

# Aligning activities

UBS Asset Management | 2019 Stewardship Report



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About UBS Asset Management

COVER

Aerial view of bridge over river Markarfljot in Iceland, east of the volcano Hekla

# Foreword

UBS Asset Management began investing sustainably over twenty years ago. During that time we have seen ESG rise to the very top of our clients' investment agenda. As our global survey of institutional investors published in 2019 revealed, 78% already integrate ESG, environmental, social and governance factors within their investment processes. Sustainable investment (SI) matters to our clients and it matters to us.

We believe that acting as good stewards of our clients' assets is a critical element of our SI activities, which is why we regard engagement and proxy voting as intrinsic parts of the investment process. As well as adding financial value, an effective stewardship strategy can also be instrumental in helping investors meet societal targets.

For over two decades we have reported regularly on our stewardship activities, ensuring that our proxy voting and engagement activities are transparent and a matter of public record.

During the course of 2019 we conducted 358 engagements. We cast votes at 10,432 company meetings, voting on a total of 104,372 resolutions. All these activities were global in nature. As our engagement case studies highlight, in many cases our dialogues and sharing of best practice are influencing corporate behavior and we are starting to see a number of positive outcomes.

For many of our clients, climate considerations are one of their primary ESG concerns, which is why we devote considerable time and expertise so they have the tools and products which can help them align their investments towards a climate-smart future. In 2018 we established a strategic climate engagement program to underpin those efforts and help us better understand and influence companies' climate commitments. We are pleased to see several of those engagements demonstrate encouraging progress.

Of course, climate is just one of many topics on which we engage. During the course of 2019, other engagement topics included governance, remuneration and business models. As this report demonstrates, our engagements are closely tied to our assessment of ESG risks and opportunities, thereby deepening the integration of ESG factors within our investment process.

2019 also saw the further development of our relationships with several collaborative partners and sustainable investing initiatives, most notably, Climate Action 100+ (CA 100+), the investor initiative formed in 2017 to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. Throughout the year UBS AM engaged with a range of companies through the CA100+ coalition and in seven cases we were engagement lead.

This report sets out our Stewardship activities during 2019. It aims to be widely (or generally) aligned with the reporting requirements of the new UK Stewardship code. As well as providing insight to our engagement and proxy voting activities we also report on progress made. As in previous years we welcome all feedback from clients and stakeholders.

**Barry Gill**

Head of Investments  
UBS Asset Management

**Michael Baldinger**

Global Head, Sustainable & Impact Investing  
UBS Asset Management

# Our approach to stewardship

We regard stewardship as an integral part of our fiduciary duty and investment process. Our aim is to align our stewardship approach with clients' investment beliefs, policies and requirements. We're committed to taking an active approach through a clear and structured program which encompasses the integration of ESG factors into four strongly interlinked activities:

- Investment decision making
- Engagement with corporate management
- Exercise of shareholders rights, and
- Advocacy with policy makers and standard setters

We believe that managing both active and passive strategies brings a number of synergies to our stewardship approach. Active strategies can benefit from the increased exposure to companies generated by passive strategies. This in turn can lead to stronger corporate access and a greater ability to influence management. Meanwhile, the in-depth knowledge of expert financial analysts with sector expertise, and their relationships with corporate management, can benefit passive strategies.

This report sets out our stewardship program in detail. It covers three key aspects:

- The importance of stewardship for both active and passive strategies, across asset classes
- The ways in which our stewardship activities are conducted
- An evaluation of progress made during 2019

We start with a brief description of engagement and proxy voting – the key constituents of our stewardship approach.

## **Corporate engagement: encouraging dialogue**

Corporate engagement implies a two-way dialogue between investors and companies. Its objective: to enhance information and improve business performance, both in terms of ESG issues and strategy, risk management and capital allocation. Investors can share their expectations of corporate management and encourage practices which could enhance long-term value. Companies, meanwhile, can explain the relationship between sustainability, their business model and financial performance.

In our view, it is this two-way dialogue which defines engagement. Simply asking companies questions without providing feedback and encouraging improvements would not be classified as an engagement.

A number of factors determine which companies in our invested universe would be prioritized for in-depth research and dialogue. These include:

- High financial exposure
- Presence of high ESG risks and opportunities
- History of votes against management
- Performance on topics selected for thematic programs
- Presence of strong controversies

### **Proxy Voting: The value of the vote**

Voting at shareholder meetings is a vital component of our overall approach to the effective stewardship of our clients' assets. Voting isn't an end in itself, but rather a crucial element of our oversight role. It allows us to voice our opinion to a company on a broad range of topics and is a way of encouraging boards to listen to and address investor concerns.

It is important that proxy voting is linked to our research and investment process. If holdings are included in more than one portfolio then we aim, as far as possible, to vote consistently to send one strong, unified message to our investee companies.

We also use voting to complement and support our engagement activities. In situations when our engagement dialogue is not bringing the results we'd expected, we'll escalate and use voting as an additional means of expressing our opinion and seeking to influence boards and management. In circumstances such as these, it is essential to communicate effectively with management pre- and post-vote to explain the reasons for our dissent and to open the doors for further dialogue.

## Stewardship codes we adhere to

We're signatories to several stewardship codes of best practice.

These include:

- The International Corporate Governance Network (ICGN) Global Stewardship Principles
- The UK and Japanese Stewardship codes

We also support the Securities and Futures Commission of Hong Kong Principles of Responsible Ownership, the investor-led Investor Stewardship Group Stewardship Framework in the USA and meet the requirements of the Australian Financial Services Council Standard 23 on Principles of Internal Governance and Asset Stewardship.

# Investment decision making

## **Stewardship: the active strategy perspective**

Fundamentally, ESG integration is driven by a focus on taking better account of material risks which could enhance investment returns, rather than being driven by ethical principles or norms. Put simply, ESG integration involves a more holistic accounting of sustainability factors in the research process. We believe this leads to better informed investment decisions which could, in turn, reduce risk and enhance performance.

At UBS Asset Management the integration of sustainability is oriented around the ESG Material Issues framework developed by our Sustainable and Impact research team to facilitate the integration process. Sustainability covers a wide range of topics, so financial analysts and portfolio managers need to focus their attention on a limited set of factors that could affect a company's financial performance. The ESG Material Issues framework identifies the 3 to 5 most financially relevant factors per sector that can impact the investment thesis across 32 different industry sectors. This helps analysts focus on those sustainability factors most likely to influence investment returns.

## **Identify**

To facilitate the integration of sustainability factors through the assessment of material ESG risks, UBS AM has developed a proprietary "ESG Risk Dashboard". By combining scores and data points from our own proprietary ESG database with those from a number of the most reputable external research providers it flags companies with elevated sustainability risks. Although the methodologies of ESG ratings providers vary, consistently low scores across providers can be an efficient way to identify companies with severe ESG risks. Those companies will need more work to assess the material impact of the highlighted risks. While conducting ESG risk assessments, it's also important to consider not only performance scores but also underlying absolute signals of ESG risk - for example, poor corporate governance and elevated ESG controversy levels. This can help identify companies with significant ESG risks across portfolios.

## **Review**

While the UBS AM ESG Risk Dashboard is designed to flag companies with elevated sustainability risks, the actual assessment of these risks is conducted by the fundamental equity analyst or portfolio manager working with members of the sustainable investment research team. For companies where the equity analyst or portfolio manager disagree with the risk signal, a second level of analysis is conducted by the sustainable investment research analysts to provide an additional assessment of the ESG risk, as well as the potential to actively engage management to mitigate the risk.

## **Decide**

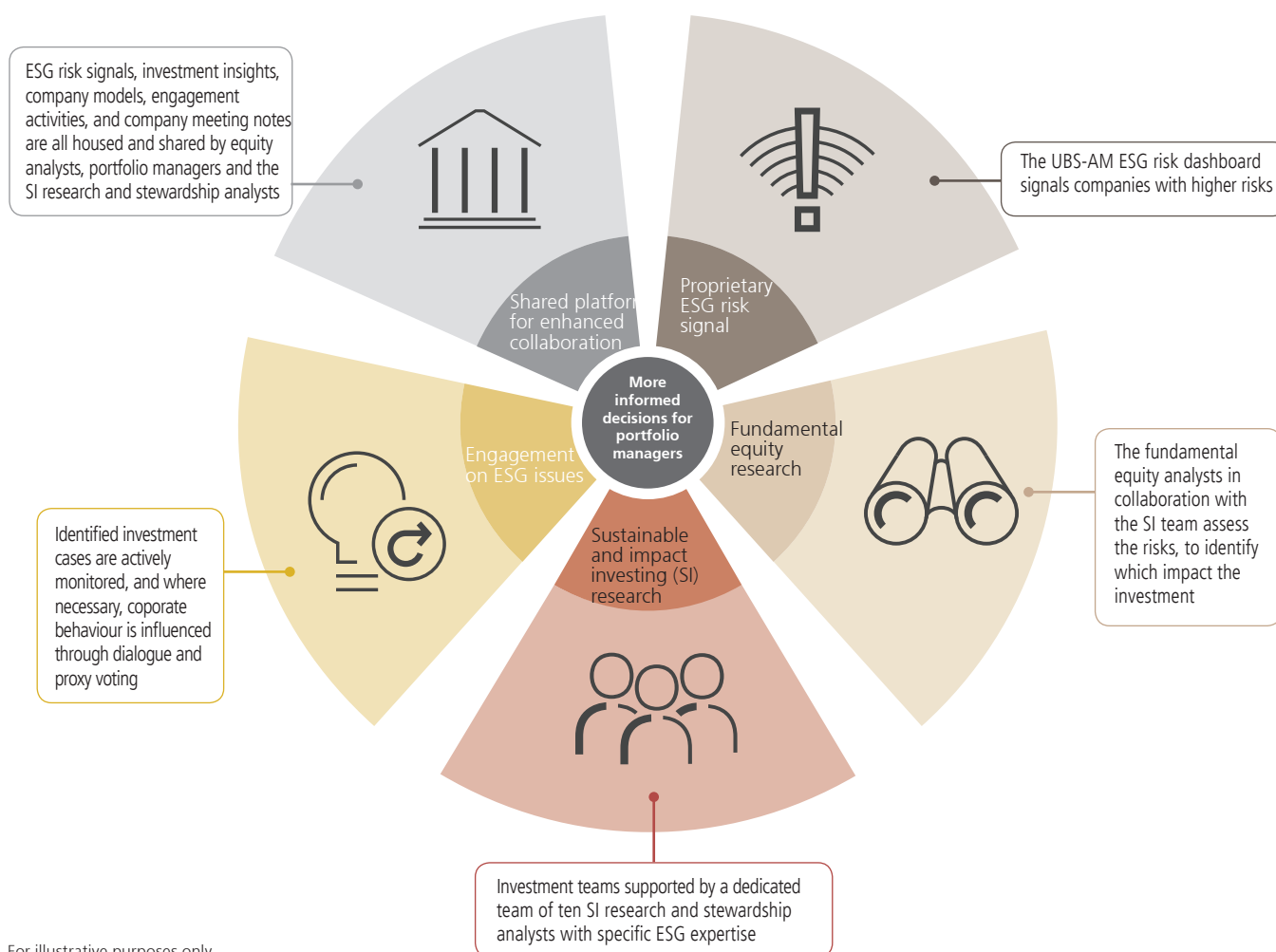
The portfolio manager may still choose to invest in a stock flagged for severe ESG risks, but only if they believe the upside potential outweighs the risks identified. If potential for improvement through engagement has been highlighted, the portfolio manager may decide that engaging with management on the identified risks represents the best strategy, and could be linked to potential upside in the share price if those risks are mitigated.

