First Sentier Investors

# GLI 2024 Sustainability Report

# Contents

# Introduction

Countries across the world are grappling with issues such as climate change mitigation, climate change adaption, energy security, reliability, and affordability. Utilities are seeing a significant increase in energy demand driven by the rapid expansion of data centers, which serve as the backbone for AI applications and cloud computing. These are complex issues requiring a wide range of financial and technology solutions. Global listed infrastructure companies will be at the forefront of the global energy transition and will play an integral part in achieving net zero emissions.

This report intends to provide transparency on how the First Sentier Investors Global Listed Infrastructure team assesses the environmental social and governance (ESG) performance of companies we invest in, how we engage with leadership, and the insights from our research. By sharing our approach to ESG, we want to illustrate how responsible investment principles are embedded within our investment approach.

Investors are demanding more transparency and accountability as to how their capital is being used to generate strong returns and contribute to solving the world's long-term challenges. We believe that incorporating ESG considerations into our investment approach can lead to better decision-making, which can lead to stronger long-term investment performance for our clients.

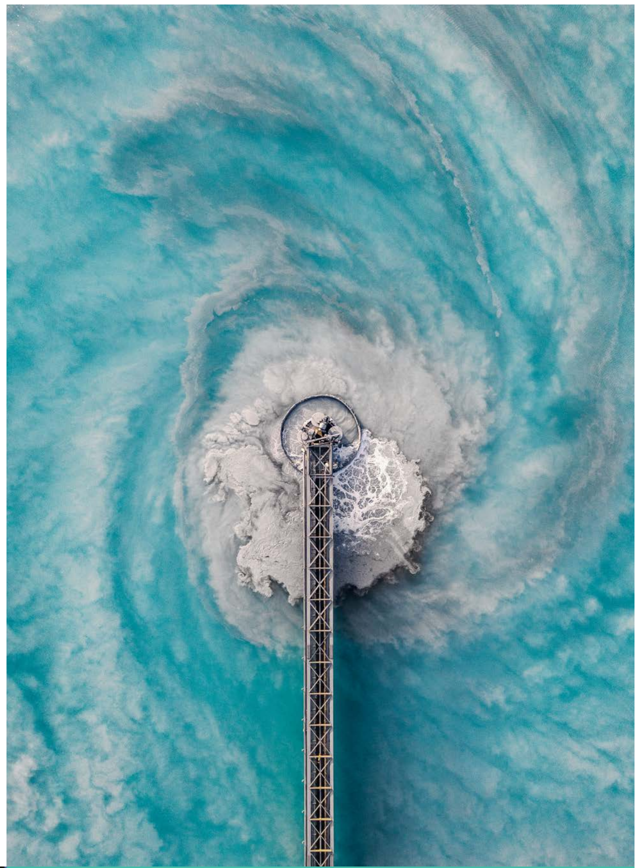
Good companies solve problems. The energy transition and physical impacts from climate change are critical problems that require infrastructure solutions. The challenge of providing clean, affordable and reliable energy is made greater by cost of living pressures and partisan politics. In our opinion, Infrastructure companies that understand and embrace these ESG risks are more likely to deliver sustainable returns for investors

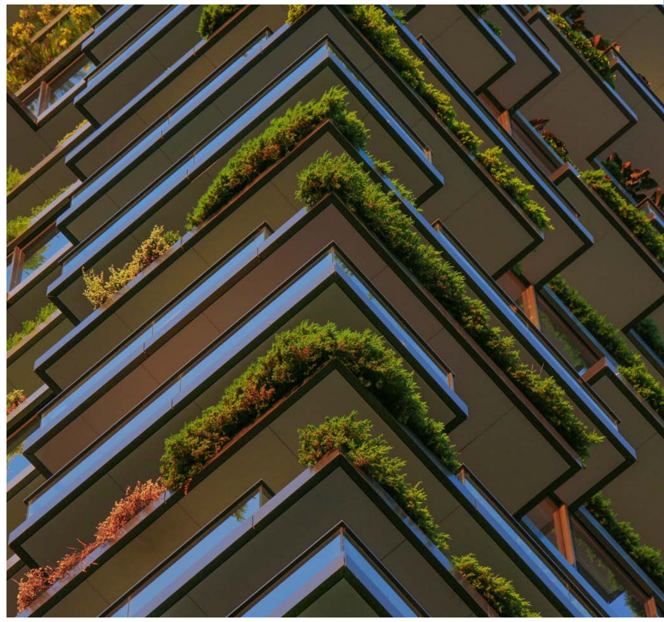
**Peter Meany**

Head of Global Listed Infrastructure Securities

Through company engagement we seek to better understand risk in our portfolio, suggest areas for improvement, increase transparency on ESG issues, and support companies that are making progress in this area. We typically engage companies on material issues to achieve specific outcomes. More broadly, we participate in industry groups such as Climate Action 100+ to push for change on complex issues such as energy transition and the pathway towards net zero.

Aligning with First Sentier Investors' firm-wide commitment, we are committed to building investment portfolios with an ambition of net zero by 2050 and are pursuing interim targets by 2030 to reduce the Weighted Average Carbon Intensity (WACI) of our investment portfolios. We will seek to prioritise the direction of capital to infrastructure companies that are aligned or aligning with a pathway to net zero by 2050 and encourage the investment of this capital into real assets that reduce absolute emissions. As stewards of our clients' capital, we will continue to engage with companies on these issues with a view to delivering more sustainable risk adjusted returns.





Global listed infrastructure companies will play a crucial role in addressing climate change by developing energy systems that enhance security, reliability and affordability. The shift to a low carbon economy requires massive investment and our companies will be at the forefront of the energy transition

**Trent Koch**

Portfolio Manager, Global Listed Infrastructure

# ESG Focus Areas

The Global Listed Infrastructure team focuses on assessing ESG risk and performance in four key areas – **Energy Transition, Climate Risk, Modern Slavery** and **Corporate Governance**.

The team's strategies include the Global Listed Infrastructure "GLI" strategy (established in 2007) and the Responsible Listed Infrastructure "RLI" strategy (established in 2017).

### Energy Transition

Energy transition is at the forefront of our engagement with companies. Transition risk represents the single largest climate-related risk for listed infrastructure companies, as the world moves away from fossil fuels and towards lower-carbon sources of energy.

However, energy transition also represents a substantial opportunity. Attempts to reduce carbon emissions are having significant implications for the way in which electricity is generated, transmitted and distributed.

### Climate Risk

Physical impact risk from climate change and global warming poses risks to society and the global economy. It affects the availability of resources, the price and structure of the energy market, the vulnerability of infrastructure assets and the valuation of companies. As investors in infrastructure assets, we understand that climate change poses a complex problem which has already impacted, and will continue to impact different assets in different ways. We believe it is our responsibility to understand and mitigate these risks within our investment portfolios.

### Modern Slavery

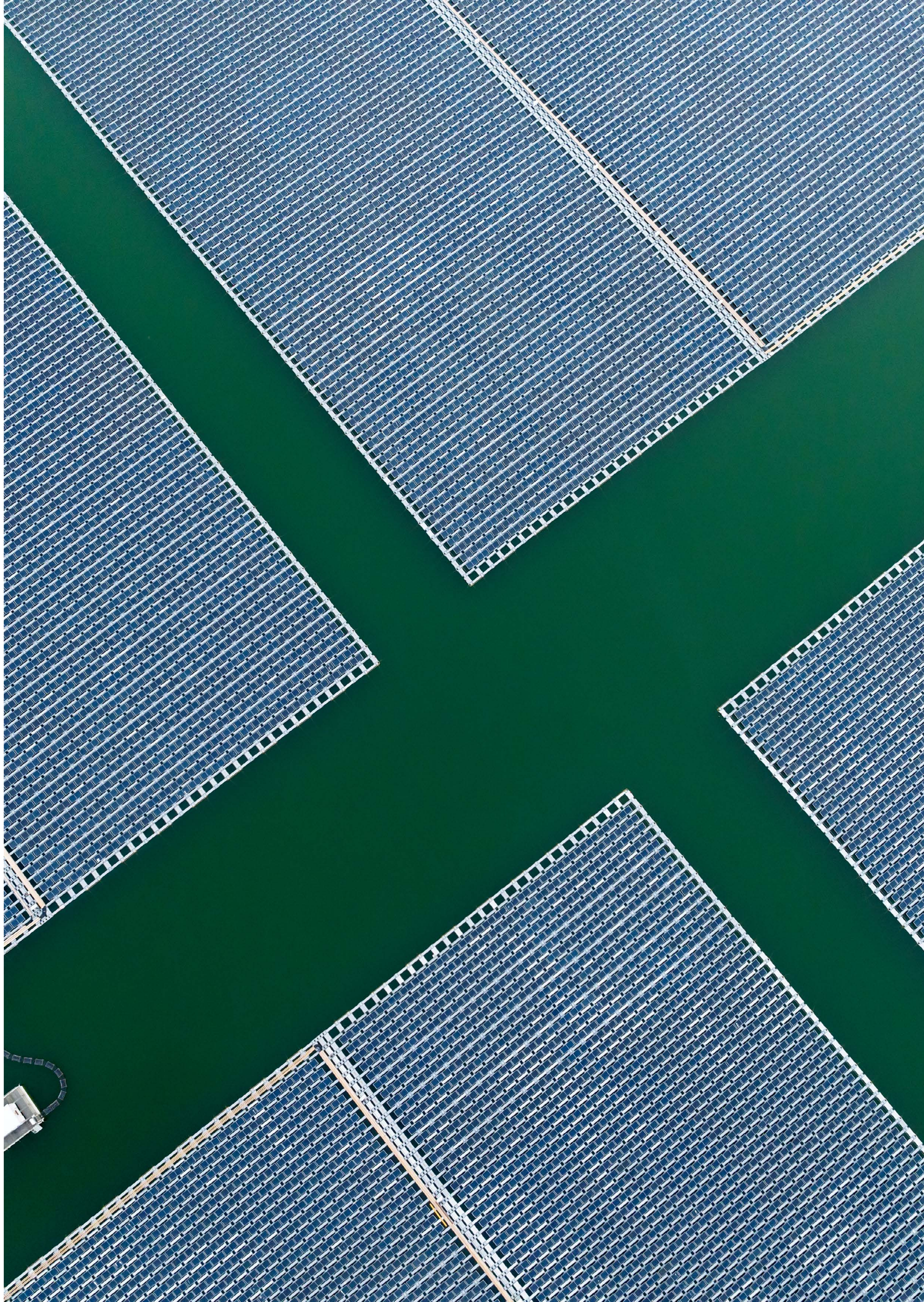
As stewards of our clients' assets, we believe we have a responsibility to identify and act to eliminate human rights abuses, including, but not limited to, modern slavery. This is part of a wider societal responsibility that impacts the performance of our investments. Companies have legal, moral and commercial responsibilities to respect human rights and to manage the impacts of modern slavery on their operations. If these responsibilities are not met, a company may face regulatory, financial, reputational and legal risks.

