure that its obligations to its shareholders and others are understood and met.

While the responsibility for implementing our approach resides with all Hermes personnel, we have a number of structures, teams and governance processes which ensure that across the firm we discharge our responsibilities in a consistent and effective manner.

**Portfolio Review Committee**, our Investment Office which reports directly to our CEO, acts as an independent oversight body across all our investment teams. A key element of this is the monthly Portfolio Review Committee which monitors in detail the performance and risk with each fund and strategy and challenges investment teams.

**Responsibility Working Group**, constituted of senior representatives from across the business and chaired by our Head of Responsibility who reports directly to our CEO, is charged with reviewing and recommending policy for decision by our Executive Committee in respect of all matters pertaining to the delivery of holistic returns.

**Dedicated Responsibility Office**, ensures that responsibility is embedded through the business. This extends to Hermes approach to its own governance and practices, as well as the integration of engagement and ESG factors into investment strategies and processes.

**ESG Policy**

**Engagement Objectives and Plan**

**Voting**

We view the vote as part of the asset that a shareholder owns and recognise we have an implicit fiduciary duty to exercise, or to recommend the exercising of this right, in a considered and intelligent fashion.

Our regional corporate governance principles provide a clear and transparent framework for our voting policy and we manage our voting via a partnership with proxy advisory firm ISS. While we have developed our own best practice regional principles which are based on local market standards, we benefit from the additional research and vote processing service ISS provide. The research received from ISS is however, only one of several inputs that we utilise in reaching a judgement and making voting recommendations to clients.

**Regional Corporate Governance Principles**

2.4. **How are ESG risks and opportunities – including those linked to climate change – understood/taken into account by company?**

Hermes’ equity and credit teams employ a long-term investment philosophy (whether value- or growth-oriented) and a process that involves focusing on business fundamentals and long-term franchise value. ESG considerations feature throughout the investment process and a number of proprietary tools supplement the investment team’s processes to enhance their fundamental analysis and result in better investment decisions.

In addition to making use of best-in-class third party research provided by ISS, MSCI, Sustainalytics, Trucost, and others, our investment teams incorporate ESG factors into their investment process by using a range of in-house proprietary tools which include:

**ESG Dashboard**

The proprietary Hermes ESG dashboard ensures that all companies (subject to the availability of the data) can be compared against their peers on a sector, regional or global basis with respect to a range of ESG considerations. Our proprietarily developed QESG score captures how well a company manages its ESG risks, and importantly whether this is improving or not. The QESG score not only incorporates third party research indicators but also the insights of our voting and engagement activity. The change in score can provide an early warning signal or suggest that management is successfully grappling with an issue. This
stock specific analysis is a valuable input to the investment process as well as ongoing monitoring of, and, where appropriate, engagement with companies.

**Portfolio Monitor**

Through the use of our Portfolio ESG Monitor we are able to observe the aggregate ESG risk across our portfolios in both absolute and benchmark-relative terms, subject to the availability of data and company disclosures. Investment teams are able to break these measures down into the constituent environmental, social or governance risks and view the ESG metrics for each portfolio company with the best and worst performers identified.

**Climate change analytics**

Our portfolio managers strive to understand all components of risk and return within their investee companies. This analysis extends beyond the financial numbers to include a company’s greenhouse gas (GHG) emissions, energy efficiency, exposure to water stress and their potential impact upon a company’s future prospects within different climate change scenarios. To do so effectively, it is crucial that analysts have straightforward access to fundamental ESG and engagement data, which are relevant and material.

Hermes investment teams can see in real-time and in detail, the level and intensity of carbon across their portfolios; which portfolio companies are the greatest emitters and most at risk. We look at the data through multiple lenses to identify those companies whom may be better or worse placed and where additional research or engagement may be necessary. Analysts are subsequently able to see the progress of ongoing engagement towards mitigating the potential risk – we have a firm-wide commitment to engage with the highest emitting stocks in each of our funds. The ability to test-out ‘what-if’ scenarios ensures that we remain forward thinking and mindful of the impact our investee companies have on the world around them in addition to the opportunity or risk of the investment.

We believe that ESG-aware investors should not rely on data alone, as it is often backward looking and updated infrequently and at a time lag. As such, active ownership is an important pillar of our investment approach. The voting and engagement activities of our stewardship team can promote positive change within companies, unlocking hidden value and also providing a forward-looking view of ESG and broader performance that can lead to opportunities.

