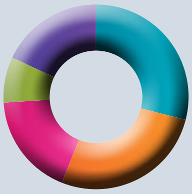
Active Ownership Report Q2-2019

BCCP | 31.03.2019 - 30.06.2019

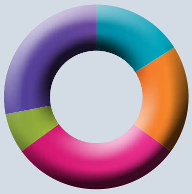
Engagement activities by region

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



Shareholder meetings voted by region

North America	16%
Europe	19%
Pacific	30%
Emerging Markets	7%
United Kingdom	28%



Voting overview

2019	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Total number of meetings voted	122	525		
Total number of agenda items voted	1.409	7974		
% Meetings voted against management	77%	74%		

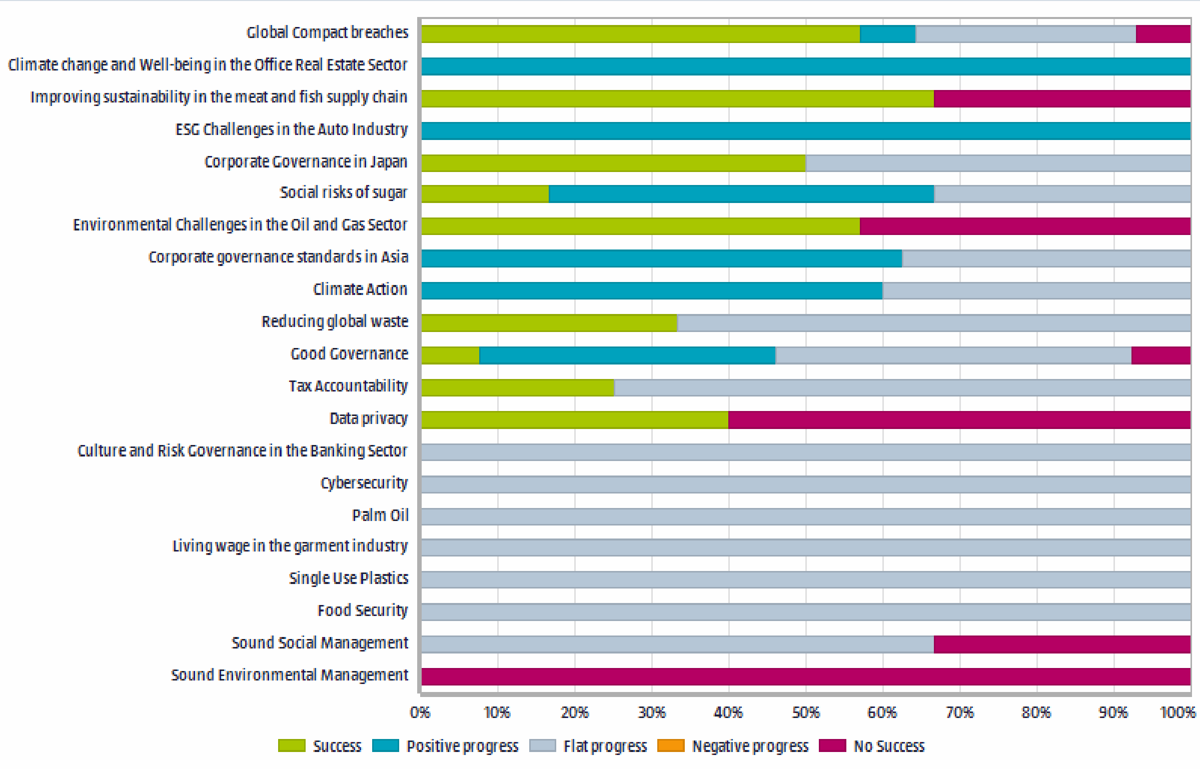
Engagement overview by topic

Environmental Management	18
Environmental Impact	3
Human Rights	4
Healthy Living	
Social Management	2
Corporate Governance	33
UN Global Compact	6

Engagement by contact type

Analysis (no actual contact with company)	19
(Open) Letter	4
Meeting at company offices	13
E-mail	26
Active voting	4
Shareholder resolution	
Conference call	25
Speaking at a shareholder meeting	4
Meeting at Robeco offices	8
Speaking at conferences	1
Issue press release	

Engagement results per theme



Contents

Good Governance P4
Following the conclusion of 2019's proxy voting season, Governance specialist Michiel van Esch gives his key takeaways on this year's developments, including regulatory developments, and the rising activism of shareholders on issues from the discharge of corporate boards to shareholder proposals.

Platform Living Wage P8
Millions of workers in the garment industry are unable to sustain themselves and their families using their own salaries. Laura Bosch and Danielle Essink have begun engaging companies that should pay a living-wage as it is a fundamental right and can ultimately advance their business.

Improving Sustainability in the Meat & Fish Supply chain P10
Global total meat consumption has quadrupled over the past two decades and is expected to double in the coming two decades, putting the pressure on sustainable meat and fish production. Peter van der Werf shares the insights from his three-year engagement program with companies in this industry.