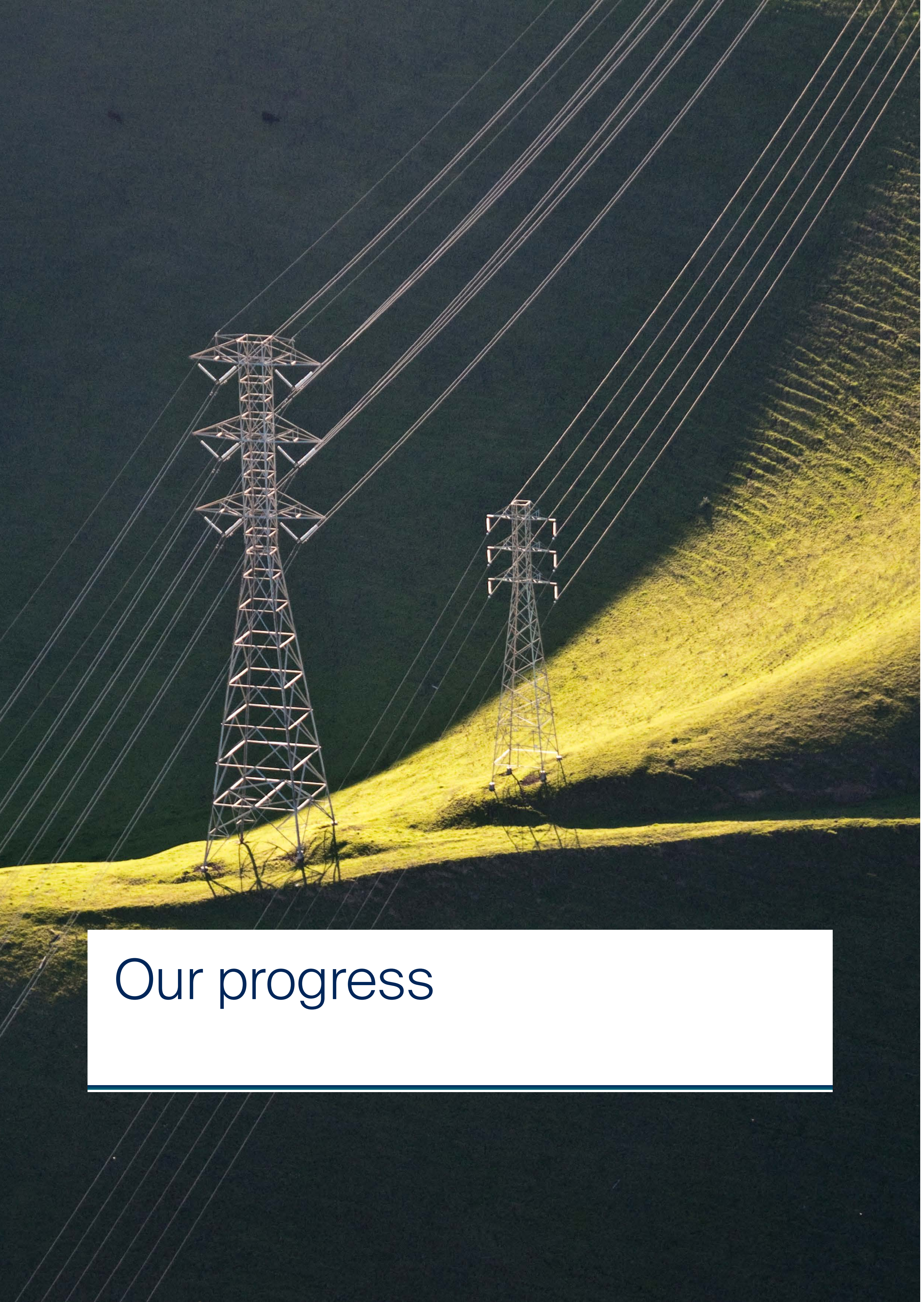
### Corporate Governance

Infrastructure companies provide essential services such as energy, transportation, water and telecommunications that are vital to the functioning of societies and economies. They are often large scale projects with significant capital expenditure requirements. Effective corporate governance means companies are managed in a manner that considers the interests of all the stakeholders I.e. shareholders, employees, customers, suppliers,
the environment and the broader community.

### Emerging areas of focus

We acknowledge the growing significance of systemic issues, including biodiversity and natural capital, water scarcity and quality, and the importance of a circular economy to minimise waste and optimise resource allocation. As these challenges gain prominence, we remain dedicated to actively engaging with our portfolio companies. Our objective is to stay well-informed about key trends, emerging risks, and opportunities. By doing so, we strive to maintain a competitive edge and effectively address these evolving issues in a proactive manner.





# Our progress

**714** meetings held

**24** countries

**10** subsectors[2]

**1,160** resolutions voted on

**8%** voted against management[3]

Net Zero targets made by

**85%** of our portfolio companies[4]

**32%** reduction in weighted average portfolio carbon intensity over last 5 years[5]

**34%**

An average 34% female representation on our portfolio company boards (23% 5 years ago)[6]

Interim 2030 WACI targets:

**-35%** for GLI strategy

**-50%** for RLI strategy

**Graded 4 stars or above in 7 out of 10 categories**

UN PRI Ranking[7]

**Leader**
RIAA ranking

2. Company meetings held during the 12 months to 31 December 2023
3. Proxy voting for the 12 months to 31 December 2023
4. Portfolio holdings as at 30 June 2024
5. Represents portfolio holdings as at 30 June 2024 for the five year period December 2018 to December 2023
6. Represents portfolio holdings as at 30 June 2024 for the five year period December 2018 to December 2023
7. Information sourced from FSI as at 31 December 2023

# Case Studies

### Engagements examples in this report

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| ENERGY TRANSITION | **Xcel Energy** | Utilities/ Renewables | United States | • Just transition<br>• Impact of coal closures on employees | 12 |
| | **Targa Resources** | Energy Midstream | United States | • Absence of quantifiable carbon reduction goals<br>• Poor disclosure on ESG targets<br>• Board tenure and independence | 14 |
| CLIMATE RISK | **Edison International** | Utilities/ Renewables | United States | • Impact of climate change and wildfires<br>• Wildfire mitigation plans, undergrounding assets<br>• Regulatory changes, wildfire funds | 16 |
| | **Entergy** | Utilities/ Renewables | United States | • Prioritise investment in resilience spend<br>• Further investment in climate change modelling | 18 |
| MODERN SLAVERY | **APA Group** | Utilities/ Renewables | Australia/NZ | • Understanding response to Modern Slavery risks<br>• Deep dive into workforce contractor arrangements | 20 |
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| CORPORATE GOVERNANCE | **Pinnacle West** | Utilities/ Renewables | United States | • Separation of Chair and CEO responsibilities<br>• Improvement in REM targets<br>• Establish targets for scope 2 emissions | 24 |
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# Xcel's coal-fired plant closures raise questions about a just transition for employees

**Xcel Energy (Xcel) has made significant strides in transitioning to renewables and closing coal-fired power stations, however the cascading impacts to employee livelihoods and the initiatives to support a just transition were less clear.**

Xcel is a regulated utility company operating in eight US states, providing electricity and natural gas services to approximately 3.7 million electric customers and 2.1 million natural gas customers. The company has made strong progress towards decarbonising its operations with the closure of coal-fired power stations and a shift towards renewables. Its coal-fired generation capacity has decreased from over 8,000 megawatts in 2006 to a forecast of 4,100 megawatts in 2025, with a target of zero by 2030. Renewables are expected to increase from 9% in 2006 to 67% in 2030.

Xcel's efforts to mitigate climate change have been successful, resulting in steady, low-risk earnings growth. However, it is important to consider the cost of shifting to a healthier economy and more sustainable production. The Paris Agreement requires a "just transition", ensuring that transition measures consider the rights of employees whose roles change or are no longer needed. In this context, we sought to evaluate the extent to which Xcel was incorporating a just transition strategy into its program of replacing coal with renewables.

In July 2023, we met with Xcel to discuss the upcoming closure of the Sherburne County Generating Station ("Sherco") in Minnesota, which is scheduled to occur in two stages: Unit 2 in 2023 and Unit 1 in 2026. This would see the workforce reduced from 187 employees to around 88 employees by 2030. During the meeting, we discussed how Xcel plans to incorporate the concept of just transition into the closure process including how the just transition plan was developed, who the main stakeholders were, what KPIs would be set, and what regulatory considerations were taken into account.

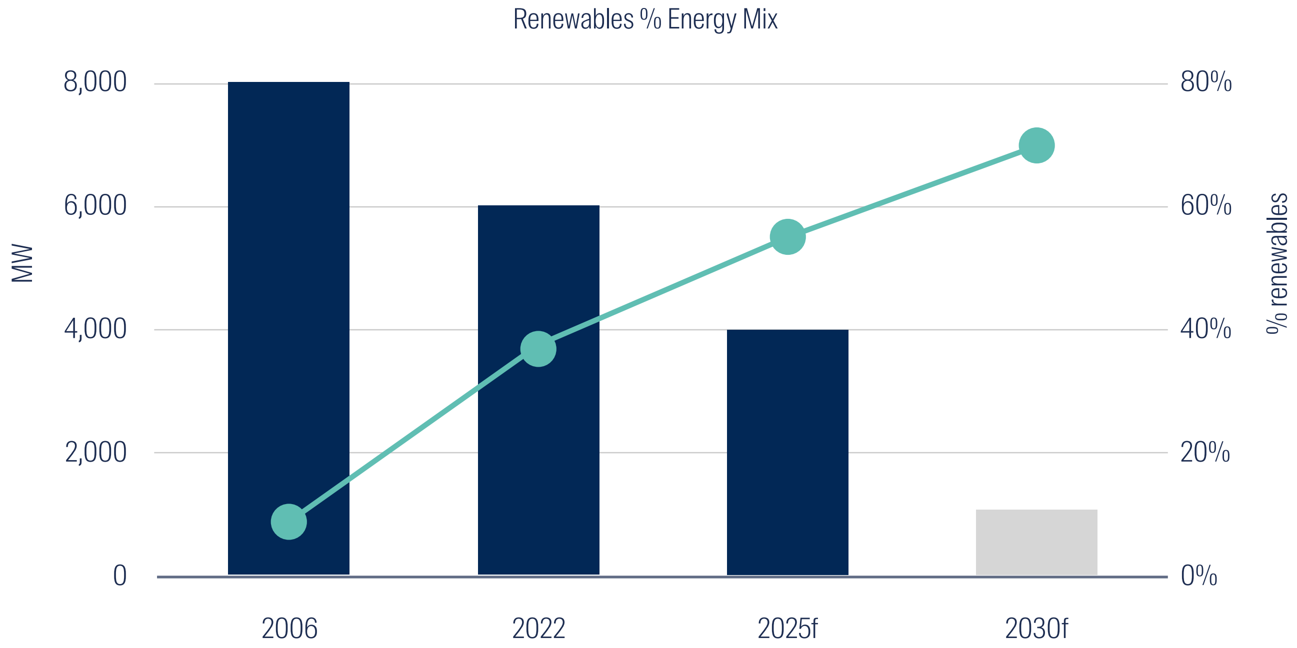
Based on our research and engagement, Xcel appears to have taken meaningful steps to reach key stakeholders involved in shutting down the coal plant. These stakeholders include employees, community colleges and clean energy groups. Xcel has also worked with the regulator to provide regular updates on the progress of community and employee conversations as the closure unfolds. This transition plan is further supported by detailed metrics, targets and KPIs, which were provided during our meeting.

We would like to see Xcel's KPIs relating to a just transition for Sherco be published. This would enable investors to undertake their own assessments and further engage with the company. We shared this feedback with Xcel and will continue to ask for further information over time.





**Coal-fired power plant closures**
**Xcel Energy target to be out of coal by 2030 (MW)**




Source: Xcel Energy, First Sentier Investors as at 31 December 2023[11]

11. 2025f and 2030f represent Xcel forecast numbers

# Opportunity to drive improvements to carbon reduction metrics and governance with Targa

**Targa is a leading US energy midstream company but still needs to address ESG issues such as the absence of quantifiable carbon reduction goals and several governance-related risks.**

Targa Resources Corp (Targa) is a fully integrated energy midstream company that primarily operates in the US. The company's core business includes the gathering, processing, storage, and transportation of natural gas, natural gas liquids (NGLs), and refined products. It has a strong balance sheet and is well positioned to benefit from increased export demand for US natural gas and NGLs. However, there appear to be opportunities to improve the managing of ESG issues such as setting quantifiable carbon reduction goals, and improving disclosure on sustainability targets as well as how these relate to remuneration. We believe there is also an opportunity to re-evaluate existing governance structures by reducing board tenure and rotating board membership.

We engaged with Targa management in May 2023. We highlighted our concerns about the company's lack of quantifiable carbon reduction goals, including a Net Zero target by 2050, and the ambiguity surrounding its Scope 1 and 2 emissions. In response, the company stated that it is still considering what targets to follow internally and what to disclose externally. Additionally, it was waiting for SEC rules and guidelines that will be required for ESG disclosures in the future.

Targa acknowledged that "investors want us to show progress" and shared that they have 2025 greenhouse gas intensity targets in place. We emphasised the importance of continuing to work on scope 1 and scope 2 emissions, as well as methane emissions, and setting and publishing quantitative targets, KPIs, and measures to address these. We also suggested that the company should include these targets in their remuneration packages to further incentivize progress.

Case study | Energy Transition | Targa Resources

We also raised concerns about management short-term incentives (STI), which are 60% financial, 30% operational, and only 10% sustainable. We recommended that Targa increase transparency and disclosure around sustainability targets. Targa acknowledged the difficulty of identifying such goals in a tight labour market given the potential of losing operational employees, but we emphasised the importance of incorporating sustainability into their incentive structure for long-term value creation and risk management.

Additionally, we questioned Targa's rationale for not including Return on Invested Capital (ROIC) targets in its management remuneration plans. Targa's view is that ROIC cannot be part of STI targets as projects take 2-3 years to come to fruition. It also believes that ROIC outcomes are already reflected in share price performance, and therefore captured in Performance Share Units. We debated the pros and cons of both approaches, and the company agreed to consider the issue further.