Hermes’ investment teams also benefit from the expertise of our specialist in-house stewardship team, Hermes EOS, which was established in 2004 and boasts one of the largest stewardship resources globally, composed of an effective group of highly and diversely skilled, multi-national professionals, all committed to influencing leading businesses on governance and sustainability matters. Hermes EOS alerts Hermes equity teams of any ESG issues affecting stocks that are included in the portfolios and votes at the general assembly meetings of companies held in the portfolios. This enables Hermes investment teams to incorporate corporate social performance and responsibility considerations into their investment process in a seamless, complementary and risk-aware manner, and further strengthens the alignment and transparency with our clients.

When the investment teams identify an issue with a company, they will not necessarily choose not to invest in it, as long as its business case is strong, the valuation already reflects the risks, and they believe in management’s ability. When this is the case, the team relies on Hermes EOS to undertake engagements with the company due to their expertise and the significant influence they wield through their many clients (Hermes EOS often has multiple clients invested in the stocks the team chooses). The aim of these engagements is to protect the value of clients’ investments by limiting risk or unlocking value or to voice clients’ concerns. Members of the investment team will often join their stewardship colleagues in these meetings with companies.

Managing climate and carbon risks remains a key priority for Hermes as the economy decarbonises, in particular by investing in opportunities that can deliver new growth areas and job creation. We are confident that by expanding on the work we already carry out in measuring carbon risk to include scenario analysis will help us, other investors and the assets themselves understand much better the scale of the carbon opportunity and more specifically on how to deliver on it. At Hermes, we will continue to manage our carbon risks, challenge the current economic and financial models to encourage the change required
to meet the scientifically guided climate change objectives and identify opportunities to improve the long-term financial performance of our assets.

We are committed to engaging with all of the highest emitting companies across each of our public markets portfolios in order to drive up disclosure levels, promote scenario testing and ensure operations are as energy efficient as is practicable. Additionally, we have actively managed down the energy efficiency of our real-estate assets for many years with detailed disclosures provided annually of performance against targets. We are members of, among other initiatives, the Portfolio Decarbonisation Coalition, the Aiming for A coalition of investors and the Institutional Investors Group on Climate Change. In our public policy engagement with the UK and European governments we call for a clear policy framework to enable the scaling up of low carbon and energy efficiency investments. In addition to our ISO 14001 accreditation and in continuation of our corporate citizenship policy, we offset our own carbon emissions by partnering with Trees for Cities. We publish our carbon risk management strategy on an annual basis and in support of the FSB Taskforce for Climate-Related Financial Disclosures (TCFD) recommendations will be enhancing the level of relevant public disclosures we provide as a firm.

As mentioned above, we aim to be ESG aware and actively incorporate relevant considerations into our investment process across all strategies and asset classes. Having a focus on each of responsible investing, responsible ownership and policy advocacy across all of our strategies, while also behaving responsibly as a firm, is, we believe, integral to delivering holistic returns. Behaving as a responsible business ourselves is critical to giving us the credibility with which to be able to fulfil these ambitions.

### 2.5. How many employees are directly involved in the company’s sustainable investment activity?

As mentioned previously, while the responsibility for implementing our sustainable investment approach resides with all Hermes personnel, we have a number of teams and personnel across the business who are directly involved in ensuring we discharge our responsibilities in a consistent manner:

**Hermes EOS Engagement team:** 27
Provide active engagement of those companies and assets in which we are invested and those we directly manage.

**Responsibility Office:** 7
Ensures that responsibility is embedded throughout the business.

**Dedicated ESG analysts/portfolio managers:** 10
Leads the ESG and responsible investment research strategy within their respective strategies

### 2.6. Is the company involved in any RI initiatives?

At Hermes we believe it is our responsibility to lead and participate in discussion and debate about the fiduciary responsibilities of institutional investors to their clients, their stakeholders and ultimately, society at large. In a similar vein we have a proud history of leading thinking around corporate governance and the purpose and responsibilities of companies and their directors towards both their shareholders and wider stakeholders. Ultimately, it is our belief that the financial system should operate in the interests of its ultimate beneficiaries.

That’s why, in addition to the thought-leadership work we do directly as a firm, we actively contribute to a wide variety of investor associations and collaborative initiatives. Of particular importance is the Principles for Responsible Investment (PRI) for which we chaired the drafting committee and became founding signatories. In addition, our Chief Executive founded the 300 Club in 2011, an independent group of leading investment professionals from across the globe, in order to respond to an urgent need to raise uncomfortable and fundamental questions about the very foundations of the investment industry and investing. In addition to relevant trade associations, we have supplied below a list of the key bodies that Hermes is actively involved with.
A full list can be found in the Delivering Holistic Returns document on page 19. Of particular importance is the Principles for Responsible Investment (PRI) for which we chaired the drafting committee and became founding signatories.

