ROBECO
The Investment Engineers

Active Ownership Report Q1-2019

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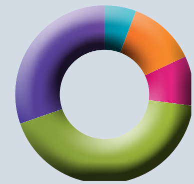
Engagement activities by region

Region	%
North America	26%
Europe	24%
Pacific	22%
Emerging Markets	4%
United Kingdom	24%

Shareholder meetings voted by region

Region	%
North America	6%
Europe	12%
Pacific	9%
Emerging Markets	43%
United Kingdom	30%



Voting overview

2019	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Total number of meetings voted	122			
Total number of agenda items voted	1.409			
% Meetings voted against management	77%			

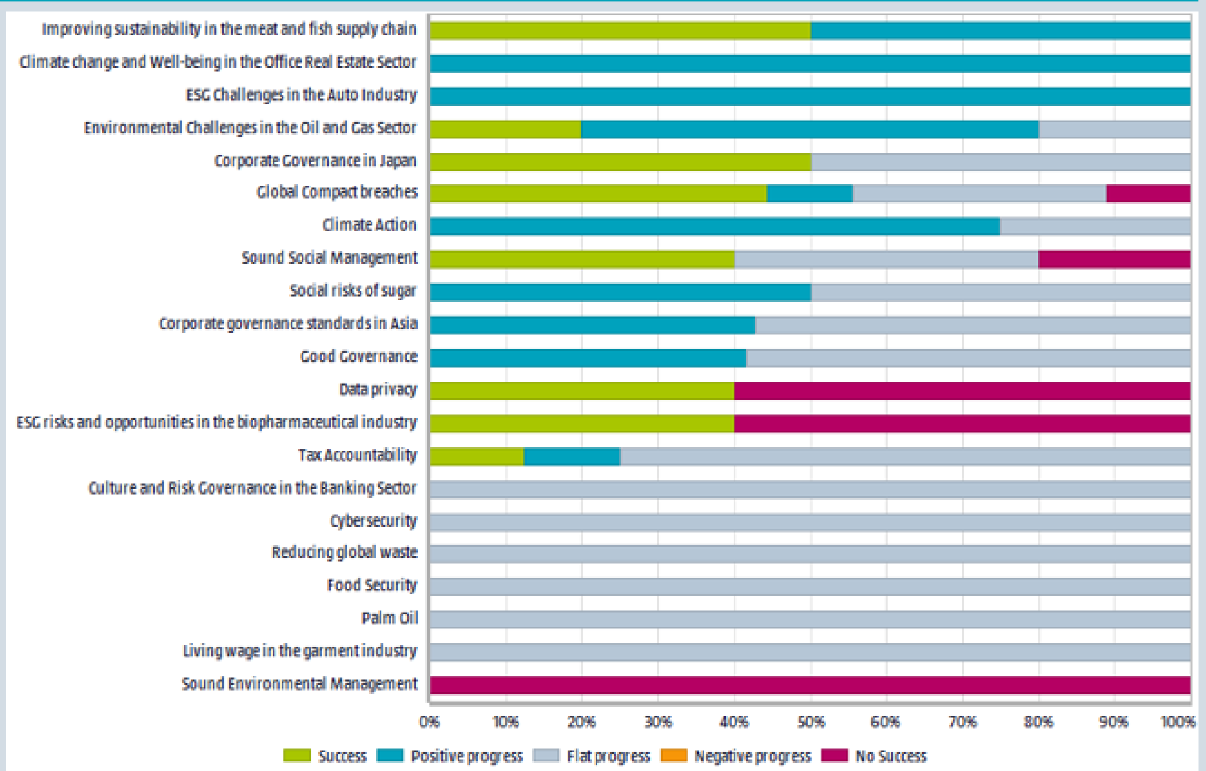
Engagement overview by topic

Topic	
Environmental Management	11
Environmental Impact	
Human Rights	3
Healthy Living	5
Social Management	1
Corporate Governance	22
UN Global Compact	4

Engagement by contact type

Contact type	
Analysis (no actual contact with company)	
(Open) Letter	6
Meeting at company offices	13
E-mail	13
Active voting	
Shareholder resolution	
Conference call	20
Speaking at a shareholder meeting	
Meeting at Robeco offices	5
Speaking at conferences	
Issue press release	

Engagement results per theme



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Introduction

Since the start of the new year, Robeco's Active Ownership team has embarked on a number of new initiatives - from participating in collaborative events to launching our new engagement themes for 2019.

In February, we actively participated at the International Corporate Governance Network (ICGN) conference, hosted by Eumedion in Amsterdam where best practices were exchanged with investors and academics from around the globe. During the academic-day of the ICGN conference, I was honored to participate in a lively panel at the ICGN academic day, where the practical implications of engagement were confronted with an academic perspective.

Also, we supported a letter to mining companies urging them to provide specific disclosure on their tailings facilities. We have been closely following the mining sector for many years and we have engaged in active dialogues with many mining companies on environmental and social topics. Robeco has joined a global group of investors (representing $10.3 trillion USD in assets under management), to improve the disclosure on tailings facilities of mining companies. This engagement is in response to the tailings dam breach in Brazil. 683 listed extractives companies received our joint letter calling on them to increase their disclosures. As an involved investor we support this joint call upon the mining sector to install a truly global and independent classification system in order to make sure that the safety of all dams are assured.

Lastly, I am pleased to announce the official launch of our palm oil engagement program, which is aimed at increasing the production of RSPO certified palm oil. In January, Robeco joined the Round Table on Sustainable Palm Oil (RSPO) and in March we published a position paper on the challenges faced by the industry. As we are focused towards improving the behavior of palm oil companies, we began an innovative engagement program that uses the RSPO certification scheme as a central theme. In addition to our new engagement, this report will provide you with an update on many of our activities.

Carola van Lamoen
Head of Active Ownership

Voting Highlights

Laura Bosch & Robert Dykstra

According to the Asian Corporate Governance Association, the long-held regulatory principle that higher standards of corporate governance make markets more competitive has come under threat in Asia. Although regulators have successfully pushed for more transparency and accountability, the fair treatment of consumers and shareholders has been neglected. Some of the most notable corporate governance developments of 2018 took place In Korea, Hong Kong, and China.

Codes of conduct

- ICGN Global Governance Principles

Corporate Governance: Proxy Voting

Our voting policy is based on the widely accepted principles of the International Corporate Governance Network (ICGN), which provide a broad framework for assessing company's corporate governance practices. We constantly monitor the consistency of our general voting policy with the ICGN principles, with laws and governance codes and systems as well as client specific voting policies. Our voting policy is formally reviewed at least once a year. We also take into account company specific circumstances and best practices when casting our votes.

China & Hong Kong

In China, one of the most pressing corporate governance concerns is the level of transparency and disclosure provided by publicly listed companies. With the growing influence of Party Committees (PC), the decision-making process at Boards is becoming more opaque. A Party Committee consists of members who oversee the board and are affiliated with the Chinese Communist Party (CCP).