## **Engage and collaborate**

If, having assessed the ESG risks, engagement is identified as a next step, the company engagement will be led by investment analysts, portfolio managers, or members of the sustainable investing team. Irrespective of who conducts the engagement, the approach will always be the same. This ensures a unique and consistent voice from our firm.

Dialogues with corporate management are conducted around specific issues related to the business strategy, capital allocation, operational management and/or ESG risks and opportunities that might positively or substantially have impacted valuation models. The goal of these interactions is to collect more information and influence corporate practices in order to trigger better financial performance in the long term (i.e., reduce risks and unlock alpha).

**Integration and stewardship: an intrinsic part of the investment decision making process in active strategies**



**Stewardship: a passive strategy perspective**

For passive strategies, stewardship activities often represent one of the most significant ways in which institutional investors can express their views on and influence company performance. It offers a way of addressing broader negative externalities to the economy which in turn could cause instability and inefficiencies within the financial markets and global portfolios.

In this context, we believe that dialogue with investee companies is essential to raise awareness and influence corporate conduct on matters such as bribery and corruption, climate change, inequality or human capital management.

As analysts or portfolio managers might not follow these companies closely, the importance of proxy voting and engagement in passive strategies is even greater, as our ability to relay our views on a company’s conduct may be limited otherwise.

In the case of those passive strategies that track sustainability indexes or apply a rules-based approach, stewardship activities can also have further impacts. Dialogue can sometimes incentivize companies to improve in order to be included in selected ESG indexes. It can also provide meaningful insights to enhance the methodologies applied in tilted approaches that consider ESG factors to inform underweights/overweights.

The role of engagement in tilted methodologies is clearly illustrated by our Climate Aware strategy, which overweights those companies in the index making the greatest progress towards a lower carbon world and underweights the laggards. As Ian Ashment, Head of Systematic and Index Investing at UBS AM commented, "Our Climate Aware engagement program allows us to deliver a clear message to those companies we're invested in: we expect them to be aligning their business to a lower carbon world. The insights we derive from our engagements are also crucial in helping us better understand the rate of progress being made by companies towards the goals of the Paris Agreement."

# Engagements: a multi-faceted approach

## **Thematic engagements**

These are engagements that are focused on specific themes considered material, analyzed by available internal and external research and aligned with the overall sustainability and sustainable investment strategy of the firm.

UBS AM runs multi-year thematic engagement program across both active and passive investments. Their focus is usually identified by:

- Taking into consideration the current performance of companies on the relevant topic
- Sectors where the issue has a high relevance, and,
- The potential for influence

The in-depth research supporting our thematic engagements is used to assess the performance of companies at the beginning and end of the engagement program.

## **Ongoing thematic engagements**

### *Climate change:*

The engagement focuses on 49 companies in the oil and gas and utilities sectors. They have been selected based on our Climate Aware methodology, which measures the ability of companies to transition to a low-carbon economy. This engagement dialogue started in 2018 and will run over three years.

It's supported by in-depth research on climate change provided by the SI team which relates to:

- Governance and oversight of climate risks
- Risk management
- Scenario analysis
- Metrics and performance
- Lobbying activities

The program is aligned with the Taskforce on Climate-related Financial Disclosure (TCFD) recommendations. More information is available on the dedicated section on stewardship in practice.

### *Gender:*

The focus is on companies showing some good practice but which also display areas for improvement. Our initial assessment has been informed by the analysis from the service provider Equileap on 19 diversity criteria, including:

- Equal compensation and work-life balance,
- Transparency and accountability,
- Gender balance
- Sustainability policies

Companies selected belong to sectors where gender diversity is material and statistically linked to financial performance. These include:

- Pharmaceuticals,
- Consumer discretionary,
- Commercial services
- IT
- Financial

### *Impact:*

In 2017, UBS AM launched a Global Engage for Impact Equity strategy. The strategy has an explicit goal: to create positive environmental and social impact while generating competitive financial returns that connect to, and support, the United Nations' Sustainable Development Goals (SDGs).

The impact engagement program draws on an innovative research collaboration which UBS AM has established with several leading universities to develop a standard for reporting on a set of impact measurement indicators.



Engagements with companies in our impact strategies help management understand the effects which their supply chain, direct operations, and final products and services have on the environment and society. In addition, the engagements aim to support companies orient towards business opportunities in connection with the UN SDGs, in particular the ones linked to climate change and air pollution, clean water and water scarcity, treatment of disease, food security and poverty alleviation.

All 17 SDGs are interconnected. However, we found that while some can be addressed through products and services (SDG 1,2,3,4,6, 7,9,11,12, 14 and 15) others can, and in our view, should, only be addressed through corporate conduct (SDG 5,8,10, 13, 16 and 17). In creating our investment universe for impact strategies, we focus on companies that impact the SDGs through products and services (with at least 20% of revenues). But when it comes to engagement, we address all 17 of the SDGs.

## Controversies

A subset of our engagement cases focus on companies that are involved in serious breaches of international standards. The United National Global Compact (UNGC) Principles are accepted as the general reference framework to define cases of concern and we have developed a process using third party research to identify red flags across portfolios and strategies.

After an initial screening, we take into account:

- Public reporting on the case
- Communications by the company involved
- Reports from NGOs and other third parties
- Results of investigations by other investors, where available.

Our engagement list includes cases that are material, relevant, or represent systemic management failure. More information on these cases is available in the sections detailing our engagement statistics and stewardship in practice.

# Stewardship: its relevance beyond listed equity

The prioritization of stewardship activities often starts with a review of our listed equity holdings. However, our dialogue with corporate management covers other asset classes as well.

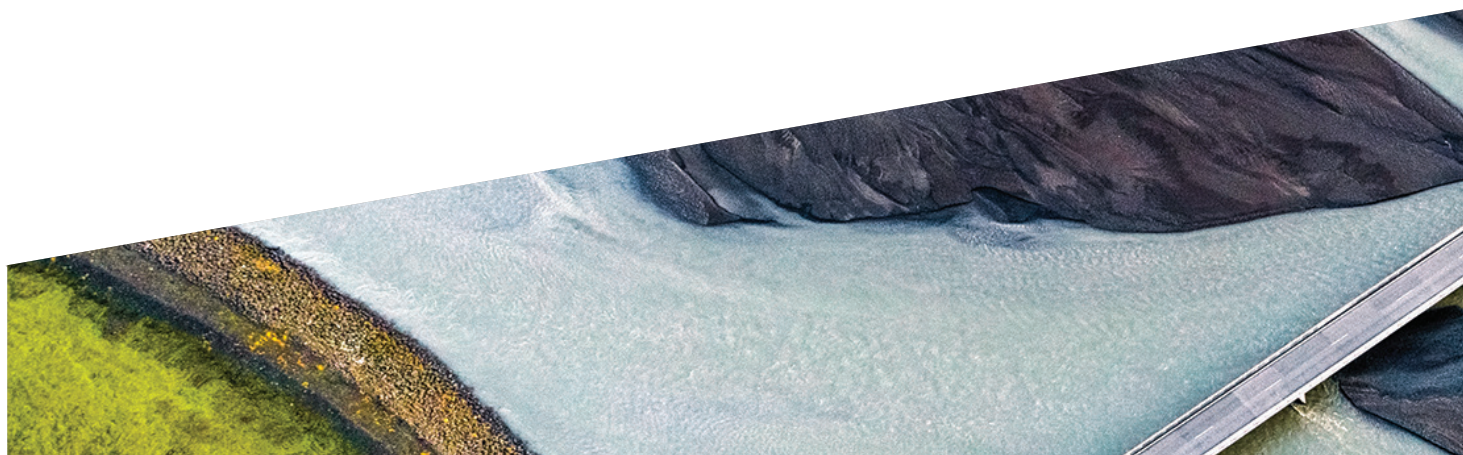
## **A Real Estate perspective**

Our Real Estate and Private Markets' (REPM) responsible investment strategy has been developed by the REPM Sustainability Workgroup. It comprises professionals from several countries and disciplines, ranging from engineering and construction, through to investment and business management. It sets strategies and objectives at a global level and ensures our sustainability objectives are appropriately integrated into REPM's investment strategies and property operations, in accordance with regional requirements.

The responsible investment strategy is implemented by all operational functions during the entire ownership cycle of an underlying project. Objectives are set in order to make achievements transparent and measurable. Performance is measured against objectives and results are reported to

investors, clients and consultants. For individual properties, sustainability performance is measured against recognized external benchmarks, such as the GRESB key performance indicators and third-party certifications (LEED, ENERGY STAR, BREEAM, MINERGIE®). Infrastructure also utilizes the GRESB Infrastructure key performance indicators and benchmark reports for individual investee companies. This helps define specific measures to enhance the performance of each property or infrastructure asset and guide dialogue with management.

When our alternative assets team invest in listed real estate companies, our proxy voting policy applies and we regularly exercise our shareholders' voting rights. If the listed equity financial analyst or SI analyst led engagements focus on real estate companies, we may also share information and coordinate our efforts in the dialogue with corporate management.

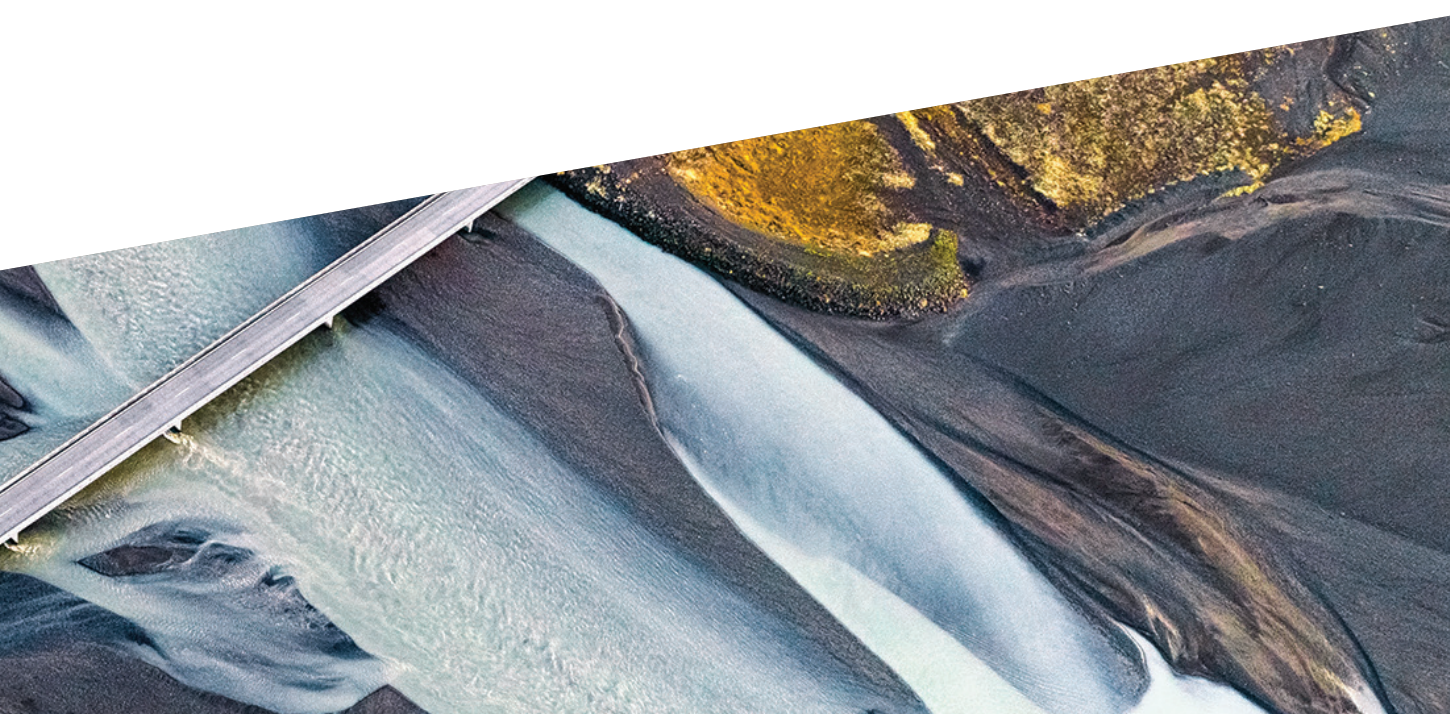


### **A fixed income perspective**

All credit recommendations by the credit research teams address the most material sustainability strengths and weaknesses of the issuer. They also assess the anticipated direction of sustainability performance in the future, as well as the material impact, positive or negative, of sustainability considerations on their fundamental credit recommendations. Through this assessment, credit analysts provide a proprietary UBS sustainability credit assessment for the issues that they cover. These offer an integrated view of the company's sustainability performance from a credit perspective. This bottom-up research is supplemented by regular top-down views of sustainability risks from the sustainable investment research team to help assess the impact of sustainability issues on sectors and individual issuers.