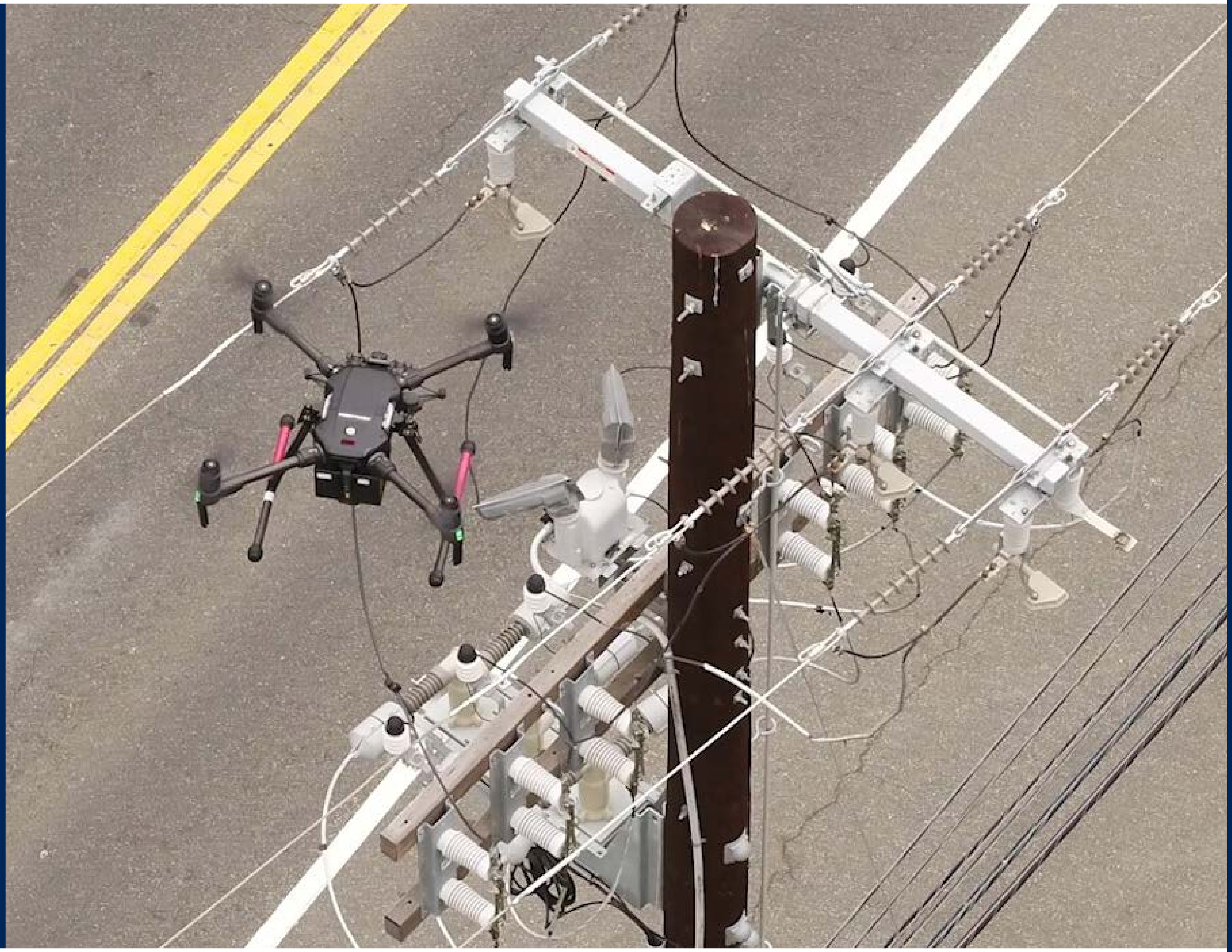
Furthermore, we discussed a possible policy on board tenure, given four directors have been on the board for over nine years. We provided feedback that, in our view, it was not appropriate to have three former executives on the board (two former CEOs and one former General Counsel). We emphasised the merits of have a diverse and independent board to ensure Targa could make well-informed decisions that consider the best interests of all stakeholders.

# Wildfire-related liabilities: A risk for investors in Californian utilities

**Wildfire risks remain a significant challenge for all Californian utilities. Although Edison International invests in technology and infrastructure to mitigate this risk, investors should monitor wildfire risk and liability developments.**

Edison International (Edison) is one of the largest electric utilities in the US, serving over 15 million people in California. Investing in Californian utilities such as Edison and Pacific Gas and Electric Company (PG&E) carries the risk of wildfire-related liabilities which includes utility companies being held liable for damages resulting from fires caused by their equipment. In 2017 and 2018, PG&E was held accountable for several wildfires that caused extensive damage and loss of life, and the company filed for bankruptcy as a result of these liabilities. Similarly, Edison has faced wildfire-related liabilities although on a smaller scale than PG&E.

In May 2023, we engaged with Edison to delve into the potential ramifications of climate change and wildfires on their business operations. Our objective was to gain deeper insights into the measures undertaken by the company to mitigate this risk, as well as to ascertain the government's response to this pressing issue.





Case study | Climate Risk | Edison International

Equipment inspections for overhead transmission, distribution and generation equipment in high fire risk areas from both the ground and air using drones and/or helicopters[13]

Edison has taken several steps to address this risk, including the implementation of a comprehensive wildfire mitigation plan. This includes equipment inspections, vegetation management, and infrastructure hardening. It is also undergrounding 600 miles of power lines, costing between US$1-1.5bn from 2025-28, as outlined in it 2023-2025 wildfire mitigation plan.

The California state government is also taking steps to address the issue of climate change and increased wildfire risk for utilities. Californian legislation AB-1054, which passed in 2019, aims to address inverse condemnation. This is the legal principle that holds utilities strictly liable for damages caused by their equipment, even if they were not negligent. This principle has been a significant factor in the wildfire-related liabilities faced by utilities in California, including Edison and its subsidiary Southern California Edison.

AB-1054 established a California Wildfire Fund, which provides funding to reimburse eligible claims from a utility. This protects utility companies from bankruptcy by covering wildfire damages that exceed $1 billion. The law incentivizes utility companies to invest in safety and reduce wildfire risks while offering financial protection. As long as the utility company obtains a safety certification from the state, they are presumed to have acted responsibly. Overall, Edison has demonstrated a commitment to addressing wildfire risk and investing in technologies and infrastructure that can help mitigate this risk. However, the risk of wildfires remains a significant challenge for California utilities, and it is important for investors to remain vigilant and monitor developments related to wildfire risk and liability. consider the best interests of all stakeholders.

13. Source: https://www.sce.com/wildfire/wildfire-mitigation-efforts

# Understanding Entergy's climate risks and regulatory cost recovery expectations

**Entergy is a leader among US utilities in the transition to net zero, however, the heightened frequency of extreme weather events increases the risk of asset damage and costly repairs. We engaged with the company to understand their response.**

Entergy Corporation (Entergy) is a US-regulated electric and gas utility that serves 2.9 million customers across Arkansas, Louisiana, Mississippi and Texas. The majority of its assets are located in southern US states that are susceptible to severe hurricanes, thunderstorms, and tornadoes. Climate change can exacerbate these events, leading to infrastructure damage, service disruptions, and costly repairs.

In recent years, we have engaged with Entergy to better understand the climate risks they face. This included how it protects its assets, expectations for regulatory cost recovery, and potential benefits of climate change modelling for system hardening. In 2023, we followed up with further inquiries on Entergy's efforts to improve grid resilience, cost implications of infrastructure, state allocation of modernization spending, and investments in climate change modelling.

Entergy has proposed a 12-year, US$15 billion resiliency plan that includes replacing working infrastructure as a proactive measure to mitigate potential storm damage.

Case study | Climate Risk | Entergy

Entergy uses concrete and steel for new and replacement high-voltage transmission structures[14]

By doing so, it aims to reduce the costs associated with storm damage by 60%. This proactive approach is expected to be more cost-effective than replacing storm-damaged equipment as needed in the long run.

The company has updated its performance standards based on recent storm history and is actively addressing key risks such as storm surges and wind loading due to hurricanes. It has increased substation elevation standards, with some being raised to 30ft, to address the risk of storm surges. The company has also prioritised the improvement of its distribution network, as 80% of major storm costs are related to this area.

Entergy confirmed that undergrounding infrastructure is not feasible in most states that it operates in due to unsuitable soil conditions in the swamp-like land of their region. In contrast, California has different incentives that make undergrounding a more viable option. It estimates that undergrounding would cost 5-10 times more than traditional above-ground infrastructure, further justifying their prioritisation of above-ground infrastructure.

The business has allocated one third of its US$33bn capex program towards grid modernization, with Louisiana receiving 50%, Texas receiving 30%, and other states receiving 20%. While there has been some investment in climate change modelling, the company has been cautious in its messaging due to increased scepticism towards climate change in some of the states where it operates.

Entergy is a leader among US utilities in the transition to a net zero future, balancing its targets with mitigating climate risks. We'd like to see further investment in climate change modelling to help identify areas that are at higher risk of damage from extreme weather events. We will continue to engage with them on this matter.

14. Source: Energy Resiliency Plan https://www.entergy.com/transmission/resiliency/

# APA makes progress in understanding modern slavery risks across its supply chains

**The largest natural gas pipeline in Australia, APA, has complex supply chains that involve procuring materials, equipment, and services from various suppliers. We engaged with them to better understand how they manage these risks.**

APA is the largest natural gas infrastructure business in Australia, owning and operating over 15,000 km of natural gas pipelines, processing, and storage. It also has a growing portfolio of gas-fired power, renewable power (wind, solar, battery), and power transmission infrastructure. However, infrastructure companies have complex supply chains that involve procuring materials, equipment, and services from various suppliers. This can make it difficult to obtain reliable and comprehensive information given upstream and downstream firms in a supply chain may not be fully transparent.

In 2023, we engaged with APA to gain an understanding of its policies regarding modern slavery. We sought clarity on multiple aspects, such as the identification of instances of modern slavery within their operations or supply chains, as well as the processes they have in place to effectively address and combat this risk. We also raised modern slavery with management at their annual investor day.

APA considers the risk of modern slavery in its operations to be low given its Australian-based workforce are covered by enterprise agreements and individual employment contracts. It has implemented recruitment and on-boarding processes, mandatory employee training, health and safety policies, remuneration policies, and code of conduct policies. The company uses the UN Guiding Principles on Business and Human Rights to manage modern slavery risks. It published its Modern Slavery Statement Report in 2023 and have a working group to address this issue. To date, it has not identified any cases of modern slavery in its supply chain, and no reports or concerns have been received.

The company has also taken measures to address the risk of modern slavery in its supply chain, requiring new suppliers to commit to respecting fundamental human rights and assess existing suppliers using APA's Modern Slavery Risk Management Approach. It has introduced modern slavery clauses in relevant procurement agreements and is increasing its visibility of its indirect supply chain.

14. Source: Energy Resiliency Plan https://www.entergy.com/transmission/resiliency/





APA has been working with an ESG data vendor and human rights consultancy group to map high-risk suppliers beyond Tier 1. While 98% of APA's spend in FY23 was with direct suppliers in Australia, these suppliers may rely on overseas operations and supply chains, particularly in high-risk regions like China. The company estimates that more than 95% of solar panels are still sourced from China. It has minimised modern slavery risks by introducing clauses into all contracts, with suppliers required to acknowledge modern slavery has been considered and to not source from particular regions in China. It recently had to remove a supplier who declined to sign this contract.

APA is making progress in understanding modern slavery risks within its operations and supply chains and we see the publication of its Modern Slavery Report in 2023 as a positive step. Its FY24 roadmap includes an initiative to conduct a deep dive into their workforce contractor arrangements. This will help to further assess the risk in their operations. We will continue to monitor the company's progress on this issue.

Case study | Modern Slavery | CCR

# Investigating CCR's policies and procedures on modern slavery

**We enquired about CCR's assessment of modern slavery risks beyond its Tier 1 supply chain, employment of migrant workers or minorities, and its audit process for suppliers.**

CCR is a diversified concession company that owns toll road, urban mobility, and airport assets located throughout Brazil. Its most significant assets include a toll road connecting Sao Paulo and Rio de Janeiro, five metro lines in Sao Paulo, and a growing collection of Brazilian airports. CCR's business involves significant construction works across all its divisions, which can increase the risk of modern slavery due to complex supply chains, short-term contracts, sub-contracting arrangements, wage theft, and reliance on low-skilled and migrant workers.

We have been engaging with CCR in recent years to better understand its modern slavery policies and procedures. In 2023, our letter to management asked if they had identified modern slavery in CCR's operations or supply chains, the processes for addressing it, and if staff were offered training to increase awareness. We also enquired about the business' assessment of modern slavery risks, employment of migrant workers or minorities, and audit process for suppliers beyond Tier 1. Our aim was to gain insight into CCR's approach to managing modern slavery risks.

CCR noted that they maintain compliance with relevant laws related to human rights through legal drafts with specific clauses, regardless of the form of hiring labour from their suppliers. The company also conducts regular audits of eligible suppliers through the use of an independent sustainability ratings agency, EcoVadis.

CCR's 'Sustainability Program' monitors the environmental, social, and ethical performance of its supply chain. Formal assessments are carried out annually to produce improvement plans that are sent to suppliers for actioning.

