

Generation Investment Management Stewardship and Engagement Policy

2022



Companies make an essential contribution to society. They can provide products and services that people need and thereby create jobs, pay taxes to governments and generate returns for shareholders.

We believe that when companies are run to make such positive contributions over the long term, they can flourish and endure.

However, in our opinion, when companies focus on short-term profit maximisation without regard to their own long-term health, they tend to stumble and ultimately fail. More broadly, many of the challenges that society faces, such as the climate crisis, inequality and obesity, are aggravated by companies operating without due regard to their consequences for society.

A company's board is responsible for confirming its strategy, overseeing management and ensuring that the interests of its shareholders and wider stakeholders are appropriately met. Effective corporate governance of companies by their boards is therefore essential for their long-term success and for the well-being of society.

In turn, investors can make a significant contribution to ensuring robust governance of the companies in which they are invested through the opportunities they have to engage with companies and to contribute to – and, in listed equity, vote on – matters of corporate governance. Such stewardship is natural for long-term investors.

Generation Investment Management LLP (“Generation”) was established in 2004 as a mission-led firm. We seek transformational change to drive to a net-zero, prosperous, equitable, healthy and safe society by:

1. **Delivering superior, risk-adjusted investment results**, utilising a ‘systems view’ to integrate sustainability and environmental, social and governance (ESG) factors into our investment framework’;
2. **Sharing our experience and voice** to promote sustainable and ESG investment.

Stewardship is central to both aspects of our mission.

As we have pursued our mission over the years, we have noticed some improvement in stewardship and engagement in the markets, with a major step forward being the introduction of the Stewardship Code by the Financial Reporting Council in 2010. However, we believe that overall standards of stewardship in investment markets remain inadequate and we are supportive of ongoing regulatory and industry measures to further enhance governance. We are hopeful that these will ultimately overcome impediments to stewardship – such as fragmented ownership, inadequate resourcing and a focus on short-term returns – so that stewardship gets the same degree of focus as stock selection.

This document describes how we approach stewardship. We hope it offers valuable perspectives on the importance of stewardship for companies, investors and society.

This policy applies to Generation Investment Management LLP and its subsidiaries Generation Investment Management US LLP and Just Climate LLP.

¹ Although Generation seeks to provide superior investment performance, this is an aspiration and there is no guarantee that this goal will be attained.

What is stewardship?

The principle of stewardship is well-illustrated by different approaches to forestry management. A well-tended forest can enable selected trees to be harvested each year.

A forest can offer a sustainable yield of timber, if it is well-tended and if selected trees are harvested each year.

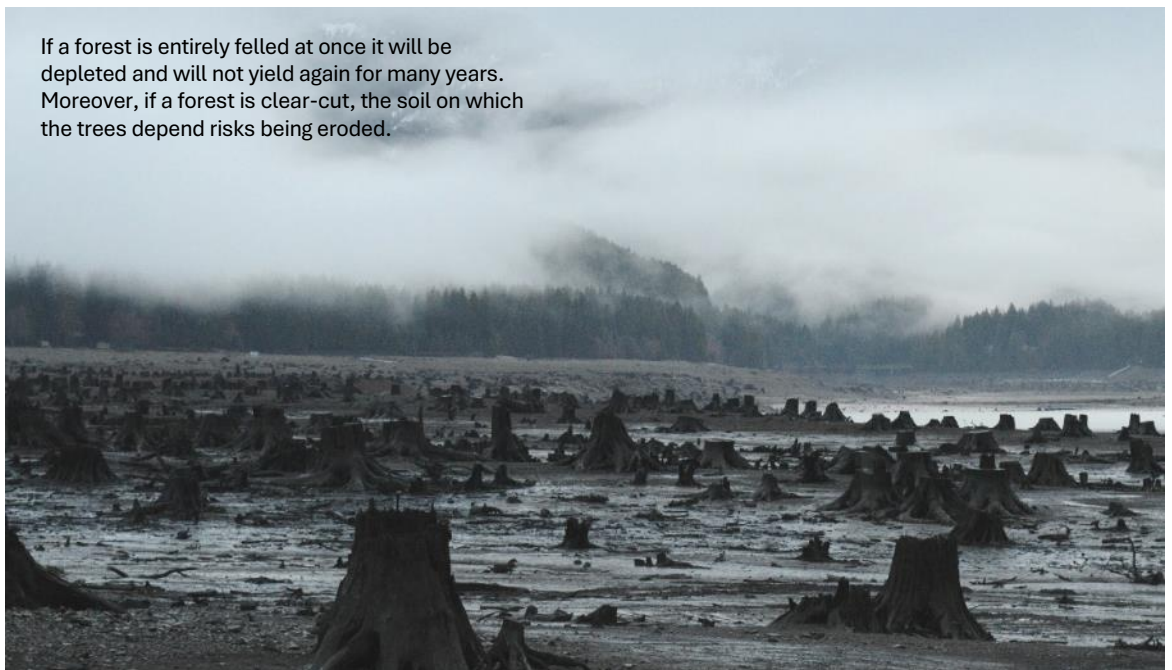
However, if a forest is entirely felled at once, it will give a short-term flush of timber. The forest will be depleted and will not yield again for many years until new trees have been replanted and matured. Moreover, if a forest is clear-felled, the soil on which the trees depend risks being eroded.

