

## Introduction

Baillie Gifford recognises that owning a company's shares on behalf of clients confers certain rights and responsibilities. At the same time, environmental, social and governance (ESG) issues, and the management thereof, are integral to the sustainability of a business. For this reason, Baillie Gifford considers ESG issues when analysing and reviewing a company, and there is a dedicated Corporate Governance Team who also take on the share-ownership responsibilities for our clients.

As active managers, a key part of our investment strategy is to assess the quality of company management, in particular, management attitudes to shareholders. When combined with financial information, non-financial business information can provide valuable insight into the overall quality of management. Given that significant ESG issues play-out over the medium to longer term and that our clients are invested for the longer term, it is important that companies' approaches to ESG issues are considered on a case by case basis.

## Approach

Our investment approach aims to add value for our clients through the use of proprietary, fundamental research, building up an in-depth knowledge of individual companies in order to develop a view on their prospects. As part of this investment process we endeavour to identify the issues, financial and ESG, within companies that we believe could have a material impact on shareholder value.

Our approach to the social and environmental aspects of share ownership is based on engagement and dialogue rather than exclusion. Using in-house and external research, we identify key issues relating to our clients' shareholdings and discuss them with the companies concerned. In this way, we encourage companies to monitor and address the material social and environmental risks and opportunities facing their businesses. We believe that this process can contribute to the long term value of our clients' investments.

The Corporate Governance Team analyses all companies in which we are invested at least once a year. We then use a rating system so that we engage with the right companies on the right issues, thereby concentrating our efforts where they can be most effective. Companies whose ESG performance or disclosure is not up to standard are identified as engagement priorities. Following identification, further analysis is undertaken which makes use of all publicly available company documents, previous research pieces published on the Baillie Gifford Research Library, and analysis provided by ESG research providers and various brokers.

## Engagement Themes

The ESG issues we focus on vary between geographic region, industry sector and between companies, and are dependant on the emphasis of a company's core business activities.

### *Key ESG issues*

The following list is neither exhaustive nor exclusive, but is representative of our detailed expectations of companies on specific ESG issues.

#### *Governance*

- Board-level responsibility for significant ESG issues
- Appropriate systems for assessment of risks and opportunities
- Formal policies and systems for implementation and subsequent monitoring of effectiveness
- Dialogues with stakeholders and disclosure of the above in publicly available reports
- Incorporation of relevant ESG issues into long term executive compensation

### *Environment*

- Have an understanding of significant environmental challenges facing the business directly or indirectly, for example through the supply chain
- Support a precautionary approach to manage and mitigate environmental impacts
- Specific environmental issues considered include:
  - pollution impacts and liabilities
  - climate change (see below)
  - water management
  - resource consumption
  - impacts on biodiversity
  - market opportunities for new products or services

### *Climate Change*

- Encourage effective management of climate change risks and opportunities
- Reduce direct and indirect greenhouse gas emissions and integrate climate change policies into business strategies
- Develop corporate reporting and disclosure on climate change so that investors can properly assess associated investment risks and opportunities

### *Labour*

- Adopt a code of conduct based on the International Labour Organization's Declaration on Fundamental Principles and Rights at Work and develop management systems to implement this code
- Monitor effectiveness of the code and take action to improve standards where risks and weaknesses are identified
- Focus on health and safety management systems and performance, particularly in high-risk sectors (e.g. oil & gas) and with business associates and contractors
- Manage employee skills base

### *Supply Chain*

- Manage exposure to all social and environmental risks up and down the supply chain
- Proactively develop risk mitigation and business opportunities within the supply chain

### *Bribery & Corruption*

- Work against corruption in all its forms including extortion and bribery
- For companies in extractive industries (such as oil, gas and minerals), support and actively participate in the Extractive Industries Transparency Initiative
- Support employees in appropriate ethical conduct through training and reporting procedures such as whistle-blowing hotlines
- Enforce robust governance and internal control systems

### *Stakeholder Relationships*

- Consider stakeholder relationships including employees, suppliers, customers, shareholders, regulators etc.

## Corporate Disclosure

Currently levels of disclosure vary between sectors and between countries. Baillie Gifford endeavours to engage with all the companies in which it is invested on corporate governance, environmental and social issues where disclosure is either limited or not aligned with best practice. Best practice is specific to the sector and the country the company is incorporated in and these differences are taken into consideration when analysing and engaging with a company.

