

Shropshire County Council

Q3 2016

The purpose of the **reo**[®] (responsible engagement overlay)^{*} service is to engage with companies held in portfolios with a view to promoting the adoption of better environmental, social and governance (ESG) practices. The **reo**[®] approach focuses on enhancing long-term investment performance by making companies more commercially successful through safer, cleaner, and more accountable operations that are better positioned to deal with ESG risks and opportunities. Through a combination of constructive dialogue and active share voting, **reo**[®] works to drive behavioural change with companies, and records successful outcomes as 'milestones' – changes in corporate policies or behaviour following intervention.

Companies engaged this quarter

Companies engaged	28
Milestones achieved	1
Countries covered	5

Milestones achieved by issue

Environmental Standards	5
Business Ethics	0
Human Rights	0
Labour Standards	0
Public Health	0
Corporate Governance	0
Social and Environmental Governance	0

Companies engaged by country



Companies engaged by issue^{***}



^{*} **reo**[®] is currently applied to £91.3bn (\$121.6billion / €109.6billion) of assets as at 30th June 2016. ^{**} Companies may have been engaged on more than one issue. ^{***} This report has been compiled using data supplied by a third-party electronic voting platform provider. The statistics exclude ballots with zero shares and re-registration meetings. Meetings/ballots/proposals are not considered voted if: ballots have been rejected by voting intermediaries (e.g. where necessary documentation (such as Powers of Attorney, beneficial owner confirmation, etc.) was not in place); instructed as "Do not vote" (e.g. in share-blocking markets); or left uninstruced. This document is for professional advisors only and should not be circulated to other investors. Past performance should not be seen as an indication of future performance. Stock market and currency movements mean the value of, and income from, investments in the Fund are not guaranteed. They can go down as well as up and you may not get back the amount you invest. © 2015 BMO Global Asset Management. All rights reserved. BMO Global Asset Management is a trading name of F&C Management Limited, which is authorised and regulated by the Financial Conduct Authority.

Priority Companies and Your Fund

The table below highlights the companies on BMO's annual priority engagement list with which we have engaged on your behalf in the past quarter and which you currently hold within your portfolio. Priority companies are selected through a detailed analysis of client holdings, proprietary ESG risk scores, engagement history and the BMO Governance and Sustainable Investment team's judgement and expertise. Each priority company has defined engagement objectives set at the beginning of each year. Engagement activity levels for priority companies are more intensive than for companies where we engage more reactively. We provide reporting on our engagement with priority companies in the form of case studies which follows the table below. For full list of priority companies please refer to the Appendix at the end of this report. For full details of our engagements with companies please refer to the online *reo*® client portal.

Name	Sector	ESG Rating	Response to engagement	Themes engaged						
				Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and Environmental Governance
Anglo American PLC	Materials	YELLOW	Good	●		●				
Barclays PLC	Financials	YELLOW	Good						●	
BP PLC	Energy	ORANGE	Good	●					●	
GlaxoSmithKline PLC	Health Care	YELLOW	Good						●	
Glencore PLC	Materials	ORANGE	Good	●			●			●
HSBC Holdings PLC	Financials	RED	Good		●				●	●
Royal Dutch Shell PLC	Energy	YELLOW	Good	●						
Tesco PLC	Consumer Staples	GREEN	Good						●	

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

Engagements and Your Fund: Red rated

The table below highlights the companies with which we have engaged on your behalf in the past quarter and which you currently hold within your portfolio. The table is split by ESG risk rating. For full details of our engagements with companies please refer to the online *reo*® client portal.

Name	Country	Sector	Priority company	ESG Rating	Themes engaged						
					Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and Environmental Governance
HSBC Holdings PLC	United Kingdom	Financials	✓	RED		●				●	●

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

Engagements and Your Fund: Orange rated

The table below highlights the companies with which we have engaged on your behalf in the past quarter and which you currently hold within your portfolio. The table is split by ESG risk rating. For full details of our engagements with companies please refer to the online reo® client portal.