The long-term effect of a PC on board independence is relatively unclear. In some cases, the PC is the highest decision-making body, whereas in other instances the PC is a means to uphold corporate interests for the government. In state owned enterprises, PCs can have the final say on material issues for the company. PCs are less common in private and foreign-owned companies, but the pressure to form them is increasing. The issue remains that little if any disclosure is given on how the PC operates, making it difficult for foreign investors to assess board quality. Although the government contends that party committees will improve corporate governance, many investors remain skeptical.

While Hong Kong can be considered a regional frontrunner in corporate governance, it can also be the first to encounter new corporate governance issues. One such issue is the introduction of dual-class share (DCS) listings on the Hong Kong and Shanghai stock

exchanges. A company with DCS can offer shares with different voting rights, allowing the company or other shareholder to retain control despite being publicly listed. In Hong Kong, the difference in voting rights between share classes cannot exceed 10:1. Nonetheless, many institutional investors including Robeco, are opposed to dual-class shares as they limit the influence of minority shareholders.
DCS is commonly employed by companies in the technology industry, which are what the HKSE hopes to attract. However, since it was introduced in 2017, the number of newly listed DCS companies in Hong Kong has been underwhelming and the promise that DCS would create a new home for technology giants has yet to be delivered.

Korea

The Korean corporate governance system remains significantly weaker than its peers in the region. Korean companies operating internationally are becoming more aware that they must benchmark their practices against global standards of governance and sustainability, rather than just their local peers. Recent changes implemented by the Act on External Audit of Stock Companies aim to improve independence, corporate accountability and regulatory control in the market.

Companies' audit committees or statutory auditors will be the designated parties to appoint the external auditor. In the past, this responsibility was placed with the companies' management team. During the first quarter of 2019, most Korean companies have put up for vote at their shareholder meetings a proposal requesting the amendment of their articles of association to reflect the new duties of the audit committee or statutory auditor board. We support this development as it reinforces external auditors' independence, and have therefore voted in favor of most of these resolutions.

Nonetheless, it remains challenging for shareholders to access the audited financial statements prior to exercising our voting rights at Annual General Meetings (AGM). According to the Korean Commercial Act, companies must disclose the notice and circular for convocation of a general meeting at least 14 days prior to the meeting date. The same regulation states that listed companies shall publish their audited financial statements at least seven days prior to the AGM.

Those shareholders voting via proxy normally need to send their voting instructions two weeks prior to the AGM. We refrain from supporting the approval of financial statements in case we do not have access to the auditor's unqualified opinion. Moreover, we believe that the chairman of the audit committee shall be held accountable for the failure to disclose this information in a timely manner for those shareholders voting electronically. Should this director be up for vote at the AGM, a vote against his reappointment is warranted.

Linking active dialogue with companies and voting at shareholders' meetings

In emerging markets, ESG issues play an important role, even more so than in developed markets. Corporate governance in particular is a factor to watch, as emerging companies have varying standards of governance and the latter can therefore have a substantial impact on investment returns. By maintaining active dialogue with our portfolio companies and voting at shareholders meeting, we expect to see further corporate governance improvements that will be beneficial to shareholders' return, writes Koos Burema, Emerging Markets Equities Analyst.

Having invested in emerging markets for 25 years, we have found that integrating ESG factors into the investment process is crucial when investing in emerging markets. Market inefficiencies caused by lower data availability, poor transparency and governance standards, and issues relating to climate change, human rights and product safety standards are a potential source of alpha for emerging markets investors. Our ESG Dashboard, that we began developing in 2001, is used as a starting point for individual company analysis. It addresses key topics like empowering shareholders, management discipline,

board structure, audit quality, operational eco-efficiency, and human capital.

For a number of companies, the outcome of ESG analysis has been beginning an active dialogue on their environmental, social or governance issues. In many instances these engagements have been successful, leading to companies improving their shareholder returns in the form of dividends and share buybacks, and the cancellation of treasury shares. Companies that are addressing environmental issues, are reducing the risk of a future liability. In other instances, voting against management proposals at their shareholders meeting have helped make top management aware of minority investors' concerns. We have found that several successful engagement outcomes benefited from adopting an integrated approach including portfolio managers working together with active ownership specialists. One prominent example has been with Hyundai Mobis withdrawing its proposal of a spin-off merger with Hyundai Glovis in May 2018.

Climate Action

Sylvia van Waveren & Cristina Cedillo

The first year of the investor-led Climate Action 100+ (CA100+) global initiative has inspired momentous progress in a number of companies. The collaborative engagement with the world's highest greenhouse gas (GHG) emitters has brought important commitments to curb emissions. Corporate leaders in the energy transition have begun to differentiate themselves from peers by adopting stronger commitments to decarbonize.

Codes of conduct
- UN Global Compact Principles 7-9
- Rio Declaration on Environment and Development
- OECD Guidelines for Multinational Enterprises, Chapter VI
- SDG 7: Affordable and Clean Energy

Environmental Management: Environmental Policy & Performance
An environmental management policy is a set of restrictions or standards designed to protect and conserve environmental resources. An effective environmental policy clearly outlines rules and expectations for companies to follow regarding preventing negative impact on the environment. Furthermore, it should be equipped to calculate the environmental performance of a company as well.

Robeco is an active member of the CA100+ initiative, in which we act as lead investor in three companies – Enel, NTPC and Royal Dutch Shell – and as a collaborating investor in companies across the oil and gas, electric utilities and chemical industries. In addition, Robeco is also member of the CA100+ Advisory Group to the Institutional Investor Group on Climate Change, serving as one of the lead investors in the European auto industry.

Emissions by end-users matter

Oil and gas companies play a systemically critical role in the energy transition. Although emissions from the production phase are relatively low, the end use of oil and gas products accounts for over half of global GHG emissions associated with energy consumption. As such, oil and gas producers have been a priority sector in our engagement. In May 2018, a group of investors including Robeco had a letter published in the Financial Times that called for the oil and gas industry to be more transparent about the financial impact of climate change, and to take responsibility for all of its emissions.

So far, only a couple of oil majors have publicly acknowledged responsibility for the emissions derived from the consumption of their products, and have committed to decreasing their entire carbon footprint. For most

energy majors, it remains unclear how they plan to evolve their business and prepare for a low-carbon scenario. On average, oil and gas producers have allocated around 1% of their total 2018 capital expenditure to their alternative energy businesses, according to data from the Carbon Disclosure Project.