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<tr>
<th>General Initiatives</th>
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<td>□ National Asset Manager Association (RI Group)</td>
<td>□ Paris Pledge for Action</td>
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<td>□ PRI - Principles For Responsible Investment</td>
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2.7. What is the total number of SRI assets under the company’s management?

3. General information about the SRI fund(s) that come under the scope of the Code

At Hermes we aim to be ESG and impact aware and actively incorporate relevant considerations into our investment processes across all strategies and asset classes. As at 30 September 2018 our specialist, high conviction investment teams manage €40.4bn in assets across our entire responsible investing spectrum which includes, equities, credit, infrastructure, private equity, private debt and real estate.

A full range of our funds can be found at the below link.

https://www.hermes-investment.com/ukw/products/

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3 Reference to Article 173 of the French TECV Act and the HLEG recommendations on INVESTOR DUTIES
4 Reference to Article 173 of the French TECV Act and the TCFD recommendations (risks and opportunities section)
3.1. What is (are) the fund(s) aiming to achieve by integrating ESG factors?

The Global Emerging Markets team considers ESG matters as part of their fundamental analysis of all companies. The analysis feeds into their allocation decisions, which are focused on risk-adjusted returns. This extra integration enables the team to incorporate ESG considerations into their bottom-up investment process in a seamless, complementary and risk-aware manner, and further strengthens the alignment and transparency with our clients.

3.2. What internal or external resources are used for ESG evaluation of the issuers who make up the investment universe of the fund(s)?

**Internal**
- Gary Greenberg is the lead portfolio manager and ultimate decision maker for the management of the Hermes Global Emerging Markets strategy. Gary is supported by a dedicated global emerging markets team of five investment professionals, a portfolio assistant and an investment director. Kunjal Gala and Amit Mehta are responsible for idea generation for Asia ex Japan; Elena Tedesco covers the CEEMEA region, with Jasper Wright, a generalist, currently providing support in this area; and Yasmin Chowdhury covers Latin America. In addition to their research responsibilities, Kunjal is the co-portfolio manager for pooled funds and segregated mandates and Elena is the co-portfolio manager for ESG strategies.
- Hermes EOS has a team of 27 engagement specialists with an average of 10 years of experience. The Hermes Global Equity team used Hermes EOS’ expertise when building the proprietary ESG Dashboard and Portfolio Monitor utilised by Hermes’ investment teams, as well as the QESG Score, which assesses a company’s current ESG characteristics and how they are changing.
- Our dedicated Responsibility team is comprised of seven full-time ESG experts.

**External**
- As well as the voting and engagement insights that are used in the QESG Score, ESG Dashboard and ESG Portfolio Monitor, a range of data from best-of-breed external providers such as Sustainalytics, MSCI, Trucost and Bloomberg is also used.
- We manage our voting via a partnership with proxy advisory firm ISS. We benefit from the additional research and vote processing service ISS provide. The research received is, however, only one of several inputs we utilise in reaching a judgement and making voting recommendations to clients.
- Data is also sourced from CDP, WRI, Factset and the World Bank.

3.3. What ESG criteria are taken into account by the fund(s)?

ESG factors form an integral part of the investment process. Hermes’ proprietary ESG Dashboard incorporates data from leading providers Sustainalytics, Trucost, FactSet and Bloomberg alongside voting information and engagement insights from Hermes EOS, Hermes’ in-house, independent team of leading governance and engagement experts. Hermes has recently subscribed also to MSCI ESG research. The Dashboard ensures that all companies (subject to the availability of the data) can be compared against their peers on a sector, region or global basis with respect to a range of ESG considerations. The Dashboard’s QESG Score captures how well a company manages its ESG risks and, importantly, whether this is improving or not. The change in score can provide an early warning signal or suggest that management is successfully grappling with an issue. This stock-specific analysis is a valuable input to the team’s investment decisions and ongoing monitoring of and engagement with companies.

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1 Elena Tedesco is currently on maternity leave, with effect from May 2018. Jasper Wright is talking over coverage of her CEEMEA names, under the supervision of Gary Greenberg and Yasmin Chowdhury. Kunjal Gala will cover her role as co-manager of ESG strategies.
Through the use of Hermes’ proprietary Portfolio ESG Monitor, the team is able to observe the aggregate ESG risk across their portfolios in both absolute and benchmark-relative terms, subject to the availability of data and company disclosures. Investment teams are able to break these measures down into the constituent environmental, social or governance risks and view the ESG metrics for each portfolio company with the best and worst performers identified. This portfolio level view enables portfolio managers to, for example, be aware of the estimated level of carbon in their portfolios, including which investments are the largest contributors to a portfolio’s carbon footprint.

