Statement on Principal Adverse Impacts

Federated Hermes

www.hermes-investment.com
For professional investors only

This statement applies to the international business of Federated Hermes ('Federated Hermes'), including Hermes Investment Management Limited, Hermes Fund Managers Ireland Limited and Hermes Alternative Investment Management Limited.

Our approach

Federated Hermes is guided by the conviction that responsible investing is the best way to create long-term wealth. Our goals are to help individuals invest and retire better, to help clients achieve better risk-adjusted returns, and consistent with client objectives and applicable requirements to contribute to positive outcomes in the wider world.

We believe the purpose of investment is to create wealth sustainably over the long term.

Sustainable, because there is no point making an investment that rises strongly in value one year, only to collapse at some point in the future. That is the risk investors run when businesses behave in an unsustainable way, both specifically, if they suffer a reputational, governance or operational failure, and systemically, if their behaviours lead to wealth destructive environmental damage, political instability or regulatory action that harms their business model.

Creating wealth, because this is not just a zero-sum game of winning at someone else's expense. It's investing to earn a share of the new wealth that is created by the investment that enriches investors, employees and society.

And **long-term**, both because investing usually has a multi-year payback and because investors' needs stretch way into the future.

We recognise that as fiduciaries, entrusted with the savings of millions of individuals, we have broad and important responsibilities to our clients and their ultimate beneficiaries. We have these responsibilities because our decisions will have impacts on the world in which beneficiaries live and work today as well as the one in which they will retire into tomorrow.

Whilst capital is at risk with any investment, in meeting the needs of our clients and beneficiaries we are cognisant of our commitment to delivering superior long-term risk-adjusted investment returns within the terms of our mandate. We also understand that the way we achieve these financial returns will have a wider economic, environmental and societal impact and will consequentially likely impact upon the real value of their savings and retirement incomes. These factors, while more difficult to quantify and measure, will be significant, not only to the real financial value of their savings but also to their quality of life and cost of living. Focusing on wealth creation at the expense of the planet and society – the very future for which investors are saving – is counterproductive over the longer-term.

It is this understanding that informs our belief that we have a duty to consider longer-term risks and opportunities when investing. We spend considerable time analysing investee companies and assets to understand the long-term financially material sustainability risks; understanding externalities, governance practices, and social and environmental impacts. It also means using our voice and economic influence to improve the behaviour of those companies in which we have invested; the operations of the assets that we directly manage; and advocating for systematic improvements to the financial system in which we participate.

Success in our mission delivers the returns needed by clients and beneficiaries over the long time-horizons over which they invest. We firmly believe our approach delivers superior risk-adjusted financial returns for our clients, through consideration of longer-term risk factors in the investment decision making process, including a company's relationship with its stakeholders as well as its impact, through both its operations and the products and services it offers, on the environment and wider society.

We have demonstrated through the almost 40-year history of our firm that responsible investment and stewardship often leads to better financial outcomes.[1] Moreover, robust research increasingly indicates the positive impact of stewardship on investment performance, with high-quality academic evidence showing that engagement can pay off financially and effect positive change on corporate behaviour. Successful engagement can translate into significant outperformance: studies have shown that engagement can generate significantly higher annualised returns[2], while also leading to lower downside risk.[3] There is no conflict between doing good and good investment management – they are one and the same thing. Sustainable wealth creation is self-reinforcing, benefiting the planet and society in a virtuous circle that protects and enhances financial value.

Due diligence regarding principal adverse impacts

At Federated Hermes, we believe there are two mutually reinforcing strands of responsible investment management: responsible investment and responsible ownership. Within these strands, we aim to generate sustainable wealth creation for the end beneficiary – the investor – by delivering superior investment returns and positive social and environmental impacts.

Responsible ownership consists of both asset engagement and advocacy. Asset engagement is the process of actively engaging with companies to encourage them to align their behaviours with the long-term interests of investors by addressing the needs of their most important stakeholders, and thereby improving their strategic, financial and ESG-related performance. Advocacy is where we engage with public policymakers, regulators and industry bodies to enhance industry norms, and market rules and regulatory requirements in relation to corporate governance, stewardship and environmental and social policy both globally and regionally.