Environmental Challenges in the Oil & Gas sector P14
Oil and Gas companies are particularly exposed to regulatory attempts to keep global warming below dangerous levels. For the last three years, Sylvia van Waveren has engaged with companies operating in the sector. Here, she shares her results.

ESG Challenges in the Auto Industry P18
As our electronic data is increasingly collected and stored online, the threat of having that data stolen has also risen. Active Ownership Specialist Kenneth Robertson delves into these risks and their implications for businesses.

Introduction

The second quarter of the year is always a busy time for Robeco's Active Ownership team, since the majority of shareholder meetings take place. In fact, we voted at nearly 4000 shareholder meetings in the first half of 2019. Climate change has been a recurring theme throughout these meetings, and continues to be a priority for our active ownership activities.

As investors, it is important that we understand how companies are positioning themselves for the market and regulatory changes that will arise as part of the global attempt to keep global warming below 2 degrees Celsius. Our engagement theme 'Environmental Challenges in the Oil & Gas sector' covers just this topic and concludes this quarter. Over the last three years, we have seen a clear divergence within the sector between companies that embrace their role in the energy transition, and those who are increasingly lagging their more forward-thinking peers.

Our efforts to combat climate change are not focused on a single sector. As Cristina Cedillo shares her insights on the automotive sector, new regulation and other trends are challenging the business models of global car makers. How companies react to these trends is likely a determinant of long-term success.

Lastly, in this report we delve into the EU Shareholder Rights Directive II - which has been in effect since early June. We also provide an update on our Living Wage engagement theme in addition to the conclusion of our three-year engagement focused on improving Sustainability in the Meat & Fish Supply chain.

Carola van Lamoen
Head of Active Ownership

Good Governance

Michiel van Esch

Europe is slowly preparing for the long-awaited second EU directive on shareholder rights. As part of the new directive, institutional investors will get a say on remuneration and related party transactions across all EU markets on a regular basis. As a result, we expect incentive structures to become a topic for discussion in all European markets in the coming years. It is a topic closely aligned with 'Say on Pay' votes, but currently is only common practice in the UK, the Netherlands and a few other EU markets.

Codes of conduct

- ICGN Global Governance Principles
- OECD Guidelines for Multinational Enterprises
- Sustainable Development Goals

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.

The EU Shareholder Rights Directive II: Ready for take-off

One might think that the directive's intent is to level the playing field in Europe on shareholder rights, but its name is somewhat misleading. The most important shareholder rights are still determined locally, often set in national company law. Issues that are still dealt with at a local level include deciding what should be on an AGM agenda, rules around multiple share classes, requirements to file shareholder resolutions or to call EGMs, shareholder protection around mergers and takeovers, and pre-emption rights for new share issues. The directive's focus, however, is to ensure that institutional shareholders fulfil their responsibility of becoming responsible stewards, requiring them to use their voting rights, engage their investee companies and report on their activities, with the aim of enhancing long-termism and accountability in the European equity markets. Overall, the directive might be more appropriately named the 'Shareholder Duties Directive'.

The discharge vote of confidence

Voting is increasingly a mechanism used to send a message, as opposed to a binary 'yes' or 'no' decision on formalized resolutions. One example is the discharge vote, which in recent years has taken on the function of voicing concern about governance practices and the way a company

interacts with its stakeholders. Discharge votes are only standard in a few markets, including the Netherlands and Germany. In many cases, a discharge vote formally releases directors from legal liability over the reporting year but can also be a wake-up-call from shareholders to improve governance.

Companies which have been facing problems with their governance practices see shareholder support for their discharge votes decline, as investors use it as a form of protest. The CEO of Deutsche Bank, who saw 25% of investors oppose a discharge vote due to governance issues at the bank, explained that he appreciated that in true shareholder democracies, support rates should no longer be at 99%, which had been the norm for many years. Directors at ING, a Dutch bank that was not able to win majority support for the discharge of its executive and supervisory boards, responded that they recognized the voting result as a clear sign that they need to continue to improve their practices. ING has faced serious issues related to money laundering and received a record fine from the Dutch regulator.

Dual share classes: having your cake and eating it

Meanwhile, in the US, the debate around dual share classes continues. Many companies that have recently staged IPOs often have multiple share classes, allowing management or a controlling shareholder to maintain most voting rights while having provided much less of the company's equity funding. Companies like Facebook, Alphabet and Snap have set up their share structures in such a way that the dominant voting power is heavily concentrated, sometimes even in the hands of just one person, giving shareholders only one effective voting option if they are unhappy with management – the one with their feet.