Fixed income has an asymmetric return profile which focuses on understanding downside risks. Engagement with corporate issuers can deepen the understanding of factors, including ESG issues, that could affect potential spread widening and default. It complements shareholder engagement and can reinforce improved practice amongst companies we invest in.

The majority of our thematic- and controversies-led engagements, and a high percentage of dialogues led by the SI team and/or listed equity team, are open to our fixed income analysts. Research and meeting notes are also systematically shared with fixed income analysts and portfolio managers. In 2019, we saw a greater number of engagements conducted by a combination of representatives from SI, listed equity and fixed income teams.



# Our top down research

Research and stewardship are intertwined with the investment process. By conducting rigorous top-down research our analysis helps us to identify leaders and laggards.

In turn, that same process also generates a set of questions which both SI and fundamental analysts can raise with companies during the engagement process to further deepen their understanding and identify areas where they might seek to influence change. The following case studies illustrate this top down approach in the context of climate change physical risks and cyber security.

## Why?

### **Gauging the effects of climate change risk: implications for the financial sector**

Why should investors consider the physical risks of climate change? The Intergovernmental Panel on Climate Change (IPCC) defines these risks as:

"... the interaction of the evolving exposure and vulnerability of human, socioeconomic, and biological systems with changing physical characteristics of the climate system."

The impacts of climate risks are starting to be felt by companies, so clearly they matter to investors. While the impacts of climate change risks don't apply equally across all sectors, for the financial sector generally, those risks matter. Thinking about insurance for example, we see the insurers as bearing the primary risk arising from climate change. For them it represents an existing risk. Meanwhile, for issuers who are uninsured against the possible consequences climate change represents an emerging risk. This ultimately leads to increased stress on the economy and financial system from reduced property values, household wealth and corporate profits.

In 2019, we evaluated preparedness across 50 insurers, creating a score-card in order to understand which ones:

- Have time horizons matching the IPCC framework
- Are adapting their modelling and scenario analysis to incorporate climate change
- Are investing in technology to better understand exposure risk i.e., flood scenarios, and
- Have created a range of solutions to help protect clients from the impact of physical risk.

Only ten insurers scored well across most categories, but as a result of this exercise we can now engage in a systematic way with insurers using our score-card methodology.

We performed a similar exercise across the banking sector, focusing on disclosure using:

- The TCFD framework
- Board-level commitment
- Integration of climate risk management

We found that of 185 banks only 20 scored well across these three categories. Given our growing concerns, climate is a topic with which we're increasingly engaging with companies.

# How?

## **How to assess data security risks in the investment process?**

A thematic case study

Recent cyber attacks have affected a number of sectors, from banks to web service providers, highlighting the fact that these are a key risk for companies. Clearly, this matters to investors. In 2019, we worked to analyze our holdings' exposure to this topic, with a focus on fixed income assets and the implications for downside risk.

We look at cyber security from a business risk perspective. We don't need to be IT experts to form a view on a company's ability to mitigate and manage the issue. While some knowledge of core cyber-related aspects is required, it needs to be put into context of the company's business and growth strategy, as well as corporate governance practices.

To bridge the existing disclosure gap and lack of standards around cyber security reporting, we developed a 5-step framework for our investment teams to assess and engage companies on the topic, combining external data with in-house research and company dialogue. This helped us better understand:

- The long-term compliance costs likely to be incurred by investees to meet increasing regulatory expectations
- Their resilience to cyber attacks, and
- Their ability to recover in case of a data incident.

While there's no crystal ball to forecast the next massive data breach, we've developed a view on companies' business risk management systems and their ability to mitigate and handle threats. Our analysis has also focused on key engagement questions to raise with management to better understand companies' preparedness and risk management tools in case of material incidents.

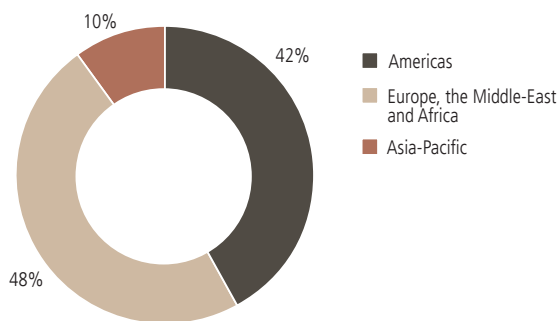
# Engagement with corporate management

## How we engage: our engagement activities

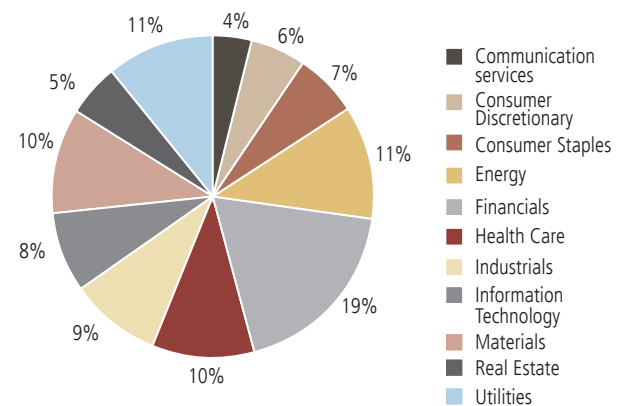
Our aim is to build relationships with company management to foster healthy dialogue and enhance performance on a variety of issues.

During 2019, we held over 1400 meetings with prospective or investee companies. Of these, 358 met our definition of engagement. Approximately one third of those meetings were thematic and 19 were focused on UNGC violations. They covered 231 companies across regions and sectors. The majority had global operations and supply chains but were headquartered in developed markets.

## Location of companies engaged in 2019



## Sectors of companies engaged in 2019



In 2019, we introduced an enhanced internal tracking system to assess the progress of dialogue against defined engagement objectives. 23% of our company engagements showed progress against identified areas for improvements to manage risks and take advantage of new opportunities. As this is a new metric (this report marks the first time we have been able to disclose it) and for some of our engagements formalized engagement objectives have only recently been introduced, we expect future reporting to record increased numbers in terms of engagement progress.

In relation to proxy voting decisions, almost one third of our engagements provided useful and tangible insights.

We engage with companies individually and in collaboration with other investors. Collaborating with peers help us convey one consistent message to companies on systemic issues which could severely impact financial markets (i.e., climate change). 13% of our 2019 engagements were collaborative.

52% of our engagement meetings were held with the CEO/CFO or another C-suite representative. In approximately 34% of cases we met the Chair or an independent Board member. 31% of our engagement meetings were conducted with an ESG expert, such as the head of the sustainability department.

### Topics addressed during our engagements

Our dialogue with companies covered a wide range of topics as the chart below illustrates. A large proportion of the engagements focused on governance, remuneration, business strategy and capital management.

One engagement meeting will likely address more than one topic. In total we held 358 engagements in 2019. The chart to the right shows the frequency with which a given topic was discussed.

#### Level of access to companies during 2019

Level of representation	Number of meetings	Percentage on the total
CEO/CFO and Other C-Suite	187	52%
Chair and Non- Executive board members	120	34%
Corporate secretary or legal counsel	50	14%
IR	279	78%
ESG expert	105	29%
Other	39	11%
<b>Total engagements</b>	<b>358</b>	

The table tracks the number of meetings in which a topic has been raised. In the same meetings multiple topics can be raised. The total meetings are an absolute number and not the sum of single rows. The percentage calculates how many times a topic has been raised out of the total engagement meetings

Topics	Number of engagement meetings in which the topic was discussed	Number of meetings in which the topic was expressed as a percentage of total meetings held
Corporate Governance	191	53%
Strategy & Business Model	150	42%
Remuneration	138	39%
Environmental Management & Climate Change	133	37%
Transparency & Disclosure	107	30%
Business Conduct & Culture	81	23%
Capital Management	82	23%
Human Capital Management & Labor Standards	63	18%
Operational Management	57	16%
Community Impact & Human Rights	28	8%
Audit & Accounting	26	7%
<b>Total number of engagement meetings held</b>	<b>358</b>	

The table tracks the number of meetings in which a type of company representative has been met. In the same meetings multiple company representatives can be present. The total meetings are an absolute number and not the sum of single rows. The percentage calculates how many times a company representative has been met out of the total engagement meetings.

# Exercise of shareholders' rights

## Our proxy voting activities and trends from the last proxy voting season

Our proxy voting process is supported by a third party proxy advisor, who is responsible for issuing voting recommendations based on our internal proxy voting policy. Having a customized policy allows us to develop and update our expectations of companies on a regular basis, across a range of material topics presented at annual general meetings (AGM).

During 2019, we voted in over 10,000 meetings and on more than 100,000 resolutions. Overall, we voted against management in 17% of the cases. In the case of North America more specifically, this percentage increased to 26% of resolutions. In 66.5% of the meetings there was at least one resolution with a vote against. In 33% of the meetings we voted with management on all proposals. We voted against management on 860 occasions because of a lack of gender diversity as measured against our defined thresholds by markets.

