Federated Hermes SDG Engagement High Yield Credit

H1 2022 Report

September 2022

Federated Hermes Limited

www.hermes-investment.com

For professional investors only

SDG Engagement High Yield Credit: H1 2022 highlights

111 companies engaged

87% of the annual target

297 engagement actions

Governance	173[1]
Environmental	117
Social & ethical	83
Strategy, risk, communications	90

Most intensively engaged Sustainable Development Goals (SDGs):

- 13 Climate Action: **102** objectives
- 12 Responsible Consumption and Production: **86** objectives
- 7 Affordable and Clean Energy: **56** objectives
- 9 Industry, Innovation and Infrastructure: **47** objectives
- 8 Decent Work and Economic Growth: **38** objectives
- 10 Reduced Inequalities: **37** objectives

27 EOS engagers delivered **141** engagement actions

3 Sustainable Fixed Income engagers delivered **156** engagement actions

We are pursuing **268** objectives for change vs **199** in H1 2021

28% of objectives progressed in H1

14 objectives completed

Source: Federated Hermes, as at 30 June 2022.

[1] Bold numbers denote number of engagements. Each engagement usually touches on multiple issues and sub-themes, so the sum of sub-theme engagement is higher than total unique engagements carried out. Sub-themes with less than two engagements are not pictured. For instance, we drove two water, one forestry and land use, one cyber security, and two bribery and corruption-related engagements which are not shown on this table.

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SECTION 1

Investment review

Mitch Reznick, CFA[2]
Head of Sustainable Fixed Income

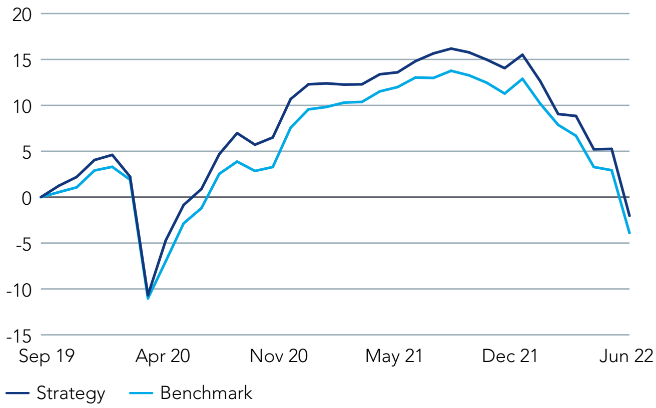
Nachu Chockalingam, CFA[2]
Senior Credit Portfolio Manager

Fraser Lundie, CFA[2]
Head of Fixed Income – Public Markets Credit

Since inception, the SDG Engagement High Yield Credit strategy has returned -0.74% in USD terms, gross of fees, which was 69bps ahead of its benchmark index for the period[3]. In H1 2022, our strategy returned -15.19% in US$ terms, gross of fees, which was 31bps behind its benchmark index for the period[4]. The strategy's underperformance in the half year period can be largely attributed to its overweight in Europe and its overweight to BB and higher rated issues.

European high yield underperformed US high yield in this period because of its closer proximity to events in Ukraine i.e. its need for gas from Russia and its lack of energy issues (the US high yield energy sector was one of the best performing in this period). The upper end of the rating spectrum in high yield was also subject to far more interest rate volatility in this period than the low quality end which was cushioned by its higher coupons.

Figure 1. SDG Engagement High Yield Credit Strategy: performance since inception



Source: Federated Hermes as at 30 June 2022. Performance shown is the Federated Hermes Int'l SDG Engagement High Yield Credit Hedged to USD Strategy. In USD, gross of fees. Inception date: 30 September 2019. Benchmark: ICE BofAML Global High Yield Constrained Index hedged to USD. Data is supplemental to the GIPS report that can be found in the appendix. **Past performance is not a reliable indicator of future returns.**

Over the course of H1 2022, the strategy's benchmark spreads were on a widening path from a low of 370bps in January to a peak of 640bps by the end of June. The first half of 2022 was a difficult period for most financial markets, largely driven by growing inflationary pressures and the impact of the conflict between Russia and Ukraine. The macro environment was dominated by increasingly hawkish central banks in the UK and around the world, in response to continued and persistent inflation. The Russian invasion of Ukraine in February also amplified the risk-off tone as heavy sanctions were imposed on Russian companies and individuals, and investors grew concerned about further escalations of the war. Inflationary pressures were exacerbated by the spike in many commodity prices post the invasion, particularly oil and gas, and China's continued push for a zero-Covid strategy which led to major city-wide lockdowns put further stress on supply chains. Most recently, investors' concerns have shifted to how and if central banks can manage a 'soft landing' i.e. taming inflation without driving economies into recession.