The value of stewardship has been recognised by many communities throughout history. For example, when the Iroquois Confederacy, a group of Native American nations, was making decisions, they considered the possible consequences seven generations into the future.

In Europe, stewardship of forests was formalised in the 17th century in Saxony, a region of what is now Germany, in response to a problem. Forests were being felled at an increasing rate to supply timber for the growing mining industry and population, and insufficient attention had been given to replanting trees to preserve the forests. When the local silver mines needed timber, it was becoming unavailable and unaffordable. A local tax accountant and mining administrator called Hans Carl von Carlowitz studied forestry practices across Europe and in his seminal book **Sylvicultura Oeconomica**, published in 1713, proposed that the...

“conservation and growing of wood is to be undertaken in order to have a continuing, stable and sustained use, as this is an indispensable cause, without which the country as we know it cannot survive”.

If a forest is entirely felled at once it will be depleted and will not yield again for many years. Moreover, if a forest is clear-cut, the soil on which the trees depend risks being eroded.



Drawing on this analogy, we understand stewardship to mean taking care of something of value, often on behalf of others, so it can deliver benefits for the long term.

HOW DOES STEWARDSHIP RELATE TO BUSINESSES?

When Generation was launched, we sought to integrate stewardship into the design of our investment approach. The principles of taking a long-term perspective and of nurturing the assets on which future yields depend inform our definition of a sustainable company.

Firstly, we recognise that a company can try to increase its profitability in the short-term through measures such as reducing product quality, squeezing suppliers or customers and postponing maintenance. However, this approach risks weakening the company and reducing its ability to generate strong future growth and profits. Conversely, if a company is managed for the long-term, it will ensure it does not ‘borrow from its future earnings’ and erode the assets on which its success depends in a bid to boost short-term results.

Secondly, we focus on what a company provides. If a company’s products or services meet real needs of its customers and society, then it is likely to continue to generate strong revenues. We seek to invest in companies that contribute to a net-zero, prosperous, equitable, healthy and safe society. If, though, a company serves more superficial or transient needs, it is less likely to endure. Companies whose products or services impose significant costs on society or the environment face risks to their growth, profitability and, potentially, existence if regulatory and consumer pressure forces them to change or to raise their prices to reflect these costs.

Thirdly, we consider how companies are managed and governed. We recognise that companies that operate responsibly, treat stakeholders – such as employees, suppliers, customers and regulators – fairly and take a long-term perspective in their decision-making tend to prosper. Research has confirmed this, finding that companies with more sustainable practices achieve better financial performance and stock market returns².

OUR INVESTMENT STRATEGY

All our investment strategies take a long-term perspective and fully integrate sustainability research within a rigorous framework of traditional financial analysis.

Generation was founded on a related set of beliefs: that much of the value of companies derives from their long-term performance, and that sustainability factors have a material impact on companies’ returns over the long term. In contrast, we observed that investment markets tended to focus on the short-term and that investors were not taking full account of sustainability factors.

We are high-conviction, active investors, with each member of the investment team covering a small set of companies within their respective strategy. This means we develop a thorough understanding of the companies in which we are invested, and insight to inform our effective stewardship of our portfolio after we invest.

² See, for example, **The Impact of Corporate Sustainability on Organisational Processes and Performance**; Robert Eccles, Ioannis Ioannou and George Serafeim; March 2012.

Stewardship is an integral part of our investment strategy.

As investors, we understand stewardship to mean using the opportunity we have to engage with companies in which we are invested, and, in listed equity, voting on their proxy resolutions, to contribute to improving their long-term performance.

We are stewards of the ultimate beneficiaries' capital. As an investment manager, we sit in the middle of a stewardship chain that runs from beneficiaries and asset owners (such as pension funds) to company boards and management teams.

In our stewardship work we draw a distinction between the closely related activities of dialogue and engagement. We view discussions with a company to share and/or gather information as dialogue. We understand engagement to be interactions with a company in direct contemplation of the company achieving a specific outcome. However, Generation is generally not 'activist' as a company, and engagement typically does not extend to participating in the formulation, determination or direction of the basic business decisions of the Company concerned. However, if we consider that the circumstances merit it, subject to applicable regulatory considerations, we may take a more directive approach.