The most common reasons for voting against management were related to:

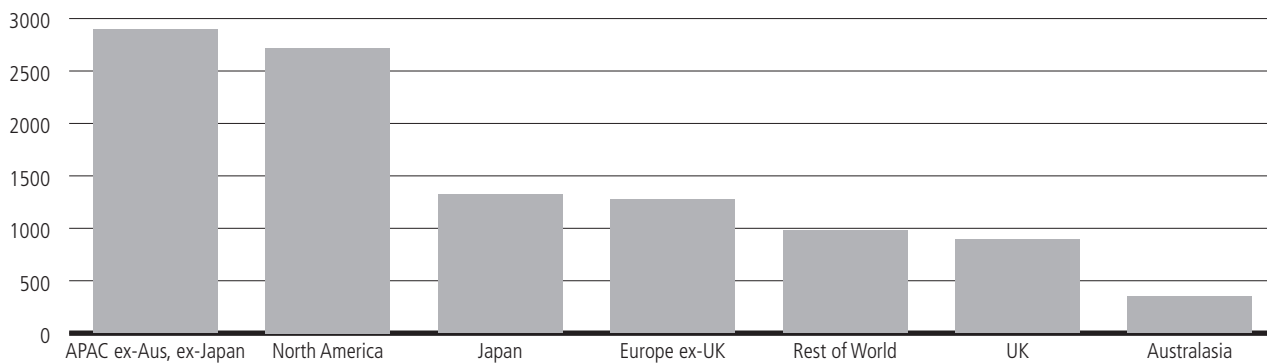
- The level of board independence falling below our policy's threshold
- Inadequate link between remuneration structure and financial performance
- Election of board's directors, including independence considerations
- Share issuance without pre-emptive rights
- Audit company tenure in excess of 20 years
- Independence of audit committee
- Lack of sufficient disclosure to allow for informed voting decisions

Region	Total number of meetings voted	Total number of resolutions	Total number of resolutions voted WITH management	Total number of resolutions voted AGAINST management	Total number of resolutions ABSTAINED <sup>1</sup>	Total number of resolutions where vote WITHHELD	% votes against management per region
APAC ex-Aus, ex-Japan	2895	23597	19753	3844	129	77	16.3%
North America	2721	24809	18308	6501	28	2010	26.2%
Japan	1323	14969	13100	1869	2	0	12.5%
Europe ex-UK	1276	16856	14040	2816	181	1	16.7%
Rest of World	977	10224	8276	1948	139	24	19.1%
UK	891	12125	11353	772	21	0	6.4%
Australasia	349	1792	1451	341	1	0	19%
<b>Total</b>	<b>10,432</b>	<b>104,372</b>	<b>86,281</b>	<b>18,091</b>	<b>501</b>	<b>2,112</b>	<b>17%</b>

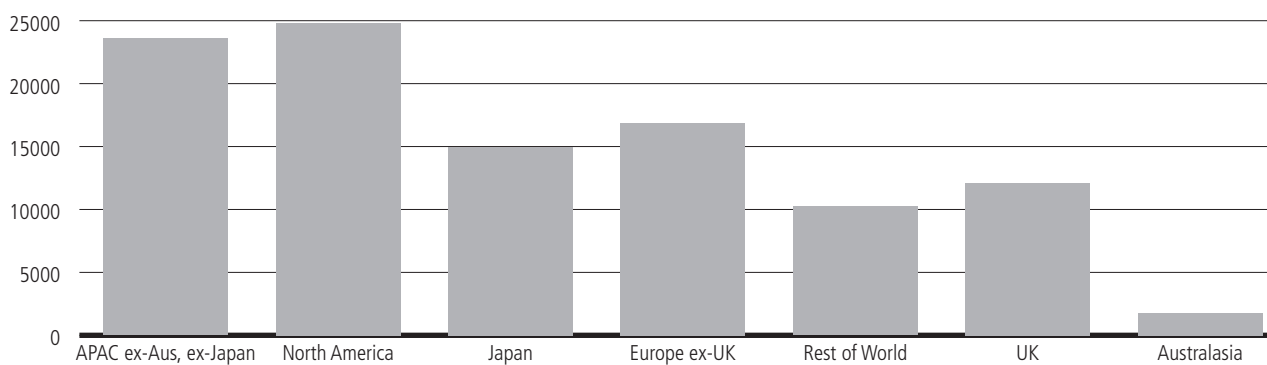
<sup>1</sup> Votes against management also include votes abstained and withheld



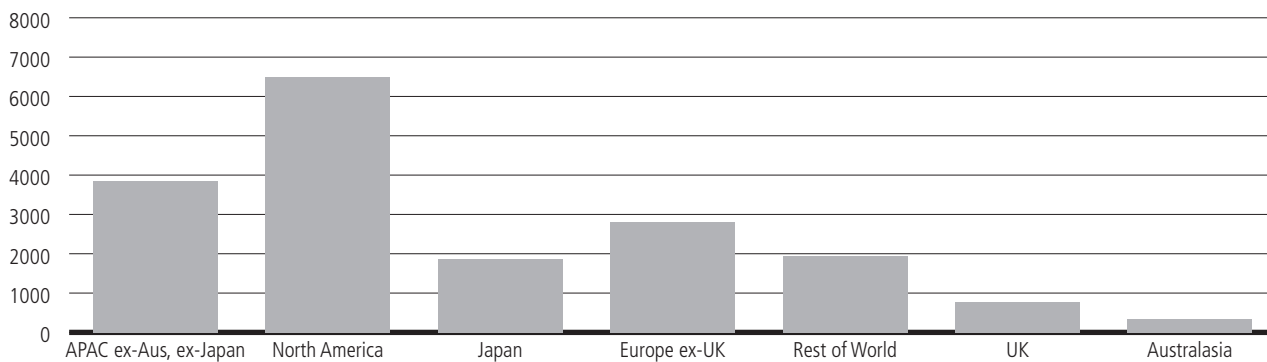
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**Meetings voted**

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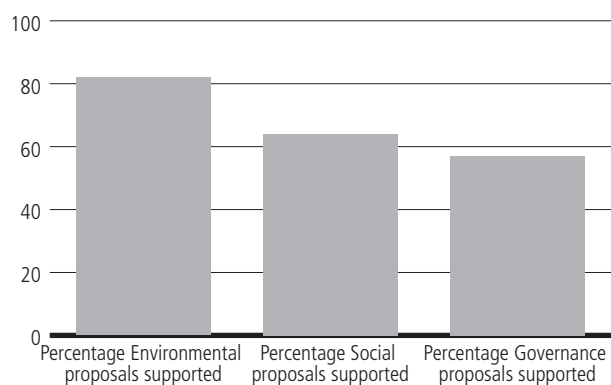
**Resolutions voted**

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**Votes against management**

In 2019 we voted on over 780 shareholder resolutions which were focused on ESG issues, supporting 60% of them. More specifically, we supported 82% of shareholder resolutions focused on environmental issues. Generally, we have not supported resolutions that were too prescriptive in nature, didn't address material issues, or which asked companies to introduce policies and practices that had already been adequately addressed.

**Our voting on ESG shareholder proposals in 2019**



**Conflicts of Interest**

In the context of the implementation of our proxy voting policy, the application of our discretion resulted in votes contrary to our policy's recommendations in just 0.35% of cases. This represented 363 resolutions out of a total of more than 104,000.

We identified a potential conflict of interest for 180 meetings. As per our guidelines, where we identify a conflict of interest we vote strictly in line with our proxy voting policy. Such votes have been overseen by our Stewardship Committee.

**Stock lending**

Stock lending can be beneficial to a fund by providing an additional income stream, and to the market by providing liquidity. Many of our funds include the provision for stocklending, with a limit of the percentage of a fund which can be used for lending purposes at any one time. The income derived from this is invested back into the funds.

However we recognize that voting rights linked to equity positions are not retained by the lending party and move under the control of the borrower. Through our voting process, when we judge a vote to be particularly contentious, or where we believe it is in our client's best interests to do so, we will look to recall stock out on loan for our collective investment schemes. This is generally in exceptional cases and not for all positions. We do not borrow shares for the purpose of gaining additional voting rights.

Regarding reasons for recall in 2019 linked to voting, we recalled for the following issuers:

- Sunrise Communications Group AG – Concerns regarding shareholder proposal to remove specific members of board of directors
- Debenhams plc – Concerns regarding financial stability of company and proposals made by majority shareholder
- BP plc – To enable the co-filing of a shareholder resolution

**UBS AM recognized for its leadership in climate change voting**

In 2019, UBS AM was highly ranked by two external bodies in relation to our engagement and proxy voting activities on climate change. In its report "Voting Matters" ShareAction ranked UBS AM Number 1 for voting on climate change resolutions. We supported over 90% of the resolutions in the study, based on voting data compiled from:

- Proxy Insight (September 2019)
- Individual investors
- Publicly available information

The study covered the world's largest asset managers by AUM according to IPE's ranking of the top 400 asset managers globally. The analysis considered:

- Climate change resolutions filed at S&P 500 companies
- Resolutions originated by CA100+ lead investors
- ExxonMobil resolutions which CA100+ lead investors were seeking votes for
- A selection of climate resolutions filed by civil society organizations between October 2018 and September 2019.

Shortly afterwards, InfluenceMap included UBS AM amongst the leaders (band A) in its study "Asset Managers and Climate Change". The report assessed the extent to which large asset managers conducted engagement with companies with the goals of accelerating the individual corporate transitions to low carbon technologies and encouraging companies to align their policy lobbying in line with the aims of the Paris Agreement. Their research analyzed public information about the engagement and proxy voting activities of the top 15 global asset managers, plus the asset management arms of BNP Paribas and Aviva.

# Stewardship in practice

## Engagement case studies



**Sector:** Financials  
**Region:** Europe  
**Topics addressed:** Corporate Governance, Business Conduct & Culture

### Engagement

The company flagged in the UBS ESG Risk Dashboard for governance risk related to the regulatory compliance and Board misconduct on the part of the CEO. Shareholder discontent has been growing, and the company has been targeted by activists holding a 5.5% stake. The fundamental analyst believes management is doing a good job in turning around the bank and expects it to deliver close to 10% return on equity (ROE) by 2020. However, performance has been hampered by reputational, litigation and cultural issues which have undermined productivity and the ability to attract and retain talent. Given these factors, the bank was selected for engagement.

### Outcome

Portfolio managers, the financial analyst and SI analyst met with the activist shareholder and Chair-elect. They concluded to support the new Chair at the AGM, given the commitment to address culture, conduct issues, talent retention and thereby improve profitability. We're actively monitoring progress through engagement as the new Chair is open to dialogue and understands that speed of change is important.



**Sector:** Industrials  
**Region:** Europe  
**Topics addressed:** Strategy & Business Model  
Corporate Governance

### Engagement

This transportation company was targeted by activist investors seeking to remove six current Directors and replace them with nominees recommended by the activists. We conducted due diligence with the CEO, Chair and Senior Independent Director of the company, and separately with the activists.

Our initial research showed that strategic plans for the company were at odds with creating the best shareholder value due to the focus on retaining the most cash generative part of the business. Hence we decided to engage with the firm. We recommended to management that pursuing the opposite strategy (selling the cash generative business and managing down the rest of the business) would be in the best interest of shareholders.

### Outcome

Based on the prevailing circumstances, we used our voting rights at the EGM and AGM to send a signal to management that we didn't support the proposed strategy or the strategy proposed by the activists. We voted to remove the current Chair, abstain on the entire Board and voted against all proposed activist nominees. After the AGM, the Chair agreed to stand down after 30% of investors voted against re-election. Ultimately, we decided to exit the position as we weren't convinced management could execute the proposed strategy in the best interest of shareholders and within a reasonable turnaround time.



**Sector:** Industrials  
**Region:** North America  
**Topics addressed:** Transparency & Disclosure

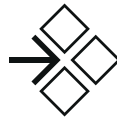
#### Engagement

This machinery company screened for elevated risks in the UBS ESG Risk Dashboard, driven by a lack of disclosure. The company has improved margins, working capital efficiency, sales leads and growth at a pace that is three times faster than peers. In addition, a strong management team is making cost improvements while expanding service capability. We determined that the company's appeal to investors could be enhanced through greater transparency on sustainability metrics and improvements in third-party ratings, so we entered into a dialogue with the company.

Specific issues we engaged with included human capital performance, given its material importance for the company's overall performance. We asked management to focus on greater disclosure on certain metrics.

#### Outcome

Going forward, we'll continue to monitor progress. Management has confirmed its commitment to greater levels of sustainability disclosure, which we believe will give investors a better insight to the quality of the company's management.



