Federated Hermes Global Equity ESG Fund

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H1 Report 2022

Federated Hermes Limited

www.hermes-investment.com
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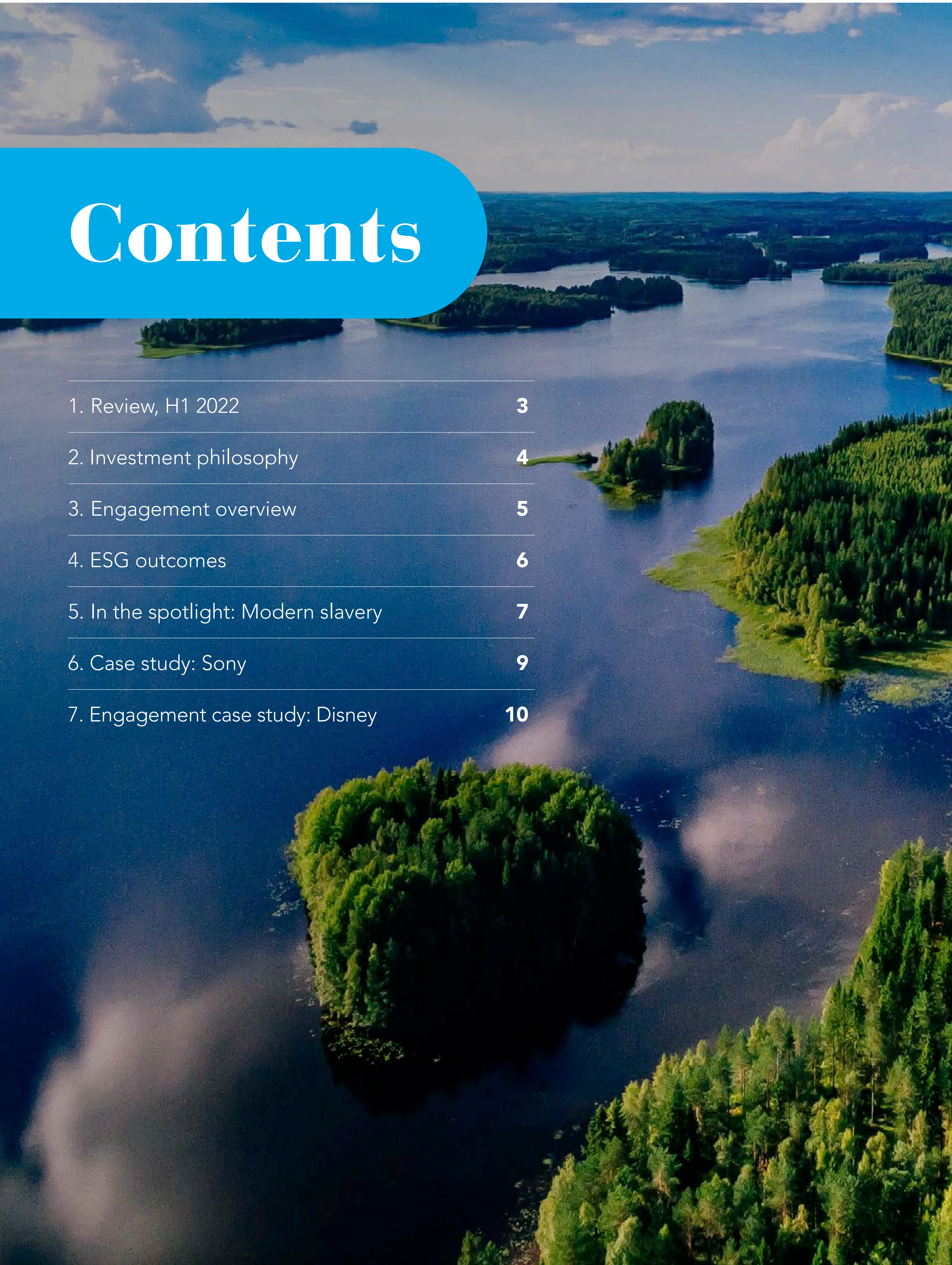


Contents

SECTION 1

Review, H1 2022

The first half of 2022 saw an extremely challenging environment for investors, with markets battered by multiple headwinds.

Rising inflation and slowing growth were exacerbated by the impact of the conflict in Ukraine, while consumer confidence fell as interest rates rose. The result was one of the worst market performances in recent memory, with all regions and sectors bar energy declining, and the MSCI ACWI Index returning -20.2% for the period.

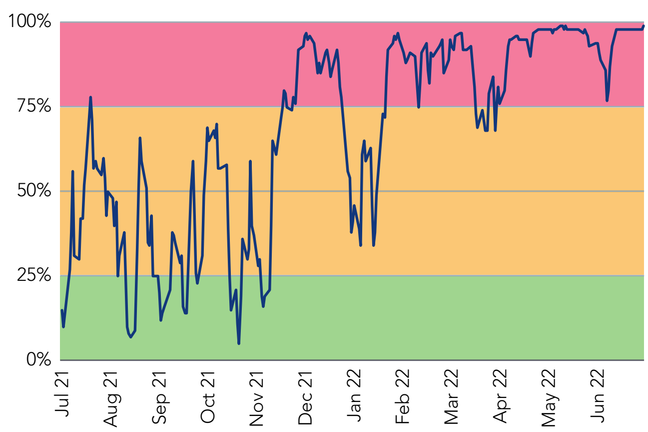
Hints of growing hawkishness from the US Federal Reserve set the mood for markets early in the year. At its December 2021 meeting, the Federal Open Market Committee voted to keep the Bank's benchmark rate anchored near zero. However, the minutes of the meeting (released on 5 January) revealed committee members' calls for more aggressive tightening as inflation continued to increase. This led many to believe rates would increase further and faster than previously anticipated and provoked the strongest swing to Value since the global financial crisis.

The preference for value continued largely unabated until towards the end of February, when Russia's invasion of Ukraine led to a brief switch towards more defensive areas of the market. The conflict amplified existing inflationary pressures, particularly energy costs, triggering fears of recession. This was reflected in growing volatility in bond markets, culminating in the inversion of yield curves towards the end of March.