CCR's supply chain team conducts on-site audits of its best-evaluated suppliers, strategic suppliers, and those with the lowest scores. These audits serve the purpose of assessing whether supplier responses provided to the regular audits are being applied in practice; and support the development of supplier policies and practices. The contract manager participates in these audits to ensure the independence of the evaluation.

In 2022, CCR noted it was in the process of developing a policy that specifically addresses modern slavery risks. However, in our 2023 follow-up with the company, it confirmed that this was no longer the case. We have emphasized the importance of developing a formal policy to manage modern slavery risks and will continue to engage with the company on this matter. We remain committed to working with CCR to ensure that it has robust policies and procedures in place to address modern slavery in its operations and supply chain.

# PNW engages with investors on important corporate governance matters

**Shareholder resolutions on the AGM agenda offer an opportunity to engage with a leading Arizona utility on key issues like board composition, remuneration packages, and corporate governance.**

Pinnacle West Corporation (PNW) is the largest utility in Arizona, with a ~US$112 billion rate base and representing ~50% of the state's electric rate base. It also operates and co-owns the Palo Verde Generating Station, the largest nuclear plant and the single-largest generator of carbon-free electricity in the US.

In May 2023, we engaged with PNW's Chief Financial Officer, Company Secretary, and Investor Relations representative to discuss various topics related to its upcoming AGM. These issues included a shareholder proposal for an Independent Chair, remuneration targets that required improvement, and ESG targets that fell below industry best practice standards.

The shareholder proposal was for an independent director to serve as chair of the board. While PNW opposed the proposal, arguing that it wanted to retain flexibility to choose an individual that would serve shareholders' interests, we indicated we would likely vote in favour of an independent chair. Our view is that an independent director would provide more objective oversight, increase accountability and reduce conflicts of interest. We did acknowledge that a joint Chairman / CEO could bring alignment if there is a clear strategy however our view is that this arrangement is typically limited to successful founder-led businesses.

We recommended that Short Term Incentives (STI's) be based on Earnings Per Share (EPS) rather than Net Profit After Tax (NPAT) targets. In our view, EPS is a more appropriate metric because it considers the number of outstanding shares and provides a more accurate measure of profitability. In contrast, NPAT does not take into account the number of outstanding shares, making it a less reliable measure. As a result, we believe EPS is a better metric for determining short term incentives as it rewards executives for actions that increase shareholder value.

Furthermore, we highlighted that the ESG targets of the company fell below industry best practice. Specifically, we noted that the company only considers Scope 1 emissions as part of their GHG reduction targets. We suggested that the company should broaden its consideration to include Scope 2 emission targets as well as setting a net zero commitment. Although we are in favour of adding clean megawatts and recognize that Scope 1 emissions are the company's largest contributor, we believe that it is now best practice to expand this and have it independently verified.

We voted in favour of the shareholder proposal for an Independent Chair. We intend to maintain an open line of communication with the company to collaborate on enhancing its remuneration and ESG targets.





# AMT capital allocation plans put additional pressure on the balance sheet

**AMT is one of the world's largest telecommunication infrastructure operators but acquisitions in recent years has put pressure on its balance sheet. We engaged with the company on capital allocation plans, board renewal and carbon reduction targets.**

American Tower (AMT) is one of the world's largest global telecommunications infrastructure operators, with over 224,000 sites in the US, Latin America, Europe, Asia and Africa. It generates revenue through long-term leases for tower space with wireless telecommunication companies. We have been actively engaging with AMT on important issues such as capital allocation, board renewal, and carbon reduction targets. To address these issues, we arranged a one-on-one meeting with AMT's sustainability team in March 2023, followed by another meeting in November 2023 to continue the discussion.

In our capital management discussion with AMT, we agreed with their plan to sell their Indian assets with consideration to regulatory and competitive challenges in that market. We also advised that AMT's reputation for effective capital management could be harmed if it were to acquire European tower company Cellnex's assets at a high multiple, especially as AMT had previous opportunities to buy Cellnex at a lower multiple over the past five years.

We believe the AMT balance sheet has become stretched in the past decade, mainly due to large deals such as the acquisition of European tower portfolio Telxius in 2021 and a premium takeover of data center company CoreSite in 2021. We recommended the Board incorporate new perspectives, rigorously evaluate management decisions and explore succession planning for long-serving directors. AMT acknowledged that it does not have tenure limits for directors, but believe it considers director tenure, exposure and experience when reviewing its Board composition annually.

AMT has set a goal of reducing its Scope 1 and 2 emissions by 40% between 2019 and 2035, with the majority of its emissions stemming from operations in Africa and India. One of the major sources of these emissions is the use of diesel generators to power towers in these countries, creating a challenge for AMT to achieve a target of net zero. AMT is looking into using bio-diesel to reduce emissions, and we discussed the challenges they face. Providing power to its African towers is crucial due to the unreliability of some electricity grids, and it is using more solar and battery solutions to decrease generator usage. We commended AMT for its efforts to reduce emissions, but recognize that this is a complex issue that requires ongoing attention and innovation.

14. Source: Energy Resiliency Plan https://www.entergy.com/transmission/resiliency/

# Environmental impact assessment for Orsted offshore wind projects

**Orsted is a global leader in the development offshore wind, however questions remain around the environmental impact of such projects, with specific concerns regarding an increase in beached whales, risks to birds, and plans for handling end-of-useful life blades.**

Orsted, a global leader in offshore wind energy, has built more offshore wind farms than any other company worldwide. In January 2023, we engaged with the company to better understand the environmental impact of its offshore wind projects, with specific focus on concerns of an increase in beached whales as a result of construction, the risk that wind blades pose to birds, and its plans for handling damaged or end-of-useful-life blades in the context of a circular economy.

Before construction of any project, Orsted undertakes a thorough environmental impact assessment, considering the possible and potential effects on biodiversity, including birdlife. The findings of the assessment are submitted to the relevant planning authority, and if required, necessary actions are taken to mitigate any predicted impacts on the environment.

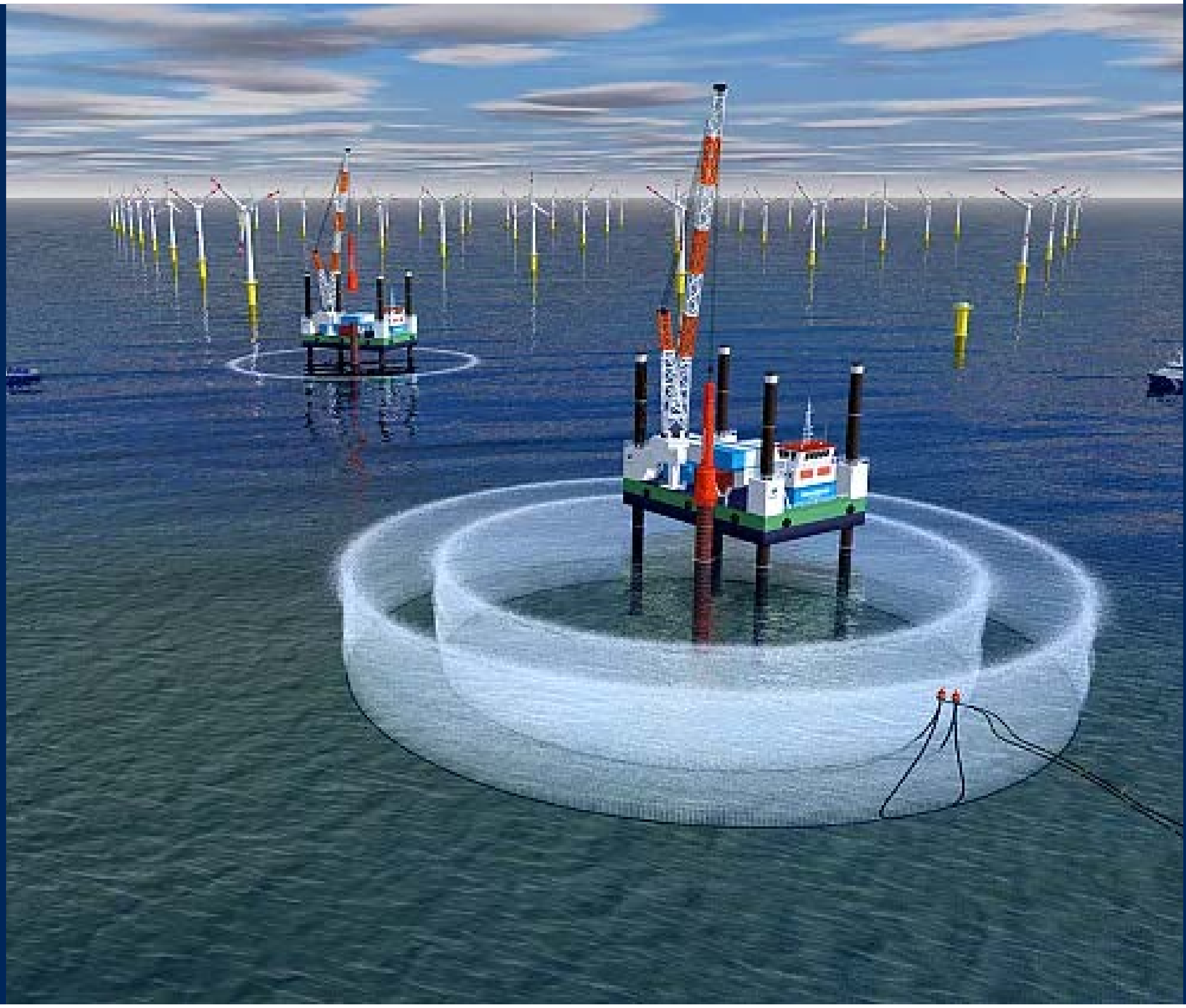
The company were keen to emphasise its commitment to preserving biodiversity, and that it has implemented several practices to achieve this goal. These practices include conducting aerial surveys, noise profiling, using soft start piling to reduce disturbance to marine mammals during construction, deploying marine mammal observers, and using bubble curtains as noise shields.

15. Source: bubble-curtains-are-being-used-to-protect-marine-life-from-noisy-wind-farm-construction



Case study | Emerging Area of Focus | Orsted

Air bubble curtains being used during construction of offshore wind farms[15]



Orsted has set a target to deliver a net positive impact on biodiversity across their renewable assets by 2030.

Orsted confirmed that it has never had a whale beach in any of its projects. It also noted that in the US, where there is limited piling, it is highly unlikely that noise activity from piling would cause whales to be beached. While it is true that some birds die every year by flying into turbine towers or blades, the actual numbers are negligible. Statistics show that in the US, wind energy facilities cause less than one in 4,000 documented bird deaths from industrial activities^.

When asked about their plans for dealing with damaged or end-of-life blades, Orsted acknowledged that this area is still being developed. However, since their fleet is relatively young, they do not anticipate many blades needing to be disposed or recycled for the next 7-8 years. Any damaged blades are currently being stored until a recycling solution is found. Orsted has an internal team dedicated to finding solutions for blade recycling and is exploring partnerships with various European companies. Additionally, its innovation team is actively seeking new solutions as they emerge in the market.

As biodiversity and the circular economy increasingly gain attention, we will maintain our active engagement with companies to deepen our understanding of these risks and opportunities for our investors.

^ Source: Orsted renewable energy solutions website

# Our approach

ESG issues are fundamental to infrastructure companies, given they have significant service obligations and moral accountability to the communities in which they operate. We assess infrastructure companies on a broad range of ESG-related factors, including but not limited to, energy transition, climate risk, modern slavery and corporate governance. We are conservative investors of our clients' capital, recognising that capital preservation is critical to achieving long-term capital growth. We focus on fundamental value and conduct thorough due diligence to minimise risk. We place strong emphasis on proprietary research and direct contact with companies and regulators.

At a group level, FSI has identified four main investment stewardship priorities: climate change, human rights and modern slavery, nature and biodiversity and diversity. These priorities address the ESG issues that pose the most significant long-term financial risks to our investments, while also presenting the greatest opportunities.

## Engage with management and board on ESG issues and performance

The most important source of research for the FSI Global Listed Infrastructure (GLI) team is internally generated analysis based on regular meetings we hold with senior management and other stakeholders including suppliers, competitors, regulators and industry bodies. When the GLI team engages with companies on ESG issues, we use meetings with management to better understand the situation from their perspective, and to openly raise concerns where we see a potential gap in ESG performance. If we don't see performance improvement, we will escalate the issue to the company's board of directors to outline our concerns. Ultimately, we will consider divestment if we do not see a willingness to change or address the issue.

## ESG assessment integrated into investment process

The assessment of ESG issues, strategy and performance represents an essential part of our investment process. We seek to understand the risks for each company and assess them in our proprietary quality ranking which consists of 25 criteria that influence stock returns for infrastructure securities. A score is assigned to each criteria; a lower quality score makes it harder for a stock to be included within the overall portfolio. ESG assessment is both a science and an art that blends data points and qualitative engagements. We then build on those findings by conducting asset tours, and spending time with company management and board directors. We have been doing this for over 15 years.

