Veritas
— Asset
Management

Real Return
Investing

Veritas Asset Management LLP

Engagement Policy

2023

Introduction

Veritas Asset Management LLP ("Veritas") seeks to buy high quality businesses at the right price. Amongst the characteristics sought when assessing the quality of a business, this will include attractive returns on invested capital, the generation of significant free cash flow, high barriers to entry to protect future cash generation and predictability in the deployment of the cash generated. In short, the investment process seeks to identify businesses that are sustainable over the long term at an attractive price.

The governance of a business is central to the investment case. The management and board of a company are accountable for its long-term strategy and should be cognisant of the risks and opportunities over at minimum a 10-year time horizon and deploy capital accordingly.

Strong management will incorporate sustainability and governance policies and be better placed to deal with emerging risks and opportunities; for example, addressing the use of plastics, developing greater fuel efficiency/ electrification of air travel, or positioning themselves for the transition of healthcare to a value-based system that focusses on reducing drug pricing. Weak management will find their businesses displaced or become uncompetitive. Therefore, it makes little sense to compartmentalize E (Environmental) and S (Social) factors from G (Governance). As active long-term investors, on behalf of clients, two main tools are used to challenge management - voting and engagement. Disinvestment is viewed as a last resort when stewardship efforts have failed.

Assessing Management

Veritas runs concentrated strategies of 25-40 stocks. The level of research is extensive and a significant element of the research effort is centered on company management. This includes assessing the following:

- Management's long-term objectives, how they intend to deploy cash and whether they have a good understanding of target markets, competitive advantages, barriers to entry, and any environmental/ social factors relevant to their business that may pose a risk or reward.

- Whether management incentives are aligned with shareholders and Key Performance Indicators (KPIs) are reasonable and not too short term. These factors will impact the rating given to management. Each Veritas attendee at a company meeting will independently rate management before they are given an overall rating. If the rating assigned deteriorates, this will result in a review and potential engagement.

- Where there is a question on sustainability/ predictability, a higher margin of safety is sought prior to investment. This means seeking a higher internal rate of return from the investment.

Engagement Approach

As active investors, Veritas has a part to play in encouraging constructive behavior, as well as engaging with management on specific issues. There are thus two tiers of Engagement.

Two-Tiers of Engagement

Tier one engagement is conducted where the item poses a material financial sustainability issue. As material issues differ from company to company, the focus is placed on material issues relevant to a particular company. An assessment from the original research as to what is material for a specific business will have been made, this will include which issues have the highest potential to affect the company's ability to create or destroy shareholder value. If the company engages in an activity that challenges the sustainability of its operations or demonstrates a lack of vision to adapt, there will be cause to engage.

Tier two engagement is more thematic in nature and involves interactions with a company to promote good business practices, which benefits all market participants. For example, in relation to environmental positioning, companies should have their transition plans independently verified by an organisation like the Science Based Targets Initiative (SBTi), irrespective of whether it is a high carbon emitter. Whilst the Veritas Funds have a lower carbon footprint than the index, disclosure of climate credentials is essential if any sense is to be made at the portfolio level, or in the industry as a whole. This has meant instigating an SBTi thematic engagement initiative where companies not signed up to the SBTi, but in our view should be, are being encouraged to do so.

Veritas introduced a specific Taskforce on Climate related Financial Disclosures ("TCFD") engagement structure, whereby all investee companies are mapped against TCFD framework and engagement will result in those companies where there is a shortfall.

Engagement with companies also occurs in relation to social areas such as gender diversity. Each year a topic of focus is chosen, and all investee companies are assessed to identify those not compliant with expectations. Where feasible, the engagement objective is aligned with industry best practices or a higher standard. As long-term global investors seeking to work with businesses, best practice must be considered on a case-by-case basis from a regional and industry perspective to ensure expectations are practical. Persistence and patience are both critical as the timeframe to achieve a thematic engagement objective will often exceed 12 months.