The Global Emerging Markets investment team also performs its own ESG research at the stock and country level. The team actively incorporates ESG factors in their assessment of the valuation, risks and catalysts of a stock or country, and they qualitatively assess the key ESG features of a company, including its shareholder structure, the risk of abuse of minorities’ rights, the relationship with stakeholders, and the long-term sustainability of its business model.

This approach is supported by regular interactions with our stewardship team to exchange views and form a holistic view on a company’s prospects.

3.4. What principles and criteria linked to climate change are taken into account in the fund(s)?

Concerning climate change, do you take the following risks and opportunities into account? If so, how?

- Physical risks, defined as exposure to the direct physical consequences of climate change;
- Transitional risks, defined as exposure to the consequential developments/trends of transitioning to a low-carbon economy;
- Opportunities benefiting a low-carbon economy.

We analyse Environmental, Social and Governance factors and believe that these factors are interlinked. For instance, we believe that a company that is not governed well, is more likely to create externalities and consume natural resources irresponsibly.

Although we will not invest in poorly governed companies, we also test the environmental and social credentials of the company, and if we encounter no major red flags, we will invest subject to the usual investment related considerations such as catalysts, risks and valuation.

We analyse the environmental performance of the company by paying attention to the following quantitative metrics:

1. Carbon footprint / intensity
2. Impact ratio
3. Trucost waste / water level
4. CDP performance score
5. Water score

In addition, we also check for any major controversies and company’s response and the likelihood of them recurring. In general, we exclude companies that have a very high carbon footprint. We do not own any energy producers and also avoid investing in companies which show little or no awareness of their role in preventing global warming.

Further information can be found here: https://www.hermes-investment.com/ukw/blog/perspective/equitorial-a-climate-for-change/

Concerning climate change, describe the screening methodology applied to issuers. For the approach chosen, please specify if applicable:

- Compatibility with the international goal of limiting global warming (issuers’ contribution to the energy/environmental transition, use of the 2°C scenario at sector level etc.);
- The effects of climate change and extreme weather conditions;
- The changing availability and prices of natural resources and their use in accordance with climate action and environmental goals;
- The consistency of the issuers’ investment expenditures with a low-carbon strategy. In particular, in the case of issuers linked to the use of fossil fuel reserves, compatibility with a low-carbon strategy of the underlying assumptions behind investment expenditures to develop such reserves;
- The measurement of greenhouse gas emissions in the past, present and future that are directly or indirectly associated with the issuers.

Global warming and climate change are real risks to most businesses especially those operating in heavily populated regions in emerging markets. Pollution of the air, water and soil have profound social consequences and can result in a backlash from the communities impacted by them. Where relevant, we engage with companies and ask them their strategy relating to sustainable operations. For instance, we spoke with Taiwan Semiconductor regarding their use of water as the process of fabricating silicon is water intensive. Similarly, we analysed the relevance of water to a Brazilian paper and pulp manufacturer Klinbin. We found the company’s awareness and approach, especially related to their new pulp mill, to be appropriate.

We speak with companies on their power requirements especially in regions where power supply has been volatile. For example, in recent months Taiwan has seen issues with its power supply and the technology industry is dependent on the government for power supplies. We try and understand alternative strategies adopted by the companies to mitigate the risks including diversifying operations to other regions in order to limit disruption to the business.

Recently, we have started analysing the impact of dairy farming on GHG emissions as we own a dairy products company in China which screens quite high on carbon emissions. We are in the process of setting up an engagement program to understand their initiatives relating to limiting the impact of dairy farming on the environment including measures to promote animal welfare.

Products / services promoting a low carbon economy are of interest to us and we have investments in companies that deliver a positive impact, namely:

- Auto components: focus on light-weighting components for use in the automobile industry
- Logistics: emerging markets are inefficient as seen from high logistic costs as % of GDP vs. developed world. We have investments in logistics in China and India which are driving a reduction in empty truck runs or promoting a shift from road to rail resulting in lower emissions in the economy
- Automation / IoT: industrial automation improves operational efficiency and reduces wastage in the process. Internet of Things is another area where we have investments in companies that promote intelligent city operations that include smart grid, building management solutions, etc. that promote energy efficiency in operations

### 3.5. What is the ESG analysis and evaluation methodology of the fund manager/fund management company (how is the investment universe built, what rating scale is used etc.)?