Our engagement with Royal Dutch Shell led to climate commitments

Royal Dutch Shell became the first oil and gas company to announce concrete plans to reduce its carbon footprint in a series of targets stretching out to 2050. The plan was announced in a ground-breaking joint statement with investors in December 2018.Shell agreed to set short-term targets for cutting GHG emissions for the first time, and said it aims to reduce its net carbon footprint by around half by 2050, with a 20% reduction by 2035 as an interim step. To put this long-term ambition into effect, Shell will start setting net carbon footprint targets for shorter-term periods from 2020. Each year, the target will be set for the next three- or five-year period until 2050.

Furthermore, in an unprecedented move, Shell will link energy transition targets with executive long-term remuneration as part of its revised Remuneration Policy. Shareholders will be able vote on it at the 2020 Annual General Meeting.

Committing only Shell to a low-carbon scenario puts the company at a competitive disadvantage in many respects. We therefore plan to concentrate our engagements on other companies in this sector to encourage them to take responsibility in preparing for the energy transition.

Moving towards a decarbonization roadmap for electric utilities

Research by Carbon Tracker suggests that European coal plants will become loss-making by 2030, while the levelized cost of energy (LCOE) from renewables is expected to be lower than coal by the mid-2020s. In the US, a lower LCOE of new gas and renewable capacity will continue to push down coal's competitiveness.

While all of the utility companies in scope for our engagement have committed to not develop any new coal-fired plants, they have been unable to commit to a phase-out date for their existing coal assets. Phasing out coal plants requires regulatory approval. Policymakers fear insecurity of supply if the intermittent energy from renewables is not backed up with reliable coal-fired power plants. In some cases, this is resulting in investments to upgrade existing coal-plants in order to reduce their emissions and extend their life.

During 2018, most of the utilities under engagement implemented the recommendations of the Taskforce on Climate-related Financial Disclosures in their annual disclosures, including scenario analyses. Moreover, we have found differences in the decarbonization strategies of utilities, the starkest being between European and US companies. While European utilities envisage achieving a net-zero scenario primarily through renewables and storage, their US counterparts see a more prominent role for both nuclear power and natural gas-powered plants that are retrofitted with carbon-capture-and-storage (CCS) technologies. It remains unclear whether CCS and battery storage will be technologically speaking sufficiently developed or financially viable by 2050, when they will be needed the most. While most companies have set long-term emissions reduction targets, it remains unclear what the energy mix of these utilities will look like under a net-zero emissions scenario. Yet, it is evident that more investment in renewables and other low-emissions energies is needed. None of the companies under engagement have over 11% of installed capacity from renewables, or more than 45% of installed capacity from zero-emission energy sources such as hydro.

In another letter to the Financial Times, published in December 2018, Robeco was among a group of investors that publicly called on utilities companies to end coal use by 2030, and to spell out their strategy to prepare for a global shift towards low-carbon fuels.

Reconciling short-term accountability with long-term ambitions

Climate change brings a challenge to the world of unprecedented proportions. Planning for the energy transition requires companies to sketch scenarios on how their businesses may evolve over the next three or four decades, a timeframe that goes well beyond most industries' planning horizons. Yet, we increasingly see business leaders committing to a low-carbon future and setting net-zero targets by the mid-century. In our engagement, we aim to develop frameworks upon which top management can be held accountable for the realization of a low-carbon scenario. Besides setting intermediate targets, we encourage companies to integrate these strategic targets into executive remuneration plans, as Shell has done. As more companies commit to decarbonizing their business in line with the Paris Agreement of limiting global warming to 2°C above pre-industrial levels, the accountability of management will increasingly become a priority in our engagement.

INVESTOR SPOTLIGHT

Chris Berkouwer, Portfolio Manager Global Stars Equity

It is no coincidence that in recent years, oil majors have taken out any reference to 'petroleum' in their company name. Instead, they view themselves as 'energy companies', illustrating the key role they have to play in the transition to a low carbon economy. 'Energy' majors have many tools at their disposal to become cleaner fuel providers consistent with the Paris Agreement to contain global warming to within 2°C. The problem that a company such as Shell faced, however, was the fact that its long-term climate ambitions were too far out and not concrete enough, making accountability difficult. Thanks to the tremendous efforts of our Active Ownership team as well as our partners, we inspired Shell to link short-term targets to its long-term ambition. We believe this sets Shell apart from its competition. In this way we are able to support Shell, and broader society, in reaching the necessary climate goals, but also unlock value for shareholders such as Robeco.

Culture and Risk Governance in the Banking Sector

Michiel van Esch & Cristina Cedillo

The banking industry has been a key issue for public debate over the last decade. The role of banks in the financial crisis, the LIBOR rate-fixing scandal, and many other controversies have changed our perception of the banking industry. Several issues have often been flagged as problematic in the sector, including risk control frameworks, the quality of corporate governance, perverse incentive structures, the lack of accountability for poor performance, and more broadly, 'organizational culture'.

Codes of conduct

- ICGN Global Governance Principles
- ICGN Corporate Risk Oversight Guidelines
- OECD Principles for Corporate Governance
- COSO II – Enterprise Risk Management Framework

Corporate Governance: Risk & Crisis-Management

A company's corporate governance structure specifies the rights and responsibilities of the various stakeholders such as the management, supervisory board, shareholders and other stakeholders. An effective corporate governance system focuses on a company's long- term business continuity and protects the shareholders' interests. A well-functioning corporate governance system can contribute to long term shareholder value. International and national principles and codes provide guidelines for good corporate governance. Effective and comprehensive risk management is an important part of a company's corporate governance.

These topics are not just relevant for policy makers, or participants in the public debate, but also for investors who need to form an opinion on whether to invest in a specific bank. Therefore, in late 2017, Robeco published a research paper on the current state of play in the banking sector as the basis for an engagement program called 'risk governance in the banking sector'. The project aims to support our investment teams in their understanding of their investments in banks, and sets engagement objectives around incentive structures (both for executives and sales staff). It also sets targets for risk governance, reporting around behavioral issues and culture, and operational risk management We started our engagement in early 2018, and after a year's work, we can report back with our first impressions.

Are we there yet?

The short answer is no. Closely following the sector gives us reason to believe that many of the problems of the last decade still persist. Quite recently, we have seen revelations about some banks being involved in widespread money laundering schemes, either knowingly or not. Conversations with some of the banks in the program support a cynical opinion. For example, while banks are trying to promote a safe working

environment for employees to speak up when they observe misconduct, the whistleblowers at some of the banks are not free from conflicts of interests. In some instances, this has allowed top management to interfere in the handling of disputes, and while this is in breach of codes of conduct, disciplinary measures are often weak, and internal controls remain largely unchanged. But the longer answer is, that things are changing… slowly. We also need to acknowledge that a lot has changed already. Most banks have tightened risk management systems, changed incentive structures and simplified many products. They have installed units that are dedicated to monitoring behavioral issues and conduct-related risk either at risk management or compliance departments. Also, boards appear to be much more aware of cultural challenges, and have prioritized conduct and behavioral issues on their agenda. Incentive structures at many banks have been re-designed so that people are not chasing sales at the cost of client interest, compliance or professional behavior. The question, though, is whether things are changing quickly enough.