## ESG Metrics

The GLI team maintains a database of key ESG metrics across the strategy's entire investible universe (focus list)[16]. These metrics include a range of climate-related statistics, including absolute carbon emissions, carbon footprint and carbon intensity. It includes key safety metrics like total recordable incident rates and lost time injury rates. We look at diversity measures including the number of independent directors and percentage of women directors, to track progress over time. We encourage companies to report climate-related statistics in a way that is consistent with the framework provided by the Task Force on Climate-Related Financial Disclosures (TCFD). TCFD compliant carbon footprint reports can be generated for each of our underlying portfolios, and for the strategy overall, based on ISS ESG data.

16. GLI investment universe includes ~140 listed companies, which meet the GLI teams' strict definition of core infrastructure

## Principle Adverse Impacts

The Principal Adverse Impact (PAIs) are part of the EU's Sustainable Finance Disclosure Regulation (SFDR). They seek to improve disclosure on how adverse impacts and sustainability risks are considered and managed by investors. While many of the metrics that fall under the PAIs were already being assessed by our team as part of our ESG assessment outlined above, the new framework provides a consistent way to meet the strategy's obligations under SFDR. As part of our approach to PAIs, we commit to assess every active equity investment for relevant adverse impacts and documenting the results. Where adverse sustainability impacts are identified, we seek to engage with the company in accordance with the commitments made under FSI's Responsible Investment and Stewardship Policy and Principles.

## Proxy voting and reporting

The GLI team seeks to vote on all eligible resolutions where we have the authority to do so. Voting rights are a valuable asset and are executed with care and diligence. We take this responsibility seriously and the research we gather ensures we make informed decisions. If we believe that our concerns and performance gaps are still not being addressed, we may vote against resolutions put forward at the annual shareholder meeting. During the 2023 calendar year, we invested in 73 infrastructure companies across 13 subsectors and in 13 countries around the world. We voted on 1,160 resolutions, of which we voted against management on 89 occasions (8%) on issues including lack of board independence, poor alignment of interests and inadequate climate-related targets. Our voting record is included for transparency on our website[17] and in the proxy voting section of this report.

## United Nations Sustainable Development Goals (SDGs)

Within our team's suite of products, the Responsible Listed Infrastructure (RLI) Strategy has an additional mandate; namely, to invest in companies that can contribute to or benefit from sustainable development, as guided by the UN Sustainable Development Goals. Given its importance to any functioning modern economy, infrastructure has a central role to play in addressing global challenges that need to be overcome in order to deliver a sustainable future.

Key areas that investment in infrastructure can have a meaningful effect on include:

- SDG 6 - Clean Water and Sanitation
- SDG 7 – Affordable and Clean Energy
- SDG 9 – Industry, Innovation and Infrastructure
- SDG 11 – Sustainable Cities and Communities
- SDG 12 – Responsible Production and Consumption
- SDG 13 – Climate Action

Each of these main categories contains several more specific secondary or "sub" goals that infrastructure investment can have a direct influence on. As part of the investment process for the RLI strategy, we monitor how much capital expenditure (capex) is being spent by each company on activities that correspond directly to the sub-goals of each of the six SDGs outlined above.

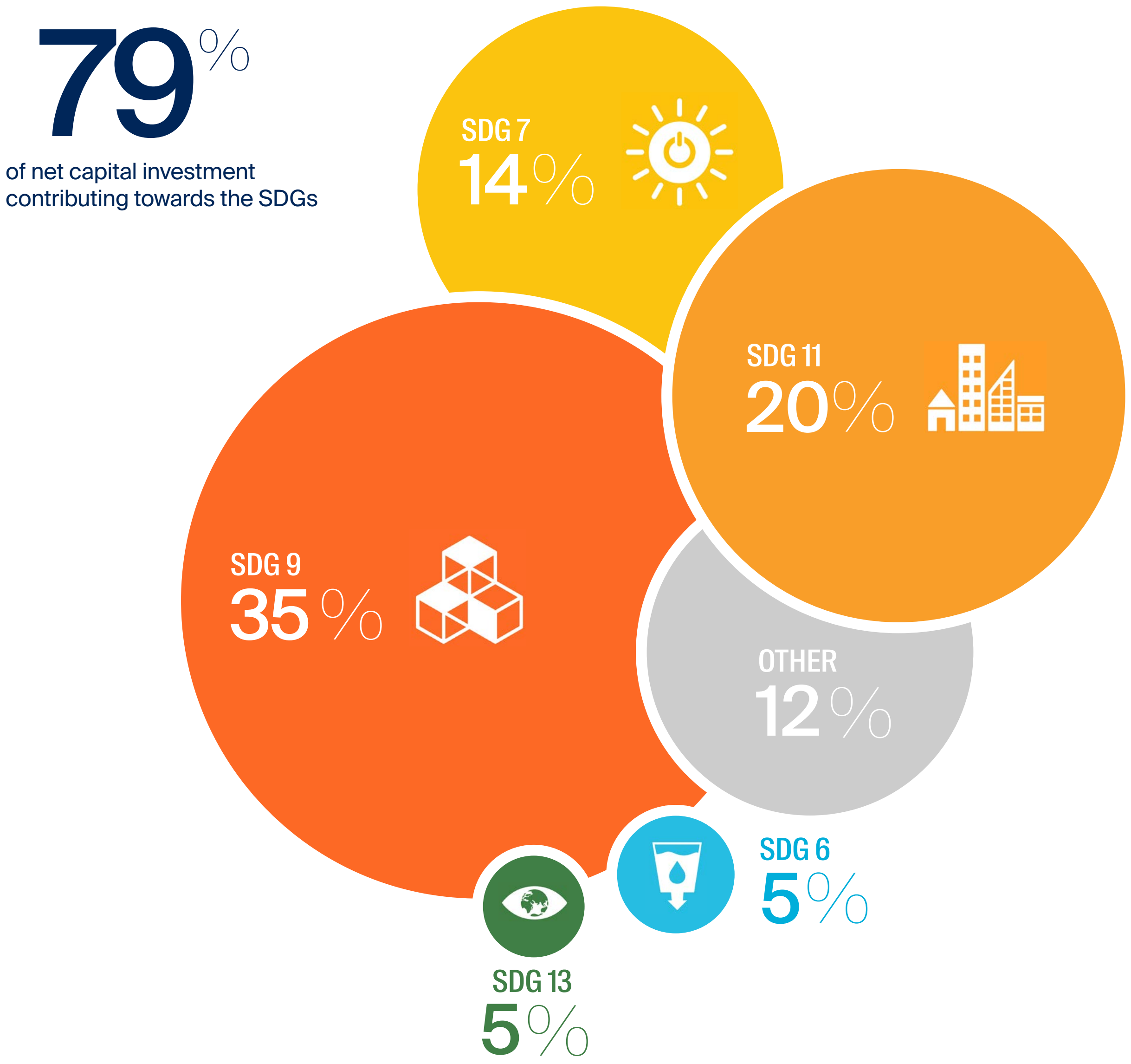
Given infrastructure's capital intensive nature, we believe this represents a sensible and consistent way to monitor a company's contribution to sustainable development. Reflecting the importance of taking a balanced approach, all capex is taken into account. We then categorise it as positive, neutral or negative. For example, Italian-listed utility company and renewables leader Enel Group is forecast to spend 50% of its capex on the buildout of renewable energy generation (such as wind farms and solar power) between 2023 and 2025[18]. Over the same period, 40% of its capex will be spent on networks, predominantly distribution grids. This will help to bring clean energy to the end-user[19].

A further 4% of capex is forecast to be invested by the Enel X division in areas that support the transition to a clean economy (such as EV charging infrastructure and energy efficiency initiatives)[20]. The remaining 6% of the company's capex is forecast to be spent on their energy retail business. We deem this capex to neither positively or negatively affect any of the SDG sub goals, and therefore assign it to the neutral category.

17. FSI Proxy voting
18. This is directly supportive of SDG 7.2 (By 2030, increase the share of renewable energy in the global energy mix)
19. This is directly supportive of SDG 9.1 (Rural access)
20. This is directly supportive of SDG 7.1 (Access to electricity), 7.2 (Share of renewable energy), 7.3 (Energy efficiency)

Overall, we are of the view that the current holdings of the Responsible Listed Infrastructure Strategy make positive contributions to SDG 7 (Affordable and Clean Energy) and SDG 9 (Industry, Innovation and Infrastructure). This reflects the portfolio's high weighting in utility stocks. Many utilities are investing substantial amounts of capex both into renewable energy generation, such as wind and solar; and into the new or upgraded transmission and distribution networks that are needed to connect these clean energy sources with population centres where the demand is.

**Responsible Listed Infrastructure Strategy' capex supporting sustainable development[21]**




21. Capex numbers reflect forecast spending levels of current portfolio holdings over the next 12 month period. "Net capital investment" figure of 83% consists of 86% positive contribution and 3% negative contribution. Positive, neutral and negative labelling represents the opinion of the FSI GLI Team. SDG 6: Clean Water and Sanitation. SDG 7: Affordable and Clean Energy. SDG 9: Industry, Innovation and Infrastructure. SDG 11: Sustainable Cities and Communities. SDG 12: Responsible Consumption and Production, SDG 13: Climate Action. "Other" represents capex spent in areas with a neutral effect on the SDGs. Source: First Sentier Investors and company reports. Data as at 31 March 2024.



Decarbonisation is happening in our asset class, particularly by utilities who are responsible for the vast majority of the emissions in our opportunity set. Our target reflects the developments that we are already seeing in this space and enables us to engage with and encourage companies to make greater efforts on this front.

### Our climate change targets

First Sentier Investors and the Global Listed Infrastructure team are targeting a reduction in greenhouse gas emissions across our investment portfolios[22] consistent with an ambition to reach net zero emissions by 2050.

Reflecting the best available science on the impacts of climate change, we acknowledge there is an urgent need to accelerate the transition towards net zero emissions and support global efforts to limit global warming to 1.5 degrees Celsius. Infrastructure companies will play a vital role in achieving this outcome given electric power and transportation are significant contributors to global emissions.

As a responsible and active manager of capital on behalf of our clients, we seek to[23]:

- Build investment portfolios aligned to net zero by 2050
- Pursue interim targets to reduce, by 2030, the Weighted Average Carbon Intensity (WACI)[24] of our investment portfolios to -35% (Global strategy) or -50% (Responsible strategy) below the 2019 benchmark index[25]
- Take account of portfolio Scope 1&2 emissions to consider material Scope 3 emissions[26]
- Prioritise the direction of capital to infrastructure companies that are aligned or aligning to net zero, as per the Paris Aligned Investment Initiative and Net Zero Investment Framework
- Encourage the investment of this capital into real assets that reduce absolute emissions, rather than into offsets
- Engage with companies to improve disclosures (e.g. TCFD[27] reporting) and accelerate change (eg. coal power closures by 2030[28]), with a focus on those companies that produce the most carbon emissions
- Implement an escalation and voting strategy consistent with achieving net zero
- Provide information and analysis on net zero progress and climate risks and opportunities
- Collaborate with industry stakeholders (e.g. PRI[29], IIGCC[30], NZAM[31], CA100+[32]) to provide a consistent and collective voice

The GLI team's climate statement can be found on our website[33]:

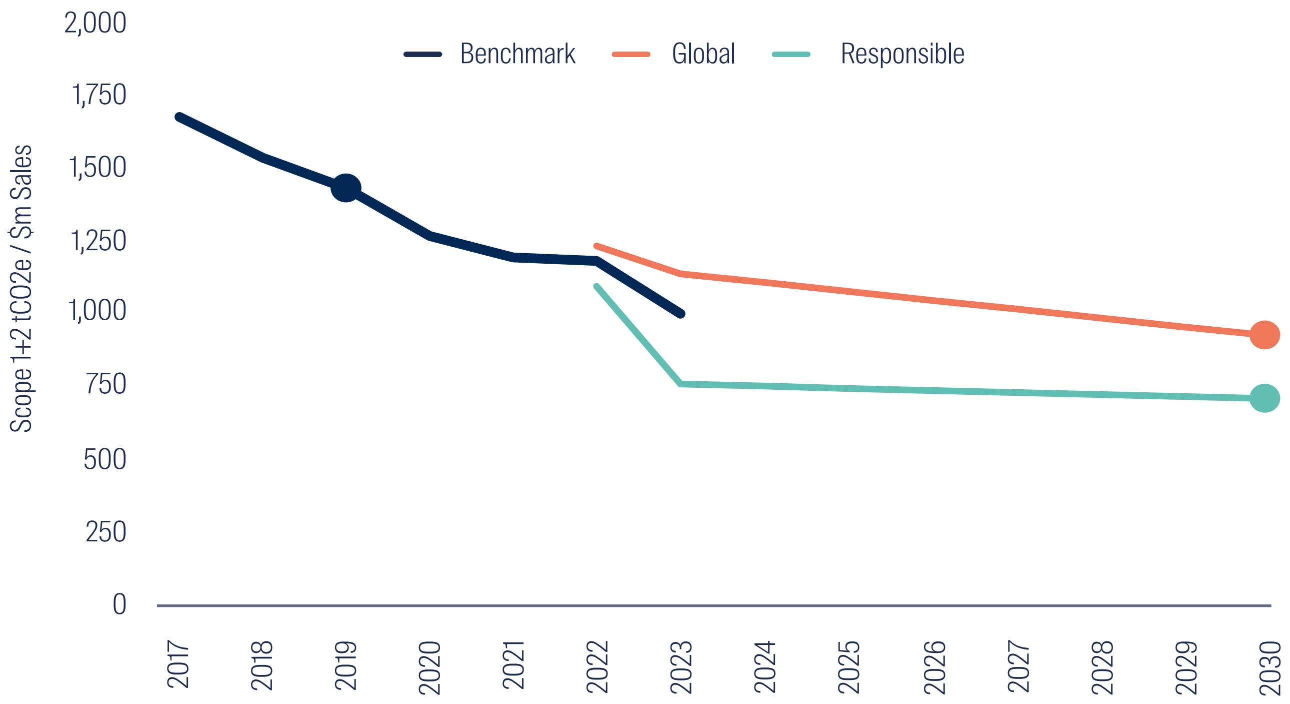
22. The team's net zero target applies to all Global Listed Infrastructure and Responsible Listed Infrastructure pooled vehicles, and to separate client accounts that are subject to equivalent investment guidelines.
23. These commitments and targets are based on information and representations made to the relevant investment teams by portfolio companies (which may ultimately prove not be accurate), together with assumptions made by the relevant investment team in relation to future matters such as government policy implementation in ESG and other climate-related areas, enhanced future technology and the actions of portfolio companies (all of which are subject to change over time). As such, achievement of these commitments and targets depend on the ongoing accuracy of such information and representations as well as the realisation of such future matters. Any commitments and targets set out in this material are continuously reviewed by the relevant investment teams and subject to change without notice.
24. Intensity being a measure of carbon efficiency, and WACI measures the exposure within a portfolio to carbon-intensive assets compared to the benchmark.
25. 2019 was selected as the base year as it represents the most recent and complete dataset which was not impacted by the pandemic. Benchmark is the FTSE Global Core Infrastructure 50-50 Index
26. Scope 3 includes encompasses emissions that are not produced by the company itself, and are not the result of activities from assets owned or controlled by them, but those that it's indirectly responsible for, up and down its value chain. Companies may currently face challenges in reporting accurate and reliable Scope 3 emissions data. Where a company is unable to calculate its Scope 3 emissions for some or all of the categories outlined in the GHG Protocol's guidance, it should still identify the relevant upstream and downstream Scope 3 emission categories relevant to it.
27. Task Force on Climate-Related Financial Disclosures
28. As per International Energy Agency (IEA) guidelines phase out by 2030 in developed markets and 2040 in emerging markets.
29. United National Principles for Responsible Investment
30. Institutional Investors Group on Climate Change
31. Net Zero Asset Managers
32. Climate Action 100+
33. The Securities and Futures Commission has not reviewed the contents of www.firstsentierinvestors.com

## Interim targets

We commit to pursuing interim targets to reduce the WACI of our investment portfolios by -35% for our Global Strategy and -50% for our Responsible strategy, by 2030 relative to the 2019 benchmark index . This target was developed through a detailed evaluation of our portfolios emissions, progress achieved to date and their likely achievements in the years ahead.

The Paris Agreement calls for a -45% reduction in emissions by 2030 from a 2010 baseline. It is important to recognise that companies have already made significant progress on this target. US utilities represent the vast majority of total emissions in our portfolios and we estimate that from 2010 to 2019 these companies had already reduced emissions by -29%. Therefore to deliver their fair share requires a further -23% reduction from 2019 to 2030. Adjusting absolute emissions to emissions intensity we arrive at the -35% target for our Global Strategy.

**Weighted Average Carbon Strategy**




Source: First Sentier Investors, MSCI as at 31 December 2023

APPENDICES

# Energy transition

Transition risk represents the single largest climate-related risk for listed infrastructure companies, as the world moves away from fossil fuels and towards lower carbon sources of energy. This transition has implications for freight railways, whose coal haulage volumes will decline materially over the next ten years. It will affect the energy midstream space, where oil and refined product pipelines could face stranded asset risk by 2040. While natural gas is likely to represent a key transition fuel, a long-term decline in demand is likely to begin once battery storage technology has advanced sufficiently.

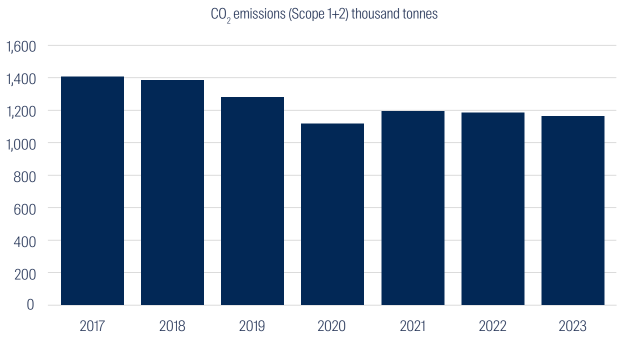
However, energy transition also represents a substantial opportunity. Attempts to reduce carbon emissions are having significant implications for the way in which electricity is generated, transmitted and distributed. Renewable energy is currently experiencing a virtuous cycle of falling costs, improving productivity and growing market share. In contrast, non-renewable energy is in a vicious cycle of declining market share, reduced revenues and rising costs.

## Portfolio carbon metrics

Across our portfolio companies we have seen a -16% reduction in absolute emissions over the last 5 years . This reduction reflects a range of initiatives including: closing coal power plants and replacing with wind, solar and batteries, signing renewable power purchase agreements, reducing transmission line losses, capturing landfill methane and processing into renewable natural gas, converting vehicles from diesel to compressed natural gas or electric, or switching ventilation systems from fixed to variable speed. The list of initiatives and technologies continues to grow.

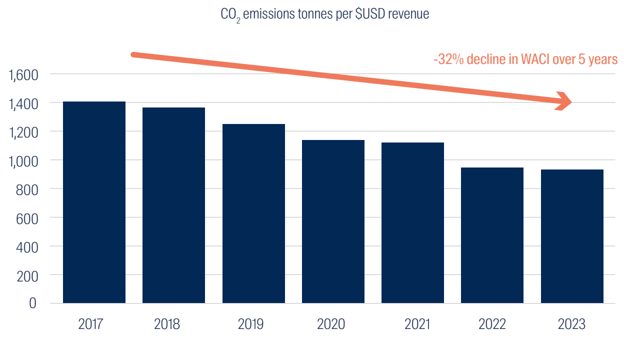
Importantly this reduction in emissions came despite substantial growth in the underlying businesses and changes in scope related to acquisitions. As an indication this -16% decline in absolute emissions translates to -32% decline in WACI when adjusted by revenue.

**Absolute carbon emissions**




Source: Bloomberg, First Sentier Investors     99% portfolio coverage

**Carbon intensity**

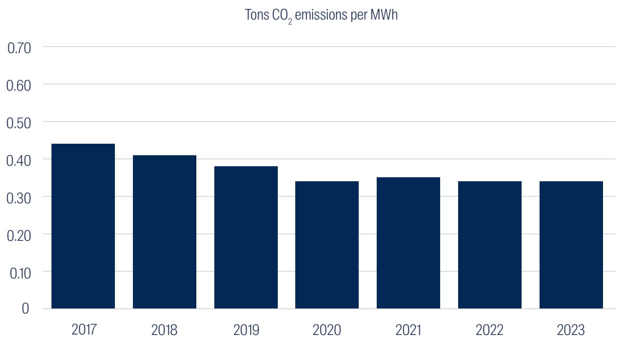



Source: Bloomberg, First Sentier Investors

The vast majority of our portfolio's emissions come from utilities so naturally this is where we invest the most time on analysis and engagement. With the main source of emissions being power generation, utilities tend to express carbon intensity as a function of power produced. This measure of carbon intensity has reduced by -18% over the last 5 years as utilities have switched from power generation fuelled by coal to natural gas to renewables.

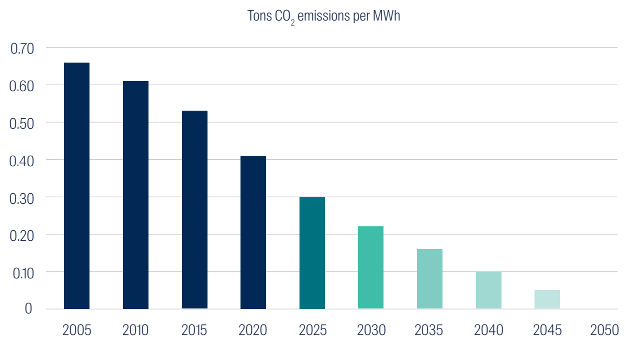
This measure of carbon intensity is also useful to consider pathways towards net zero. All of our portfolio utilities disclose historic carbon intensity and many provide a pathway forward. We can also analyse information from integrated resource plans and plant asset lives to project the likely carbon intensity of the generation fleet over time. Our portfolio utilities have already reduced carbon intensity by close to -40% from 2005 to 2020 and are on a path consistent with net zero by 2050. We recognise our level of confidence in these metrics falls materially after 2030 / 2035 given resource planning and government incentives are typically limited to 10-15 years and networks / storage are untested with 100% renewables at scale.

**Carbon intensity**



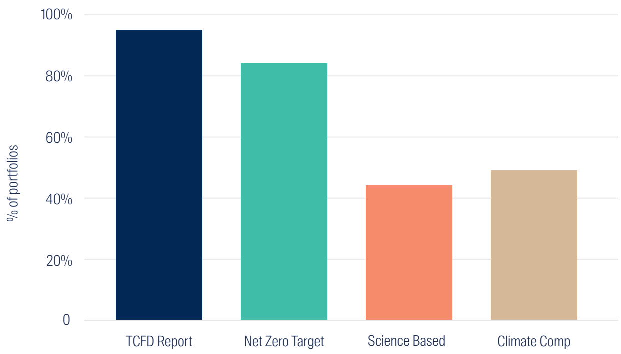

Power generated by utilities represents >80% of portfolio emissions

**Net Zero Pathway**




Source: Bloomberg, First Sentier Investors

**Commitment to energy transition**




Source: Bloomberg, First Sentier Investors



### 95% report against TCFD (no change from previous year)

Reporting against the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) has become the global standard. Disclosures around governance, strategy, risk management, metrics and targets should help investors understand how companies consider and assess climate-related risks and opportunities. Companies that do not support TCFD disclosures are generally in emerging markets. A few do not formally support TCFD but do have credible disclosures and commitments. For example, Flughafen Zurich (Zurich Airport) supports the Global Reporting Initiative (GRI) and Airport Carbon Accreditation (ACA) and has set a target for net zero without offsetting by 2040. We will continue to engage to achieve 100% support of TCFD.

### 85% have set a net zero target (vs 71% in 2022)

Most companies target net zero by 2050. A few have set more aggressive targets including NextEra Energy by 2045 and CenterPoint Energy by 2035. Companies that have not set a net zero target are generally in energy midstream (not credible), emerging markets (not priority) or wireless towers (not material). Other sectors like railroads and waste have set strong interim targets but are not yet ready to commit to net zero. For example, waste company Republic Services has set an (SBTi approved) interim target for -35% reduction in emissions by 2030 but does not yet see a pathway to 100% capture of landfill methane gas. We will continue to engage with these companies to push for a commitment to net zero.

### 44% are approved as science based (vs 37% in 2022)

Adding a pathway to achieving net zero including interim targets is critical for transparency and accountability. We will continue to engage with companies to align net zero pathways with science and seek external validation. The Science-Based Targets Initiative (SBTi) is widely used for validation of net zero pathways. We acknowledge criticisms that it relies on a single scenario to achieve net zero and does not capture historic carbon reductions – this is important for US utilities given what was achieved between 2005 and 2020. We will also seek further disclosure of specific plans to achieve these outcomes, for example coal plant closures and renewable / storage / transmission projects.

### 49% have climate-linked compensation (vs 42% in 2022)

Incentives drive behaviours and we believe execution of the pathway towards net zero is more likely to be successful if management are remunerated accordingly. Depending on the materiality for the company and the responsibilities of the individual, we recommend 10-30% of variable remuneration is linked to ESG-related risks. For an example of best practice, Xcel Energy has linked 100% of short-term incentives to ESG metrics including safety, reliability, customer, environment and diversity, with a 50-150% overlay for earnings per share relative to guidance range. It has also linked 30% of long-term incentives to carbon reduction with 70% on relative total shareholder return.