Name	Country	Sector	Priority company	ESG Rating	Themes engaged							
					Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and environmental Governance	
BP PLC	United Kingdom	Energy	✓	ORANGE	●						●	
Experian PLC	Ireland	Industrials		ORANGE							●	
Glencore PLC	Switzerland	Materials	✓	ORANGE	●			●				●
Lloyds Banking Group PLC	United Kingdom	Financials		ORANGE							●	
Smith & Nephew PLC	United Kingdom	Health Care		ORANGE							●	

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

Engagements and Your Fund: Yellow rated

The table below highlights the companies with which we have engaged on your behalf in the past quarter and which you currently hold within your portfolio. The table is split by ESG risk rating. For full details of our engagements with companies please refer to the online *reo*® client portal.

Name	Country	Sector	Priority company	ESG Rating	Themes engaged							
					Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and Environmental Governance	
Anglo American PLC	United Kingdom	Materials	✓	YELLOW	●		●					
BAE Systems PLC	United Kingdom	Industrials		YELLOW							●	
Barclays PLC	United Kingdom	Financials	✓	YELLOW							●	
GlaxoSmithKline PLC	United Kingdom	Health Care	✓	YELLOW							●	
Royal Bank of Scotland Group PLC	United Kingdom	Financials		YELLOW							●	
Royal Dutch Shell PLC	Netherlands	Energy	✓	YELLOW	●							
Sage Group PLC/The	United Kingdom	Information Technology		YELLOW							●	
Ted Baker PLC	United Kingdom	Consumer Discretionary		YELLOW				●			●	
Tullow Oil PLC	United Kingdom	Energy		YELLOW	●							
Unilever PLC	United Kingdom	Consumer Staples		YELLOW		●					●	●

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

Engagements and Your Fund: Green rated

The table below highlights the companies with which we have engaged on your behalf in the past quarter and which you currently hold within your portfolio. The table is split by ESG risk rating. For full details of our engagements with companies please refer to the online *reo*® client portal.


Name	Country	Sector	Priority company	ESG Rating	Themes engaged							
					Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and Environmental Governance	
AstraZeneca PLC	United Kingdom	Health Care		GREEN		●					●	●
BT Group PLC	United Kingdom	Telecommunication Services		GREEN							●	
Centrica PLC	United Kingdom	Utilities		GREEN	●							
Diageo PLC	United Kingdom	Consumer Staples		GREEN	●		●				●	
Marks & Spencer Group PLC	United Kingdom	Consumer Discretionary		GREEN	●	●	●	●	●		●	●
Mears Group PLC	United Kingdom	Industrials		GREEN							●	
Mondi PLC	South Africa	Materials		GREEN							●	
National Grid PLC	United Kingdom	Utilities		GREEN							●	
Next PLC	United Kingdom	Consumer Discretionary		GREEN				●			●	
Standard Chartered PLC	United Kingdom	Financials		GREEN							●	
Tesco PLC	United Kingdom	Consumer Staples	✓	GREEN							●	
Vodafone Group PLC	United Kingdom	Telecommunication Services		GREEN							●	

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

Milestones and Your Fund

The table below highlights the companies with which we have recorded milestones on your behalf in the past quarter and which you currently hold within your portfolio. Milestones are engagement outcomes which we have identified and is rated on the extent to which it protects investor value. For full details of our engagements which led to these milestones please refer to the online *reo*® client portal.

Name	Country	Sector	Priority company	ESG Rating	Themes engaged							
					Environmental Standards	Business Ethics	Human Rights	Labour Standards	Public Health	Corporate Governance	Social and environmental governance	
 Barclays PLC	United Kingdom	Financials	✓	YELLOW	●							

ESG Risk Rating: Rating of a company's ESG risk exposure and risk management compared to industry peers. Source: MSCI ESG Research Inc.

Top quartile: GREEN Second quartile: YELLOW Third quartile: ORANGE Bottom quartile: RED

ESG Viewpoint

September 2016

Rosey Hurst, Member of the Responsible Investment Advisory Council

Emma Lupton, Analyst, Governance and Sustainable Investment

Manuel Isaza, Associate Director, Governance and Sustainable Investment

Human capital management as a mainstream performance indicator

➤ **Goal:** Incorporate human capital management as a key indicator of corporate performance

➤ **Engagement since:** 2007 and intensively since 2013

➤ **Sectors involved:** Consumer staples, energy, information technology, materials

Key Summary

- Over the past few years, we have stepped up our engagement on human capital management in companies' direct operations and supply chains to reflect its impact on company performance, as well as the growing global concerns around inequality and unfair labour practices.
- Even in labour intensive industries, a company's workforce continues to be viewed purely as a cost, despite a growing number of corporations referring to employees as their greatest asset.
- Reporting remains weak and lacks transparency as companies assume that the provision of human capital management information is not considered material as part of the fundamental stock analysis process.
- While there is still significant work to be done, we have observed encouraging progress in a number of our engagements and we continue to advocate for a greater inclusion of human capital management performance indicators as part of our issuer due diligence process.