This is not a debate that is only taking place in the US. Hong Kong has played host to similar discussions over recent years, and even index providers, including MSCI, have involved shareholders in consultations to downplay the weight of non-voting stock in several of their indices. In the US and Hong Kong, authorities are not taking a strong stance on the 'one share, one vote' principle. Prohibiting dual share classes often scares new companies into listing their shares, in the fear of losing control of the company. One interesting suggestion to solve the problem was voiced by a commissioner of the SEC, proposing a grace period for new IPOs, allowing dual share classes only for a few years. The 'sunset clause' would then require a shareholder vote on a transition to a 'one share, one vote' structure. We have not seen concrete action for such regulation, and without additional pressure from shareholders, we do not expect this to come into being any time soon.

A gradual rise of shareholder democracy in the US

Also, in the US, the SEC recently provided more leeway for companies to disregard shareholder resolutions, provided there is a clear case that the issue at hand was sufficiently addressed by the board. We have seen a couple of these cases during 2019's AGM season. One notable example was ExxonMobil, which was successfully granted 'take no action' relief from the SEC on a shareholder resolution asking the company to set emission targets to align with the Paris climate agreements, and to follow several of its peers who already communicated their climate ambitions. This led to widespread protests by many shareholders, including Robeco, given that ExxonMobil lags many of its peers in its approach to climate change. The company's action also strengthens the feeling of many investors that the board is not sufficiently addressing the contribution it makes to global warming.

Yet, we continue to see many shareholder resolutions in the US, rendering this mechanism a valuable tool for shareholders to hold management to account. Such resolutions ask for traditional governance best practices such as separating the role of CEO and chairman, or facilitation of proxy voting access. Increasingly, we see other ESG topics gaining traction as well, including climate reporting, gender pay gap disclosure, and publishing policies on equal rights for a company's labor force. We also notice the support rates for shareholder resolutions picking up. Even though most resolutions do not surpass the 50% support threshold, many get very close, especially when considering votes in favor from unaffiliated shareholders. Only a few years ago, a 10% support rate was considered to be newsworthy.

Paying a Living Wage in the Garment Sector

Laura Bosch

Millions of workers employed throughout the garment industry's global supply chain are not able to make ends meet with the salary they receive at the end of their working day. Although most sourcing countries have minimum wages in place, these are often on the poverty line, and insufficient to cover workers' basic living expenses. Multinational corporations with long supply chains are deeply embedded in many economies, and the level of wages that they and their suppliers pay has a huge impact on many people's lives.

Codes of conduct

- UN Global Compact Principles 3 and 4
- OECD Guidelines for Multinational Enterprises Chapters
- SDG 1: No Poverty
- SDG 8: Decent Work and Economic Growth

Human Rights: Social Supply Chain Standards

Companies are increasingly being held accountable for poor labor conditions in their operations and that of their supply chains. This is the result of a number of different trends. The first of these is the transfer of production to low-wage countries, resulting in companies being faced with non-Western labor standards and conditions in their supply chain. Then there is a trend towards the more rapid and wider dissemination of information on the external effects of corporate activities. Furthermore, non-governmental organizations (NGOs) are playing an increasingly important role as social watchdogs and, finally, consumers are becoming more aware and more demanding in terms of corporate social responsibility. It is very important for companies, especially those that operate internationally and have well-known brand names, that generally accepted labor standards are followed throughout the supply chain.

There is a growing awareness of the need to respect the fundamental human rights of workers, included in the UN's Sustainable Development Goals' SDG 8 – 'Decent work and economic growth' – for which earning a living wage plays a key role. This is defined as the minimum income necessary for workers to meet basic needs for themselves and their families, including some discretionary income, earned within legal working hour limits.

In 2018, we joined the Living Wage Financials Platform, a global coalition of financial institutions. It has initiated an engagement program which aims to encourage, support, assess and monitor investee companies regarding their commitment to paying a living wage to the workers in their supply chains. Our dialog focuses on leading brands in the clothing and footwear sector who work with suppliers in sourcing countries that have poor labor practices.

Nowadays, corporate success and brand values are increasingly dependent on intangible assets. A key factor within labour-intensive sectors is human capital management, and the level of wages plays a key role in this field. Studies have shown that paying a fair wage leads to increased worker morale, better health and access to basic services. Workers who earn a living wage can meet their own basic needs and those of their families, as well as put aside savings, thus being more likely to find

their way out of poverty. The focus on a living wage also advances respect for a number of other fundamental human rights in global supply chains, and underlines our role as a responsible investor.

Promoting fair wages provides benefits for our investee companies from a financial standpoint. It ultimately improves their productivity by contributing to lower absenteeism and turnover rates, and lowers recruiting and training costs. The overall efficiency of companies' production models may also improve, as companies review their purchasing practices and work with their suppliers to improve performance and identify production efficiencies. Another vital intangible asset for companies is their reputation. Responsible investors, consumers and other stakeholders are becoming more critical of organizations that do not respect their social license to operate, representing a material risk for the business. Companies are expected to respect the rights and needs of their employees, including paying living wages.