The difficult market environment continued in the second quarter. As inflationary pressures continued to increase, the trajectory of interest rate rises steepened. In turn, expectations of higher prices and rising borrowing costs saw consumer confidence indices fall sharply.

Risk aversion remained stubbornly high through April and May as markets continued to decline (see Figure 1 below). Investor patience had all but evaporated and a short-term mindset emerged, with companies being heavily punished for missing quarterly earnings or guidance, even when they remained confident of meeting expectations over the next 12 months and beyond. As June ended, developed markets had seen one of their worst H1 periods for returns in the past 50 years.

Figure 1. Risk aversion remains stubbornly high



Source: Federated Hermes, as at 30 June 2022.

For most of the period, markets were driven by style and macro factors and a more short-term outlook, rather than long-term fundamentals. This proved difficult for our investment approach, which focuses on long-term fundamentals.

In terms of investment style, increasing inflationary pressures and more hawkish central bank policy triggered a pivot to a clear preference for value at the expense of growth. This was particularly evident during the inflection point in January; our proprietary Alpha Model showed valuation had one of its best-performing months since the model's inception in 2003, while growth underperformed by a magnitude rarely seen. A similar pattern was evident for much of the rest of the period, albeit not to the same degree, although quality factors such as capital structure started to perform well later in the period.

The preference for value was perhaps best reflected in the stellar performance of the energy sector, which benefited from the accelerating oil price after Russia's invasion of Ukraine. With value being driven by areas of the markets typically off limits to them, funds with a sustainable bias struggled (the fund is underweight in energy for this reason). While our diversified approach provided a degree of protection, the headwinds were too strong to completely overcome.

Even for many professional investors, this market environment will be a new experience. For a lot of retail investors, it defies everything the memes foretold. So where are we now and what does the future hold?

> **For long-term investors, the story is essentially unchanged, in fact, falling markets offer more attractive valuations on high-quality companies with a competitive edge.**

Controlling inflation was always likely to push the global economy towards a recession. By this definition the Fed seems to have succeeded, at least temporarily, with commodity prices tumbling from their highs as recessionary fears grow. As investors ponder the true cost of rate rises, equity markets remain highly sensitive to every new data release or talking point. Negative sentiment dominates the conversation as the excesses of the bull market are cleared out, yet the VIX[1] volatility index is only marginally elevated. So, for equities at least, this is an orderly bear market rather than outright panic.

For long-term investors, the story is essentially unchanged, in fact, falling markets offer more attractive valuations on high-quality companies with a competitive edge. The key will be understanding who has that competitive edge in this inflationary environment. Sustainability has perhaps become less of a focus for some, particularly those considering short-term energy needs in a world of soaring gas and oil prices. Yet the movement towards a more sustainable economy will continue. We therefore maintain our view that companies increasing their focus on sustainability have a structural growth advantage over peers and are destined to be tomorrow's leaders. Diversification will remain key to weather the current storm, but over the long term, that continues to represent an exceptional market opportunity.

The value of investments and income from them may go down as well as up, and you may not get back the original amount invested.

Please refer to the glossary for an explanation of key terms used.

[1] VIX is the ticker symbol for the Chicago Board Options Exchange's CBOE Volatility Index, which measures market expectations of volatility based on S&P 500 index options.

SECTION 2

Our investment philosophy

We believe in:

Pragmatism: a combination of time-tested fundamental and ESG characteristics that are attractively priced

Responsibility: integration of ESG factors and active ownership minimises the probability of negative surprises and can unlock hidden value

Sustainability: companies with a competitive advantage and sustainable business models are more likely to offer visibility of earnings growth

Long-term focus: investing over the long term allows companies to reach their true potential

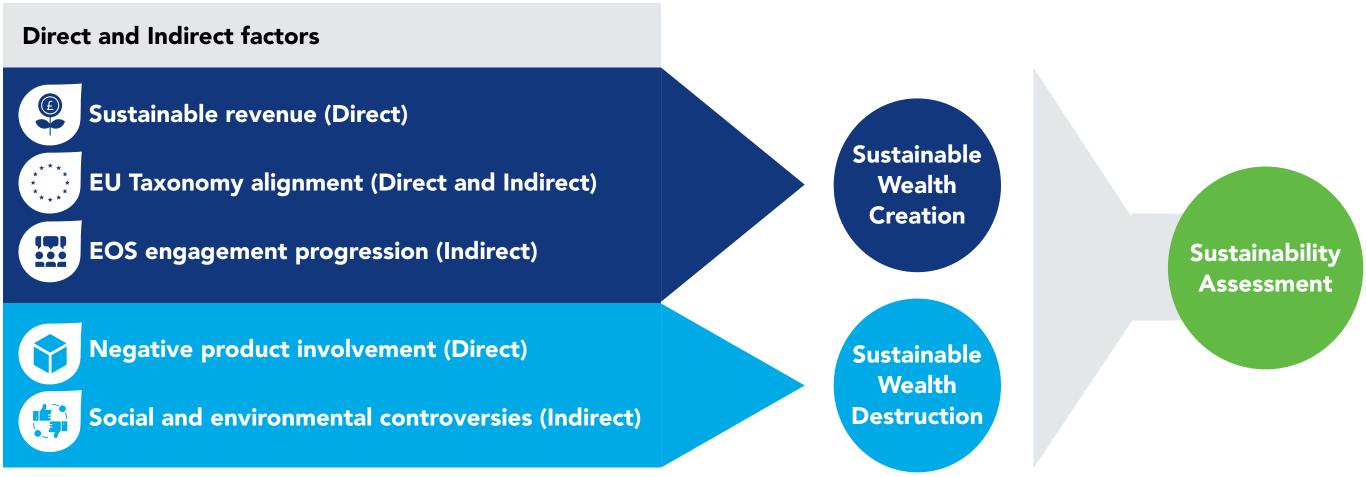
Validating the philosophy

We like stocks with robust financial statements, competitive strength and a proven ability to consistently beat revenue and earnings expectations. Ideally, these companies should also be guided by impressive management teams, mitigate ESG risks and appear cheap relative to peers. But very few stocks embody such an ideal investment, so we identify those with the most attractive combinations of characteristics in every market environment.