**Sector:** Consumer staples  
**Region:** Asia  
**Topics addressed:** Transparency & Disclosure, Environmental Management & Climate Change, Community Impact & Human Rights

#### Engagement

The company was selected for engagement due to:

- Insufficient ESG disclosure
- Lack of evidence about the reduction of corporate environmental footprint
- Lack of communication about its approach to premium products, including plant-based, low sugar, and organic products

Based on our initial research, we encouraged the company to use best practice frameworks for disclosure, take actions to reduce GHG emissions, establish a water and animal feed / treatment strategy, and increase information on initiatives to grow the share of healthy / premium products.

#### Outcome

Progress is proving positive. A lengthy engagement took place, where we explained the reasons and rationale for engaging and also shared expectations / recommendations for improvement (including sharing of best practice examples.) A follow-up was held following release of the new corporate social responsibility (CSR) report. We saw significant improvements around reporting. The company now uses the Global Reporting Initiative (GRI) framework and works with an external consultant to continue improving disclosure. It's also engaging with FAIRR on enhanced environmental practices. More information has been shared by the company on their strategy towards premium / more nutritious foods. We continue to engage to encourage the company to:

- Extend its water strategy to its suppliers
- Set carbon reduction targets for its suppliers.

## Engagement case studies (continued)



**Sector:** Healthcare

**Region:** Europe

**Topics addressed:** Transparency & Disclosure, Business Conduct & Culture, Corporate Governance

### Engagement

The company was selected for engagement due to insufficient ESG disclosure, especially with regards to anti-bribery and ethics policies, as well on the CEO's remuneration and tenure of Board members.

Good progress is being made on the dialogue. We held three engagements during 2019, meeting with the CEO, IR team and legal counsel. The company welcomed our input to enhance its disclosure to shareholders, including:

- Sharing of information on the various frameworks it could use for future reports going forward
- Sharing best practice examples from their peers.

### Outcome

The company committed to enhancing the quality of subsequent reports in line with best practice. We also discussed the importance of anti-bribery and ethics policies, including their implementation practices and disclosure. We regard such policies as important given the company works with large pharma partners to bring products to market (often relying upon equivalent policies from those partners). The company acknowledged the significance of the issue. We also encouraged the company to refresh the Board to ensure long-tenured members make space for new Board members. In addition, we encouraged the company to enhance disclosure on CEO pay. It was receptive on both issues. After the engagement we voted on the board structure and corporate remuneration in accordance with the insights collected through the dialogue with management.



**Sector:** Healthcare

**Region:** Asia

**Topics addressed:** Corporate Governance, Remuneration

### Engagement

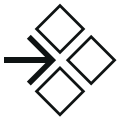
We engaged with this company on behalf of the Access to Medicine (AtM) Foundation (of which UBS AM is an active member). We also wanted to discuss the firm's response to significant shareholder dissent at their latest AGM and the development of its executive pay framework post its integration with a US based pharmaceutical company.

Based on our initial research we found the firm has made significant improvements to its AtM programs over recent years and ranked favorably in the Access to Medicine Index. However, we believe there are continued enhancements it could make to its strategy in order to optimize its access programs, hence our collaborative engagement on the topic. We also wanted to discuss concerns over the complexity, lack of transparency and potential size of pay outcomes. Additionally, we sought to clarify how executive remuneration would develop after the recent acquisition.

### Outcome

The dialogue is progressing well. The company is highly engaged with AtM and was open to explore further opportunities to optimize its practices. A follow up meeting is scheduled for next year, when the company will be able to inform us about progress made in relation to enhancements of its programs (i.e., equitable pricing strategies and planning for access).

On remuneration, the company's Board showed willingness to respond positively to the 2019 AGM votes, including the two shareholder proposals on executive pay. They committed to introduce a claw-back policy for all elements of executive pay. We notice less receptiveness on the simplification of the incentive framework and quality of disclosure. The key challenge for the company is to balance future pay practices in light of a very diverse workforce and shareholder base.



**Sector:** Consumer staples

**Region:** North America

**Topics addressed:** Transparency & Disclosure, Strategy and Business Model, Corporate Governance, Community Impact & Human Rights

### **Engagement**

The company was selected for engagement due to lack of ESG disclosure, concerns over its ability to adapt product offering to fast changing consumer preferences towards healthier products, and a lack of alignment for shareholders in remuneration strategy.

Following our initial research, we decided to engage with the company on the following topics:

- Disclosure around the reduction of its environmental footprint
- Tangible actions taken or planned to achieve the SDGs
- R&D efforts to focus on changes in consumer preferences towards sustainable and healthier products
- Appropriate severance pay, retention pay and returns for shareholders

We had two dialogues with the company last year including with their Global Head of Sustainability.

### **Outcome**

The company committed to include climate change targets aligned with the 2°C scenario in their next report. They also confirmed their enhanced focus towards transitioning to healthy and sustainable food products, as evidenced by their recent hire of a Chief Strategy and Transformation Officer. The company launched a 2019 impact report with enhanced information about contributions towards the SDGs. Furthermore, they agreed to work with us in the World Wide Generation pilot. Together with our Wealth Management colleagues, we participated in their G17Eco pilot - an initiative that aims to launch the first interoperable data platform for the public good and a global system solution to truly

accelerate financing and delivery of the SDGs. We introduced some of our portfolio companies to World Wide Generation pilot to test the G17Eco platform for the digital collection, aggregation and dissemination of trusted sustainability data between all stakeholders in the value chain. We will continue monitoring the initiative and contributing to it.

In the last AGM, we voted against the company remuneration. During the dialogue with us, the company committed to cap the Long Term Incentive Plan (LTIP) when Total Shareholder Return is negative, as well as to respond to significant shareholder concerns (including those of UBS). Going forward, awards upon appointment for new executive recruits will be performance-based. In the future, we would like to see executive pay linked to strategic corporate targets measured by sustainability key performance indicators (KPIs).

## Engagement case studies (continued)



**Sector:** Consumer staples

**Region:** Europe

**Topics addressed:** Business Conduct & Culture, Strategy & Business Model, Transparency & Disclosure, Human Capital Management & Labor Standards

### Engagement

Our initial research highlighted that while the company is a leader on sustainability, it is currently reshaping its strategy and we were keen to provide input. We also identified labor related controversies which we wanted to better understand.

### Outcome

In our first engagement dialogue, management was receptive and committed to share more information on setting sustainability targets and the process to link their economic and sustainability strategies. With regards to the labor relations issues, the company had recently experienced an employee strike which was encouraged by unions before negotiations had taken place. The outcome was a deal that the company had already budgeted / accounted for. Dialogue with management showed the strike was purely based on poor union planning. The company confirmed that they will continue working to strengthen labor relations and that they understood their importance to their success.



**Sector:** Consumer discretionary

**Region:** North America

**Topics addressed:** Strategy & Business Model, Corporate Governance, Remuneration

### Engagement

While we like the company's attractive North America business, we had increasing concerns around the performance of the European business and saw a case for simplification. Starting in the summer of 2018, SI and equity analysts undertook a targeted engagement program, holding repeated engagements with the CEO, Chair and Investor Relations, via in-person meetings and calls. These meetings were also followed up with a letter to the Chair to reiterate our position. Our message was that the opportunity to unlock shareholder value lies in improving returns and free cash, and a deeper infusion of operating talent from outside the industry will be necessary to achieve this. We also emphasized the need for Board refreshment, succession planning and a change in the compensation structure.

### Outcome

Improvements consistent with our engagement targets have been positive since the beginning of 2019, starting with a change in executive compensation by the addition of a free cash flow metric. Later in 2019, the Chair agreed to completely refresh the board by 2021. In the summer, the company brought in an external European COO, consistent with our request to introduce operating talent from outside the industry who was then promoted to European CEO after few months. In the last quarter, the company announced a major restructuring and free cash flow jumped to its highest level in several years as changes to incentive compensation began to flow through to the profit and loss (P&L).





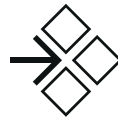
**Sector:** Consumer discretionary  
**Region:** North America  
**Topics addressed:** Transparency & Disclosure

#### **Engagement**

As one of the largest investors, we engaged the company on the disclosure of ESG information given management is planning to enhance sustainability reporting and make it more relevant to investors. We encouraged the company to understand how ESG topics are linked to metrics such as cost savings, customer service improvements, employee retention and operational excellence etc. For this sector in particular, we highlighted the relevance of human capital management and supply chain management as factors we consider critical for long term business success. We would also like to see more information on cyber-security risk management, given the firm's handling of sensitive consumer data. Lastly, we explained the importance of good corporate governance in our investment process and ESG assessment and invited the company to offer an annual investor dialogue with the Chairman.

#### **Outcome**

The company committed to set measurable goals to track progress and to focus on financially material topics, linking identified ESG themes to the overall business strategy.



**Sector:** Consumer staples  
**Region:** Europe  
**Topics addressed:** Corporate Governance, Remuneration, Strategy & Business Model

#### **Engagement**

The key causes for concern at this company were the strategic direction (including capital allocation) and succession planning for the Board Chair and CEO. We initially met with the non-executive Chair of the Board and the Chairs of the Audit and Remuneration committees at a collective investor meeting ahead of the 2019 AGM. We discussed issues related to the Company's strategy, succession planning and remuneration. The initial meeting was followed by a second collective meeting with the then newly-appointed Senior Independent Director (SID). During that meeting additional issues discussed included dividend policy, and expansion into new products were also covered.

#### **Outcome**

We recently met again with the SID, both in a 1:1 meeting and in collective meetings, to monitor progress and developments on the issues described above. While some progress has been made on succession planning, concerns remain over the strategy. These relate particularly to opportunities for reinvesting the resources generated by the established side of the business in growing but very competitive and resource-intensive products.

## Engagement case studies (continued)



**Sector:** Information Technology  
**Region:** North America  
**Topics addressed:** Remuneration

### Engagement

The company has a history of problematic executive remuneration practices. In 2017 its 'say-on-pay' vote was defeated at its AGM due to lack of alignment with long-term shareholder interest and poor evidence that pay was effectively linked to performance.

### Outcome

Following that failed vote, the company initiated an extensive engagement with shareholders (including UBS). This resulted in a number of improvements to its executive compensation framework. These included:

- Bringing the annual incentive performance period from two six-month periods to one year
- Extending the performance and vesting timeframes for performance shares under the LTIP from two to three years
- Capping payouts under the LTIP if absolute Total Shareholder Return is negative.

In light of the progress made, we supported the say-on-pay vote at the 2019 AGM. The company also made progress on Board diversity due to the appointment of two new female non-executive directors and succession planning in order to make the Board less long-tenured.



**Sector:** Healthcare  
**Region:** Europe  
**ESG topics addressed:** Corporate Governance, Capital Management

### Engagement

At the 2019 Extraordinary General Meeting (EGM), the Board sought shareholder approval for the authority to issue shares, with or without pre-emptive rights, by up to 20% of its issued share capital after developing a collaboration with a third party company. Even though the company stated that the proposed authority was related to the collaboration agreement, the call ahead of the General Meeting did not provide us with enough confidence on the management's decision.

### Outcome

We were concerned that the authority could be excessively dilutive and we voted against the proposal at the EGM. Overall, management failed to obtain support from over 20% of votes cast.



**Sector:** Industrials

**Region:** Europe

**ESG topics addressed:** Corporate Governance

#### **Engagement**

This transportation company had historic issues related to Board independence, lack of succession planning, problematic industrial relations and overall lack of responsiveness to investors' concern. The engagement with the company involved 1:1 calls with the management, meeting the Board together with other major UK institutional investors, and engaging with other stakeholders, such as trade unions. In 2019, after years of difficult conversations and little progress, the company showed some progress on governance standards, particularly in relation to Board independence and remuneration.