Learning to assess culture

When we started this project, our main concern was that to form an educated opinion on an organization's culture as an outsider would be a big challenge. Although such an assessment is indeed very challenging, it is not impossible. Sometimes, even the annual report can be a good starting point, as the CEOs and chairs of boards of directors often use them to flag their opinion about how they would like their employees to behave. For the attentive reader, these statements can provide insights into what type of behavior will be rewarded.

Much more insightful, however, are meetings with various representatives of the bank, whether they be board members, executive directors, risk managers or investor relations people. So far, we have been very fortunate with the corporate access given to us to conduct this project. At several of the biggest US banks, we found ourselves having private meetings with board chairs, heads of risk, and VPs of compensation. For example, we spoke with the new CEO of a major UK bank on the date of his appointment, and at a Dutch bank we spoke with the CRO and various members of the board. Often, our discussions are very open about the challenges around risk management, corporate culture and the role of the different stakeholders in the governance of the company.

Tackling Money Laundering

Some of the recent problems around money laundering have provided some interesting insights into how well boards and executives understand their risk culture and the quality of their control framework. Preventing money laundering requires a combination of strong controls (including client diligence), flagging transition patterns, exception-handling, and the reporting and escalation of issues. Recent issues with large money laundering incidents reveal problems in internal control frameworks, the organizational culture, and the quality of oversight from the board.

One of the central questions in this engagement project is: do executive management and the board have a grip on the organization's culture and the quality of the risk control framework? Often, we find that this is also a difficult assignment for a board, and board members are usually frank enough to admit that there is work to be done on this front.

Understanding the Cultural Weave

One thing that has become blatantly clear throughout our work so far is how important culture is in risk management. Most organizations have a similar set-up for their risk management framework. Most of the time, the board approves a risk appetite framework, setting allowances and limits for all risks. These are often translated into several risk policies for different departments and different types of risk.

Companies then apply the 'three lines of defense' system, starting with working procedures and organizational controls used in daily practice, with risk management and compliance teams checking that this is being correctly applied, and then internal control teams taking a broader look

at the overall picture. The way this set-up is applied depends largely on how people work, and the culture of an organization. In order to assess this, one needs to know how these three lines of defense interact with each other. Do problems just "need to go away", or are they escalated? If a client's account needs to be opened quickly, does that mean that due diligence documents may be collected a little bit later?

Understanding culture is also a prerequisite for understanding the quality of the company's control framework. While there is not a single definition of what would be the best type of organizational culture, and there is no definitive way to measure it, in our engagement we are learning more about how organizations can shape their culture. Some important factors include the tone-from-the-top, staff performance evaluations and incentives, and mechanisms to hold individuals accountable for their conduct. This framework will contribute to our assessment of banks in our engagement in the coming years.

Palm Oil

Peter van der Werf

The palm oil industry is often associated with significant environmental and social issues such as deforestation and poor labor standards. Although Robeco has actively engaged with companies on these issues since 2010, there is still much room for them to improve. For this reason, Robeco published a position paper on palm oil in early 2019. With this paper, we presented our new approach, using the certification scheme of the Roundtable on Sustainable Palm Oil (RSPO) as a central pillar.

Codes of conduct

- UN Global Compact Principles 1-9
- OECD Guidelines for Multinational Enterprises Chapters IV-VI
- Sustainable Development Goals 15

Environmental Management: Environmental Supply Chain Standards

Palm oil is a commodity with many positive attributes. It is a versatile product that can be used for many purposes and it is a very efficient crop producing five to eight times more oil per acre than other oil crops. This has made palm oil a very important commodity around the globe, being used in many products, ranging from food to personal care and biofuels. Despite being such an important crop, the growth of palm oil production is challenged by a number of the significant environmental and social issues that have become a reputational risk and can potentially undermine the industry's growth model.

Robeco joined the RSPO in January 2019, and will become part of its Financial Institutions Task Force, in collaboration with a number of global banks that are active in the credit financing of palm oil companies. At the same time, we began an engagement program with palm oil producers, focused on increasing the production of RSPO certified palm oil. We place certification levels at the heart of our engagement for one key reason. It is essential for the industry to transition to a more sustainable means of producing this vital crop.

A key ingredient

Palm oil is, and will likely continue to remain, a key ingredient in a diverse range of consumer products from chocolate to shampoo. The reason for its prevalence in such products derives mainly from its high productivity and profitability. The palm plant yields much larger amounts of oil than other oil crops over the same area of land use, in turn bringing higher income to producers.

Palm oil cultivation has subsequently expanded globally, bringing economic benefits to many producers, including smallholder farmers in emerging

markets. However, in tandem with this, palm oil production faces several significant environmental and social issues, ranging from deforestation and biodiversity loss, to pollution and human rights/labor rights violations.

Palm oil, deforestation and climate change

A recent RSPO study showed that between 1990 and 2010, 3.5 million hectares of forest in Indonesia, Malaysia, and Papua New Guinea was converted to palm oil plantations. This is of particular importance in that deforestation has a significant impact on the global carbon balance, as the removal of trees releases carbon dioxide into the atmosphere, contributing to climate change. Additionally, peatland degradation is a further issue related to palm oil plantation development, with further negative impacts on climate change. Peatland ecosystems are considered to be one of the most important carbon sinks for the planet. Yet, according to the RSPO study, most of the extensive peatland in Indonesia, Malaysia and Papua New Guinea has already severely degraded.

From biodiversity to monoculture

The conversion of forest to monocultural palm oil plantation also results in significant loss of biodiversity, representing a further ESG risk to consider. Since the growing of palm oil takes place in some of the world's most biodiverse locations, it impacts the life of many animals, including endangered species such as the orangutan, pygmy elephant and Sumatran rhino.

The clearing of forest to make way for palm oil development is however only one issue. Another is the actual clearance process itself with burning being a common method to clear both natural forest and peatland. This in itself leads to the release of a massive amount of greenhouse gas emissions, creating air pollution that leads to smog haze. The haze that occurred in 2015 resulted in over 100,000 deaths across Indonesia, Malaysia and Singapore.

Then there is the issue of water contamination, which occurs when palm oil mill effluent (POME) is discharged into waterways. Major palm oil-producing countries such as Malaysia and Indonesia have legislation in place to restrict companies from discharging POME before treating it properly. However, such treatment is neglected by some companies in the industry. Meanwhile, the use of agrochemicals in palm oil plantation further contaminates water supplies.

Social risks of production

Palm oil companies operate in remote rural areas that are more vulnerable to human rights and labor abuses. Major controversies relate to land grabbing and the displacement of indigenous people. Subsequently, the development and clearance of land has deprived many local communities of vital land and water resources. The increasing number of lawsuits indicates that these communities are fighting for the restitution of their land, and for fair compensation, which pose serious reputational risks for companies operating in this sector. Several palm oil companies have also been linked to major labor rights violations, including the use of child labor in remote areas of Indonesia and Malaysia. Workers often face poor and degrading working conditions and struggle to earn a living wage to support their families.