Issues material to investors should be set out succinctly in the annual report. Disclosure should contain a policy element, description of company wide implementation plans, indication of recent performance, and targets against which future performance will be evaluated.

In accordance with the ABI's (Association of British Insurers) revised Guidelines on Responsible Investment Disclosure, Baillie Gifford believes that: ESG risks should be reported in the context of the whole range of risks and opportunities faced by the company; that the ESG-related reporting should contain an outlook; and that it should describe Board actions to reduce risks. We also fully endorse the International Corporate Governance Network's (ICGN) Statement and Guidance on Non-financial Business Reporting.

## Evaluating the effectiveness of our intervention

When engaging with companies on ESG, we set clear objectives. Our underlying aim is to develop a good understanding of a company's policies, systems and performance. We encourage improvements where we believe these do not meet an appropriate standard and are not in our clients' best interests.

We monitor companies' progress and follow up on any meetings we have with companies when necessary. We actively consider whether or not the objectives we set at the time of our meeting with the company have been met.

## Industry Groups

We build and maintain strong connections with other shareholders to increase the influence we can bring to bear on our clients' behalf. We do this through formal and informal means. In 2007 we became a signatory to the UN Principles for Responsible Investment (UNPRI). The UNPRI are a set of principles which encourage the incorporation of ESG issues into mainstream investment decision-making and ownership practices. Having analysed and engaged with companies on ESG issues for a number of years, becoming a signatory was a natural progression towards greater transparency and accountability to our clients on ESG issues.

Less formally we often meet and network with ESG peers and when appropriate arrange joint meetings with company representatives.

In addition, we have significant input into UKSIF, the UK Sustainable Investment and Finance association, and therefore the UK's ESG agenda, through our participation in the UKSIF Advisory Group. Baillie Gifford has also been a signatory to the Carbon Disclosure Project (CDP) since its inception in 2000. It provides a secretariat for the world's largest institutional investor collaboration on the business implications of climate change. We are also members of the Extractive Industries Transparency Initiative.

## Client requirements and servicing

In addition to our normal engagement process, our Corporate Governance Team can communicate our clients' concerns to companies on request. We also have several clients for whom we avoid investment in specific companies or sectors. Our clients receive quarterly reports on corporate engagement, summarising our activities and conclusions from meetings with senior management at the companies in which we invest. We are transparent and accountable on ESG issues.

## Conclusion

Our ESG engagement policy is consistent with Baillie Gifford's overall aims, which are to provide good long-term performance to our clients, and place principal importance on our clients' interests. When considering ESG issues, our main objective has always been to add value for our clients by engaging with company management and developing an understanding of how companies' approach to ESG issues impacts investment returns. Having a separate Corporate Governance Team has facilitated this. Through our ESG engagement process, we aim to ensure the companies we invest in are well managed and are taking all material risks and opportunities into consideration. We believe this improves the returns for our clients.

### Further Information

Carbon Disclosure Project: <http://www.cdproject.net>

Extractive Industries Transparency Initiative: <http://eitransparency.org>

Guidelines on Responsible Investment Disclosure: <http://www.abi.org.uk>

ICGN Statement and Guidance on Non-financial Business Reporting: [http://www.icgn.org/news/releases/ICGN\\_Statement\\_NFBR.pdf](http://www.icgn.org/news/releases/ICGN_Statement_NFBR.pdf)

International Labour Organization's Declaration on Fundamental Principles and Rights at Work: <http://www.ilo.org/declaration/lang-en/index.htm>

OECD Guidelines for Multinational Enterprises: <http://www.oecd.org>

The Rio Declaration on Environment and Development: <http://www.un.org/esa/sustdev/documents/agenda21/index.htm>

UK sustainable investment and finance association: <http://www.uksif.org/uksif>

UN Convention Against Corruption: <http://www.unodc.org/unodc/en/treaties/CAC/index.html>

UN Global Compact: <http://www.unglobalcompact.org>

UN Principles for Responsible Investment: <http://www.unpri.org>

UN Universal Declaration of Human Rights: <http://www.un.org/Overview/rights.html>