#### **Outcome**

The extensive engagement led to positive changes proposed at the 2019 AGM. These included a firm commitment to Board succession planning (both the long-tenured Chair and Senior Independent Director ('SID') will leave by the 2020 AGM), and an improved LTIP. Despite ongoing concerns over Board independence and, contrary to standard practice, the participation of Non-Executive Directors in stock-based awards, we considered it wasn't in the interests of the company and its shareholders to have a wholesale exit of Board members. We therefore decided to support the election of the designated SID and other non-executives with the exception of the Board Chair, the current Senior Independent Director and the Chairs of the Remuneration and Audit committees.



**Sector:** Materials

**Region:** Europe

**Topics addressed:** Business Conduct & Culture, Human Capital Management & Labor Standards, Community Impact & Human Rights

#### **Engagement**

The company was identified as a potentially interesting investment based on valuation but suffered from low external ESG ratings and a generally poor reputation amongst sustainability-focused investors. Having established that the three key ESG topics were ethical conduct, community relations and health and safety, the investment analysis identified that there was a link between all three in the form of the company's risk culture. The engagement has focused on this overarching topic as well as the individual issues.

#### **Outcome**

Change is clearly taking place in the company. In the last year we have seen new board appointments, a reorganization of the management team, a strengthening of environmental & social management and the compliance structure of the company. Going forward, we will encourage further developments on these fronts, as well as focusing on the need for improvements in health and safety.

## Engagement case studies (continued)



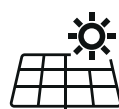
**Sector:** Materials  
**Region:** South America  
**ESG topics addressed:** Environmental Management & Climate Change, Community Impact & Human Rights

### Engagement

The company was identified for engagement as the result of a major environmental incident with many fatalities and significant impact on local communities. Our review identified the need to ensure that the company effectively responded and remedied the incident, communicated on its progress, and took action to ensure this could not happen again. Given that this also represented a repeat of an earlier, similar incident, it indicated deeper concerns with the internal governance and environmental risk management of the company. While we have been using a bilateral engagement approach, collaboration has also been an important and efficient means of contact.

### Outcome

The company has reported on its emergency response as well as significant changes to management personnel and structures. We continue to engage with a view to ensuring that the response to the incident is completed and that cultural and management changes ensure that the specific risks in these incidents have been eliminated. Given the significant reduction in market value that accompanied the announcement of the environmental incident, engagement has been an important means of understanding what investment direction to take with this company and to drive the right steps to improving the situation.



**Sector:** Energy  
**Region:** North America  
**Topics addressed:** Environmental Management & Climate Change, Corporate Governance

### Engagement

We decided to engage with the company given its large carbon footprint, lack of exposure to renewable energy and poor emissions reduction setting. After limited access to management and the company's decision to omit a shareholder resolution on climate target setting from the ballot, we decided not to support management on various proposals. In particular we withheld support for the re-election of the Chair of the Governance Committee. At the AGM we further supported a shareholder resolution focused on physical climate change risks. Since the AGM, we have held two meetings: one with the sustainability department regarding their recent climate change report and another with the CEO and two independent directors of the company in relation to the overall company strategy. Both meetings were helpful to understand the position of the company.

### Outcome

While the company is gradually aligning its climate report to the TCFD recommendations we believe that there are areas for improvements in future reporting/practices around using scenario analysis linked to a below 2°C scenario and setting GHG emissions targets connected to this analysis beyond methane emissions targets. There remains limited evidence or interest in testing the business model or setting of GHG emissions targets for the mid-long term. The company's disclosure in regards to climate change has improved, however we do not regard the company as being as advanced as its peers in setting ambitions aligned with the Paris agreement. Going forward we would expect the company to set intensity targets (beyond the upstream business), applying more aggressive scenario analysis and define their R&D/capex ambitions in relation to new technologies. Given current insights from this engagement dialogue and financial research on this stock, we have decided not to invest in this company in active equity strategies.



**Sector:** Industrials

**Region:** Europe

**Topics addressed:** Human Capital Management & Labor Standards, Remuneration

#### **Engagement**

We decided to engage with this company given our financial exposure, concerns on excessive pay and the presence of third parties' allegations on poor working conditions in developing countries. We met with the company's Vice CEO and head of CSR to discuss our analysis. While the company's financial performance has been strong, we believe that the level of quantum and vesting for CEO and Vice-CEO is too high compared to peers. The relationship with some trade unions is tense, based on allegations of poor practices across international operations. The company's disclosure on human rights has improved in the last two years. However, there is still limited evidence of a comprehensive human rights assessment and inclusion of a full range of stakeholders in the exercise. The overall gender performance of the company is positive, although female representation at senior management could be improved to better reflect the current workforce composition. During our dialogue with the company, we made reference to the detailed scorecard analysis provided by Equileap within our gender engagement program.

#### **Outcome**

At the end of 2019, the company had not addressed our concerns. So we will continue dialogue with management on these topics and we will meet company representatives before the next AGM to provide further feedback and inform our proxy voting decisions.



**Sector:** Healthcare

**Region:** Europe

**Topics addressed:** Business Conduct & Culture, Corporate Governance

#### **Engagement**

The company had experienced repeated business ethics controversies which not only hurt its reputation, but also resulted in high fines and negatively impacted its license to operate in some markets. However, following a change in leadership, we saw positive momentum for engagement. Cultural transformation has become a new strategic priority for the company. Considering the company's track record, we wanted to gain confidence in its commitment to transform business practices and create transparency on concrete measures taken to drive change, top down as well as bottom up. Since 2018, our equity and fixed income investment teams, together with the SI analyst, have had repeated dialogues with members of the Board (Chair, Remuneration Committee Chair), Executive Board (CEO, CFO, General Counsel, Chief Risk Officer) and Investor Relations.

#### **Outcome**

Despite a recent setback, we see the company making good overall progress to drive change, with a clear tone from the top. Organizational changes are creating an integrated risk, compliance and business ethics function, and various enhancements are being made in trainings and employee engagement. In addition, over the past few years, pay structure and disclosure have improved further which is positive. We have been encouraging in our ongoing dialogue and this has been reflected in our proxy voting decision-making process. While we see further opportunity for enhancements and continue to closely monitor the progress of cultural transformation and board refreshment, we're encouraged by the pace of progress and company's receptiveness to feedback thus far.

## Engagement case studies (continued)



**Sector:** Information Technology

**Region:** Europe

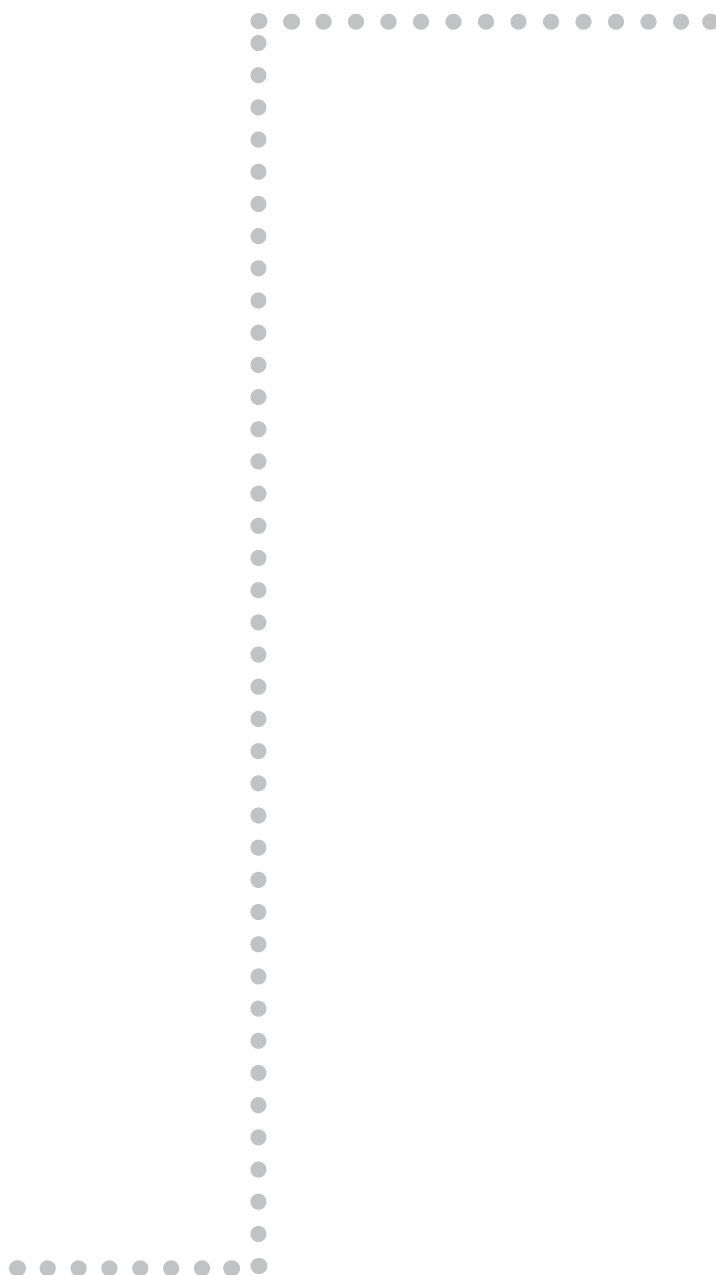
**Topics addressed:** Strategy & Business Model, Corporate Governance, Remuneration, Capital Management

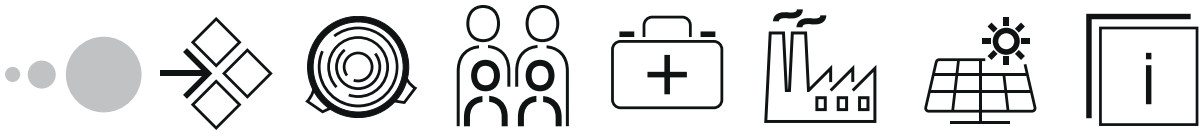
### Engagement

We've engaged with this software company since 2018 at Chair, Executive and Investor Relations level. The company is in a process of transformation, expanding into new business solutions, including via acquisitions. It has also been evolving its traditional license business model to one where subscriptions comprise a significant portion. These changes have recently been accompanied by succession at the Executive level. While overall ESG performance is considered robust, our engagement has focused on strategy and capital allocation, as well as corporate governance. Joint analysis by the SI analyst, fundamental analyst and PM teams identified potential risks linked to the executive compensation structure, the eventual succession of the co-founder and chairman and the potential changes on the Supervisory Board to ensure adequate management oversight to support the business transition and relevant capital allocation decisions. During our engagement dialogue the company provided more clarity on the chair succession plan and announced the election of a new Chair of the Audit committee.

### Outcome

As a result of this successful dialogue, we supported the re-election of the Co-founder/ Chair, and that of a long-tenured Director for a reduced term of three instead of the usual five years, with the aim of ensuring a healthy balance between new and experienced Board directors. Our dialogue with the Chairman after the announcement of the CEO changes, as well as a dedicated dialogue on the further evolution of the remuneration system to increase pay performance link, gave us further confidence in the company's oversight mechanisms and the investment case.









# Climate change engagement program:

In 2018, we launched a three-year engagement program on climate change. The objective of our dialogue with 49 oil & gas and utilities companies is to support the transition to a low carbon economy.

From the start of the program through to the end of 2019, we've organized 128 meetings with the companies in the focus list. 29 of the 49 target companies have been engaged collaboratively through Climate Action 100+ (CA100+). We're also leading an increased number of CA 100+ coalitions: seven in 2019, compared to five in 2018.