Palm oil and the investment community

While palm oil companies present an attractive value proposition, such unsustainable practices can cause regulatory and reputational risks to companies involved in its production. When these risks are not managed properly, they can also in turn result in financial and reputational risks for the investors in these companies. Therefore, the management of palm oil issues has a strong correlation with investors' interests.

Engaging for sustainable palm oil: A new approach

What can investors do to ensure that the ESG risks associated with investing in palm oil are appropriately managed and mitigated? Our engagement program aims to address all of the

issues outlined above by focusing on a number of areas we see as essential to develop a more sustainable palm oil value chain. Robeco acknowledges that RSPO certification – an internationally recognized standard – plays a crucial role in ensuring the sustainability of palm oil production. Hence, we have aligned our approach to measuring sustainable performance with the RSPO standard.

Defining a standard

To establish a baseline, we conducted a sector screen, benchmarking companies according to the amount of RSPO certified land owned by each producer. We will continue this screen on an ongoing basis to monitor progress. Using the results of this screen, we will begin to engage with all producers identified as having 20% to 80% of land RSPO certified. The main goal of this three-year program is to support companies in improving their performance on material sustainability issues.

Upon completion of the engagement program in December 2021, we expect the selected palm oil producers to reach at least 50% of RSPO certified. We further expect that companies with a lower percentage of RSPO certification at present to meet the 50% threshold within three years, bringing them to a substantially better sustainability performance from today's low base.

INVESTOR SPOTLIGHT

Wim-Hein Pals, Head of Emerging Markets Equities
Harfun Ven, Portfolio manager Asia-Pacific Equities

Palm stands out as a particularly efficient crop. In fact, a hectare of land planted with palm trees can produce 4 tons of oil, which is roughly eight times the output for soybeans. From an investor's perspective, once the tree is planted, it will start yielding in five years and continue to yield for the next 25 years. This gives oil palms a very attractive long-term cashflow profile, and an asset that is difficult to displace and replace.

Malaysia and Indonesia account for the bulk of global palm oil production. Yet there are no new developments in Malaysia, and it is getting increasingly difficult to acquire new land for plantation development in Indonesia. In the last five years, most large plantations have consistently missed new plantation targets, primarily due to the increased awareness of the impact on the environment.

Weak prices and excess supply

Palm oil prices have also been exceptionally weak in the past few years, as heavy planting in the past starts to yield full harvests now, causing excess supply to the market. However, looking out into the next couple of years, we believe supply growth will taper off. In addition, in a bid to reduce its current account deficit, the Indonesian government mandated that vehicles and heavy machinery running on diesel engines will have to use fuel that contains a 20% biodiesel blend (the B20 program). Successful implementation would not only help reduce Indonesia's diesel imports, but also allow it to export biodiesel, which could help narrow its current account deficit. Under the reinforced B20 regulation which began on 1 Sep 2018, all Indonesian fuel stations are not allowed to sell unblended diesel fuel from that date onwards.

The importance of sustainability

Sustainability is therefore a very important consideration when investing in this sector. Many investors have excluded coal from their portfolios, for example, and we've seen a huge de-rating in that sector that goes far beyond its intrinsic value. Palm oil is also a controversial commodity, so best practice and proper use of ESG factors are of the utmost importance. The industry needs to move forward, not only to push palm plantations to adopt better practices, but also to pressure buyers to source only RSPO-certified products. This is where the difficulty lies, as the industry is still extremely fragmented, and since the commodity is traded in an open market, many buyers are reluctant to pay any premium for RSPO-certified products.

Cyber Security

Kenneth Robertson & Cedric Hille

Cybersecurity continues to be a highly material topic for investors to consider, particularly in sectors where protecting consumer data is a key tenet of companies' license to operate. However, as investors, it is often difficult to assess the extent to which companies are adequately protecting their IT architecture, in many cases due to a lack of disclosure around the topic.

Codes of conduct
- UN Global Compact
- UN Guiding Principles on Business and Human Rights
- OECD Guidelines for Multinational Enterprises Chapters II, III, VII

Corporate Governance: Risk & Crisis-Management
A company's corporate governance structure specifies the rights and responsibilities of the various stakeholders such as the management, supervisory board, shareholders and other stakeholders. An effective corporate governance system focuses on a company's long- term business continuity and protects the shareholders' interests. A well-functioning corporate governance system can contribute to long term shareholder value. International and national principles and codes provide guidelines for good corporate governance. Effective and comprehensive risk management is an important part of a company's corporate governance.

It has been clear for some time that cybersecurity has transitioned from an emerging threat to a very clear and present danger to companies' bottom lines. Research by Credit Suisse, for example, showed that the annual cost of cybercrime reached approximately USD 500 billion in 2017, consisting of everything from small breaches and targeted attacks to incidents with global implications, as seen in the cases of the recent WannaCry and NotPetya attacks.

Cybersecurity: A highly material issue

Translating this into a verifiable impact on share prices is, admittedly, not an exact science. However, what we can see is an average organizational cost of data breaches in the United States of approximately USD 7.35 million. Combined with associated indirect costs and reputational damage, cyberattacks cause an estimated 5% drop in US companies' share prices in the immediate aftermath.
Recent examples demonstrate the potential for significantly more damaging impacts, with total direct costs related to one recent mega breach wiping out as much as 30% of the affected company's market value. The problem for both companies and their investors is evident. Yet, cybersecurity disclosure lags behind the

level of information that investors need to make informed decisions.

Transparency at the root of the problem

Whilst many potential issues exist, including potential underinvestment, lack of accountability for management, and difficulty in recruiting appropriate skills sets, such issues can be hard to detect due to the opaque nature of many companies cyber reporting.

It is therefore of the upmost importance that investors can assess whether their investee companies are adequately managing their cyber risk, and in turn can be deemed cyber resilient. Yet given an overall lack of transparency around companies disclosure of cybersecurity practices, this can be notoriously difficult.

A 2018 study by consultants EY cast considerable light on the state of the problem. Following an analysis of Fortune 100 companies, they presented stark results outlining the scale of the issue. Whilst 100% of companies included cybersecurity as a risk factor in their annual report (with 92% of these prominently highlighting the topic), only 14% highlighted cybersecurity as a strategic focus. The knock-on effect is that very little additional and comparable information was disclosed by companies as to their spending, management reporting, and oversight of cybersecurity.

SEC ups reporting expectations in face of investor pressure

Subsequently, in early 2018, the US Securities and Exchange Commission (SEC) issued guidance to companies with the expectation that they improve disclosures to their investors around cybersecurity risks and incidents. In particular, the guidance stated:

"... we believe disclosures regarding a company's cybersecurity risk management program and how the board of directors engages with management on cybersecurity issues allow investors to assess how a board of directors is discharging its risk oversight responsibility in this increasingly important area."