We identify companies using a systematic approach based on solid time-tested fundamentals. The process also applies a proprietary risk management framework. Further details on how we integrate ESG considerations in the process is included in our paper 'A truly integrated approach'. During H1 2021 as part of our research we identified an opportunity to measure how a company contributes to sustainability. We set out further details in our research paper 'Introducing our sustainability assessment framework'.

We are currently using the score to inform our analysis while we learn more about the companies that the score positively identifies and in time we will determine how we will use the score in our investment process based on these observed outcomes. One key aspect to the score, continues to support our existing philosophy, focussing on evaluating both the level and change of how a company is addressing sustainability.

Figure 1. The Federated Hermes Global Equities Sustainability Assessment



SECTION 3

Engagement overview

Alongside our colleagues at our stewardship business, EOS at Federated Hermes ('EOS'), we seek to drive change through board and executive-level interactions. Our engagements with portfolio companies often include meetings with divisional heads, investor relations teams, board members, chairs, lead independent directors and chairs of board committees.

Through our interactions, we gain information relating to specific engagement objectives and issues. Our proprietary milestone system allows us to track our engagement progress. Furthermore, we benefit from the wider research universe covered by EOS, a diverse team with backgrounds including law, banking, sciences, academia, accountancy, climate change and corporate strategy, and the collective ability to speak fluently in over 10 languages. In turn, the team's skills, languages, connections and cultural understanding enable local language dialogues which are of great importance.

1. Raise concerns
2. Concerns acknowledged
3. Company commits to change
4. Change Implemented

Milestone progress

Engagement progress, H1 2022

Total engagements **86**

Engagement objectives by theme

Environmental	Social and Ethical	Governance	Strategy, Risk and Communication
22.0%	26.0%	31.0%	21.0%

Source: Federated Hermes, as at 30 June 2022.

Voting, H1 2022

Voting is a key part of demonstrating active ownership and ensuring companies are meeting the needs of shareholders.

Voting breakdown

Meetings where we voted in favour:	Meetings where we voted against, against and abstained, or with management by exception:
25%	75%

Source: Federated Hermes, as at 30 June 2022.

SECTION 4

ESG outcomes

We recognise that every company has both positive and negative impacts when it comes to its operations. Here we present a snapshot of our fund's carbon metrics:

Carbon footprint (scope 1 and 2) per $m invested

Fund: **36.9**

Benchmark: **90.6**

59% lower than the benchmark index

Carbon intensity – tonnes per $m of sales (scope 1 and 2)

Fund: **89.8**

Benchmark: **220.6**

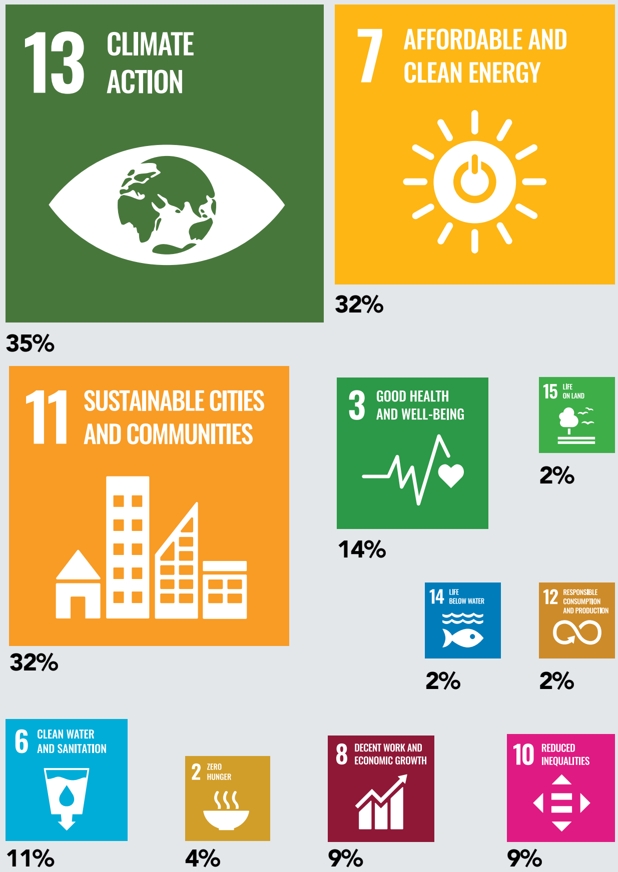
59% lower than the benchmark index

Environmental opportunities exposure **38%**

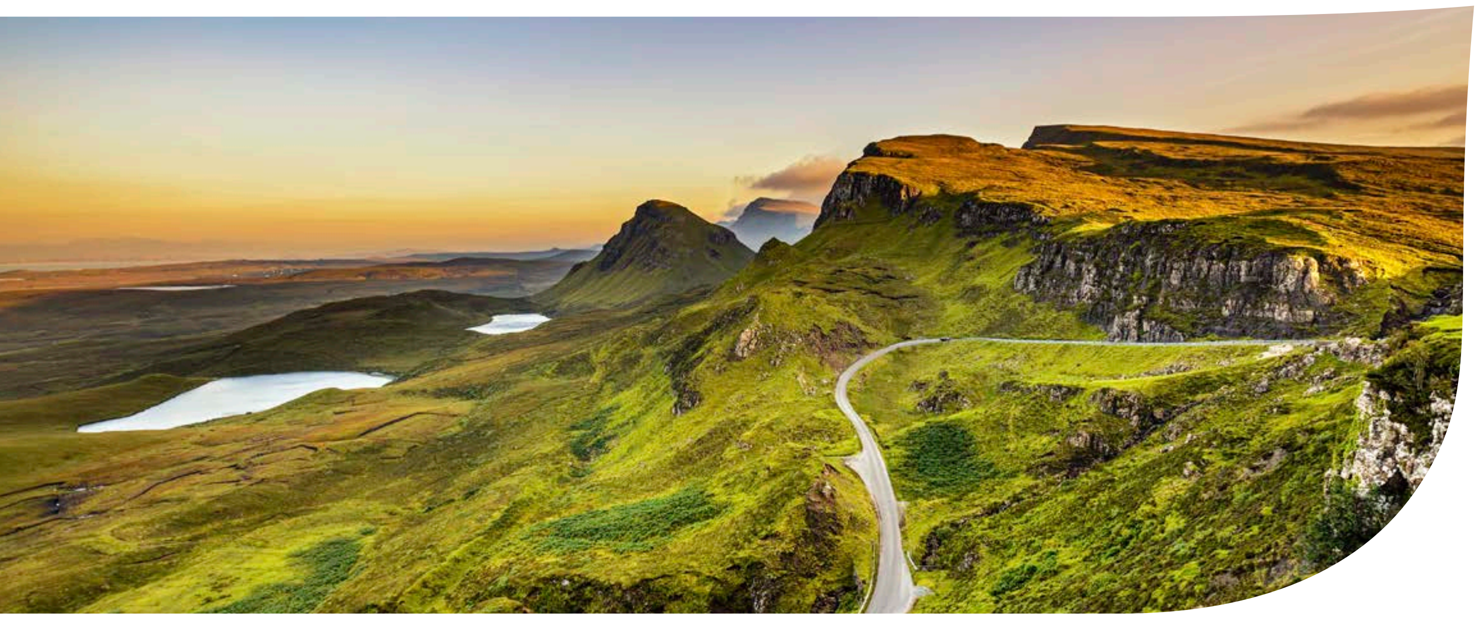
Source: Federated Hermes, as at 30 June 2022.