In-depth analysis on the companies in the focus list has been completed to assess:

- Alignment with the Taskforce on Climate-related Financial Disclosure (TCFD) recommendations
- Evidence of the Board's oversight of climate related risks and opportunities and integration in remuneration packages and board selection processes
- Evidence of integration of climate change in risk management
- Existence of scenario analysis and reflections on impact on the business model
- Disclosure on strategy and initiatives for reducing GHG emissions
- Disclosure of goals and progress to reduce normalized GHG emissions
- Ensure consistency of indirect and direct lobbying activities on climate change with the Paris Agreement

Based on this original assessment we've identified tailored engagement objectives for each company in the list. After more than eighteen months of dialogue with the companies, we have been able to assess progress against these objectives for 26 companies. For the remaining 23, we decided to coordinate at least another additional meeting with management before being able to assess the current level of responsiveness.

The table below summarizes our measure of progress in the engagement focus list so far:

Progress	Number of companies	Percentage
Limited (0-25% of objectives met)	7	27%
Some (25-50% of objectives met)	10	38%
Good (50-75% of objectives met)	4	15%
Excellent (75-100 of objectives met)	5	19%
<b>Total</b>	<b>26</b>	

As a reflection of these interim results, UBS AM has decided to include a new provision in the firm-wide proxy voting policy which, from 2020, allows us to vote against the board as a result of poor dialogue progress on climate change risks and opportunities.

## Examples of positive dialogue with companies on climate change



**Sector:** Oil & gas  
**Region:** Europe  
**Topics addressed:** Strategy

### Engagement

UBS AM has been engaging with the company within Climate Action 100+, alongside two other investment managers. The engagement has been focused on the company's strategy to transition to a low carbon economy.

### Outcome

During the course of the dialogue, the company took significant steps to meet shareholders' requests on climate change. These included the development of an intensity reduction target, including scope 1,2 and 3 emissions, and the increase of climate change targets linked to executive pay. Management is expanding low carbon energy activities and intends to increase its market share in gas and electricity distribution in its local market. At the end of 2019, the company committed to undertake a global review of lobbying activities by Q3 2020 and pursue positive lobbying dialogue on climate change. The company has also committed to net zero emissions by 2050 in alignment with the Paris Agreement, becoming the first oil & gas company to do so. Future dialogue will focus on actions which can deliver on these positive ambitions and enhanced information on scenario analysis.



**Sector:** Utilities  
**Region:** North America  
**Topics addressed:** Strategy

### Engagement

In 2019, we met with the CEO and CFO of the company as a follow up to an earlier meeting in 2018. We were impressed by the progress from the company over the last 12 months, including scenario analysis and targets aligned with below 2°C global warming, a first climate assessment report aligned with the TCFD expectations and increased uptake from consumers of energy efficiency programs.

### Outcome

In December 2019, the company announced a plan to reduce carbon emissions by over 90% by 2040 compared to 2005 levels. In addition, they've announced a target of net zero methane emissions for the company's gas delivery system by 2030. Financial performance has also been positive. Future conversations will focus on the inclusion of climate targets in executive compensation and the potential commitment for net zero total emissions by 2050.



**Sector:** Utilities

**Region:** Europe

**Topics addressed:** Strategy

**Engagement:**

During 2019, we met with the company's chair of the Supervisory Board and the head of sustainability on several occasions to discuss the implications of recent regulatory developments on retiring coal plants and the company's overall climate change strategy. Topics under discussion included:

- Imminent acquisitions in the space of renewable energy
- Science based targets
- Executive remuneration linked to climate change targets
- Oversight of lobbying activities on climate change

**Outcome:**

At the end of 2019, the company set the target of net zero GHG emissions by 2040, raising standards for peers in the sector. The company has also committed to future disclosure in alignment with the TCFD recommendations and the introduction of climate targets in LTIP plans from 2021. Finally, the results of a global review of lobbying activities on climate change will be shared with the market before the next AGM in 2020. Future dialogue will focus on the definition of a coal phase-out plan in alignment with the Paris Agreement. As a result of this engagement dialogue, we've increased exposure to this company through some of our active equity strategies.



# Advocacy with policy makers and standard setters

## **Measurement of impact**

We acknowledge the lack of standards on impact / SDG frameworks and disclosure guidance for companies. That said, there are industry initiatives in place to address these gaps which we think should help facilitate:

- More action from companies to enhance their impact / contribution to the SDGs
- Investor integration of impact / SDG information
- Allocation of capital to SDG / impact strategies

Hence our enhanced focus, during the year and also going forward, on contributing towards guidance and disclosure.

**Impact Management Project** – Together with our Wealth Management colleagues, we continued our engagement with the Impact Management Project, joining the Advisory Group. The aim of this group is to continue consensus-building to establish norms for best practices around impact measurement and management.

**World Wide Generation** – Together with our Wealth Management colleagues, we participated in their G17Eco pilot, an initiative that aims to launch the first inter-operable data platform for the public good, and a global systems solution to accelerate financing and delivery of the SDGs. We will continue monitoring the initiative and contributing to it.

**DNB SDG Impact Assessment Working Group.** We are an active member of the working group. We are contributing towards developing further guidance for companies on impact / SDG disclosure.

**SASB IAG** – We are active members of the SASB IAG. SASB metrics can be, and are, used to measure corporate impact, although their primary use is for material ESG assessment. SASB has launched a project to be completed in 2020 to work on mapping SASB indicators to the UN SDGs.

## **Update on our dialogue with policy setters**

Through the work of our Regulatory Intelligence unit, the policy, and regulatory, issues we engaged on span a wide spectrum of asset management, investment and market issues. Current and recent topics include sustainable investment (SI), notably the EU's Action Plan on Sustainable Finance, as well as a focus on systemic risk, in particular regulators' and asset managers' approaches to liquidity and leverage.

## **Our feedback on the new UK stewardship code**

During 2019, we hosted a seminar in collaboration with the PRI (Principles for Responsible Investment) and FRC (Financial Reporting Council) to present the results of a consultation with investors and stakeholders and provide further feedback on the new upcoming UK Stewardship code. When the new code was launched, we joined a UK Investment Association working on scenario analysis

## **Our dialogue with the International Energy Agency (IEA) on scenario analysis**

We've provided feedback on the Sustainable Development Scenario for the IEA flagship World Energy Outlook. We supported the content of the IIGCC written letter to IEA. The key messages are that investors are looking for a 1.5°C scenario that extends to 2050 without overshoot and without over-reliance on negative emissions technologies. We also need emissions pathways for a range of sectors from oil, gas, coal to industrials, materials and agriculture.

## **Our contribution to the TCFD report on progress**

In 2019, we submitted a case study on the energy sector for the Report on Progress of the TCFD. In September, we have also joined a panel discussion on the implementation of the TCFD recommendations during the PRI in Person conference in Paris.

## **Advancing sustainable investing in Switzerland**

We are members of the Swiss Funds & Asset Management Association (SFAMA)/Suisse Sustainable Finance (SSF)

Throughout 2019, members of the SI team have been presenting on issues related to ESG and sustainable investing, participating in 62 industry and thematic events across regions.

Working Group on Sustainable Asset Management which was established in March 2019. The goal of this group is to develop guidelines for sustainable asset management for the Swiss asset management industry.

#### **Awareness and collaboration**

Where we believe the effectiveness of engagement and the chance of success can be increased, we're willing to work both formally and informally with collective bodies, or to collaborate with other shareholders. By speaking to companies with a unified voice, investors can communicate their views more effectively and allow the companies to focus on a smaller and more co-ordinated number of requests from the financial community.

Collaboration with peers can bring clear benefits, such as building knowledge and skills, sharing resources and increasing attention from corporate management. However, there's a chance that negotiation and coordination costs might hamper the advantages of collaborating. Therefore, at the outset, we must try to confirm that:

- Working with other investors is permitted by law and/or regulation
- A general alignment of views and agreement on issues of concern and potential solutions exists
- Dialogue will be undertaken privately
- We, as an investment firm, have the resources to effectively contribute to the research of, and dialogue with, selected companies.

Collaborative engagements are not the only channel for us to work with our peers and raise awareness on sustainable investing. We're also active members of industry working groups and advisory committees.

In 2019, we shared our expertise and worked within the following groups and collaborations:

- **CA 100+**. Climate Action 100+ is a collaborative engagement initiative coordinated by five partner organizations: Asia Investor Group on Climate Change (AIGCC); Ceres; Investor Group

on Climate Change (IGCC); Institutional Investors Group on Climate Change (IIGCC) and Principles for Responsible Investment. Launched in December 2017, it now has the support of over 450 investors, representing more than USD 40 trillion of assets under management. The initiative's aim is to engage with high greenhouse gas emitters, together with other companies across the global economy that have significant opportunities to drive the clean energy transition and help achieve the goals of the Paris Agreement on climate change. Of those chosen for engagement, there are 100 'systemically important emitters', which together account for two-thirds of annual global industrial emissions, plus more than 60 others which have significant opportunities to drive the clean energy transition. UBS AM is currently directly involved in 29 coalitions of investors within Climate Action 100+ and leads seven of the company dialogues across regions. UBS AM is also a member of the IIGCC Climate Action 100+ European Advisory Group.

- UBS AM is participating in the **IIGCC Paris Aligned Investment Initiative** where we're helping to strengthen the clarity and the call for an investment oriented climate change transition scenario
- **FAIRR** Supporting dialogue on ESG risks caused by intensive livestock production, the FAIRR Initiative is a collaborative investor network that raises awareness of the material ESG risks and opportunities caused by intensive livestock production. We're members of the initiative and are actively involved in Phase 4 of its sustainable protein supply chain engagement, leading and supporting on various dialogues with companies. We also use the Initiatives' research in our own integration and engagement activities.
- **PRI**; we've been members of the SDGs in Active Ownership working group and provided a case study example, available on the PRI website. We're also a member of the PRI Academic network Advisory Group, which aims to provide feedback on the PRI's efforts to bridge the gap between academic research and practitioners. Finally, we're members of the PRI fixed income engagement working group.

# Information provided to clients and public

We aim to make our stewardship activities transparent through regular reporting to our clients and via other information reported publicly online.

Client reporting is conducted quarterly. It includes details of voting and corporate engagement activities undertaken during the quarter.

Our stewardship report is published annually. Where practical our reports include both qualitative and quantitative information.

We're always mindful that our engagement activity, especially current activity, may be confidential or sensitive. We may choose not to fully disclose all information, particularly if we feel this could hinder the outcome of our discussions with companies.

Our approach to implementing the PRI, including Principle 2 on stewardship across asset classes, is published on our website together with the relevant assessment report.

Our voting record is disclosed publicly online on a quarterly basis with details on abstentions or votes against the board. For our regulated funds in the USA, Canada and Australia we disclose our annual voting record on a fund-by-fund basis.

## **Conflict of interest**

Our principal objective when considering how to vote, or whether to engage with a company, is to fulfil our fiduciary duty by acting in the interests of our clients at all times.

Situations can arise where actual or potential conflicts of interest occur. For example:

- The interests of one client may conflict with those of another client of UBS AM
- UBS AM may invest in publically listed shares of UBS Group AG on behalf of our clients
- The listed company whose shareholder meeting is being voted upon or included in our engagement list may be a client of UBS AM
- Affiliates within the wider UBS Group might act as advisor to the company
- The interests of an employee of UBS AM may directly conflict with the interests of a client of UBS AM

UBS AM has implemented clear guidelines to address conflicts of interests that arise in connection with our stewardship activities on behalf of clients. More detail about these guidelines can be found in our [proxy voting policy](#).