[1] https://www.hermes-investment.com/uki/insight/equities/esg-investing-a-social-uprising/ ; https://www.hermes-investment.com/uki/press-centre/fixed-income/new-research-shows-relationship-esg-factors-credit-spreads/ ; https://www.hermes-investment.com/uki/insight/fixed-income/pricing-esg-risk-sovereign-credit/
[2] Dimson, E., Karakas, O. and X. Li. (2015). Active Ownership. The Review of Financial Studies, 28(12), 3225-3268.
[3] Hoepner, A.G.F., Oikonomou, I., Sautner, Z., Starks, L.T., and X.Y. Zhou. (2020). ESG Shareholder Engagement and Downside Risk. ECGI Finance Working Paper 671/2020.

Identification of principal adverse sustainability impacts and indicators:

Given our belief that the purpose of the investment industry is to create wealth sustainably over the long term, we consider the assessment of principal adverse impacts to be a natural and necessary part of our investment process. As such, we integrate ESG considerations and engagement insights into our investment processes in all of our products, across all asset classes. Such principal adverse impacts may already be financially material or may become so over the longer time periods over which our clients invest. The consideration of principal adverse impacts – and how to mitigate them – is also key to achieving our goal of contributing to positive outcomes in the wider world. The identification of principal adverse impacts is therefore part of our ESG integration and our approach to engagement.

All our investment activity is supported by our dedicated Investment Office and Responsibility Office, both of which report directly to our CEO. However, it is the responsibility of our investment teams to effectively integrate stewardship and ESG information into their investment processes. Ultimately our fund managers have discretion on individual investment decisions. ESG factors – including consideration of the impact of investees on sustainability factors – are fully integrated into investment analysis and decision making. The investment teams are best placed to assess the materiality of ESG factors for investments and the impacts they may have, relative to mitigation efforts. The work of the Investment Office and Responsibility Office oversee this process and verify and challenge the approach.

Research and analysis by all of our investment teams includes an evaluation of performance on strategy, financials, risk and material ESG factors, and the overlaps between these elements. Insights from engagement with company management, boards, subject specialists and other shareholders and stakeholders – including the extent of engagement progress - is a key input into this process and investment strategy. Such engagement is carried out both by our investment teams and by EOS at Federated Hermes, our stewardship business. These factors influence decisions to invest and are also actively monitored after investment, with the potential to influence decisions to sell an asset. Where concerns arise in relation to one of our existing investments, engagement is often a means to both raise concerns with the company and seek to reduce the risk.

The teams supplement fundamental financial analysis with information provided through a range of proprietary ESG and engagement tools, qualitative analysis and the insights gleaned through engagement. Engagement is in itself a form of due diligence, enabling us to establish a clearer picture of the practices and impacts of a company beyond the information available in corporate publications. Our Responsibility Office is tasked with monitoring and overseeing every investment team's approach to integrating ESG and engagement insights into their investment decisions and the monitoring of investees. To that effect, the Responsibility Office meets with every investment team on a quarterly basis to review the portfolio holdings from an ESG point of view and flag, if necessary, particular holdings which our third-party ESG data vendors might have highlighted as controversial.

This integrated approach enables us to identify principal adverse impacts. While the most pressing material risks are those that will crystallise in the short term, we are long-term investors that strive to deliver sustainable wealth creation for our end investors. This means that our definition of materiality is necessarily wider. We believe that a wider range of risks will ultimately become material over a longer timeframe and that we need to engage proactively to mitigate them. The assessment of principal adverse impacts is therefore inextricably linked with our assessment of sustainability risks as over a long-term horizon, such impacts can become material risks to the investment, for example through reputational damage or regulatory interventions.

Prioritisation of principal adverse sustainability impacts and indicators:

Our investment teams consider all material investment factors, including those relating to material ESG risks and opportunities. As described above, given our long-term approach to investment, this would include an assessment of principal adverse impacts, integrated into the analysis of ESG factors.

The presence of ESG risks – including principal adverse impacts - does not necessarily preclude investment, but rather helps investment teams reach a more holistic view of the risk profile of a company. Investment teams may also identify opportunities in companies that are improving their ESG practices including social and environmental impacts, particularly given our strong engagement capabilities.

We assess material areas of concern for each of the sectors and industries, with an overlay of material ESG issues by region. This is done by using the SASB Materiality Map, and primary research as well as insights from EOS at Federated Hermes. Relevant ESG issues – including adverse impacts on sustainability factors – are then considered on a company-by-company basis, with implications for both inclusion and weighting in an investment portfolio, as well as engagement.