SDG exposure

Here we demonstrate our SDG exposure – that is, companies where there is revenue exposure to investable themes which are aligned to the UN Sustainable Development Goals (SDGs).



Source: Federated Hermes, as at 30 June 2022. Note that percentages shown add up to more than 100% as companies can be exposed to more than one SDG.



SECTION 5

In the spotlight: Modern slavery

In the Western world we tend to view slavery as a dark stain on our past, but something from which we are separated by centuries of history. Unfortunately, the reality is different. Recent revelations by Sir Mo Farah that he was trafficked for domestic servitude as a child represent just one high profile example of a crime that's widespread, if often hidden from view.

What is modern slavery?

The UK Modern Slavery Act (2015) defines modern slavery as the offences of 'slavery, servitude and forced or compulsory labour' and 'human trafficking'. Estimates from the International Labour Organization suggest that under this definition there are as many as 40 million slaves worldwide[2].

Aside from the use of physical force, modern slavery often involves coercion. This can range from threats to the person themselves or their family members to false imprisonment, the withholding of passports, or debt bondage through exorbitant 'recruitment fees' repaid at crippling interest rates. Victims are often subjected to inhuman treatment and forced to work under extremely poor pay and conditions. They are also often trafficked into such situations, isolating them from friends and family.

> **The UK Modern Slavery Act (2015) defines modern slavery as the offences of 'slavery, servitude and forced or compulsory labour' and 'human trafficking'.**

Who is involved?

Given the scale of the problem, most international companies are likely to have slaves working at some level in their complex supply chains. For enlightened businesses, this shifts the emphasis from 'if' they have issues to how hard they are looking for the problems and what they are doing to address them.

Estimates from the International Labour Organization suggest that under this definition there are as many as

40 million

slaves worldwide

The United Nations 'Protect, Respect and Remedy' Framework[3] sets out clear expectations regarding corporate responsibility around human rights. Firms must not only act with due diligence to avoid infringing the rights of others and address harms, but they must also ensure victims are able to seek redress. Unfortunately, currently firms do not have the granular data to fully understand, the resources to properly investigate, or the ability to effectively influence what is happening in their global supply chains. Properly addressing the underlying drivers of modern slavery will require a collaborative approach involving governments and NGOs as well as the companies themselves.

> **The United Nations 'Protect, Respect and Remedy' Framework sets out clear expectations regarding corporate responsibility around human rights.**

Aside from being an important moral issue, modern slavery creates supply chain management, regulatory and reputational risks. A number of high-profile cases involving major companies have gained widespread media attention. Among the most notable are alleged human rights abuses affecting hundreds of thousands of migrant workers preparing for the 2022 Qatar World Cup[4], and a total of 83 multinationals including Nike, Adidas, Apple, Microsoft and Samsung being linked to exploitation of the Uyghur ethnic minority in the Xinjiang region of China[5].

[2] *Global Estimates of Modern Slavery*. International Labour Organization and Walk Free Foundation. First published 2017, https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_575479.pdf

[3] For more information, see here: https://media.business-humanrights.org/media/documents/files/reports-and-materials/Ruggie-protect-respect-remedy-framework.pdf

[4] See for example: https://www.amnesty.org/en/latest/news/2022/05/qatar-fifa-should-match-440m-world-cup-prize-money-to-fund-compensation-programme-for-migrant-workers/

[5] See for example: https://www.forbes.com/sites/siminamistreanu/2020/03/02/study-links-nike-adidas-and-apple-to-forced-uighur-labor/

Modern slavery regulations around the world

UK: The Modern Slavery Act 2015 requires commercial organisations with an annual turnover of £36m or more, who carry on business in the UK and supply goods or services, to publish an annual modern slavery statement[6].

EU: Slavery and forced labour are prohibited under Article 4 of the European Convention on Human Rights, 1950[7]. In addition, Directive 2014/95/EU requires large companies with 500 or more employees to include information on respect for human rights in their management reports[8].

Australia: The Modern Slavery Act 2018 requires entities based, or operating, in Australia, with annual consolidated revenue of AUS$100m+, to report annually on the risks of modern slavery in their operations and supply chains, and actions to address those risks[9].

US: The Uyghur Forced Labour Prevention Act prohibiting imports made by forced labour in the Chinese province of Xinjiang came into effect on June 21, 2022[10]. At state level, *The California Transparency in Supply Chains Act* requires specific measures relating to slavery and human trafficking of retail sellers or manufacturers doing business in the state with annual revenue of $100m+[11].