Building on the SEC's previous missive on the topic, the guidance strengthened requirements in two key areas:

1) Added focus on having strong disclosure controls and procedures to enable timely and accurate disclosures of cybersecurity risks and incidents by public companies, and;
2) Strengthening insider trading restrictions around cybersecurity incidents.

In theory, this should result in more complete information being available to investors with regards to the current state of a company's cybersecurity practices, a point reinforced by SEC Chairman Jay Clayton in his public statement accompanying the new guidance. The timing of the 2018 guidance gave companies a full year to implement the changes required, with the SEC further stating late last year that regulators now expect significantly expanded disclosures during this year's annual reporting cycle.

What do we expect?

Given the clear materiality of cybersecurity as a topic, Robeco has been engaging with companies since late 2018, with the aim of encouraging those companies under engagement to strengthen their cyber resilience. Our engagement with companies focuses on 5 objectives: 1) Governance and Oversight, 2) Policy and Procedure, 3) Risk Management and Controls, 4) Transparency and Disclosure and 5) Privacy by Design.

Particularly on the topic of transparency, we expect companies to inform stakeholders about the costs and effects of cyber incidents (including the materiality threshold used for reporting). When customer data is exposed, companies should clearly communicate this to their customers to avoid further negative impact on reputation. The updated SEC guidance should be useful in increasing corporate disclosure on the topic. With this in mind, we see several topics within our engagement peer group where expanded disclosures could be of assistance in helping investors better understand the suitability of company's cyber readiness.

From opaque cyber governance to transparent cyber reporting & performance

Despite the near inevitability of cyber incidents, disclosure on related governance structures is often weak. Especially for holding companies or Groups, security across brands is poorly defined and disclosed. Nonetheless, there are examples of robust governance and oversight, which involve executive team members explicitly in charge of cybersecurity (a CISO or CIO, for instance), as well as expertise in the technology sector at the board level.

Whilst cyber risk management systems are likely to be in place at all companies under engagement, disclosure on tools to actively prevent or redress cyber incidents is relatively thin. This is especially concerning given that we have discovered a pattern of reliance on third-party network infrastructure or service providers. These partnerships are often a key source of risk, but are insufficiently addressed in public disclosure. More work must be done in this area to provide investors with reassurance going forward.

Materiality thresholds: Confidence in numbers

An important component of transparency that is missing across the engagement peer group is a clearly defined materiality threshold for disclosing cyber incidents. Such a threshold would be vital for stakeholders' confidence in data protection systems and a company's cyber maturity. Our baseline research has also revealed varying approaches to communication on confirmed breaches, ranging from a complete absence of public disclosure to disclosing an incident's effect on the company's financial results. The effect of the most recent guidance from the SEC in this area remains to be seen, but we hope to report progress following a full review of company disclosures in the second quarter of 2018.

In summary, there is little doubt that businesses recognize the risks emanating from the cyber sphere. Companies are evidently investing significant resources into protection against the operational, regulatory, and reputational risks that would accompany a cyber breach. On the other hand, whilst companies might be implementing robust security systems, a central component of cyber maturity – transparency – shows significant scope for improvement.

INVESTOR SPOTLIGHT

Angela Saxby, Cybersecurity in the SAM CSA

It's often said that there are two types of companies: those that have been hacked, and those who don't know they have been hacked. The Internet was built 30 years ago on the basis of trust where information would be shared openly and freely. Today, the Internet threat landscape has fundamentally changed and proactive security measures that protect the organization responsibly, mitigate risk, and adapt to an ever-changing world are imperative. The costs of cyberattacks are manifold and can impact an organization in different ways. Internal costs are operational costs and relate to dealing with the cybercrime and incidence prevention. External costs include the consequences of the cyber-attack such as the loss or theft of sensitive information, operations' disruption, fines and penalties, infrastructure damage, or revenue losses due to loss of customers, reputation and impact on brand. Cyber- and IT Security, once considered material to just the technology and finance sectors, today with digital transformation, almost every company is an IT company in some way. Whilst digital transformation fuels business innovation, there are new risks such as increasingly sophisticated cyber-attacks, cost and complexity of regulatory pressures around compliance (e.g. GDPR) and shortage of cybersecurity skills. To encourage transparency and disclosure in 2019, more detailed questions on both Cybersecurity and Privacy Protection in the SAM Corporate Sustainability Assessment (CSA) have been added; companies from more than 25 different industries will be assessed. The SAM CSA assesses both cybersecurity risks and cybersecurity risk management frameworks: from digital governance (cyber board level oversight, engagement and director level experience of cybersecurity) through to the cyber strategy, compliance and cyber awareness and culture across the organization. The assessment extends to the cyber tactical capabilities including additional focus on Vulnerability Analysis which are an essential part of operational cyber hygiene. Cybersecurity disclosure in proxy statements and annual reports varies widely. The SAM CSA highlights emerging best practices, industry and regional differences and seeks to identify companies that are leading in their handling of cybersecurity issues.

Improving capital management at Japanese companies

Ronnie Lim

Despite governance improvements, Japanese companies continue to suffer from low valuations, which we ascribe to the absence of an appropriate financial strategy. As a result, our engagement in Japan focuses on improving companies' performance on capital management, a topic which can be addressed both via direct engagement and in proxy voting practices.

Codes of conduct
- Japanese Stewardship Code
- ICGN Global Governance Principles
- SDG 16: Peace, Justice and Strong Institutions; SDG4: Gender Equality

Corporate Governance: Accountability & Transparency
A company's corporate governance structure specifies the rights and responsibilities of the various stakeholders such as the management, supervisory directors, shareholders and other stakeholders. An effective corporate governance system focuses on a company's long term business continuity and protects shareholders' interests. A well-functioning corporate governance system can contribute to long term shareholder value. International and national principles and codes provide guidelines for good corporate governance. Corporate governance covers a number of important issues. Relevant subjects are: remuneration policy, shareholder rights, transparency, effective supervision of management, independent audit and risk management.

Following the publication of Japan's Stewardship Code in 2014, there has been an increase in both foreign and domestic institutional investors engaging with Japanese companies to persuade them to adopt governance reforms. We began our engagement theme focused on improving governance practices in Japan in 2016, with one of our main objectives being to improve board composition and structure. Here, some progress can be seen in the market as a whole, in that there has been a marked increase) in companies with boards comprised of one-third independent directors or more, rising from 6.4% in 2014 to over 33% in 2018.

While there has been a significant increase in the appointment of independent directors at some leading companies, Japanese companies' valuation (both absolute and relative) generally continue to be depressed by the lack of economic value creation. Our active ownership strategy has therefore also targeted engagement with policymakers as well as with our portfolio companies.