Our engagement dialog firstly assesses whether the company identifies living wage as a key issue, and whether it has policies addressing this matter throughout its supply chain. Due to the existing divergent definitions of fair wages, special attention is given to the scope of the living wage definition used by the company. We encourage them to increase transparency regarding wage data at supplier facilities while undertaking a wage gap analysis of supply chain regions and key suppliers. Identifying wage gaps within the supply chain enables companies to work with suppliers to calculate how much it would cost to raise salaries to a living wage level.

Purchasing practices can have a positive impact on a supplier's ability to pay a living wage. Through our engagement, we encourage companies to seek active collaboration with stakeholders at different levels to advance the case for a living wage. This includes improving purchasing processes to lower the negative impacts on supplier operations and on workers' human rights. We find it crucial to have a grievance mechanism in place covering external stakeholders, and to make sure that complaints are independently assessed. Transparency on how a company operates this grievance procedure and how it has responded to the complaints received is key to being able to assess its overall effectiveness. Although we are in the first year of this engagement program, some garment companies already identify living wages as a salient human right issue. Nonetheless, the industry will need to work together to lay the foundation for living wages.
The average standard of disclosure in the sector is notably improving, although the level of detail in the data reported often remains inadequate. At this stage, few companies are able to identify wage levels at their suppliers, and therefore cannot calculate the true labor cost per unit purchased. This hinders their ability to account for wage levels in their purchasing practices, while also making it difficult to identify and mitigate potential wage gaps.

Paying living wages is not as simple as it looks, since most brands do not own factories, and instead buy ready-made garments from suppliers who manage the factories and employ workers.
For that reason, it is crucial to ensure a level playing field and a common wage standard, so that brands paying a higher purchasing price avoid being competitively disadvantaged by doing the right thing. Going forward, we expect companies to take ownership over the living wage implementation process.

Improving sustainability in the meat supply chain

Peter van der Werf

Total demand for animal protein products continues to grow globally. Developed markets have experienced either flat growth rates or a small decline in the consumption of meat. But the growing middle class in emerging markets is driving significant growth, as with growing affluence comes a growing taste for animal protein.

Codes of conduct
- UN Global Compact
- OECD Guidelines for Multinational Enterprises Chapters
- SDG 12: Responsible Production and Consumption
- SDG 14: Life below Water
- SDG 15: Life on land

Healthy Living: Product Safety
Trends such as the liberalization of global trade and the shifting demands of consumers towards more healthy, tasty and safe options, are changing the quantity oriented food production. Therefore, food safety issues may become non-tariff trade barriers that prevent national meat industries from getting access to international markets. There is increased consumption of food that is not or less processed than branded products. There are many opportunities for companies to respond to this trend. Certification (i.e. Organic and Fair Trade) and good animal husbandry might enable companies to enter a premium market segment and charge a premium price. These options are available for both processors, retailers and restaurants.

US consumers continue to be the world's leading meat eaters, with an annual average of 102 kilograms of meat per person. In contrast, a developing nation such as Ethiopia still averages only at 7 kilograms per head but is set to catch up with developed countries as they continue to grow. Global total meat consumption has quadrupled over the past two decades and is expected to double in the next two. Therefore, improving sustainability in the meat and fish supply chain is crucial for the long-term sustainability of investments in this sector. Since 2016, Robeco has engaged with 11 companies active in the value chain, ranging from animal nutrition companies and meat producers, to quick service restaurants and retailers that cover the full supply chain.

Overuse of antibiotics in livestock production poses a risk to human health

In partnership with the Farm Animal Investment Risk and Return (FAIRR) group and the Interfaith Centre on Corporate Responsibility (ICCR), we have dedicated many dialogues with livestock production companies to encourage less use of antibiotics that are important for human use. Continuing the prophylactic application of antibiotics is projected to cause 10 million human deaths by 2050 due

to antimicrobial resistance. As part of our engagement efforts, we co-filed a shareholder resolution in 2017 at a quick service restaurant calling on it to adopt a global antibiotics policy. This achieved 27% shareholder support and the company updated its antibiotics policy just four months after its AGM was held. Our discussions with the animal nutrition companies focused on opportunities in the development of probiotics that can replace some of the antibiotics. These improve gut health in the animals and thereby reduce the need to use antibiotics to prevent diseases. Companies operating in this field are set to benefit from phasing out antibiotics, which many producers have committed to during our engagement program.

Significant impact on climate change through land use change

In recent years, awareness has grown regarding the significant impact on climate change arising from meat production, predominantly through the production of animal feed such as the protein-rich soybean in South America. This land use change through deforestation leads to the loss of a large carbon sink and its associated biodiversity. This shift is driven by consumer choices in the US, China or Europe, where much of the beef or the soy is exported. The call to reduce the climate change impact of the western diet was also clearly made in the EAT Lancet study published in January 2019, which was embraced by many dietary guidelines in developed markets. Robeco has also actively supported the Cerrado Manifesto since 2018, with the aim of developing a mechanism to halt deforestation in the Cerrado, the second-most important biome in Brazil and home to a large portion of the soy and beef production in the country.