Canada: Bill S-211, *An Act to enact the Fighting Against Forced Labour and Child Labour in Supply Chains Act and to amend the Customs Tariff*, passed its second reading in the Canadian House of Commons on June 1, 2022, and is now at the committee stage[12].

What metrics are available?

When considering an investment, we examine the policies and processes companies have in place, such as supply chain audits and codes of conduct. We also look for membership of or adherence to internationally recognised principles and agreements. These include:

United Nations Guiding Principles on Business and Human Rights (UNGP)[13] — Companies can put out a statement adhering to the principles.

United Nations Global Compact (UNGC)[14] — As a minimum we would expect companies to adhere to the UNGC framework. Businesses can also sign up to the Global Compact Initiative.

UN Principles for Responsible Investment (PRI)[15] — Publishes useful guidance on how investors can apply the UNGP to investing. It is also setting up a stewardship initiative called Advance promoting enhanced levels of engagement on human rights, which Federated Hermes is signing up to.

Data is also improving, with several smaller organisations seeking out and making available scores for specific companies:

Corporate Human Rights Benchmark (CHRB)[16] — Provides a comparative snapshot year-on-year of the largest global companies, looking at policies, processes and practices, as well as responses to allegations. Since 2020 it has been part of the World Benchmarking Alliance.

KnowTheChain[17] — Provides benchmarks and resources to understand forced labour risks within global supply chains, including sector overviews and individual company rankings.

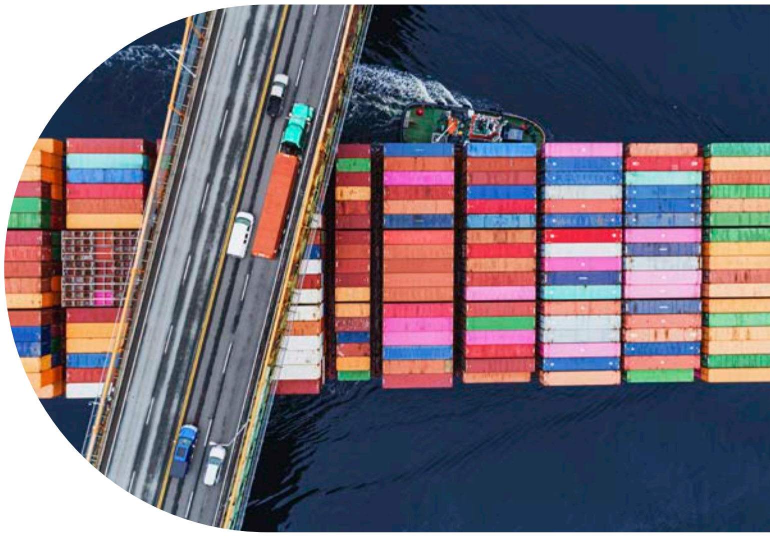
Our investment approach

For individual investments, we use a quantitative framework overlaid with qualitative insights to assess companies. We believe this is the best way to obtain unbiased insights while avoiding a tick-box approach, ensuring that nuances around issues which are rarely black and white are effectively captured. For example, effective qualitative analysis can avoid ruling out a company simply because it has not signed up to a specific initiative. Our analysis will seek to cover not just direct employees but the whole supply chain, including contractors and subcontractors. At a portfolio level, we monitor aggregate indicators relative to our benchmark and we plan to start reporting these in our December report.

[6] https://www.legislation.gov.uk/ukpga/2015/30/contents
[7] https://www.echr.coe.int/Documents/Convention_ENG.pdf
[8] https://eur-lex.europa.eu/eli/dir/2014/95/oj
[9] https://www.legislation.gov.au/Details/C2018A00153
[10] https://www.state.gov/implementation-of-the-uyghur-forced-labor-prevention-act/
[11] https://oag.ca.gov/SB657
[12] https://www.parl.ca/legisinfo/en/bill/44-1/s-211
[13] https://www.ohchr.org/sites/default/files/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf
[14] https://www.unglobalcompact.org
[15] https://www.unpri.org
[16] https://www.worldbenchmarkingalliance.org/corporate-human-rights-benchmark/
[17] https://knowthechain.org

Human rights are right up there with climate change as an issue of interest to clients of our EOS stewardship services.

Our sector-neutral approach means we aim to always be invested in best-in-class performers across the market spectrum. Ideally, we are looking for leaders, but we will also consider improvers and those with momentum on the issue, depending on the sector.



How do we engage on the issue?

Human rights are right up there with climate change as an issue of interest to clients of our EOS stewardship services. Our engagements are guided by questions stemming from the United Nations Guiding Principles on Business and Human Rights:

- **Policy and governance:** What policy commitments and governance structures are in place? Does the company have a clearly articulated position and demonstrate meaningful consideration of the issue? How well is it setting its own objectives to engage on the issue? How is it integrating the issue with competing pressures such as commercial concerns around cost, quality and timeliness?

Our engagements are guided by questions stemming from the United Nations Guiding Principles on Business and Human Rights

- **Due diligence:** How does a company investigate its supply chains and how does it acknowledge and articulate potential issues relating to involvement in particular regions or sectors? If higher risks are present, what is the firm doing to understand specific concerns?
- **Remedy:** Where issues have been identified, how are they being addressed? For example, providing support for victims; strengthening controls to prevent reoccurrence.

- **Reporting:** Does the company have a robust reporting framework underlying its approach? This should include internal data at the disposal of the executive team to aid application of policies, as well as adequate levels of external reporting.

When engaging with companies, we take sectoral nuances into account. For example, our expectations for the oil & gas and mining industries are high, since these sectors have been in contact with the issue for a long time. Companies should therefore be mature in their understanding and able to engage directly with people on the ground. For consumer goods brands, the issue tends to exist deeper in the supply chain and the dynamics are less mature, however, we would still expect a good understanding of potential risks and how to respond.

In conclusion, pressure on larger companies from regulators, investors and consumers means transparency is improving, but most still struggle to shine a light into the depths of their supply chain. Meanwhile, smaller companies are often less affected by legislation and investor and consumer pressure. With supply chains still fragile and input costs rising, there is a danger of companies turning a blind eye to issues just as the higher cost of living and geopolitical issues risk making poorer people in the developing world more susceptible to exploitation. Engaging on potential modern slavery and trafficking issues will therefore remain a key part of mitigating the risks companies, and investors, are exposed to.

