

BAILLIE GIFFORD ESG RESEARCH PROGRAMME

*ENVIRONMENTAL SOCIAL AND GOVERNANCE
THEMES FOR 2016*

BAILLIE GIFFORD

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Head of Corporate Governance

Andrew graduated from London’s School of Oriental and African Studies (SOAS) with an MSc in International Development in 2001, after completing an MA in History at the University of Edinburgh in 1999. Andrew joined Baillie Gifford as Head of Corporate Governance in May 2015. In his previous role as Chief Sustainability Officer for RBS he was responsible for rebuilding RBS’s approach to corporate responsibility, ethics and sustainability in the wake of the financial crisis. He is on the sustainability advisory committee at ICAS and Edinburgh University Business School, and is a former Chairman of the UK Global Compact Network.



MICHELLE O’KEEFFE

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Michelle graduated BSc (Hons) in Zoology from Cardiff University in 1999 and has an MSc in Climate Change and Risk Management from the University of Exeter, awarded in 2009. She joined Baillie Gifford in March 2015 as an analyst in the Corporate Governance team bringing expertise in climate change, resource governance and European policy assessments gained through previous roles with the Carbon Disclosure Project as Technical Director of reporting and as a research associate with University College London’s Institute for Sustainable Resources.



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BAILLIE GIFFORD ESG RESEARCH PROGRAMME

Baillie Gifford has been a research-led firm since the earliest days of the partnership, using our proprietary research to identify the best investment opportunities for our clients. This approach has extended in recent years to our work on Environmental, Social and Governance (ESG) factors, with the in-house team producing a number of specialist reports on emerging themes to supplement research work on specific companies. Recent examples include papers on corporate governance developments in Japan and global climate change issues.

Following the significant expansion of the Corporate Governance team in 2015, we will be taking our research commitment a stage further in 2016. After a comprehensive review of current and emerging ESG issues, we have selected four key themes that will serve as a framework for a structured research programme over the course of 2016. This broader strategic research will complement the ongoing company level research undertaken by the team, helping

to develop deeper insights into the key ESG issues affecting different sectors of the economy. The focus of our work will evolve and adapt over time as new themes emerge but, initially, in 2016 the projects will focus on the following key areas:

- Governance for Growth
- Climate Change
- Sustainable Production
- Modern Living



WHY PRODUCE OUR IN-HOUSE RESEARCH ON ESG ISSUES?

Before fleshing out these themes, it is first worth considering why we think it is important to conduct our own independent research on ESG matters.

At Baillie Gifford, we are interested, in particular, in understanding the long-term investment performance implications of ESG indicators. Despite the increasing numbers of external research providers looking at ESG topics, and notwithstanding some of that research being of a high quality, it is difficult to find research that addresses our interests fully.

Conducting our own additional ESG research allows us to focus on areas important to us. We are also able to leverage our in-house knowledge and relationships with companies to supplement available data on ESG issues, something that external providers are often unable to do. In many cases, ESG issues have no clear right or wrong – issues evolve over time and best practice emerges from comparative approaches taken by different companies and sectors. We can use this insight to help other companies we invest in to make better long-term decisions on ESG matters.

INTEGRATING ESG RESEARCH INTO THE INVESTMENT PROCESS

With our focus on supporting the investment process and understanding the long-term investment performance implications of ESG matters, our research findings, whether company specific or theme-based, are integrated into the investment process in three principal ways:

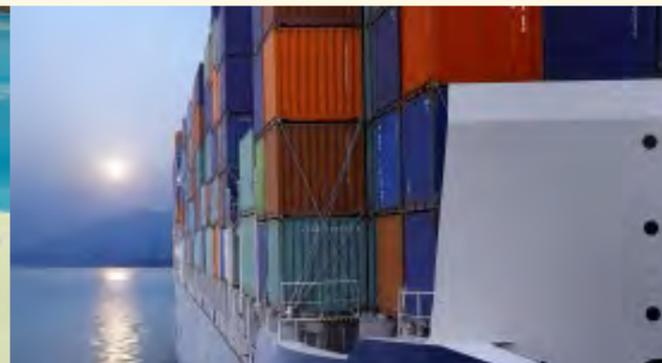
Assessing companies: Many aspects of a company are considered before we invest, such as financial strength, competitive environment and quality of management. ESG is another important part of this research mosaic. ESG research not only helps to identify a fuller picture of the long-term growth opportunity for a stock, but it also highlights some of the risks. Where we identify ESG risks, these may not stop us from purchasing a stock, but it does help us to consider whether such risks are fully understood by the company's management.

Engagement: We aim to own stocks for the long term. We believe that with this ownership comes responsibility. Throughout our ownership we will engage with companies on issues that we think will affect them over the long term either positively or negatively. Our ESG research often highlights issues relevant to specific companies that we wish to engage on. Where we do identify what we believe to be current best practice approach to an ESG issue within a sector, we will then use this as a basis for discussions with other companies.