ESG factors form an integral part of the investment process. The Hermes’ Global Emerging Markets team have a number of tools available to them which they use to monitor companies they invest in. These include the ESG Dashboard, our QESG Score (proprietary ESG rating) and a Portfolio ESG Monitor. These tools highlight potential high-risk behaviour from an ESG perspective within companies, at which point the investment team liaises closely with our stewardship team Hermes EOS in order to engage with the company in order to better understand the risk and where necessary seek positive beneficial change.

The ESG Dashboard amalgamates Hermes EOS’ records on voting and engagement on ESG issues with data from a range of carefully-evaluated external providers. It gives transparent access to key ESG-related information on every company across a global universe. The risk factors which each company is measured by are either generic, such as board structure, or sector specific, focusing on the major risks in their respective industries, such as carbon dioxide emissions and fleet consumption for the automobiles industry, paper sourcing for media and energy efficiency for airlines.
The QESG Score is a ranking applied to each company, distilling the information collated on the ESG Dashboard into a single number. Not only does this score capture how well a company manages ESG risks, but also the trend in its exposure to these risk.

The QESG Score is designed to capture a company's behaviour on various ESG issues as well as observed change in its ESG behaviour. A change in a company’s ESG profile would be highlighted by a change in the QESG Score, which would be flagged to the portfolio managers. Any such significant change would be questioned, firstly to validate, but also to inform the investment case on a stock.

The quantitative rating, importantly, is complemented by a fundamental bottom-up review of ESG issues, which critically leverages on our direct contact with companies which provides the investment teams with greater colour and more up to date picture of the current positioning of a company with respect to its ESG performance. The outcome from the subjective analysis may lead to a company being removed from the trade list depending upon the materiality of the issue and also the anticipated change as demonstrated by the company.

The Portfolio ESG Monitor delivers a portfolio perspective of ESG risk exposures. It reports on the ESG characteristics of holdings, both in absolute and benchmark-relative terms, and highlights companies with potentially controversial practices. The monitor captures thematic ESG risks as well as identifying the best and the worst companies according to various ESG metrics.

We have developed an internal Carbon Footprint tool, to enhance our ability to integrate ESG into our investment strategies, In particular, we want to bring together ESG, financial, and our in-house QESG rating and engagement data into a multi-faceted approach. Also our focus is not only on aggregate positioning relative to the benchmark but also on identifying outlier companies through various lenses. For instance, among other applications, we can identify companies that may have lower carbon efficiency than industry peers, lower returns, deteriorating QE score, with an engagement that is not progressing, which then may be more at risk and thus less attractive.

The Global Emerging Markets investment team complements the above elements with its own qualitative assessment of the key ESG features of a company, including its shareholder structure, the risk of abuse of minority shareholders’

3.6. How often is the ESG evaluation of the issuers reviewed? How are any controversies managed?

Our QESG Scores are designed to capture a company’s behaviour on various ESG issues as well as observed change in its ESG behaviour, as a result ratings will be continually updated as new information is made available.

A significant change in a company’s ESG profile would be highlighted by a large change in the QESG Score, which would be flagged to the portfolio managers, or a communication from our ESG specialists, Hermes EOS. Any such significant change would be questioned, firstly to validate, but also to inform the investment case on a stock.

The investment team closely monitor companies in their portfolio and formally speak with colleagues in our stewardship team in order to stay abreast of the latest insights gleaned from ongoing engagements with companies in the portfolio. The team continues to research new data sources as they become available and will incorporate these into its systems as appropriate and following a robust testing process.

Hermes operates a firm-wide exclusion policy with respect to pure-play cluster munitions companies and manufacturers of anti-personnel land mines.

Implicit within our mission is also a recognition that the investment decisions we make will have impacts wider than the returns they generate. As a result, we question a company’s purpose, how and where it generates its profits and whether these come at the expense of externally imposed costs. The answers to these questions inform our investment decisions. Each of our investment teams has the flexibility to form their own judgements based upon their own detailed analysis, however, each team is expected to have documented their considerations and be able to justify any investment decision both internally to our Portfolio Review Committee as well as, importantly, to clients.

A very negative ESG profile (as indicated by a low QESG Score) would not necessarily exclude a stock from investment. From a quantitative aspect, governance is only one of several measures going into the Corporate Behaviour factor, meaning that a very negative figure would tilt the resulting score, but not
entirely negate it. During the subjective analysis that follows the modelling, a portfolio manager would consider the impact of very negative remarks and how they may change the investment case. However, if the negative remarks were fully understood and other factors compensated for the ESG issues, an investment may still be considered.