### Challenges

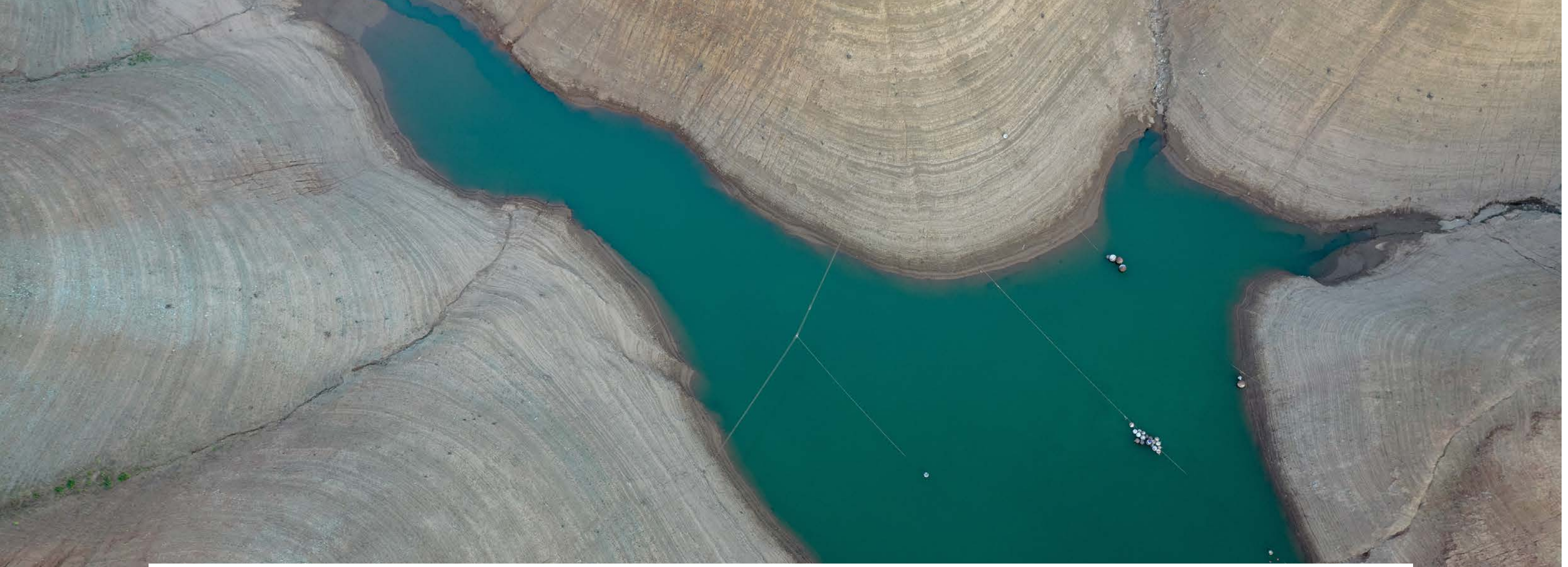
Carbon intensity (measured in TCoe2/Gwh[36]) is a key component of our GHG reduction targets. While the longer-term trend of this metric follows a clear downward trajectory, a utility's carbon intensity can sometimes increase year-on-year owing to changes in energy demand levels, utility capacity factors[37] and corporate structure. Whilst longer term targets such as Net Zero 2050 are important, our immediate priority is to set medium-term expectations and assess company performance against those measures. We challenge management on where they expect to get to by 2025 and 2030. We need to be forward looking and also identify the laggards who could be the leaders of the future.

We recognise the challenges of addressing scope 3 emissions. Many companies do not have the systems in place to track and report emissions that occur outside their operation but associated with their activities. A lack of standardised methodologies and reporting frameworks also makes it challenging to compare emissions across different companies. We will continue to engage with companies to raise awareness about the importance of Scope 3 emissions.

### Future steps

We actively encourage companies to take the energy transition seriously and provide high quality climate-related reporting in line with TCFD recommendations. Across all ESG issues, we need sustainability reporting that has the same rigour as financial reporting (i.e. double materiality) and we are aware of our responsibility as active owners to encourage this from the companies we invest in. We will report on our progress against our net zero target at an underlying portfolio level on an annual basis.

36. Tonnes (t) of carbon dioxide (CO2) equivalent (e) per gigawatt hour (Gwh)
37. How often different power plant types are being run at maximum power



# Climate risk

Climate change and global warming are increasing the frequency and unpredictability of extreme weather events like droughts, fires and floods, which pose risks to society and the global economy. It impacts the availability of resources, the price and structure of the energy market, the vulnerability of infrastructure assets and the valuation of companies. As investors in infrastructure assets, we understand that climate change poses a complex problem, which has already impacted, and will continue to impact, different assets in different ways. We believe it is our responsibility to understand and mitigate these risks within our investment portfolios.

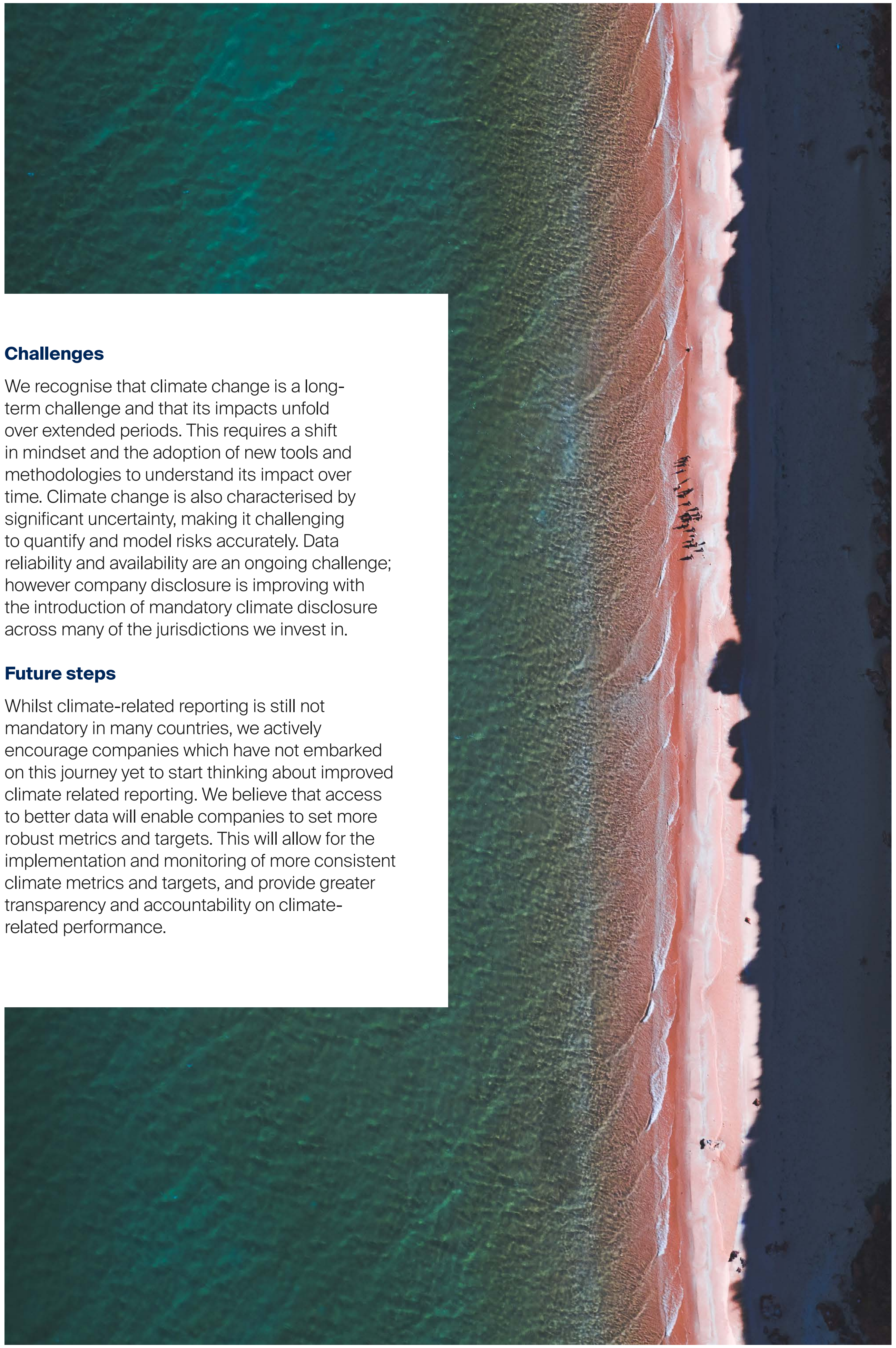
Examples of climate risk for infrastructure assets include:

- Extreme weather events including hurricanes, storm surges, floods and high wind events
- Droughts and the impact this has on water resources
- Increased risk of wildfires causing damage to utility electricity transmission networks
- Rising sea levels causing damage to coastal infrastructure assets.

Climate change-related criteria are incorporated into the quality scores that are assigned to each company that we research and analyse. Our quality scores consider factors including operational risks and the impact extreme weather events may have on a company's cash flows or licence to operate.

We conduct regular meetings with senior management and other stakeholders including suppliers, competitors, regulators and industry bodies. Given the investment experience across the team, we understand companies and markets intimately and believe we are well positioned to form a view on the companies' approach to climate change and the materiality of climate change-related risks and opportunities.

Our engagements on climate risk cover the four pillars of the TCFD disclosures: governance, strategy, risk management, and metrics and targets.



### Challenges

We recognise that climate change is a long-term challenge and that its impacts unfold over extended periods. This requires a shift in mindset and the adoption of new tools and methodologies to understand its impact over time. Climate change is also characterised by significant uncertainty, making it challenging to quantify and model risks accurately. Data reliability and availability are an ongoing challenge; however company disclosure is improving with the introduction of mandatory climate disclosure across many of the jurisdictions we invest in.

### Future steps

Whilst climate-related reporting is still not mandatory in many countries, we actively encourage companies which have not embarked on this journey yet to start thinking about improved climate related reporting. We believe that access to better data will enable companies to set more robust metrics and targets. This will allow for the implementation and monitoring of more consistent climate metrics and targets, and provide greater transparency and accountability on climate-related performance.

# Modern slavery

At FSI, we understand we must do all that we can to ensure our investment decisions, operations and supply chains do not have direct or indirect ties to modern slavery. The GLI team is dedicated to enhancing our systems and processes to identify and combat various forms of slavery and human trafficking, including forced labour, child labour, domestic servitude, and workplace abuse. We acknowledge that suppliers employing lower wage staff may pose higher risks, and we encourage companies to thoroughly map out both their direct and indirect suppliers.

In 2020, FSI formed a modern slavery working group, comprising investment team members including the GLI team and led by the FSI Responsible Investment team. The group aimed to enhance our efforts in human rights by integrating risk identification and governance into our processes. As part of their work, they developed and published the Modern Slavery Toolkit.

The toolkit sets out the steps that investment teams take at both pre- and post-investment stages:

1. Risk identification: Utilizing various data sources and considering factors like complex supply chains to identify potential risks.
2. Risk mitigation: Providing guidelines and sample questions for engaging with companies at risk of modern slavery. It also highlights other forms of leverage, such as policy advocacy and partnerships.
3. Escalation: Outlining actions for escalating, remediation, and ongoing monitoring of any identified instances of modern slavery.
4. Internal governance: Describing the internal governance framework in place to monitor modern slavery risks and the effectiveness of our approach.
5. Reporting: provides a reporting template for investment teams to be completed each year.

The GLI team assessed the risk of modern slavery in our focus list, considering sectors, geographies, and companies. External data sources, including the Transparency International Corruption Perceptions Index, helped identify countries associated with modern slavery risks. Each company in our focus list was ranked based on the vulnerability index of the countries where they operate. Our engagement efforts are prioritised towards companies with higher exposure in countries ranked higher on the index. Two company engagement examples on this important ESG issue are described below.

36. World Economic Forum Global Gender Gap Report 2023



### Challenges

Infrastructure companies have complex supply chains that involve procuring materials, equipment, and services from various suppliers. Companies may not always be fully transparent about their supply chain practises, making it challenging to obtain reliable and comprehensive information. These risks tend to be higher in developing markets such as parts of Asia and Latin America, hence our focus on companies operating in these markets.

Modern slavery laws and regulations vary across jurisdictions, creating a lack of consistent global framework for assessing these risks. The UK and Australia have existing modern slavery legislation, New Zealand and Canada in the process of enacting a Modern Slavery Act, and Japan is developing guidelines on Human Rights Due Diligence. To improve data quality, it will be crucial to translate qualitative social objectives, such as modern slavery, into quantitative indicators.