Background

The materials sector, specifically mining, has had more than its fair share of issues related to labour management and therefore we have been engaging with a number of mining companies on this for several years. We escalated our engagement in 2012 on the back of violent strikes at Lonmin's Marikana mine. We travelled to South Africa in 2014 following a wider strike in the country's mining industry, which resulted in a negotiation deadlock over wages and wiped out over \$400 million in revenues. The connection between these long-neglected labour management issues and the performance of the companies involved was undeniably material.

At the time, we pressed those companies to adopt a more progressive approach to managing labour relations. We asked the companies to formalise relations with trade unions to safeguard fair employee representation, to work more collaboratively across the sector to improve working conditions (including safety and wages) and to demonstrate greater engagement with local communities and governments.

The learnings from our engagement with mining companies on labour issues presented us with an opportunity to undertake similar work with garment manufacturers, as well as with retailers sourcing from vulnerable areas. After the Rana Plaza disaster in 2013, we travelled to Bangladesh where we had the opportunity to engage directly with local suppliers, activists, non-governmental organisations, multi-stakeholder institutions and brands about the pace and impact of safety and worker rights' reform in the garment industry.

We focused on the material impact on performance should companies fail to address basic working conditions to safeguard the wellbeing of workers. It was evident that the conditions which led to the Rana Plaza catastrophe were a by-product of under-investment in structures and facilities by factory operators and poor governance by regulators. We encouraged companies to collaborate to achieve higher safety and worker protection standards, to improve governance and regulation, and to link improved human resource management with higher productivity. Our continuous engagement on this topic has contributed to expedite the much needed change and to address the failures caused by previous lax provisions, thus creating greater impact. As we continued to roll out our work on various topics related to human capital management, including our engagement project on the living wage in the textile industry, the materiality of our topics of engagement

continued to become increasingly prominent. The companies we were engaging with on various labour issues were certainly facing performance issues as well. Consequently, we sought to develop a framework to bring the discussion on human capital management risks and opportunities to the mainstream. We then co-led a number of global investors in a collaborative project and formulated a guide for analysts to incorporate the topic of human capital management as part of their stock research process and ultimately into investment decisions.

Accounting for human capital opportunities and risks

We have been engaging on this issue since 2007 (see timeline below). Since our focus on this area intensified in 2013, we have undertaken more than 500 engagements on human capital management issues and have achieved over 30 milestones since we escalated our work on this topic after the issues around Lonmin's Marikana mine.

Such vast numbers prompted us to take a more all-encompassing approach to our engagement on this topic and to create a framework to facilitate the incorporation of human capital management questions at the core of company analysis.

Engagement timeline

Our Engagement	Background	Action	Verdict
2007 – Tesco's supply chain issues.	Persistent allegations of poor labour standards in supply chain.	Escalated engagement to the office of Tesco's chairman and worked with other stakeholders.	Tesco strengthened implementation of its labour standards policy and enhanced disclosure.
2007 – Wal-Mart's declining performance and poor employment practices.	Repeated violations of domestic employment policies that indicate failures in internal controls.	Participated in multi-investor engagement to encourage the company to enhance anti-discrimination policies. Site visit to audit supply chain.	Wal-Mart agrees to enhance its non-discrimination policy and training for global workforce. Site visit resulted in enhanced whistle-blower mechanisms.
2010 – Managing commodity labour standards in global clothing and retail.	Endemic child and forced labour in the important Uzbekistan cotton harvest threatening reputation of and supply to clothing brands and retailers.	Encouraged brands to cease sourcing of Uzbek cotton unless produced under frameworks with appropriate labour standards.	Leading brands respond and forge new partnerships to tackle a complex supply chain issue.
2010 – Spotting "rotten apples" in IT supply chains: labour standards and human rights risks in the tech sector.	Manufacturing for tech industry takes place in markets with underdeveloped labour frameworks and minerals are sourced from troubled regions subject to human rights issues.	Engaged companies to protect and improve supply chain labour standards and human rights, in order to reduce the risk of labour violations, avoid work stoppages and avert reputational risk.	Promoted enhanced disclosure of supply chain management labour standards and compliance with internationally accepted practices.
2011 – US food retailers and employee relations.	Ongoing employment-related risks for food retailers in the US, including anti-union allegations which impact performance.	Sector-wide engagement focused on promoting policies and practices that are implemented throughout entire operations and not only where mandated by domestic regulations.	Varied levels of response by target companies with very diverse standards. Successful identification of best practices to foster appropriate benchmarking and identification of leaders and laggards.