Animal welfare is key to reducing ethical concerns from western consumers

During the three years of engagement, we have spoken with companies directly handling livestock in their slaughterhouses on ensuring animal welfare. We undertook a collective engagement with other investors in the Business Benchmark for Farm Animal Welfare (BBFAW) group to tackle this topic. For the objective of 'animal welfare' we encouraged companies to increase video surveillance in their slaughterhouses. This was mainly necessary on the kill floor, where cows and pigs need to be humanely slaughtered, but where employees are under pressure to increase the speed of the processing line. Regarding the objective 'labor standards, we challenged companies active in poultry for exposing their laborers to a higher risk of significant health and safety incidents after increasing the processing line speed to 175 birds per minute. We also asked poultry companies to install video surveillance on chicken harvesters – workers who collect chickens from farmers and deposit them in collection carts to transport them to the slaughterhouse. In many instances, the abuses that were reported took place at suppliers who didn't comply with the animal welfare policies of the meat processing companies. Better oversight is crucial, and we have seen good progress in that respect.

High labor standards are crucial to prevent fines and lawsuits

As previously mentioned, meat processing is a high-risk sector for occupational health and safety incidents, due to the repetitive nature of the work. The same cutting movement is repeated for every animal that passes through the processing line during an entire shift. We encouraged companies in the US to reduce the line speed, enable workers to swap activities, and enable labor union representation for workers to ensure freedom of association and collective bargaining opportunities.

Product quality and safety management: a risk factor in Brazil

Several Brazilian companies faced large problems with product quality and safety management that led to a temporary export ban on their beef products to many markets in Europe and China. We extensively discussed their risk management and compliance systems, focusing on maintaining product integrity, but also on the facilitation payments made to veterinarians with the aim of releasing the products from processing plants into export channels more quickly. For those companies with government investigations into their product quality and safety management practices, we have closed our dialogue on this topic, believing it to be non-effective.

Norwegian aquaculture practices need to be translated into global operations

We spoke with a Norwegian salmon producer about its practices and how they should be judged against the Aquaculture Stewardship Council (ASC) certification standard. The company is on its way to getting 100% certification but faces challenges in its operations in Scotland and Chile, where standards are lower compared to Norway. In addition, sea lice infestations and algae have wiped out fish, questioning the sustainability of the industrial aquaculture model. On the positive side, farmed fish has a significantly lower carbon footprint due to a more efficient feed-conversion ratio compared to land-based livestock. This makes for another argument in its favor, next to the cited health benefits of eating more seafood.

Innovation management is driving a transition to sustainable protein production

Finally, for the topic of innovation management, we have discussed the acquisition of sustainable protein sources with the quick service restaurants and retailers. While they initially cited consumer demand as leading factor, they are now expressing a growing awareness of the overall footprint of their animal protein products, and a need to work on preventing deforestation to mitigate this impact.

INVESTOR SPOTLIGHT

Taeke Wiersm, Co-Head of Credit Research

The successful IPO of Beyond Meat in the US in May 2019 has drawn attention to the alternative meat products trend. Food companies will try to benefit from this by introducing their own lines of plant-based products, or acquire companies already making these products, leading to more M&As in the sector. Companies that have already had some products in this category will allocate more advertising and promotion resources to give the segment a push.

Barclays research estimates that the value of the alternative meat market can reach USD 140 billion in the next 10 years (versus USD 14 billion today), with alternative meat players capturing 10% of the USD 1.4 trillion global meat industry. Market penetration of plant-based meat in the US is around 1% versus an estimated 13% share for plant-based milk (almond, oats, coconut, etc.). Research shows that in the US, as many as 50% of consumers are seeking more plant-based foods in their diet, and 40% are open to reducing their traditional meat consumption.

Alternative meat products' taste profile has strongly improved over the years. There are concerns that alternate meat offerings may not necessarily be much healthier than their meat equivalents. While the calories that they contain are similar, the sodium level is higher, but the amount of cholesterol is lower. However, the reduction in the environmental footprint of the consumer's diet is an important reason for a growing number of people to embrace a flexitarian diet, or even further to a vegetarian or vegan diet, using these alternative protein products.

IMPROVING SUSTAINABILITY IN THE MEAT SUPPLY CHAIN

Environmental challenges in the oil and gas sector

Sylvia van Waveren

Robeco has engaged with companies in the oil and gas sector since 2016. In that time, we have seen fundamental changes taking place, as companies grapple with the shifting future of their industry. As our engagement theme comes to an end, following a three-year program, we look back at the progress made during that time.

Codes of conduct

- UN Global Compact Principles 7-9
- Rio Declaration on Environment and Development
- OECD Guidelines for Multinational Enterprises Chapters
- SDG 7: Affordable and Clean Energy
- SDG 13: Climate Action

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.