# The governance of stewardship

UBS AM's proxy voting and engagement activities are overseen by the Stewardship Committee. This committee is chaired by the Head of Investments and comprises the Head of the Sustainable and Impact Investing team, the Head of Active Equities, the Head of Systematic and Index Investing, the Head of Sustainable and Impact Investing Research and Stewardship, and the Head of Global Institutional Client Coverage.

In addition to the Stewardship Committee's oversight, we regularly review our stewardship approach. In this regard, a detailed internal audit was performed in 2019 to ensure our practices were in our clients' interests. Agreed policies and procedures were found to be appropriately implemented.

## **The research and stewardship team**

This team is part of the wider sustainable and impact investing team. It is responsible for conducting and supporting ESG integration and stewardship activities across asset classes. Our sustainability research analysts specialize by topics and sectors. They lead on providing specific company analysis and contribute to thought leadership research on sustainability topics. SI analysts conduct direct dialogue with companies and provide support to investment teams across all strategies to structure engagement cases and relevant objectives. The research and stewardship team collaborates closely with the Global Sustainable Equity (GSE) team which is responsible for developing and managing active equity strategies with explicit ESG/SI mandates. Both the SI and GSE teams represent UBS AM in collective bodies and initiatives aimed at advancing ESG topics and sustainable investing.

For further information on our policies and activities, please visit:

<https://www.ubs.com/global/en/asset-management/investmentcapabilities/sustainability.html>.

For any queries, please contact our team at:

[dl-si-research-stewardship@ubs.com](mailto:dl-si-research-stewardship@ubs.com)

# Appendix

## Appendix 1

List of companies we engaged with in the last 12 months (A–Z)

- 1&1 Drillisch AG
- A2A S.p.A.
- AGCO Corporation
- AGL Energy Limited
- Alcoa Corp.
- Alcon, Inc.
- Allergan plc
- Alliant Energy Corp
- Amazon.com, Inc.
- Ameren Corporation
- America Movil SAB de CV
- American Electric Power Company, Inc.
- American International Group, Inc.
- Ameriprise Financial, Inc.
- Anadarko Petroleum Corporation
- Anglo American plc
- ArcelorMittal SA
- arGEN-X SE
- Arista Networks, Inc.
- Ashtead Group plc
- ASR Nederland NV
- Automatic Data Processing, Inc.
- AXA SA
- Babcock International Group PLC
- BAE Systems plc
- Baker Hughes Company
- Banco Bilbao Vizcaya Argentaria, S.A.
- Banco Santander S.A.
- Bank OZK
- Bankia, S.A.
- Barclays PLC
- Barratt Developments PLC
- Bayer AG
- BHP Group Ltd
- BHP Group Plc
- BNP Paribas SA
- BP p.l.c.
- Brambles Limited
- British American Tobacco p.l.c.
- Carnival plc
- Cenovus Energy Inc.
- CenterPoint Energy, Inc.
- Chevron Corporation
- China Mengniu Dairy Co., Ltd.
- Chr Hansen
- Chubu Electric Power Company, Incorporated
- Clariant AG
- CLP Holdings Limited
- CMS Energy Corporation
- Coca-Cola Company
- Cogna Educacao S.A.
- COMET Holding AG
- Compagnie Financiere Richemont SA
- Companhia de Saneamento Basico do Estado de Sao Paulo SABESP
- Conagra Brands, Inc.
- Concho Resources Inc.
- ConocoPhillips
- Continental AG
- CoreCivic, Inc.
- Corestate
- Costco Wholesale Corporation
- Credit Suisse Group AG
- Croda International Plc
- Daimler AG
- Digital Realty Trust, Inc.
- Direct Line Insurance Group Plc
- Dominion Energy Inc
- Dormakaba Holding AG
- DTE Energy Company
- Duke Energy Corporation
- EastGroup Properties, Inc.
- Electronic Arts Inc.
- Enel S.p.A.
- Eni S.p.A.
- EOG Resources, Inc.
- Equinor ASA
- Erste Group Bank AG
- Evraz PLC
- Exxon Mobil Corporation
- First Republic Bank
- FirstEnergy Corp.
- FirstGroup plc
- Forbo Holding AG
- Fortum Oyj
- Fresenius Medical Care AG & Co. KGaA
- Frontera Energy Corporation
- Fuchs Petrolub
- Galapagos NV
- Genmab A/S
- GeoPark Ltd
- Georg Fischer AG
- Gilead Sciences, Inc.
- Glencore plc
- Global Blood Therapeutics Inc
- GoDaddy, Inc.
- Grupo Financiero Banorte SAB de CV
- Hammerson plc
- Hartford Financial Services Group, Inc.
- Hong Kong & China Gas Co. Ltd.
- HSBC Holdings Plc
- Hudson Pacific Properties, Inc.
- Imperial Brands PLC
- Imperial Oil Limited
- Incyte Corporation
- Intesa Sanpaolo S.p.A.
- Intu Properties plc
- Itron, Inc.
- John Wood Group PLC
- Johnson & Johnson
- JPMorgan Chase & Co.
- Julius Baer Gruppe AG
- Jungheinrich
- Kansai Electric Power Company, Incorporated
- Kasikornbank Public Co. Ltd.
- KB Financial Group Inc.
- Laboratory Corporation of America Holdings



- Landis+Gyr Group AG
- LANXESS AG
- LEG Immobilien
- LG Chem Ltd.
- LiveRamp Holdings, Inc.
- Livongo Health, Inc.
- LKQ Corporation
- Lloyds Banking Group plc
- Lonza Group AG
- Lundin Petroleum AB
- MagForce
- Marathon Oil Corporation
- Marvell Technology Group Ltd.
- MetLife, Inc.
- Microsoft Corporation
- Mitsubishi Chemical Holdings Corporation
- Mondelez International, Inc.
- Morgan Stanley
- Mothercare plc
- Mowi ASA
- MTU Aero Engines AG
- Munich Re
- MyoKardia, Inc.
- Nasdaq, Inc.
- Naspers Limited
- Neste Corporation
- Nestle S.A.
- NiSource Inc
- NMC Health PLC
- Nordea Bank Abp
- Novagold Resources Inc
- Novartis AG
- NXP Semiconductors NV
- OMV AG
- OneSpaWorld Holdings Ltd.
- Origin Energy Limited
- Outokumpu Oyj
- Palo Alto Networks, Inc.
- Petroleo Brasileiro SA Pfd
- Pinnacle West Capital Corporation
- Pioneer Natural Resources Company
- POSCO
- PPL Corporation
- Premier Oil plc
- Prologis, Inc.
- Proto Labs, Inc.
- Prudential Financial, Inc.
- Prysmian S.p.A.
- PT Bank Mandiri (Persero) Tbk
- PTC Inc.
- Public Storage
- Qorvo, Inc.
- Reckitt Benckiser Group plc
- Repsol SA
- Rio Tinto plc
- Riverstone Energy Limited
- Rolls-Royce Holdings plc
- Royal Ahold Delhaize N.V.
- Royal Bank of Scotland Group plc
- Royal Dutch Shell Plc
- Royal Mail plc
- RWE AG
- Ryanair Holdings Plc
- Safehold Inc.
- Sampo Oyj
- Samsung Electronics Co., Ltd.
- SAP SE
- Sarepta Therapeutics, Inc.
- Scor
- Serco Group plc
- SFS Group Public Co. Ltd.
- Sika AG
- Simon Property Group, Inc.
- Sims Ltd
- Skyworks Solutions, Inc.
- Sonos, Inc.
- South32 Ltd.
- Spectris plc
- State Bank of India
- Stericycle, Inc.
- Straumann Holding AG
- Stroeer SE & Co. KGaA
- Ströer AG
- Swedbank AB
- Swiss Life Holding AG
- Swiss Re AG
- Synthomer PLC
- Takeda Pharmaceutical Co. Ltd.
- Telefonica SA
- Teleperformance SE
- Teradyne, Inc.
- Tesco PLC
- Thales SA
- UBS Group AG
- Unilever PLC
- United Internet
- UnitedHealth Group Incorporated
- Universal Insurance Holdings, Inc.
- Vale S.A.
- Veeva Systems Inc Class A
- Vertex Pharmaceuticals Incorporated
- VINCI SA
- Vista Oil & Gas SA de CV
- Voya Financial, Inc.
- Wayfair, Inc. Class A
- WEC Energy Group Inc
- Wells Fargo & Company
- Western Digital Corporation
- Westlake Chemical Corporation
- Woodside Petroleum Ltd
- Wuliangye Yibin Co., Ltd. Class A
- Xcel Energy Inc.
- Yandex NV Class A
- Zur Rose Group AG
- Zurich Insurance Group Ltd

## Appendix 2 List of collaborative initiatives

UBS Asset Management is currently a member of, or supporting, the following global groups and initiatives:

- Asian Corporate Governance Association (ACGA)
- DNB SDG Impact Assessment Working Group
- EFAMA Stewardship, Market Integrity and ESG Investment Standing Committee
- Farm Animal Investment Risk & Return (FAIRR)
- GRESB
- IFC Operating Principles for Impact Management
- Impact Management Project (IMP)
- Institutional Investors Group on Climate Change (IIGCC)
- International Corporate Governance Network (ICGN)
- Investor Statement of the Access to Medicine Index
- National Association of Real Estate Investment Managers
- Principles for Responsible Investment (PRI)
- Sustainability Accounting Standards Board (SASB)
- Swiss Sustainable Finance (SSF)
- Taskforce on Climate Related Financial Disclosure (TCFD)
- Transition Pathway Initiative (TPI)
- UK Governance Forum
- UK Investor Forum
- US Green Building Council
- Workforce Disclosure Initiative (WDI)

## Appendix 3 Our commitment to constructive dialogue

We believe in building relationships with the corporate management we engage with. We're asking our investee companies to be responsive to our invitations for dialogue and provide material and forward looking information to us. Equally, companies can expect the following behavior from us to allow for fruitful and effective conversations:

- 1 Solid preparation:** before entering into dialogue with a company, we'll review and analyze the most up-to-date and relevant information on financial and ESG performance provided by the company. We'll also access third party research on issues considered material for the specific company and sector.
- 2 Local and sectorial expertise:** before starting dialogue with a company, we'll look for internal expertise and views on relevant local markets and sectors across teams.
- 3 Connection with investment decisions:** during our meetings with corporate management, we'll explain how the information collected will be taken into consideration in investment decisions. Whenever possible SI staff and investment staff will co-join meetings with companies. In any situation, the information collected during engagement meetings will be shared internally through a platform.
- 4 Feedback:** during and after meetings, we'll provide feedback on current company actions and plans to solve any existing concerns. Companies can also ask our opinions on areas of interest for them. After initial conversations, we'll share with management our engagement objectives.
- 5 Best practice:** whenever relevant, we'll share best practice examples from peers that have shown leadership and good performance on material ESG matters. Equally, we'll recognize the companies we engage with for any innovative practice and solution in relation to ESG challenges and opportunities.
- 6 Commitment:** we'll allocate adequate resources and time for our dialogue with companies. If we believe that corporate practice should improve in order to trigger long-term value, we'll engage with the management and the board on a continuous basis and over a certain period of time.
- 7 Collaboration:** as part of our commitments to support investor networks and drive the ESG agenda in financial markets, we'll monitor other investors' activities on engagement and join efforts whenever beneficial for us and investee companies.

# About UBS Asset Management

UBS Asset Management (UBS AM) is a large-scale asset manager with a presence in 22 markets. Offering investment capabilities and investment styles across all major traditional and alternative asset classes to institutions, wholesale intermediaries and wealth management clients around the world, our firm offers a wide range of strategies, both passive and active. At 31 December 2019, assets under management stood at USD 903 billion.

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**Americas**

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