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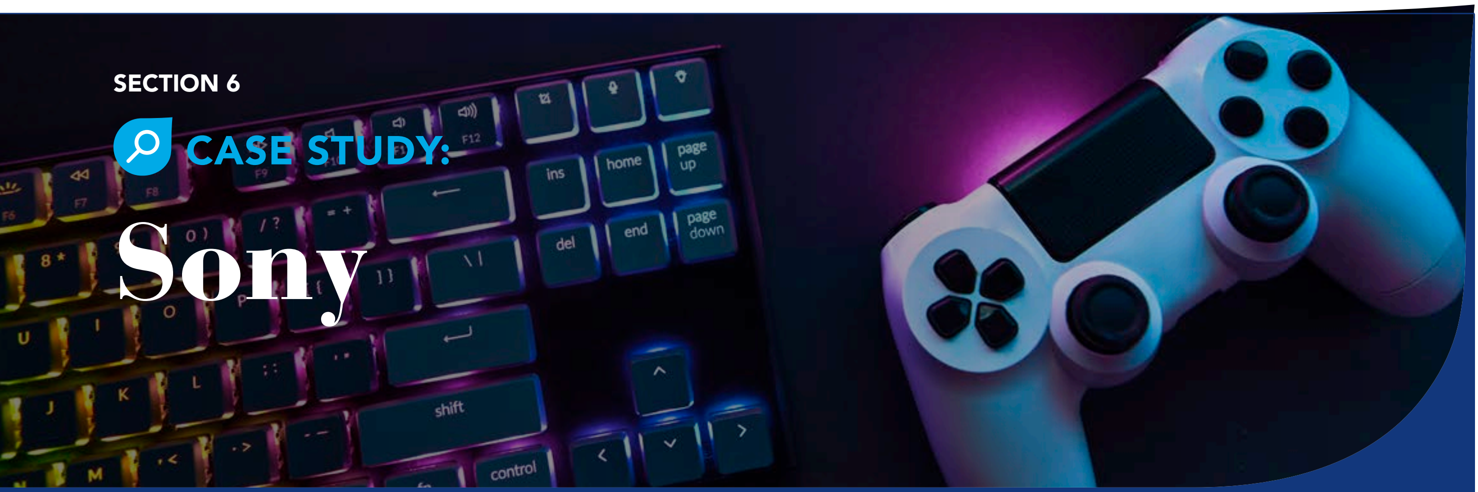
SECTION 6

CASE STUDY:

Sony



Sony Group Corporation is a Japanese multinational technology conglomerate founded in 1946 and listed on both the Tokyo and New York stock exchanges. Successful in segments including consumer electronics, gaming, music, visual entertainment and electronic components, it also offers banking, insurance and other financial services through its subsidiary, Sony Financial Group.

Historically best known for consumer electronics, today Sony describes itself as 'a creative entertainment company with a solid foundation in technology'. Popular with consumers and investors alike, it has a strong corporate purpose based around 'Kando' (emotional connection), and emphasises responsibility and contribution in its corporate messaging.

> **A strategic pivot towards the gaming segment is therefore likely to subdue profits in the near term, but heavy investment in intellectual property, including live games and PC/mobile gaming, should generate greater upside in the longer term.**

Investment perspective

Sony is a cash generative company with a strong balance sheet and attractive valuation. It is a leader in the Japanese tech space and has resilient earnings and strong momentum across gaming, music and image sensors, the latter giving it exposure to iPhone success. Although the company missed its latest earnings estimates in May, buybacks were strong.

Looking forward, Sony Music (a traditionally resilient segment during recessions) and Sony Semiconductor Solutions Group (including imaging and sensors) were expected to do better than Sony Pictures and Sony Interactive Entertainment. A strategic pivot towards the gaming segment is therefore likely to subdue profits in the near term, but heavy investment in intellectual property, including live games and PC/mobile gaming, should generate greater upside in the longer term. In the meantime, the company says supply chain issues affecting its PlayStation 5 console are finally easing (although it still expects to struggle to meet demand).

An alliance with Honda is expected to generate future growth, while completion of a merger with media conglomerate Zee Entertainment Enterprises in India should be accretive to profit by 2024. Inflation in Japan is rising but remains relatively low, however, near-term, macro recessionary risks weigh on the name (Sony is high beta).

ESG profile

Sony consistently ranks above peers across Environmental, Social and Governance metrics and maintains a triple-A rating from MSCI. Given the sectors the firm is involved in, concerns would typically focus around supply chain management and business ethics, however as of July 2022 there are no significant controversies to report.

The company is making good ongoing progress on social, ethical and governance issues. Local market practices mean Japanese companies are often downgraded on governance in global models. However, Sony manages to achieve a top overall ranking for Governance from US advisory firm ISS, scoring favourably on board structure, shareholder rights, and audit and risk oversight. Supply arrangements are long-term and secure, and the company has a Supply Chain Code as well as a Group Code of Conduct. It audits its suppliers of raw materials, components and final assembly where possible, and recently engaged Business for Social Responsibility, an independent non-profit organisation, to evaluate the risks of slavery and human trafficking in its supply chains.

Sony was the first Japanese company to have its carbon reduction aims approved as a Science-based Target (SBT) and has also had its new 2025 target approved as an SBT. The firm continues to lead on environmental issues, accelerating its 'Road to Zero' plan which aims to achieve a net-zero environmental footprint throughout the lifecycle of its products and business activities. Its latest targets bring forward the date for carbon neutrality throughout its value chain from 2050 to 2040, while its target for achieving 100% renewable energy in its own operations has moved from 2040 to 2030.

> **Sony was the first Japanese company to have its carbon reduction aims approved as a Science-based Target (SBT) and has also had its new 2025 target approved as an SBT.**

Engagement

Our history with Sony dates to 2007 and we have been actively engaging with the company since 2014. Historically the firm has been responsive to engagement on topics including diversity, human rights, human capital management, remuneration, and a review of its business portfolio. On the latter, Sony sees its conglomerate structure as offering diversification, which mitigates risk and helps provide some financial stability. However, we continue to seek an ongoing review and particularly question the firm's ownership of its financial services subsidiary.