The business model of oil and gas companies is being eroded by rising capital intensity and diminishing returns. This effect is amplified by technology dynamics such as the rise of renewable energy, the benefits of energy storage, and the potential of electrified transportation. At the same time, the threat of tighter environmental and climate change legislation on a global, regional and national level is looming in the background, and pressure for more concerted climate-policy coordination has increased with the COP21 agreement reached in Paris in 2015. In 2016, we therefore launched a three-year engagement program to prompt companies to keep pace with the energy transition, which at that time was already underway. Our peer group consisted of six international and five national oil and gas companies, allowing us insight across the sector as a whole. It also brought an understanding into the differing levels of ambition on the energy transition of companies with different market backgrounds and free floats.

From Goals to Results

Our engagement objectives were designed to encourage companies to embrace the energy transition and

the drivers that will shape the new energy world. Our focus therefore fell on the implementation of a future-proof business strategy, striving for operational carbon efficiency, assessing asset portfolio resilience, and working on product stewardship. Public policy was also a focus of our engagement, due to our belief that companies should, at the very least, not lobby against stricter climate change regulation. On each objective, we are happy to report that progress has been made.

While operational (scope 1 & 2) emissions represent a small fraction of the greenhouse gases linked to used products, a tremendous effort has been undertaken to reduce these. Companies have improved their energy efficiency, reduced their methane emissions, and eliminated almost all routine flaring emissions. Exiting highly carbon-intensive production arenas such as oil sands by some companies under engagement also illustrates this positive development in the sector.

We examined which companies are investing in low-carbon assets and embracing innovative technologies. We have seen a wave of new energy investments in the sector such as an increase in the sales of biofuels and the development of negative emissions, including natural sinks such as (re) forestation. Companies have been spreading their investments across various technologies, looking to capture the upside potential. Different strategies exist, with some companies developing in-house capabilities, and others using M&A to quickly establish a market presence.

Planning for Tomorrow, Today

The shift from producing oil to natural gas is expected to continue, as production forecasts for 2022 show companies increasing the share of natural gas in their portfolios by roughly 14% to 55%. We have also witnessed an increase in refining crude oil and gas into petrochemicals, and an expansion downstream into gas and supplying power to the retail market, including through the use of renewables.

Many companies are increasingly thinking of the long-term, with some even going so far as to set reduction targets for product emissions. Despite this positive development, we also regrettably noticed that some companies are deploying a 'last-one standing strategy', in which they resist the energy transition. In this scenario, we need to be conscious that not all companies can claim to be the 'last one'. Lastly, national oil companies with a low replacement cost of reserves may prove to have the best chance of becoming the 'last ones'.

Scaling up Climate Change

Whilst each objective was designed and measured at a company level, events taking place at the sector-wide level have also been an important driver for progress during the three years of engagement. In many cases, these led to new requirements and indicators, which we used in our program.

With the publication of the Task Force on Climate-related Financial Disclosures (TCFD) recommendations in 2017, a framework was set by the international financial industry to disclose climate-related financial data in a standardized way. Our engagements have since then increasingly focused on requesting companies to use this framework in their reports. Four of our engaged companies now publicly say that they are committing to the TCFD.

Another development was the set-up of the Transition Pathway Initiative (TPI). Launched in January 2017, this is a global initiative led by asset owners and supported by asset managers. The TPI tool enables the assessment of companies' carbon management quality and carbon performance within a selected sector. We have used the TPI results extensively in our engagements by using it as a peer group analyses, motivating the companies to step up their efforts in order to get a higher rank in the TPI framework.

Collaboration leads to magnified results

Finally, Climate Action 100+ (CA100+) was launched, creating an enormous momentum for the engagement efforts with the oil and gas industry. CA100+ is an investor initiative to ensure that the world's largest corporate greenhouse gas emitters take the necessary action on climate change. Since its launch in December 2017, Robeco has been an active member, (co)-leading engagements with one oil and gas company and one utility. Robeco is also coordinating the engagement strategy in the automotive industry. In the AGM season of 2019, the CA100+ collaborators presented a joint statement in relation to climate change at two European companies that we have under engagement. For one of these companies, Robeco co-filed a shareholder resolution and was one of the leaders in the joint-statement.

Looking back on three years of engagement

Our engagements with the oil and gas companies have in general led to some successful outcomes. Of the 11 companies within the peer group, we have been able to close seven successfully, based on their progress on the underlying objectives set at the beginning of the program. For three of the companies, regrettably we were unable to make sufficient progress, due to their lack of ambition over their climate change strategies and management, and therefore closed these engagements unsuccessfully. For the remaining company, we believe that while it has not made sufficient progress for the engagement to be closed successfully, its trajectory is positive, and therefore we can report that positive progress has been made.

Engagements with the five national oil companies progressed in a mixed way. In general, these companies have been more difficult to engage, largely because they are more difficult to approach. Typically, state-owned oil companies also have less capital flexibility, which means they may be less agile and slower to mobilize in response to future disruptions such as increased climate regulation. Still, we were able to successfully close our engagement with two of them and report positive progress at one.