Idea generation: Our investors generate investment ideas from multiple sources and as a firm, we deliberately cultivate a rich diversity in our sources of insight. We remain open-minded about sources of growth and we believe that our ESG research can contribute to discovering and exploring new investment ideas.

2016 THEMES

This focus on ESG as an integral part of a long-term approach to investing in companies has helped guide the selection of what we believe to be commercially relevant and material research themes from an ESG perspective. As such, we take a closer look at each of our 2016 themes.



GOVERNANCE FOR GROWTH

There is one overriding question in this theme: which governance structures within companies support sustainable business growth and promote innovation, transformation and long-term success? We will look to explore all aspects of governance globally to understand how we can best identify and encourage positive governance for long-term growth. In exploring this topic we anticipate key sub-questions being: what are the pros and cons of the different governance models and share class structures that have emerged globally? How can we evaluate corporate tax practices amongst multi-national companies? What are we looking for in positive diversity and inclusivity strategies? And, importantly, what governance characteristics are common throughout our most successful growth-driven investments? Collectively, this research theme will move beyond ‘tick box’ governance to explore and understand the nuances, context and ultimately positive features of different corporate governance systems.

CLIMATE CHANGE

Continuing on from 2015, climate change remains an important theme for 2016 as the practical outcomes of the Paris climate negotiations become apparent. Regardless of these negotiations, however, we can expect to see a continuation of the increased levels of awareness and action by companies in carbon mitigation and climate change adaptation.

For 2016 we will continue to work on understanding carbon risk within our portfolios. We will look to move the conversation away from a supply dominated one that focuses on the fossil fuel industry. Instead, we will consider the impacts of a carbon constrained world from a demand perspective across all aspects of the economy, alongside the positive impacts of a transition to a low carbon economy, as well as considering how climate change impacts on natural resources such as water and forests.

SUSTAINABLE PRODUCTION

Looking at all stages and components of the process, this theme will look at what sustainable production really means in practice. For example, how are natural resources utilised in the production of food, and how will climate change, water and energy considerations drive changes in production methods? How are the leading companies successfully mitigating or solving these challenges?

Yet, the theme of sustainable production is broader than this, equally including the human aspects of the production process, where the most sustainable approach is not always obvious – improving health and safety standards and other working conditions, as well as managing the complex issue of child, youth and forced labour are all important considerations. Finding the best ways of assessing companies in sectors which have traditionally had labour challenges, and understanding the complexity of addressing these issues is a key component of this theme.

MODERN LIVING

New technologies are bringing unprecedented opportunities to improve living standards, but also significant challenges. This, the broadest of our four themes, aims to encapsulate ESG developments associated with the rapidly changing world we live in. Through exploring this theme, we aim to focus most specifically on the recent accelerated changes that have occurred in the way we move, work, live, eat and shop, and how this affects societies’ interactions with corporations, locally and multi-nationally. We want to identify the types of companies that are best placed to benefit from these changes. The range of issues considered under this theme will include the implications of the technology age on data privacy and cyber security, changing trends in consumption and their knock-on effects for society and business, and the ethical dimensions of advancements in healthcare, amongst others. Many of the topics under this theme will look at the high-income end of consumption, but it may also address new consumers from emerging economies and the so-called ‘base of the pyramid’, and the opportunities that this may present from an ESG perspective.



Associated with the themes are a series of detailed research projects which will look to address the subject areas from a range of perspectives. These projects will evolve over time, some examples are provided in the table below.



EXAMPLE PROJECTS

Pros and cons of the different international governance models	Portfolio carbon foot printing – understanding the carbon risks	Trends in food production	Data privacy and cyber security
How can we evaluate sustainable corporate tax practices?	Practical outcomes of the December 2015 climate negotiations	Human aspects of production process	Changing trends in consumption
Share structures – The development of multi-class share structures	What opportunities from the transition to a low carbon economy?	Production challenges in the extractives sector	Ethical dimensions of advancements in healthcare

RELEVANT SECTORS

All sectors	Energy, Mining and Metals, Travel and Tourism, Food, Chemicals	Food, Electricals, Clothing, Extractives	Aviation, Pharma, Technology, Food and FMCG
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CONCLUSION

It is our belief that robust and independent ESG research can form a valuable input into the investment decision making process. Our approach to ESG at Baillie Gifford has continued to evolve over the last year, and in response to the remit of providing further strategic support to investment colleagues, the team has been significantly expanded and the levels of experience increased. This paper encapsulates the first significant step in expanding the research base of the team, and we look forward to sharing our findings with you over the next year including updates within our governance letters in our quarterly client reports. If the companies in which we invest benefit from our proactive engagement and insight over the long term, then so should our clients.

CURIOUS ABOUT THE WORLD

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