Board level diversity and independence is higher than average for a Japanese company and Sony recently appointed the first black American to its executive team.

> **Board level diversity and independence is higher than average for a Japanese company and Sony recently appointed the first black American to its executive team.**

Despite this, the proportion of women in senior management and other levels of its workforce is low. The company flagged its US$100m social justice fund, which will be headed by a black woman with a background in the non-profit sector. However, we encouraged Sony to explore more ways to close its diversity gap, including setting targets, and to aim to lead on racial diversity — particularly as the issue of racial inequality is not widely understood in Japan.

The company's Australian music division has recently been involved in a controversy relating to allegations of historical workplace abuse by its former CEO. While this is concerning, we feel materiality is limited, since Sony Music Australia is a small part of the group's overall business and there is no evidence of similar issues elsewhere. We have, however, reflected the issue in the company's Social score, which has led to a modest fall in our proprietary QESG Score[18] for the firm; this is consistent with both MSCI and Sustainalytics, who also rate the issue as a moderate controversy.

The company flagged its
US$100m
social justice fund, which will be headed by a black woman with a background in the non-profit sector.

This document does not constitute a solicitation or offer to any person to buy or sell any related securities or financial instruments.

The above does not represent all of the securities held in the portfolio and it should not be assumed that the above securities were or will be profitable.

[18] Note: QESG scores, generated by our Global Equities team at the international business of Federated Hermes, rank each stock worldwide in accordance with its ESG risk.

SECTION 7

ENGAGEMENT CASE STUDY:

Disney

The Walt Disney Company is a multinational entertainment conglomerate which operates media networks, film studios and parks experiences, and sells consumer products, across the globe. As well as Disney itself, the company's brands include ABC, ESPN, Pixar, Marvel, Lucasfilm, FX, National Geographic and 21st Century Fox.

Founded in 1923 as a film studio, Disney has grown to become one of the largest media companies in the world. Its list of globally recognised brands was further bolstered in 2019 with the acquisition of 21st Century Fox, in one of the largest and most complicated media-sector deals in history.

Investment perspective

Disney is a high-quality and well-diversified business. The company draws around 75% of its revenue from its media networks and studios, with the remaining 25% coming from parks, experiences and consumer products. Stable 45% gross margins mean profitability is strong, while capital structure is also robust, and the company boasts an excellent corporate behaviour score.

The company draws around **75%** of its revenue from its media networks and studios, with the remaining **25%** coming from parks, experiences and consumer products.

Disney's strategy shift to streaming will be crucial, with the company aiming for 230-260 million paid subscribers by FY2024, at which point Disney+ is expected to break even.

The company's growth is diminishing somewhat from relatively high levels, but should still be around 12% on an annualised basis over the next five years. Growth factors include high-quality assets in its studio business, investment in its parks businesses (including themed Star Wars, Toy Story and Avatar areas), and above-consensus subscriber growth for its relatively new Disney+ streaming service. The strategy shift to streaming will be crucial, with the company aiming for 230-260 million paid subscribers by FY2024, at which point Disney+ is expected to break even.

On the downside, content is severely undervalued by the market and current investor sentiment is weak. Covid has presented challenges to growth and legacy TV assets remain a drag, while the company's dividend was cut during the pandemic and has not yet resumed. Operating in the entertainment industry, Disney is potentially vulnerable to talent management challenges. However, it leads peers on programmes to identify new talent and has formal grievance channels to help resolve staff issues.

ESG profile

Disney is a clear outperformer on our proprietary Environmental, Social and Governance metrics which includes assessing both the level of progress on ESG factors and the pace of change. It can be considered best-in-class on the 'E' pillar, with excellent disclosures resulting in strong scores from external ratings agencies MSCI and Sustainalytics, although Trucost highlights the need to improve on environmental impact. Disney is making progress on this issue; as well as using low-carbon fuels and renewable energy, the company has invested in forest restoration and conservation projects. As a result, it looks on track to hit its target of reducing greenhouse gas emissions by 50% from 2012 levels by the end of this year. A series of initiatives have diverted 57% of its waste away from landfill or incineration. It has also reduced single-use plastics and introduced reclaimed water facilities, which have kept overall consumption at 2013 levels despite the growth in the business.

In terms of Social metrics, Disney runs multiple training and development programmes, including the Disney Institute, to attract, motivate and retain talent. It has also issued a code of conduct for manufacturers in its supply chain consistent with International Labour Organization guidelines. Finally, Governance metrics look particularly strong, reflecting a diverse and independent board as well as say on pay and business ethics policies.

We note that the company is currently involved in a class action relating to allegations of underpayment of wages. The case was dismissed with the judge ruling in favour of Disney, but employees are seeking an appeal. We will continue to monitor this issue.

In terms of Social metrics, Disney runs multiple training and development programmes, including the Disney Institute, to attract, motivate and retain talent.

Engagement

In the past we have raised concerns with Disney around issues including human capital, board structure, executive compensation, corporate culture and conduct, and diversity, equity and inclusion (DEI). Human capital concerns were initially addressed with the launch of a whistleblowing hotline, and there are now plans for the board to have oversight of all concerns raised. Meanwhile, following the creation of two senior leadership councils focused on workforce and content, DEI has improved remarkably in recent years. The company now discloses workforce diversity data, which shows an ethnically diverse, majority female workforce, including at board level. It is also working to improve representation in front of the camera, with a commitment to having 50% of regular and recurring characters in scripted content come from underrepresented groups.

Issues where the company can still improve include privacy (particularly around AI and cyber security, which is especially important considering its focus on children), executive compensation and climate risk.

A plan has been established to improve corporate culture and conduct, and some action has been taken on compensation, although the high quantum, low CEO share ownership requirement, and use of short-term options continues to be of concern. Meanwhile, after a lengthy period of engagement, the company finally appointed an independent chair in December 2021.

Engagement has been constructive and while there are some ongoing issues, we do not see these as particularly material. We have therefore reduced the engagement intensity, making dialogue less frequent but still regular.