The point of interaction on the spectrum between dialogue and engagement that is selected in respect of a company will vary from case to case at our discretion. It will depend upon a broad range of factors, including the company's existing approach to the matter concerned and its willingness to embrace change. To the extent we select a more directive approach, certain regulatory consequences may flow from that, which need to be carefully balanced against the perceived upside of the dialogue and/or engagement. Our approach to this is set out in more depth at **A Perspective on Activism** below.

Our dialogue with companies usually starts before we invest. Across our strategies, our investment process follows a structured process through three stages: Roadmaps and Research, Company Diligence and Selection, and Review and Approval. Portfolio positions result from this 'bottom-up' research, selection and approval process.

As part of our due diligence, we aim to form as thorough a view as we can of 'Business Quality' and 'Management Quality', among other factors, through our own research and by talking with a company's management³.

Discussions are an opportunity to learn about companies and how they are managed. We also share insights from our research that we believe are material for each company. As we are a specialist sustainable investment manager, we often find management teams to be particularly interested in discussing our perspectives on how sustainability factors are materially affecting their company and sector. As we are long-term investors, the relationships formed with companies often deepen over many years.

³ More information on our investment process and the role of sustainability in diligence is set out in [Sustainability in the Investment Process](#)

Building on our pre-investment diligence and dialogue, we continue to monitor our companies' performance on relevant financial and sustainability-related indicators. Although the specific sustainability indicators may vary across our public and private markets strategies due to data availability and other considerations, indicators considered include the Minimum Principal Adverse Impact (PAI) indicators set out in our [PAI Assessment Policy](#), and typically relate to environmental performance, governance and, in the social sphere, employee matters, respect for human rights, anti-corruption and anti-bribery matters.

We leverage this information to approach engagement with companies constructively after we invest, in line with our funds' investment strategies and in the best interest of our clients.

Engagements with individual companies generally focus on company-specific matters where our investment team's judgment suggests that a specific action or inaction by the company may generate material opportunities or risks.

Cross-portfolio engagement initiatives focus on specific outcomes, in line with our sustainability goals and targets. For example, in our public equity strategies, we seek to engage with all companies on topics that we view as material for all companies such as the climate crisis and equity, diversity and inclusion (EDI). On climate change, across our public and private equity strategies, we seek to engage with companies to improve management awareness of climate-related opportunities and risks, to ensure that all companies disclose their carbon emissions and encourage all companies to set Science-Based Targets for carbon emissions reductions, or to make progress on their targets. Topics covered in company-specific engagements vary: from business strategy, to financial issues such as capital allocation, corporate governance considerations such as board composition and remuneration, social issues such as human capital management and human rights, sustainability reporting matters such as tracking and disclosure of various impacts of the company, and broader areas of interest such as corporate culture.

In line with our integrated investment strategy, investment teams are responsible for ongoing portfolio monitoring, dialogue and engagement with companies. We believe this to be beneficial, as the analysts have a thorough understanding of each company and can incorporate insights gained from discussions into their appraisal of the companies.

We escalate engagement when dialogue has not succeeded in achieving key objectives. Our main recourse in listed equity strategies is usually to exercise votes against management at company general meetings, such as voting against the re-election of directors or voting against management on remuneration. We may also seek the views of other investors and consider collaborative engagement. Finally, in listed equity, we may exit the investment and can additionally choose to remove the company from the Focus List of investable companies for the strategy.

CONFLICTS OF INTEREST

We take the issue of conflicts of interest very seriously. In the course of our stewardship activity, and our overall business, we seek to identify potential conflicts of interest and to mitigate the risks they may pose.

We believe our risk of conflicts of interest is relatively reduced as we only invest in one asset class and only undertake investment management. However, in the course of our stewardship work we recognise the potential for conflicts of interest in areas such as acting on behalf of clients with different objectives, and engaging with a company with which we have a commercial relationship. Our Conflicts of Interest Policy explains how we seek to manage such risks.

In our public equity strategies, during conversations with companies, we generally seek to avoid becoming ‘insiders’ as we are conscious that this may impact our ability to effectively manage our clients’ assets. However, should circumstances warrant it, following advice from the Firm’s General Counsel and adhering to all required protocols, a senior portfolio manager may become an insider. The key rationale in making this decision would be based upon the seriousness of the issue and the prospect of influencing a satisfactory outcome. It will be appreciated that one of the primary consequences of becoming an insider is an accompanying inability to trade the position, and this has the potential to have negative effects on our clients. For this reason, the decision is only taken after detailed consideration to the relative merits.

A PERSPECTIVE ON ‘ACTIVISM’

On occasion, clients of our public equity strategies ask us about our position on ‘activism’ within the public equity context.

While there is no common definition of activism, we note the comments by past SEC Commissioner Daniel M Gallagher that, “it is simply the actions of investors who are dissatisfied with management’s decision-making and corporate strategy and who, rather than selling their shares, try to force those companies to change”. We think this is a helpful summary.