Setting the agenda for investor dialogues

In March 2017, the Council of Experts Concerning the Follow-up of Japan's Stewardship Code and Corporate Governance Code sought feedback

for the proposed revision of the latter. Specifically, it wanted to establish the Guidelines for Investor and Company Engagement to provide the agenda for investor dialogue. As part of our engagement, we provided feedback to this process.

We recommended that companies provide a credible financial strategy to help investors assess their management of debt and equity capital, and the framework on how they plan to deliver returns above their cost of capital. In recent years, Robeco, together with the Asian Corporate Governance Association and other investors, have engaged with several policymakers and influential stakeholders during many meetings in Japan to formally include this critical issue in future revisions.

Drilling down into the details

On 1 June, 2018, the Tokyo Stock Exchange announced revisions to the Corporate Governance Code, while the Financial Services Agency finalized the Guidelines for Investor and Company Engagement. These guidelines aim to supplement the Corporate Governance Code and Stewardship Code. Later that year in September, the Ministry of Economy, Trade and Industry announced revisions to the Corporate Governance System Practical Guidelines. In a statement, the International Corporate Governance Network further supported the "improvement of corporate disclosure reflecting discussions on capital cost, shareholders return, growth strategy and cash usage... and how this relates to the company's long-term value creation".

From high-level milestones to granular requests

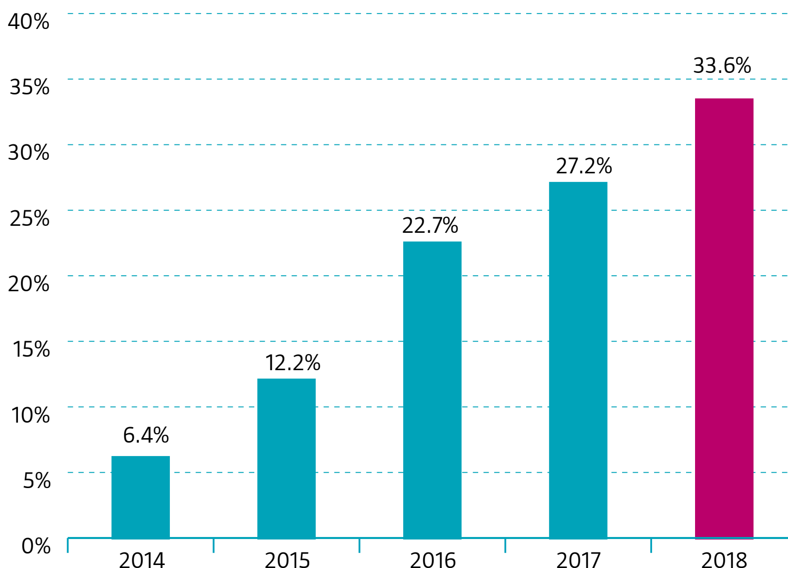
Our engagement with portfolio holdings in Japan has gradually evolved from seeking high-level milestones – like increasing the number of independent directors – to encouraging the company to improve its capital management through the adoption of specific measures. These include reducing their cross-holdings, and cutting excess cash levels by increasing dividend payout ratios and share buybacks.

In our previous research on the topic, we argued that in order to achieve sustainable economic value creation, a company's return on invested capital (ROIC) should exceed its cost of capital. Our analysis concluded that the overwhelming majority (70%) of companies in Japan had poor capital management, with 70% of over 2,000 TOPIX companies having a five-year negative return on their ROIC when compared with their weighted average cost of capital (WACC). Our current analysis shows that the same universe of companies had a median five-year ROIC of 5.4% compared to 5.1% at the end of 2017, representing a small improvement on a rolling basis.

Progress made, but challenges remain

So, what does this mean in practice? Some companies in the peer group

Ratio of Japanese companies with one-third or more independent directors



have improved, while others have not. Change is also taking place at differing rates. For example, one athletic footwear maker currently under engagement is still struggling with its operating profitability in a challenging retail environment, but at the same time is introducing new management performance criteria which are aligned to economic value creation (inventory cash conversion) and targets to reduce excess inventory. The company continues to reduce its non-core assets, and further raised its total payout ratio from 40% to 50%.

Furthermore, a leading real estate company has improved the disclosure of its capital management, and now manages its capital by balancing three objectives: appropriate financial leverage, investments in property assets and shareholder return enhancements. Tangible improvements include raising the total shareholder return ratio from 25% in 2017 to 35% including dividends and buybacks, and some return targets, including a 5% return on assets by 2025.

Focusing on the essentials of engagement

Our stewardship in Japan and Asia has typically involved engagement with local regulators and stakeholders in parallel with meetings with management representatives of our portfolio companies. We have found that effective company engagement requires a few essentials, which include meetings in person as well as written communication; demonstrating the financial as well as societal benefits following a course of action; and asking for specific milestones such as board incentives or increased payouts. We also find that meetings which include our portfolio managers enhance the credibility of our agenda, and in many cases enhances the usability of engagement results in investment cases.

IMPROVING CAPITAL MANAGEMENT AT JAPANESE COMPANIES

Reducing global waste
Xylem, Inc.
Total

Climate Action
BASF
Chevron
Hitachi Ltd.
Royal Dutch Shell

Environmental Challenges in the Oil and Gas Sector
BP
ConocoPhillips
Eni
ExxonMobil
Total

ESG Challenges in the Auto Industry
Bayerische Motoren Werke
Honda Motor
Toyota Motor

Sound Environmental Management
Jardine Matheson Holdings Ltd.

Palm Oil
Wilmar International
Genting Bhd.

Climate change and Well-being in the Office Real Estate Sector
Great Portland Estates Plc

Food Security
Bayer
Deere & Co.
DowDuPont Inc.

Living wage in the garment industry
The Home Depot
Adidas
NIKE

Data privacy
Vodafone
Facebook, Inc.
Apple
AT&T, Inc.
Singapore Telecommunications

Improving sustainability in the meat and fish supply chain
DSM
McDonald's

ESG risks and opportunities in the biopharmaceutical industry
Amgen
AstraZeneca Plc
Biogen IDEC, Inc.
Johnson & Johnson
Novartis

Social risks of sugar
Coca-Cola
Danone
Kellogg Co.
Nestlé
The Kraft Heinz Co.
Unilever

Sound Social Management
Wilmar International
Genting Bhd.
Bayer
DowDuPont Inc.
InterContinental Hotels Group Plc

Corporate Governance in Japan
Mitsui Fudosan Co. Ltd.

Corporate governance standards in Asia
ROHM Co. Ltd.
Hyundai Motor
Samsung Electronics
Hynix Semiconductor, Inc.
SK Holdings Co. Ltd.
INPEX Corp.