Engagement Triggers

Engagement can be triggered in several ways:

- Action that is not aligned with shareholder interest. This can include buying or attempting to buy a company that adds no value to shareholders (i.e., poor deployment of cash) or changing the compensation scheme to include targets that do not align interests with shareholders.
- Breach of the ESG Red Lines within the Voting Policy. The Voting Policy consists of an ESG specific tier. There are 29 Red Lines related to ESG factors that if breached could lead to a vote against management but there is likely to be engagement before doing so.[1]
- If a company's actions are deemed to breach the principles listed under the UN Global Compact ("UNGC"). Analysts receive an email prompt of any breach of the UN Global Compact 10 Principles. Should they not already be aware of the infringement, the analyst may request a meeting to discuss with management.

[1] *Applicable to Global Investment Strategies. The Red Lines will be introduced to the Asian Investment Strategies during the second half of 2023.*

- Task Force on Climate-related Financial Disclosures ("TCFD") shortfalls that are specific to climate transition and reducing the overall temperature on the portfolio. Investee companies are mapped according to disclosures made in line with TCFD guidelines and where there is a shortfall, it will be raised with management.

- Deterioration in the rating of management, which may prompt company engagement[2].

Engagement Process

1. Once the engagement objective has been identified, in the first instance the Investment Team will write to company management explaining the issue and what action should be taken,
2. If the issue is not addressed, the Team will seek to speak with senior management (CEO, CFO, COO etc.) to address the issue.
3. In cases where there is a regulatory or political angle, the Team may have already spoken to third party professionals through an expert network.
4. Post meeting with management, where relevant, the Team will follow up again in writing. At this juncture, the expected timeframe will be determined for any suggested actions to be achieved and how they will be monitored/ measured.
5. If the Team believes that company management is not addressing the matter efficiently or the timeframe to action any changes is not being met, the Team may choose to vote against management at the next opportunity and notify them of our intentions to do so.
6. If engagement and voting fail, the Team may choose to exit the position, and the company will be removed from the Universe List. All activity and milestones are recorded in the engagement log.

Constructive Dialogue

Veritas believes that management should be dealt with in a confidential manner and engagement activity should be conducted away from the press/media. Working with management to give them time to implement a strategy is the preferred approach, e.g., introducing more Non-Executive Directors ("NEDs") to the board. Where one of the ESG Red Lines within the Voting Policy is breached, but is not deemed to be an imminent and material risk to the investment thesis, management may be informed that on this occasion the vote instructed will not be against management. However, a suggested course of action will also be provided to prevent a vote against in the future.

Collaborative Engagement

Veritas aims is to engage with management on an individual basis to resolve an issue. In cases where management is unresponsive or there is a small holding in the company, the firm may collaborate with other interested parties. Given our concentrated investment approach, all holdings are important irrespective of the significance of our holding in terms of the issued share capital. Thus, if the issue is material and collaboration with other shareholders to elicit a response is required, this approach will be taken.

[2] *Applicable to Global Investment Strategies. The Red Lines will be introduced to the Asian Investment Strategies during the second half of 2023.*

Measuring Engagement Success

A successful engagement is evident if the engagement objective is achieved. For example, reversing a decision that is deemed to harm shareholder value, removing a Board member, implementing suggestions, e.g., introducing more NEDs, signing up to the SBTi, introducing KPI suggestions. Selling a position due to the refusal to implement recommendations on material issues is a last resort and would only be used once other options have been explored.

Specific to climate transition and the TCFD thematic engagement, Veritas expects independently validated SBTi approved temperature ratings across all assets to fall in line with the firm's Net Zero commitment.

Engagement Records

An engagement log is maintained to monitor engagement objectives, timeframes, and results. Objectives related to remuneration or disclosure practices can often require multiple interactions with management that extend over a period of several months. The engagement log is forward-looking and if the engagement objective has not been met, a follow-up date is set to review the engagement status, which may trigger further interactions with the business. Veritas does not outsource the monitoring or reporting of engagement activities.

Reporting

Within the ESG Section of the quarterly investment report, an update on any significant engagement activity undertaken during the quarter is provided. This will include any outcome or next steps, both positive and negative. Furthermore, an ESG Dashboard is available in-house to assist with more complex investor queries that assess engagement activities across various areas such as category, region, topic, status, and method of communication.

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