Our Engagement	Background	Action	Verdict
2012 - South Africa's mining strikes.	Sector-wide strikes over employment conditions representing material costs to companies operating in South Africa.	Pressed companies to design effective and direct communication strategies between management and employees, and to reframe remuneration arrangements.	Engagement contributed to enhanced dialogue between companies and unions leading to improved reputational risk management.
2013 – Bangladesh garment industry.	Appalling working conditions exposed following the Rana Plaza disaster which threaten the viability of an important part of the garment industry's supply chain and the reputation of companies sourcing from Bangladesh.	Extensive engagement, including site visits to Bangladesh factories. Pressed companies to endorse and uphold internationally accepted standards for better working arrangements and conditions throughout the supply chain.	Through our escalated engagement, including site visits and collaboration with other stakeholders, we were able to influence the pace and impact of reforms and to encourage companies to prioritise real-life improvements.
2015 – Bangladesh garment industry; phase two.	Follow up engagement on sustainable supply chain to address remaining issues of non-compliance by certain suppliers.	Promoted greater collaboration across companies to achieve higher safety and worker protection standards and to link improved human resource management with higher productivity.	Considerable increase in transparency of disclosures related to work on sustainable sourcing by participating companies. Investment in building safety also increased, improving workers' conditions.

Conventionally, most of the time spent on company research has been on financial performance indicators. However, with the ever-growing trend of integration of environmental, social and governance (ESG) factors into the investment research process, it is unsurprising that certain non-financial metrics are starting to make their way into the list of data points included when considering companies as part of stock selection. The United Nations' Sustainable Development Goals have provided an additional momentum to this trend and investors' interest in how well companies manage environmental, social and governance factors continues to grow.

Human capital management has become an area increasingly scrutinised by analysts given the likely material impact on performance. Nevertheless, given that there is still no systematic market-wide demand for performance data in this area, company disclosure remains substandard. We have been co-leading the joint-investor Human Capital Management Coalition's Analysts Questions Project. This seeks to encourage better disclosure from issuers on this topic and to aid investment analysts in their due diligence process.

We have structured the framework with the aim of facilitating early identification of potential risks and/or opportunities via a few high-level questions. We assess the need for escalation based on the robustness of the company's answers to the following in relation to their own direct operations as well as their supply chains:

- What is the company's human capital management strategy?

- What metrics does the company use to measure strategic success? Why?
- How does the company benchmark progress and what are its future targets?
- How does the company analyse the relationship between these metrics and performance?

Beyond the initial assessment, we have identified five areas of human capital management with measurable performance indicators that enable us to better quantify opportunities and risks. These five areas are:

- Talent attraction and retention
- Workforce composition
- Employee engagement
- Health (safety and wellness)
- Returns (financial impact of investments in human capital)

Our extensive engagement on a wide range of human capital issues has evidenced the material impact that these can have on company performance. Our view is that this trend will continue as investors – and a growing number of issuers – increasingly see a company's workforce as an asset worth developing instead of a cost that needs to be curtailed. Human capital management will therefore undeniably continue to gain relevance as part of company analysis. We believe that our proposed framework is a practical and applicable approach for investors to use that will bring these issues into the mainstream and move the agenda forward as the demand for improved corporate disclosures on human capital increases.

The information, opinions, estimates or forecasts contained in this document were obtained from sources reasonably believed to be reliable and are subject to change at any time. © 2016 BMO Global Asset Management. All rights reserved. BMO Global Asset Management is a trading name of F&C Management Limited, which is authorised and regulated in the United Kingdom by the Financial Conduct Authority. FRN:119230. CM10584 (09/16).