At Hermes, we prefer to engage with companies rather than divest. In our view, successful engagements reduce risks to shareholders, unlock value, and benefit wider society. We believe investors should be involved shareholders, encouraging responsible behaviour and effecting positive change. Alongside communicating with senior management and board members, we undertake filing or co-filing shareholder proposals, where appropriate, and voting proxies in accordance with investors’ views and policies, supporting transparent and effective governance structures that encourage stakeholder dialogue. We believe that working with firms to mitigate ESG risks – while reserving the option to sell down where a company is unable or unwilling to improve – can provide the greatest holistic benefits. As such, we seek investments with good or improving ESG characteristics, which should contribute to outperformance over the long term. While ESG issues are important in themselves, we recognise that helping a company to lift its ESG performance can both benefit society and realise financial gains for investor.

Hermes clients benefit from intense engagement activities covering well over one third of the portfolio, in addition to AGM voting on all portfolio stocks. Hermes engagement projects have set targets and are reviewed for progress.

Supply chain, product safety and brand value: Chinese dairy

Significant product safety shortfalls and the consequent drop in the share price offered us the opportunity to invest in a market leader in an underpenetrated consumer industry in China. We invested in the stock in early 2012 with the view that scandals often turn into catalysts for positive change, especially when the Chinese government acknowledges the need to improve.

Following our investment, we started engaging the dairy producer. Our engagement put pressure on the new management to deliver swift change and improve communication on the progress made so as to strengthen the brand and customers’ perception. The group delivered concrete actions including a new quality-control division reporting directly to the CEO, detailed guidance for its suppliers, streamlined supply chain focused on fewer trustworthy intermediaries, and more third-party checks on product quality.

4. Investment process

4.1. How are the results of the ESG research integrated into portfolio construction?

The team’s bottom-up research approach is augmented with the integration of ESG analysis at the stock and country levels. The fundamental research which accompanies the quantitative screen provided by the QESG dashboard is essential for a comprehensive understanding of the risks and opportunities in emerging market companies. The team actively incorporates ESG factors in their assessment of the valuation, risks and catalysts of a stock or country.

To determine whether to invest in a certain stock and to assess any impact on discount rates, the team considers elements such as shareholder structure, risk of abuse of minority shareholders’ rights, sustainability of the business model, carbon emissions, exposure to workers’ strikes and community protests, and/or the country’s political stability and the level of corruption.

The Hermes Global Emerging Markets equity fund avoids investing in companies having more than 20% of total turnover coming from coal production. Furthermore, it avoids specific tobacco and military equipment companies.

4.2. How are criteria specific to climate change integrated into portfolio construction?

Climate change criteria are integrated into portfolio construction via our QE Score as described above. In addition the portfolio is subjectively assessed from a top down and from a bottom up perspective. From a top down perspective on environmental issues this could present itself as a concentration in a single risk factor which we would look to avoid or minimise. From a bottom up perspective the QESG Score and the ESG Dashboard are used along with fundamental analysis from the investment team and the EOS team on management of pertinent environmental issues.
4.3. How are the issuers that are present in the portfolio, but not subject to ESG analysis evaluated (not including mutual funds)?

*Please specify how much the funds can hold.*

All companies within the Hermes Global Emerging Markets strategy are subject to an assessment of their ESG characteristics. The team incorporates ESG factors into their investment process by using a range of in-house proprietary tools as mentioned previously.

Additionally, the team will speak to management prior to any investment and typically look to meet with management prior to investment, where possible, or within three months of an initial investment, to establish a detailed picture of its financial health, its long-term prospects and ESG profile.

The team incorporates responsible investment into its stock analysis by:

- Meeting with company management whenever possible to assess their quality, strategy, credibility, accountability and ESG.
- Reviewing Hermes’ proprietary ESG Dashboard to assess and quantify ESG impact where the information is available.
- Assessing the company’s exposure to reputational, legal and financial risks, and what they are doing to mitigate these.
- Communicating with the Hermes EOS team when an issue that may affect the business or its reputation exists, and understanding what the company is doing to improve the situation on behalf of Hermes’ clients.
- Determining if the company’s governance structure leaves directors and managers accountable to shareholders.

The team analyses these components and consolidates the key points into its research reports, alongside a view on the business model, investment thesis, catalysts and risk factors.

4.4. Has the ESG evaluation or investment process changed in the last 12 months?

In January 2017, the team also moved from carrying out the formal asset allocation review from a quarterly basis to a semi-annual basis, with country and sector reviews being held in alternating quarters: macro environment changes evolve gradually.