Good Governance
DSM
Heineken Holding
Unilever
Royal Dutch Shell
Samsung Electronics
Sun Hung Kai Properties Ltd.
Vale SA
Persimmon Plc
Royal Mail plc
Schneider Electric SA
Daiwa House Industry Co., Ltd.
Sumitomo Mitsui Financial Group, Inc.

Tax Accountability
Amgen
AstraZeneca Plc
Johnson & Johnson
Biogen IDEC, Inc.
RELX
SAP
Pfizer
Nestlé

Culture and Risk Governance in the Banking Sector
Wells Fargo & Co.
HSBC
ING Groep NV
Barclays Plc
JPMorgan Chase & Co., Inc.
Citigroup, Inc.
BNP Paribas SA

Cybersecurity
Reckitt Benckiser Group Plc
Visa, Inc.
Worldpay, Inc.
Deutsche Telekom
Vodafone

Global Compact breaches
During the quarter, nine companies were engaged based on potential breaches of the UN Global compact.

Robeco's Engagement Policy

Sustainability investing is integral to Robeco's overall strategy. We are convinced that integrating environmental, social and governance (ESG) factors results in better-informed investment decisions. Further we believe that our engagement with investee companies on financially material sustainability issues will have a positive impact on our investment results and on society.

Robeco actively uses its ownership rights to engage with companies on behalf of our clients in a constructive manner. We believe improvements in sustainable corporate behavior can result in an improved risk return profile of our investments. Robeco engages with companies worldwide, in both our equity and credit portfolios. Robeco carries out two different types of corporate engagement with the companies in which we invest; value engagement and enhanced engagement. In both types of engagement, Robeco aims to improve a company's behavior on environmental, social and/or corporate governance (ESG) related issues with the aim of improving the long-term performance of the company and ultimately the quality of investments for our clients.

Robeco adopts a holistic approach to integrating sustainability. We view sustainability as a long-term driver of change in markets, countries and companies which impacts future performance. Based on this belief, sustainability is considered as one of the value drivers in our investment process, similar to the way we look at other drivers such as company financials or market momentum.

The UN Global Compact

The principal code of conduct in Robeco's engagement process is the United Nations Global Compact. The UN Global Compact supports companies and other social players worldwide in stimulating corporate social responsibility. The Global Compact became effective in 2000 and there are now approximately 9,000 participating companies. It is the most endorsed code of conduct in this field. The Global Compact requires companies to embrace, support and adopt a number of core values within their own sphere of influence in the field of human rights, labor standards, the environment and anti-corruption measures. Ten universal principles have been identified to deal with the challenges of globalization.

Human rights

1. Companies should support and respect the protection of human rights as established at an international level
2. They should ensure that they are not complicit in human-rights abuses.

Labor standards

3. Companies should uphold the freedom of association and recognize the right to collective bargaining
4. Companies should abolish all forms of compulsory labor
5. Companies should abolish child labor
6. Companies should eliminate discrimination in employment.

Environment

7. Companies should adopt a prudent approach to environmental challenges
8. Companies should undertake initiatives to promote greater environmental responsibility
9. Companies should encourage the development and diffusion of environmentally friendly technologies.

Anti-corruption

10. Companies should work against all forms of corruption, including extortion and bribery.

International codes of conduct

Robeco has chosen to use broadly accepted external codes of conduct in order to assess the ESG responsibilities of the entities in which we invest. Robeco adheres to several independent and broadly accepted codes of conduct, statements and best practices and is a signatory to several of these codes. Next to the UN Global Compact, the most important codes, principles, and best practices for engagement followed by Robeco are:

- International Corporate Governance Network (ICGN) statement on Global Governance Principles
- United Nations Sustainable Development Goals
- United Nations Guiding Principles on Business and Human Rights
- OECD Guidelines for Multinational Enterprises

In addition to our own adherence to these codes, we also expect companies to follow these codes, principles, and best practices.

Robeco's Voting Policy

Robeco encourages good governance and sustainable corporate practices, which contribute to long-term shareholder value creation. Proxy voting is part of Robeco's Active Ownership approach. Robeco has adopted written procedures reasonably designed to ensure that we vote proxies in the best interest of our clients. The Robeco policy on corporate governance relies on the internationally accepted set of principles of the International Corporate Governance Network (ICGN). The ICGN principles have been revised

in June 2014. The exercise of voting rights is limited to those companies held in our portfolios. This concerns shares held in the mandates of our clients, where Robeco has been requested to vote on the client's behalf. By making active use of our voting rights, Robeco can, on behalf of our clients, encourage the companies concerned to increase the quality of the management of these companies and to improve their sustainability profile. We expect this to be beneficial in the long term for the development of shareholder value.

Collaboration

Where necessary, Robeco coordinates its engagement activities with other investors. Examples of this includes Eumedion; a platform for institutional investors in the field of corporate governance and the Carbon Disclosure Project, a partnership in the field of transparency on CO2 emissions from companies. Another important initiative to which Robeco is a signatory is the United Nations Principles for Responsible Investment. Within this context, institutional investors commit themselves to promoting responsible investment, both internally and externally.

Robeco's Active Ownership Team

Robeco's voting and engagement activities are carried out by a dedicated Active Ownership Team, working in close collaboration with Robeco's Investment Teams, and RobecoSAM's Sustainability Investing Research team. This team was established as a centralized competence centre in 2005. The team consists of 12 qualified active ownership professionals based in Rotterdam, the Netherlands, and Hong Kong. As Robeco operates across markets on a global basis, the team is multi-national and multi-lingual. The team is headed by Carola van Lamoen.

About Robeco

Robeco Institutional Asset Management B.V. (Robeco) is a global asset manager, headquartered in Rotterdam, the Netherlands. Robeco offers a mix of investment solutions within a broad range of strategies to institutional and private investors worldwide. As at 31 December 2017, Robeco had EUR 161 billion in assets under management. Founded in the Netherlands in 1929 as 'Rotterdamsch Beleggings Consortium', Robeco is a subsidiary of ORIX Corporation Europe N.V. (ORIX Europe), a holding company which also comprises the following subsidiaries and joint ventures: Boston Partners, Harbor Capital Advisors, Transtrend, RobecoSAM and Canara Robeco. ORIX Europe is the centre of asset management expertise for ORIX Corporation, based in Tokyo, Japan.

Robeco employs about 877 people in 15 countries (December 2017). The company has a strong European and US client base and a developing presence in key emerging markets, including Asia, India and Latin America.

Robeco strongly advocates responsible investing. Environmental, social and governance factors are integrated into the investment processes, and there is an exclusion policy is in place. Robeco also makes active use of its voting right and enters into dialogue with the companies in which it invests. To service institutional and business clients, Robeco has offices in Bahrain, Greater China (Mainland, Hong Kong, Taiwan), France, Germany, Japan, Luxembourg, Singapore, Spain, Switzerland, Sydney and the United States.

More information is available at www.robeco.com

ROBECO
The Investment Engineers

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