There is a marked difference in preparedness for a low-carbon energy transition between companies in Europe versus the US and the rest of the world. The European companies are better engaged with the transition and are more successfully taking the necessary steps to limit their exposure to climate risks than companies elsewhere. This could be a timing effect, with European companies responding earlier to normative pressure and regional economic incentives. All our engagements with European companies were successfully closed.

INVESTOR SPOTLIGHT

Chris Berkouwer, Portfolio manager, Global Stars Equities

As investors, we need to know how oil and gas companies will deal with these changes in their industry, how they will address the huge risks, and how they plan to profit from the opportunities that arise. This will allow us to pick the winners of this transformation.

It's unlikely that the world can completely shy away from fossil fuels in just a few years. There are still too many pockets of the economy where substitution to bio-based alternatives or renewables cannot yet be made, or is prohibitively expensive. In the meantime, the higher profit returns from conventional fuels will provide energy companies with the firepower to fund the re-direction to a low-carbon future.

Engaging with oil and gas companies help to craft their future strategic direction to a low-carbon economy. We should not forget that these companies often have the means, both cash flow wise and technologically-wise, to provide solutions to the climate problem. The creative destruction and re-inventing capabilities of energy companies is often underestimated, but herein lies the key to keep them onboard in our fight against climate change. Our engagements efforts to, tie long-term climate ambitions to short-term incentive structures, for example, is an important first step in the right direction.

ENVIRONMENTAL CHALLENGES IN THE OIL AND GAS SECTOR

ESG challenges in the auto industry

Cristina Cedillo

As greenhouse gas emissions from the transport sector continue to rise in US and European markets, policymakers are setting increasingly stringent fuel economy and fleet emissions standards. The past year has been an important period in creating the regulatory framework that will shape the industry's technology development for the next decade, says engagement specialist Cristina Cedillo.

Codes of conduct

- UN Global Compact Principles 7-9
- Rio Declaration on Environment and Development
- OECD Guidelines for Multinational Enterprises Chapters
- SDG 11: Sustainable Cities and Communities

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.

In March 2019, the EU set a target to reduce the average CO2 emissions from new cars by 15% in 2025 and by 37.5% in 2030, both relative to a 2021 baseline. Attaining these standards can only be achieved through a significant introduction of electrified vehicles (EVs) – accounting for about a third of new car sales by 2030.

Meanwhile, in the US, the appetite for mitigating fleet emissions is waning. In August 2018, regulators announced that they would abandon the long-term fuel economy standards for passenger cars and light trucks developed by the Obama Administration for 2022-2025, declaring that they are "too high".

The US Environmental Protection Agency is also seeking to revoke a waiver that allows California to set vehicle emissions standards and sales quotas on zero-emission vehicles that each automaker must comply with in California and 13 other states.

These developments illustrate the challenging and inconsistent regulatory environment that automakers are facing across key markets. Despite the Paris Agreement's ambition of limiting global warming to well-below 2°C above pre-industrial levels, the policies pursued in the EU and the US clearly show contrasting levels of commitment. Yet, both regulatory

developments have in common an underlying phenomenon – corporate lobbying.

Are carmakers walking the talk?

European trade associations in the auto industry denounced the proposals on fleet emissions standards in the EU, calling them unrealistic, very aggressive and overly challenging. The EU's target is 50% stricter than the auto industry had lobbied for, but more lenient than some city authorities and campaigners had demanded. In the US, once the Trump Administration came into power in 2017, the auto industry associations strongly advocated for the review and adjustment of the Obama era fuel economy standards.

These developments have revealed that the policy positions and arguments used by these associations are not always aligned with the more virtuous public statements made by car manufacturers, and their support for the goals of the Paris Agreement of 2015.

There is a growing concern among investors about the apparently inconsistent approach of companies to lobbying on climate-related policies. The misalignment between companies and their memberships in trade associations obfuscates the actual policy position that carmakers have, potentially sending mixed signals to policymakers and investors. More importantly, the transition to alternative drivetrains, such as EVs, can only be successful with a consistent and progressive regulatory framework. As carmakers start committing substantial investments to EVs, it only makes sense to support regulation that sets an even playing field for the industry and adopts the right incentives.

Robeco joined a campaign led by the Church of England Pensions Board and Swedish pension fund AP7 that aims to address the perceived inconsistencies in climate lobbying in the auto industry. We ask corporate boards to assess their memberships and act to reconcile identified misalignments. In addition, Robeco co-filed a shareholder resolution at the annual general meeting of Ford in 2019 that asked for disclosures on company policies and procedures governing lobbying, the payments used for lobbying, and the management's decision-making process and the board's oversight for making such payments. The resolution received support from 16.5% of the votes, sending a clear signal to the company to act.

So far, our dialogue with the companies has provided little evidence that there is adequate oversight by the board on the policy positioning that they are advocating for directly and indirectly via industry associations. We have also consistently heard from carmakers that consumer demand for EVs is one of the biggest challenges to meet more stringent fleet emissions standards and to accelerate the electrification of their fleets.