Issues where the company can still improve include privacy (particularly around AI and cyber security, which is especially important considering its focus on children), executive compensation and climate risk. We have offered to advise the company and will share reporting examples based on the Task Force on Climate-Related Financial Disclosures (TCFD), for example. We have also raised our concerns over remuneration and are encouraging the company to place less emphasis on short-term targets.

In the past we have raised concerns with Disney around issues including human capital, board structure, executive compensation, corporate culture and conduct, and diversity, equity and inclusion (DEI).

Glossary

Active management: refers to a portfolio management strategy where the manager makes specific investments with the goal of outperforming an investment benchmark index or target return.

Active ownership: Means to actively exercising your rights as a shareholder. The two main ways to do this are voting at shareholder meetings and engaging – having an active dialogue – with investee companies.

Alpha model: Our proprietary model assesses a company's long-term prospects, by identifying those with the most attractive combination of fundamental characteristics or "factors". It is then used to create a portfolio that aims to generate consistent, positive relative returns regardless of market direction or the wider geopolitical environment.

Capital structure: the mix of various forms of external funds, known as capital, used to finance a business. It consists of shareholders' equity, debt (borrowed funds), and preferred stock, and is detailed in the company's balance sheet.

Carbon emissions: Scope 1 – All direct emissions from the activities of an organisation or under their control. Scope 2 – Indirect emissions from electricity purchased and used by the organisation. Scope 3 – All other indirect emissions from activities of the organisation, occurring from sources that they do not own or control.

CDP: an international non-profit organisation based in the United Kingdom, Japan, India, China, Germany and the US that helps companies and cities disclose their environmental impact.

Cyclical: Companies that follow the trends in the overall economy, which can make their stock prices volatile. When the economy grows, prices for cyclical stocks go up. When the economy turns down, their stock prices will drop.

Defensive stocks: a stock that provides consistent dividends and stable earnings regardless of the state of the overall stock market. With constant demand for their products, defensive stocks tend to be more stable during the various phases of the business cycle.

ESG: Environmental, social, and governance (ESG) criteria are a set of standards for a company's operations that socially conscious investors use to screen potential investments.

ESG Dashboard/ESG Portfolio Monitor/QESG Score: Proprietary tools used by our Global Equities team to capture a company's ESG profile

EU taxonomy: A classification system, providing companies, investors and policymakers with appropriate definitions for which economic activities can be considered environmentally sustainable.

Factors: Fundamental characteristics which we analyse to assess the attractiveness of each company within our investible universe.

Generally Accepted Accounting Principles (GAAP): a set of accounting principles that US companies must follow when putting together financial statements.

Growth: An investment style focusing on shares in companies whose earnings are expected to rise at an above average rate, for which investors are usually prepared to pay a premium.

Human capital: The skills, knowledge, and experience possessed by an individual or population, viewed in terms of their value or cost to an organization or country.

Investment style: The method and philosophy followed by an investor or fund manager in selecting investments for a portfolio.

Macroeconomic: a branch of the economics field that studies how the aggregate economy behaves.

Monetary policy: action that a country's central bank or government can take to influence how much money is in the economy and how much it costs to borrow.

Multiples: Investors use multiples to quantify a company's growth, productivity, and efficiency. For example, a multiple can be used to show how much investors are willing to pay per dollar of earnings, as computed by the price-to-earnings (P/E) ratio.

Net Leverage: A measure of a business' net debt relative to EBITDA (earnings before interest, taxes, depreciation and amortisation). It reflects how long it would take a business to pay back its debt if debt and EBITDA were constant.

Net zero carbon emissions: This means any emissions would be balanced by schemes to offset an equivalent amount of greenhouse gases from the atmosphere, such as planting trees or using technology like carbon capture and storage.

Operating Income: Operating income is a measurement that shows how much of a company's revenue will eventually become profits. Operating income is similar to a company's earnings before interest and taxes (EBIT).

Profitability: a business's ability to produce a return on an investment based on its resources in comparison with an alternative investment.

Quality: defined by low debt, stable earnings, consistent asset growth, and strong corporate governance. Investors can identify quality stocks by using common financial metrics like a return to equity, debt to equity and earnings variability.

Rising yields: Yield refers to the earnings generated and realised on an investment over a period of time. Higher yields are perceived to be an indicator of lower risk and higher income.

Risk on and risk off: An investment setting in which price behaviour responds to and is driven by changes in investor risk tolerance. Risk on risk off refers to changes in investment activity in response to global economic patterns.

Science-based targets: Science-based targets provide companies with a clearly-defined path to reduce emissions in line with the Paris Agreement goals.

Sentiment: The general prevailing attitude of investors as to anticipated price development in a market. This attitude is the accumulation of a variety of fundamental and technical factors.

Solvency II: a Directive in European Union law that codifies and harmonises the EU insurance regulation. Primarily this concerns the amount of capital that EU insurance companies must hold to reduce the risk of insolvency.

Stewardship: The role in which investment managers use the rights – if not the obligation – of financial stakeholders to engage with companies or assets to pursue the objective of sustainable wealth creation for investors.

Supply chain: A network between a company and its suppliers to produce and distribute a specific product to the consumer.

Sustainable Finance Disclosure Regulation (SFDR): Imposes new EU transparency and sustainability-related disclosure requirements on financial market participants – the aim is to direct capital away from harmful activities and towards activities that are more sustainable.

Task Force on Climate Related Financial Disclosures (TCFD): an organization that was established in December 2015 with the goal of developing a set of voluntary climate-related financial risk disclosures. These disclosures would ideally be adopted by companies to help inform investors and members of the public about the risks they face related to climate change.

Value: An investment style that focuses on shares where the investment manager considers the market price to be less than its real value.

Voting: Exercising the rights given to equity holders in companies to vote on business matters and director elections during annual and extraordinary general meetings.

Federated Hermes
Limited

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 Investment Management are now undertaken by Federated Hermes Limited (or one of its subsidiaries). We still offer the same distinct investment propositions and pioneering responsible investment and stewardship services for which we are renowned – in addition to important 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

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