In 2018, the team introduced a target to engage with all portfolio holdings where ESG engagement is necessary. As Hermes EOS already engages with 50% of the team’s assets under management, the team will engage with the remainder of the portfolio within 12-18 months on any ESG issues identified.

They have also standardised their DCF models and now use the following metrics for all companies valued using a DCF approach:

- The current local 10-year bond yield as the risk free rate (which is tied to Bloomberg, so it changes as the yield changes)
- A 5% market risk premium
- 3% as the perpetuity discount rate (1% real growth plus 2% inflation)

In January 2018, following the implementation of MIFID II, Hermes now pays for all investment research from its own P&L account. In making this decision, Hermes has put the interests of clients and their beneficiaries first.

Strengthening the investment process has enabled the team to increase its conviction, which has led to a more concentrated portfolio.

4.5. Is a part of the fund(s) invested in entities pursuing strong social goals/social enterprises?
Our ‘Getting Engaged: Uniting performance with positive change in emerging markets’ white paper written by Gary Greenberg, Head of Hermes Emerging Markets, goes into further details on how we look at environmental, social and governance risks in emerging markets and how they are integrated into the investment decisions (giving practical examples) and ultimately the process.

4.6. Does (do) the fund(s) engage in securities lending activities?

If so,
(i) is there a policy in place to recall the securities so as to exercise the voting rights?
(ii) does the process for selecting the counterparty(ies) integrate ESG criteria?

No.

4.7. Does (do) the fund(s) use derivative instruments?

If so, please describe
(i) their nature;
(ii) their objectives;
(iii) potential limits in terms of exposure;
(iv) if appropriate, their impact on the SRI nature of the fund(s).

No.

4.8. Does (do) the fund(s) invest in mutual funds?

If so, how do you ensure compatibility between the policy for selecting mutual funds and the SRI policy of the fund(s)? How many funds can be held?

No.

5. ESG controls

5.1. What internal and/or external control mechanisms are in place to ensure compliance of the portfolio with the ESG rules on managing the fund(s) as defined in section 4?*

All of our investment activity is supported by our dedicate Investment Office and Responsibility Office both of which report directly to our CEO. The Investment Office provides a robust and transparent risk framework. On a look back, real time, and forward-looking basis the team actively monitors fund risk and helps to deliver sustainable risk adjusted alpha, while acting as an early warning system to identify potential problem areas. It has overall responsibility for the consistency of performance and thus ensures that investment teams stay true to their processes, this includes oversight of ESG and engagement integration. A key element of this is the monthly Portfolio Review Committee which monitors in detail the performance and risks with each fund and strategy and challenges investment teams.

We have established a Responsibility Working Group, which meets on a quarterly basis and is constituted of representatives from across the business, including Hermes’ CEO. This group is charged with reviewing and making recommendations to the Hermes Executive Committee (ExCo) with respect to our policy and
approach to all matters related to the delivery of holistic returns to the beneficiaries of Hermes’ owner and clients and to share best practice across the organisation.

The Hermes Global Emerging Markets team integrate risk management into the portfolio construction process at multiple stages. The team buys stocks that demonstrate a margin of safety to cushion any downside risk. Risk is assessed at the stock, sector and country level, integrated with ESG analysis and incorporated into the evaluation of the individual stock when it is presented and/or re-evaluated.

The Hermes Compliance team monitors fund guidelines, including objectives and constraints; the firm-wide exclusion policy with respect to cluster munitions and anti-personnel land mines. These automated checks for compliance with fund guidelines and constraints are conducted by thinkFolio, our trade order management system. Pre-trade portfolio parameters, counterparty limits and other guidelines are coded into the system. Coding is undertaken via a robust rule summary process and is always subject to further review by a senior member of the Compliance team. Once client risk limits have been input into thinkFolio, they cannot be overridden by portfolio managers. thinkFolio is also coded to ensure that any trade with a prohibited counterparty or jurisdiction is prevented before execution.

Finally, while Hermes receives an annual independent external assurance on our internal controls which includes those relating to our proxy voting processes, we have committed to obtaining independent assurance over the policies and procedures which underpin our stewardship policy statements in line with the AAF 01/06 Stewardship Supplement for FY 2018. We are also continuing to review what further external assurance we can obtain on our ESG integrations processes to supplement the periodic reviews that are undertaken by our internal audit function.

6. Impact measures and ESG reporting

6.1. How is the ESG quality of the fund(s) assessed?

We believe that companies with strong governance and astute management of their environmental and social responsibilities, such as emissions control or labour rights, not only make a more positive contribution than those that do not, but also provide greater long-term value for shareholders.