The challenge of balancing emissions

Carmakers have tough choices to make to meet both tougher regulation and shifting consumer preferences towards larger vehicles like SUVs, which are less fuel efficient. Decarbonizing their fleets will come at a cost, with estimated technology costs of EUR 3,000 per vehicle. To comply with European fleet emissions standards, carmakers are challenged to reach a level where EVs account for approximately 20-30% of sales. These projections, however, are still far from achieving the emissions reductions needed to limit global warming to well below 2°C. The industry should therefore be prepared for persisting – if not increasing – climate policy pressure.

Overall, the auto industry has taken a cautious stance towards alternative drivetrains. Uncertainties around policy developments (particularly in the US), technology costs and developments, and consumer acceptance have led some carmakers to adopt a "wait-and-see" attitude. Moreover, the adoption of EVs is expected to vary across regions, with China and Europe expected to drive the majority of EV sales globally. Therefore, carmakers' exposure to these EV markets will be key in accelerating the shift to alternative drivetrains.

To date, only three of the traditional carmakers in the peer group of our engagement have committed to achieving a carbon-neutral fleet. The Japanese carmakers were the first to announce their ambition to achieve net-zero operations and fleet by 2050. More recently, earlier this year, one of the European carmakers in the peer group took aim at achieving a carbon-neutral fleet by 2039. Most of the incumbents are yet to develop longer-term strategies and targets that extend beyond 2025.

Moreover, 2021 will be a critical year for carmakers with large exposure to the European market. Complying with the EU's 2021 fleet emissions standards remains an open question for some of them. A substantial roll-out of EVs and fuel efficiency gains will be needed. As carmakers announce the launch of new electrified models across various segments in the coming years, their EV offering will significantly expand – and consumer demand for EVs will be tested.

The coming decade will be critical for the auto industry. Although the direction of travel is clearly pointing at the full decarbonization of passenger vehicles, there is still uncertainty around the speed of change, technological development, and the carmakers' ability to weather the fundamental transformation that needs to take place. In our engagement, we will continue to encourage companies to assess how the energy transition will affect their business, incorporate in their strategies a long-term ambition to decarbonize their operations and fleets, and detail how exactly they plan to meet such ambitions.

INVESTOR SPOTLIGHT

Evert Giesen, Credits Analyst

In the last few years we have seen most traditional car manufacturers announcing large EV model programs. In 2018 and early 2019, we saw the first models coming to the market, but most product introductions will be later in 2020 and 2021. The first model introductions show that the traditional original equipment makers (OEMs) have the capability to manufacture EVs.

To reach the 2021 EU emission targets, a small number of EV sales will probably be sufficient. For the more ambitious 2025 and 2030 targets, EV sales need to increase a lot. This will require substantial investments from the car manufacturers to meet this production. It also remains questionable whether production costs of EVs will decline enough to attract consumers without fiscal incentives. In addition, it will be a challenge to produce EVs at similar profit margins to combustion engines. The transformation to EVs will be a challenge for the industry and a drag on profitability in the coming years.

We don't think that new entrants will be able to grab a big share of the EV car market. As recent examples have shown, it can be a big struggle for new entrants to produce them in high volumes. New entrants will also face the same production cost hurdles as existing players. In addition, they need to build up a production footprint, build a dealer network, and gain expertise in high volume production. We expect that the traditional auto OEMs will largely maintain their market share. Given the high value of required investments, and the expected low profitability of EVs, we prefer larger players that have sound profitability. For some smaller players, the required investments could be too big.

Reducing global waste
China Everbright International Ltd.
Taiwan Semiconductor Manufacturing Co. Ltd.
Xylem, Inc.

Climate Action
BASF
Chevron
Hitachi Ltd.
Lukoil Holdings OAO
Royal Dutch Shell

Environmental Challenges in the Oil and Gas Sector
BP
ConocoPhillips
Eni
ExxonMobil
Total
Rosneft NK OAO
Petroleo Brasileiro

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

Single Use Plastics
Nestlé
Procter & Gamble Co.

Food Security
Bayer
Deere & Co.
DowDuPont Inc.

Living wage in the garment industry
The Home Depot
Adidas
NIKE
Burberry Group
Inditex

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

Improving sustainability in the meat and fish supply chain
DSM
McDonald's
WH Group Ltd. (HK)

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

Sound Social Management
Bayer
InterContinental Hotels Group Plc
Facebook, Inc.

Corporate Governance in Japan
Mitsui Fudosan Co. Ltd.
OMRON Corp.

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

Good Governance
DSM
Heineken Holding
Unilever
Royal Dutch Shell
Petroleo Brasileiro
Samsung Electronics
Sun Hung Kai Properties Ltd.
Hon Hai Precision Industry Co. Ltd.
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.
Bank of America Corp.
BNP Paribas SA

Cybersecurity

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

Global Compact breaches

During the quarter, fourteen companies were engaged based on potential breaches in 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

1318-08'19