On this definition, as noted above, our public equity strategies would typically not be viewed as activist in the classic sense. We generally do not seek to invest in companies that are ‘broken’ and subsequently express our dissatisfaction with the decision-making and corporate strategy that got them there. Rather, the opposite is true: we will have formed a broadly positive view on the Management Quality of the business – possibly with some reservations or expectations for improvement. We therefore tend to work in a constructive way alongside management teams, helping them to develop companies in which we have conviction. This approach is increasingly being termed ‘constructivism’ and is the bedrock of our approach to engagement.

It is, of course, possible that companies in which we have conviction at the start of our investment process subsequently meet management and strategy challenges. Should this occur, we may consider moving from a constructive approach to one that is more activist, but this step is unlikely to occur frequently. A key reason for this is the impact of a range of regulations around the world which can constrain our flexibility to manage portfolios on behalf of our clients where we may be viewed as an activist investor (which definition may differ in different regulations from how the term may normally be viewed). Some specific examples under US regulations are given in the Notes section at the end of this document.

HOW WE APPROACH VOTING

We see exercising our shareholder voting rights as an essential part of stewardship of the publicly listed companies in our portfolio.

In accordance with appropriate regulations, boards have a fiduciary duty to ensure companies are managed in the interests of their shareholders and other stakeholders. Voting is a way of signalling to a company's board our views on corporate governance matters and also a way of holding a board to account. Where relevant, we coordinate our engagement and voting activities. For example, if a company is unresponsive to engagement on a particular topic, we may vote against the most relevant proxy at the next opportunity.

We vote our own proxies and undertake engagement activity ourselves, rather than employing service providers to handle these activities on our behalf. We aim to vote all of the proxies of companies in which we are invested, drawing on the research of an independent voting service provider to help inform our voting decisions. However, we do not automatically adopt global proxy voting rules from any third-party service as a default setting. This is because we believe each analyst should review the relevant corporate governance issues on a case-by-case basis and exercise their best judgement on how to vote given their deep knowledge of the company. In part, this is feasible because we have a small portfolio.

We disclose our voting publicly and to clients in our Stewardship Report on an annual basis. Our [Proxy Voting Principles](#) describe further our approach to voting.



Forests are home to around four fifths of the world's terrestrial biodiversity, help regulate global weather systems, and contribute to mitigating climate change by absorbing carbon dioxide. Around half of the world's forests have been lost since 1950.

**HOW WE
COLLABORATE
ON
STEWARDSHIP**

We recognise that as participants in the capital markets we have an opportunity and responsibility to work with other investors to protect and enhance long-term shareholder value in line with our collective clients' best interests.

We tend to engage with companies on an individual basis as we find personal, direct conversations are often most effective and contribute to building long-term relationships with management teams. However, where appropriate and subject to careful legal analysis around 'concert party', 'group' and related regulatory issues, we consider collective engagements.

At a systemic level, collaboration with other shareholders, stakeholders and policy makers is essential to promote continued effective functioning of the financial markets and to address the sustainability challenges we face.



The Pando aspen in Utah (USA) is the largest living organism on Earth. Around 47,000 trunks share a common root system.

**OUR
FOUNDATION'S
WORK ON
STEWARDSHIP**

At Generation Foundation, we focus on advocacy and policy work to address systemic risks created by sustainability factors.

Our Foundation identifies opportunities for collaboration with policy-makers, NGOs and other investors on policy engagement topics that are high priorities for protecting systemic integrity and on which its insights are particularly applicable. Since its establishment, it has, for example, focused its systemic engagement work in the areas of the climate crisis and fiduciary duty.

Notes

Example of regulations relating to activism

An example of this occurs in the United States. Under US disclosure rules, Generation will typically be a 'Schedule 13G' filer, which in broad terms means that we are subject to fewer market disclosure rules because we are seen to be a 'passive' investor. Schedule 13G allows a welcome degree of nimbleness to passive investors. Active investors, on the other hand, file under 'Schedule 13D', which is considerably more onerous. In addition to more frequent and onerous disclosure, a particular consideration here is the potential need for a 'Hart-Scott Rodino Act' (HSR) filing as a Schedule 13D filer. There is an exemption for filers of Schedule 13G. HSR requires parties to mergers, acquisitions and certain other transactions to file pre-merger notification with the Federal Trade Commission and the Department of Justice Antitrust Division, and then observe a 30-day statutory waiting period before consummating the transaction. Such a filing would typically not reflect our intention in acquiring securities but may be triggered by an approach that is considered to be 'activist' under the HSR parameters. These filings are complex and relatively costly, so are not undertaken as a matter of routine. Similar considerations apply around the world.

Important Information

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