In the context of the increasing evidence and our responsibility as a fiduciary for our clients, we seek to:

- integrate awareness of ESG risks into our investment decision processes;
- ensure we remain cognisant of these risks within individual investments and across our portfolios;
- actively engage as appropriate, with those companies in which we, and our clients, have invested, and utilise our rights as investors in a considered and informed fashion to promote long-term success, and;
- work with policy makers to promote responsible investment and advocate for a global financial system that operates in the interests of its ultimate beneficiaries, not its various agents.

We believe that our focus on responsible investing, responsible ownership, policy advocacy and behaving responsibly are integral to delivering holistic returns.

6.2. What ESG indicators are used by the fund(s)?

ESG factors form an integral part of the investment process for Hermes Global Emerging Markets Strategies. The investable universe is defined using the exclusion criteria described above. Hermes proprietary ESG Dashboard incorporates data from leading providers MSCI, Sustainalytics, Trucost, FactSet and Bloomberg alongside voting information and engagement insights from Hermes EOS. The dashboard ensures that all companies (subject to the availability of the data) can be compared against their peers on a sector, region or global basis with respect to a range of ESG considerations. Hermes proprietarily developed QESG score captures how well a company manages its ESG risks, and importantly whether this is improving or not. The change in score can provide an early warning signal or suggest that management is successfully grappling with an issue. This stock-specific analysis is a valuable input to our investment decisions as well as ongoing monitoring of, and, where appropriate, engagement with companies.
The team complements the above elements with its own qualitative assessment of the key ESG features of a company including its shareholder structure, the risk of abuse of minority shareholders’ rights, the relationship with stakeholders, and the sustainability of its business model in the long term. The team's approach is supported by regular interactions with Hermes EOS to exchange views and form a holistic view on a company’s prospects.

Through the use of our proprietary Portfolio ESG Monitor we are able to observe the aggregate ESG risk across our portfolios in both absolute and benchmark-relative terms, subject to the availability of data and company disclosures. Investment teams are able to break these measures down into the constituent environmental, social or governance risks and view the ESG metrics for each portfolio company with the best and worst performers identified.

This portfolio level view enables portfolio managers to, for example, be aware of the estimated level of carbon in their portfolios, including which investments are the largest contributors to a portfolio’s carbon footprint.

The investment team closely monitor companies in their portfolio and formally speak with colleagues in our stewardship team in order to stay abreast of the latest insights gleaned from ongoing engagements with companies in the portfolio.

6.3. What communication resources are used to provide investors with information about the SRI management of the fund(s)?

Our publicly-available annual report and accounts has evolved to include details and statistics on responsibility and ESG. We now report on corporate social responsibility-related activities, such as our carbon footprint, with our future targets also outlined. This is included alongside our engagement activities and financial reporting.

Additionally, Hermes EOS produces quarterly public engagement reports and voting disclosures, which are distributed to clients and available to view on our website. These reports give a detailed insight and analysis of the stewardship activities undertaken by Hermes EOS during the previous quarter, including their results.

Our investment teams also provide take notes and whitepapers, all of which are made available via our website and distributed directly to Hermes’ clients.

We also provide clients voting and engagement information for each fund on a quarterly basis. This includes statistics on voting across geographical regions, as well as highlights of engagement relating to investee companies. In addition, we provide examples of how ESG factors were incorporated into investment decision making. We aim to continuously improve our reporting so that our clients can fully understand our approach to responsible investing.

6.4. Does the fund management company publish the results of its voting and engagement policies?\(^\text{10}\)

If so, please include links to the relevant activity reports.

As mentioned above, Hermes EOS produces quarterly public engagement reports and voting disclosures, which are distributed to clients and available to view on our website. These reports give a detailed insight and analysis of the stewardship activities undertaken by Hermes EOS during the previous quarter, including their results. These reports can be found at the following link https://www.hermes-investment.com/stewardship/eos-literature/

Please provide a link to the latest report on exercise of the voting policy, the latest report on engagement and the latest report on internal evaluation of the voting policy.

Hermes EOS Public Engagement Report Q3
Hermes EOS Voting Disclosure Q2
Hermes EOS Annual Voting and Engagement Report
We do not have a report on our internal evaluations of our voting policies. Our policies are updated at least annually, typically following the voting period.

8 Reference to Article 173 of the French TECV Act
9 Reference to Article 173 of the French TECV Act
10 Reference to Article 173 of the French TECV Act and the HLEG recommendations on GOVERNANCE