### Future steps

We will continue to engage with our focus list companies to promote the mapping of their complete supply chain, including direct and indirect suppliers. In our discussions, we intend to focus on remedies and preventive measures to address the challenges mentioned earlier. As we gather more data, case studies, and best practices, we will contribute to updating FSI's Modern Slavery Toolkit, ensuring continuous improvement in our investment approach.

### Addressing the sheer scale of modern slavery

The International Labour Organization[38] has estimated that there are nearly 50 million victims of modern slavery, including crimes such as forced labour, debt bondage, human trafficking, child labour and forced marriage. It means there are 5 victims of modern slavery for every 1,000 people in the world today. And sadly, one in four victims of modern slavery are children.

Modern slavery is a complex and multi-faceted issue. There is no gold standard for identifying and addressing the risks associated with modern slavery and how it is addressed varies between markets and industries.

Generally, we expect leaders to have mapped out their supply chains and to work on building relationships with their suppliers, to have a sense of where the key risks lie and to have robust training and remediation measures in place. We see red flags in instances where companies assert that there is no issue, that the issue has been resolved, no remediation processes are in place and if no examples or case studies of issues identified and addressed can be provided.

38. International Labour Organization, "Forced Labour, modern slavery and human trafficking": https://www.ilo.org/global/topics/forced-labour/lang--en/index.htm

# Corporate governance

Effective governance and board oversight is critical for translating sustainable targets to outcomes. We look at factors including director independence, board size, gender diversity and relevant skills and experience when assessing governance standards. We also look to ensure that the board of directors meets regularly, retains control over the business and are clear in the division of their responsibilities, as well as maintaining a system of risk management. Alignment of interest is important because it ensures that decision making processes are focussed on maximising shareholder value whilst also promoting accountability, risk management and long- term sustainability.

### What makes a good board?

A board that truly adds value is one with a balanced team of high-performing individuals that have complementary skill sets and a culture that allows them to work together to make the most effective decisions for the organisation. Whilst leadership from the chair is crucial, it is the participation of every board member that contributes to the overall effectiveness of a board.

We believe a good listed infrastructure company board has the following characteristics:

- Board size of between 8-10 directors, with the significant majority independent
- Diversity by gender (at least 30% female representation), age and race
- Separation of Chairman and CEO duties, with the Chair being independent*
- Balance of skills and relevant experience, such as industry, finance, regulation, technology, customer, and local knowledge. Sustainability and climate change is a skillset of increased importance
- Regular board refreshment and clear succession planning.

Good boards set the strategy, appoint the Executive and oversee the execution of that strategy. They delegate effectively, have honest conversations with management and are committed to the organisation particularly when it comes to problem solving. We also observe the growing importance and pressure for Boards to also focus on sustainable, socially responsible and environmentally aware business practises.

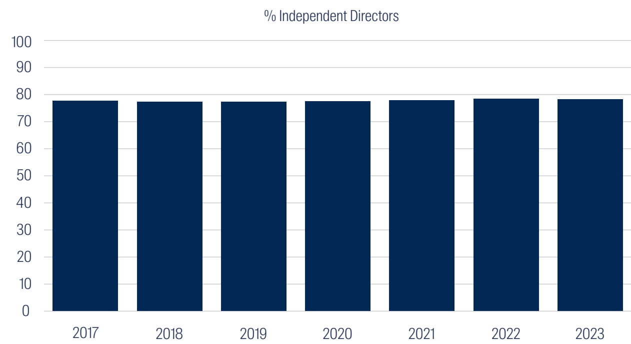
*We acknowledge that a joint Chairman/CEO can also bring alignment if there is a clear strategy and direction with 'skin in the game'. We have seen some successful founder-led examples.

In 2023, we focused on two key corporate governance areas: board independence and gender diversity.

### Board independence

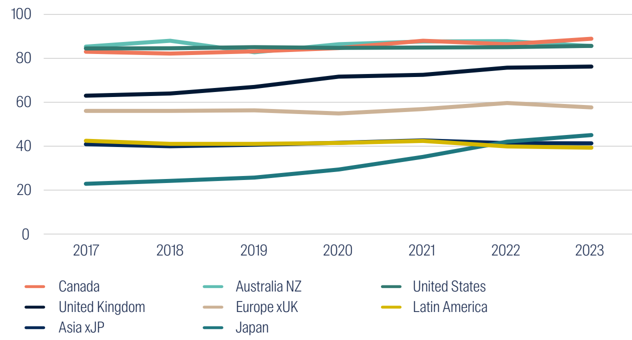
Over the past six years, board independence has consistently remained robust across our portfolios, with an average of around 80%. This reflects the emphasis on developed markets within our portfolio. Notably, infrastructure companies in the United States, Canada, and Australia have set a benchmark for best practices, with typically 80-90% of directors being independent. Japan remains a laggard but there has been a noticeable improvement in recent years, driven by reforms aimed at enhancing corporate governance and attracting foreign investment. We are committed to fostering further progress in this area and will actively encourage companies to prioritize board independence.

**Board independence** Portfolio holdings as at 30 June 2024




Source: First Sentier Investors

**Board independence** Focus list ~140 listed infrastructure companies




Source: First Sentier Investors

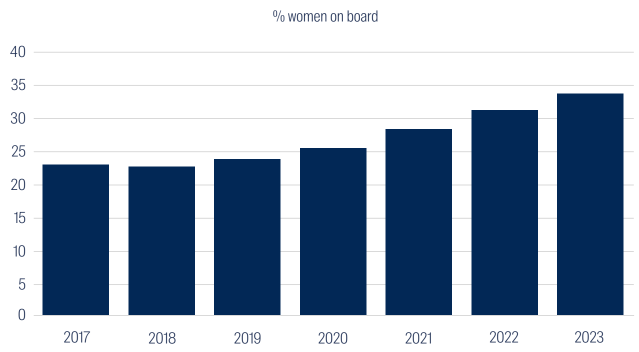
### Gender diversity

For several years, we have been diligently evaluating companies based on their board gender diversity. This is due to the fact that gender balance is typically disclosed publicly and forms an integral part of a company's assessment of its social and governance performance. We firmly believe that a diverse board and leadership team, encompassing a wide range of thoughts, experiences, and perspectives, fosters more comprehensive and informed decision-making processes. Furthermore, diverse companies tend to be more adept at effectively managing risks. We believe by having a diverse workplace and leadership team, potential risks that might be overlooked in a less diverse environment can be identified and addressed proactively.

In recent years, there has been a steady improvement in the percentage of women on boards at the portfolio level, with the figure reaching 34% by the end of the year in 2023. Notably, the United Kingdom has emerged as a leader in gender diversity, achieving a remarkable 50% representation for utilities companies SSE, Pennon, and Severn Trent[¥]. The UK Financial Conduct Authority (FCA) took a significant step forward in April 2022 by introducing new rules that mandate listed companies to report information and disclose their progress towards targets in terms of the representation of women and ethnic minorities on their boards and executive management teams. This move signifies a commitment towards promoting diversity and inclusivity in corporate leadership.

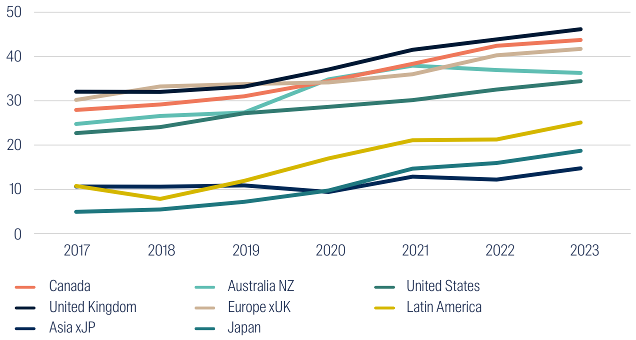
¥ Source: Bloomberg, First Sentier Investors

**Diversity** Portfolio holdings as at 30 June 2023




Source: First Sentier Investors

**Diversity** Focus list ~140 listed infrastructure companies




Source: First Sentier Investors

At a firm level, we continue to be involved in industry collaborations designed to boost gender diversity on boards (Australian Institute of Director's 30% Club) and senior management (40:40 Vision). We are also committed to bringing more women into our own investment teams and continue to work towards our commitment to have women comprise at least 40% of investment management staff by 2033 (currently 30% for the GLI team).

### Challenges

We tend to be cautious when investing in emerging markets, where poorer corporate governance can impact investor confidence. Many infrastructure companies in emerging markets are controlled by a single or group of dominant shareholders, often family-owned or connected to the government. This concentration of power can lead to conflicts of interest, abuse of power, and inadequate checks and balances, resulting in poor governance outcomes. Emerging markets often have less stable political environments and weaker regulatory frameworks compared to developed countries. Frequent changes in government policies, regulations, and laws can create uncertainty and increase the risk of investing in infrastructure projects.

### Future steps

We continue to actively engage with companies to promote good governance practices. Active ownership encourages companies to be more accountable, transparent, and responsive to shareholder concerns. By voting on important governance matters, such as board composition, executive remuneration and shareholder rights, we can support changes that enhance governance standards and align company practices with shareholder interests.



# Proxy voting

The GLI team exercises voting rights on all resolutions where it has the authority to do so. Voting rights are crucial for upholding corporate governance, risk management and protecting investor interests. We believe voting rights are a valuable asset, which should be managed with the same care and diligence as any other asset.

Engaging with a company provides an opportunity to gather information and insights directly from company management. Through meetings with the company we are able to understand the company's strategy and gain a deeper understanding of its governance practises. It enables us to evaluate shareholder proposals, board nominations, executive compensation plans and other matters put to a vote.

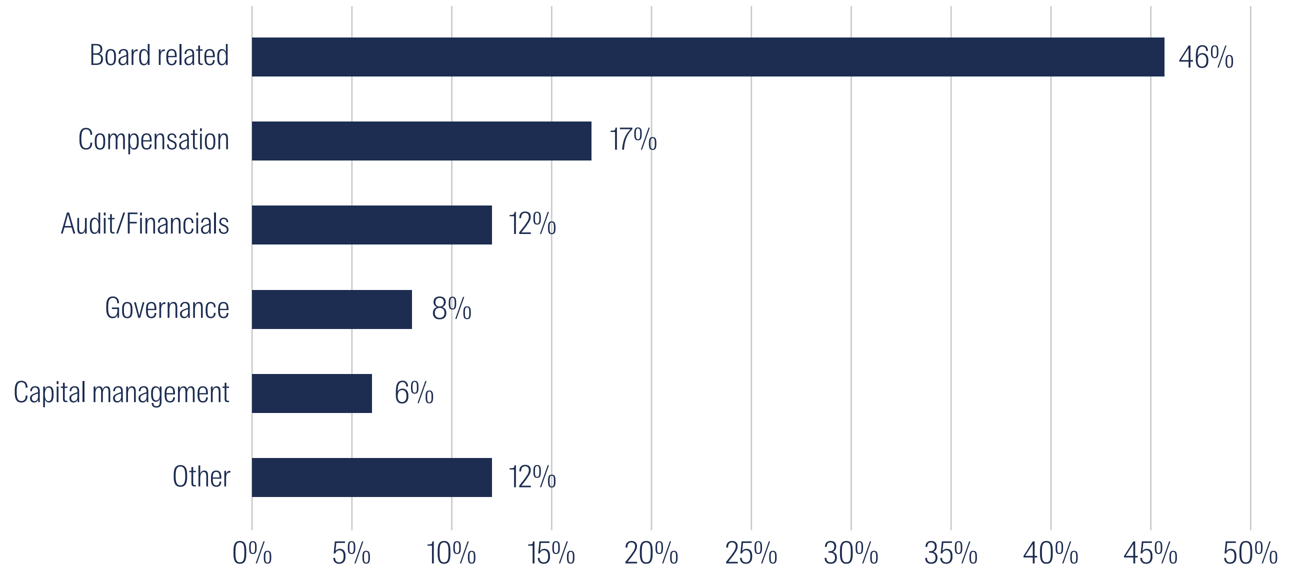
While we seek recommendations from independent research providers, we maintain full control over our voting decisions. If we plan to vote against a proposal, we may engage with the company beforehand for consultation, with a view to achieving a satisfactory solution. In the absence of a positive outcome and if the concerns persist, we may escalate the issue to the board and/or cast a vote against. Ultimately, divestment is considered if there is no willingness to change or address the issue.

Our team maintains records when we vote against management or against the recommendations of our proxy voting advisor, Glass Lewis. Our proxy voting record, at a strategy level, is available on the First Sentier Investors website.

## Proxy voting over 2023

During the 2023 calendar year, we invested in 73 infrastructure companies across 13 subsectors and in 13 countries around the world. We voted on 1,160 proposals, of which we voted against management on 89 occasions on issues including lack of board independence, poor alignment of interests and inadequate climate-related targets.

**Breakdown of votes against management**




Source: Glass Lewis for the 12 months to 31 December 2023