Principal adverse sustainability impacts

Principal adverse impacts

Given the range of asset classes, sectors and geographies in which we invest, the principal adverse impacts that our investments may have are not homogenous and may include impacts on:

- climate and other environment-related matters, for example through greenhouse gas emissions of investee companies; or
- social and employee, respect for human rights, anti-corruption and anti-bribery matters, for example in relation to the diversity of employees or gender pay gaps at our investee companies.

There are a range of actions we may take to mitigate such impacts. Firstly, our assessment of the adverse impacts as part of our investment analysis may impact investment decisions that we take, such as whether to buy, hold or sell an asset or change our investment exposure, particularly where we feel adverse impacts may represent a material financial risk.

Secondly, as well as helping us to identify instances of adverse impacts in the first place, engagement with investee companies and assets is a crucial part of our approach to mitigating potential or existing adverse impacts. We may also see an investment opportunity where there is potential for improvement through engagement. Our approach to engagement is outcomes-driven and focused on ensuring that the assets we invest in are creating wealth sustainably. Given our long-term approach, we are able to engage on particular issues over multiple years with key decision makers in the companies, such as executives and the board of directors, to encourage fundamental change within our investee companies and assets. For listed equities, voting is an integrated part of our engagement approach. As such, our voting decisions are informed by the insights and experience from engagement with the investee company and support our engagement objectives. We escalate the intensity of an engagement over time as required using our rights as an investor and may engage in collaboration with other investors to avoid or mitigate principal adverse impacts. We believe that this approach delivers the best results for our clients and end beneficiaries. More information on our engagement approach and outcomes is available on our website.

We recognise that as investors we have an opportunity and a responsibility to help address market-wide and systemic risks. We therefore also engage constructively with regulators and policymakers globally to address environmental, social and other market failures that may prevent the financial system from operating in the best interests of its ultimate asset owners. This includes tackling thematic issues that impact the assets in which we invest.

Engagement policy

Federated Hermes honours its responsibility as a fiduciary for investors and their beneficiaries and seeks always to act in their best interests. We undertake stewardship and long-term engagement to exercise active ownership of the assets we invest in on behalf of investors, and to deliver our purpose of helping investors achieve their financial objectives. For Federated Hermes, stewardship is both a responsibility and an input to achieving optimal investment performance, in particular over the long-term. We take a comprehensive approach to stewardship, engaging globally with our companies and other investees and with other industry participants, in particular policy makers, standard setters and regulators. The majority of engagement with our public markets investees is undertaken for Federated Hermes by the dedicated stewardship services of EOS at Federated Hermes. We benefit from the long engagement history and established relationships of EOS at Federated Hermes in relation to both Federated Hermes investee companies and its broader investable universe.

Our full Engagement Policy is available on our website.

Adherence to codes and standards

We adhere to a number of responsible business conduct codes and internationally recognised standards for due diligence and reporting, including:

- We are signatories of the UN Global Compact, and report annually on our implementation of these principles.
- We are founding signatories of the UN Principles of Responsible Investment and report annually using the Reporting Framework.
- We publish an annual climate-related financial disclosures report in line with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).
- We are a signatory of a number of stewardship codes, including the Financial Reporting Council's UK Stewardship Code.
- Our stewardship business, EOS at Federated Hermes, is a signatory of the Best Practice Principles for Providers of Shareholder Voting Research & Analysis and reports annually on implementation of these principles.

We comply with all relevant regulatory disclosures, including the requirements of the UK Modern Slavery Act (2015) and the EU Shareholder Rights Directive II.

Federated Hermes
International

Federated Hermes

Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns, and to contribute to positive outcomes that benefit the wider world.

All activities previously carried out by Hermes now form the international business of Federated Hermes. Our brand has evolved, but we still offer the same distinct investment propositions and pioneering responsible investment and stewardship services for which we are renowned – in addition to important new strategies from the entire group.

Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by four decades of experience
- **Private markets:** real estate, infrastructure, private equity and debt
- **Stewardship:** corporate engagement, proxy voting, policy advocacy

For more information, visit **www.hermes-investment.com** or connect with us on social media:

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