Figure 2. Spreads on a widening path

Source: Bloomberg as at 30 June 2022.

[2] CFA® is a trademark owned by the CFA Institute.

[3] **Past performance is not a reliable indicator of future results.** Source: Federated Hermes as at 30 June 2022. Performance shown is the Federated Hermes Int'l SDG Engagement High Yield Credit Hedged to USD Strategy. It is annualised, in USD and gross of fees. Inception date: 30 September 2019. Benchmark: ICE BofAML Global High Yield Constrained Index hedged to USD. Data is supplemental to the GIPS report that can be found in the appendix.

[4] Source: Federated Hermes as at 30 June 2022. Performance shown is the Federated Hermes Int'l SDG Engagement High Yield Credit Hedged to USD Strategy. In USD, gross of fees. **Past performance is not a reliable indicator of future results.** Data is supplemental to the GIPS report that can be found in the appendix.

Our credit analysts and our engagement specialists had a very fruitful H1, with many of our engagement successes providing crucial portfolio-positioning insight.

Turning to our ambitions regarding the impact potential of the strategy, both our credit analysts and our engagement specialists had a very fruitful H1, with many of our engagement successes providing crucial portfolio-positioning insight.

We strongly believe that a wide range of companies in our strategy have the potential to benefit society and the environment – their key challenge is in the progressive development of clean, future-resilient and more equitable next-generation industries and value chains. In short, it is the job of many of these companies to provide the building blocks for economies and essentials for everyday life and employment. Their value chains must be transformed if we are to meet the aims of a cross-section of environmentally and socially-focused SDGs.

We strongly believe that a wide range of companies in our strategy have the potential to benefit society and the environment – their key challenge is in the progressive development of clean, future-resilient and more equitable next generation industries and value chains.

We had significant engagement success in H1 2022, with many of the strategy's holdings making meaningful operational and management changes to increase their alignment with key SDG issues such as climate change and social inclusion. However, there were also companies in the portfolio that failed to demonstrate the engagement progress we would have liked to have seen from them.

- **Caixa Geral de Depositos** exited the strategy because we did not see sufficient progress in our engagement with them over a number of quarters. The bank has a range of products and services where SDG-related impacts are a focus, but we were disappointed that there were no quantified outcomes and little clarity on what proportion of revenues these offerings presented. We also observed through our engagement that the bank was moving far more slowly on its overall sustainability agenda relative to its peers, and that this was more in-line with the policy planning of its state owner.
- **Petrobras** was downgraded and exited the strategy as we concluded through our engagement that, with their current climate plan, Petrobras will fall further behind its peers on a full production basis and much of its absolute reductions will result from simply selling high-carbon refining operations. When compared, for example, with British Petroleum (BP), an oil major with similar energy comparability, we estimate that its Scope 1 and 2 emissions intensity is c. 45-50% higher per unit of production and its overall flaring is c. 50% higher, despite it producing c. 30% less energy than BP.

The DNA of the fund: Colinear objectives

The SDG Engagement High Yield Credit (SDGHY) Strategy seeks to deliver on colinear objectives: strong financial performance for investors, and future, positive, social and environmental impact that contributes to achieving the United Nations' Sustainable Development Goals (SDGs)[5].

We believe an investor's financial stake-holding allows, if not obliges, them to engage in constructive dialogue with companies. We recognise that turning engagement[6] into meaningful change takes time, so we require portfolio companies to be survivors in a levered universe[7]. Within the global hard currency[8] and high-yield market, we favour companies with:

- A recurring presence in capital markets
- A stable investor base
- An ethos of transparency in disclosures and reporting
- The necessary credit strength to participate in long-term dialogue and to evolve their businesses to the benefit of a range of stakeholders.

Measuring our progress and impact using milestones and objectives

Figure 3. Engagement milestone system

Source: Federated Hermes.

Establishing a causal link between engagement efforts and real world outcomes is often difficult. There are occasions when a company directly credits our intervention for actions it has taken, but we often need to rely on other measures of success.

We use a four-stage milestone system to track the progress of our engagements relative to the objectives set for each company. When we set an objective, we also identify the milestones that need to be achieved. Progress is regularly assessed and evaluated against the original engagement objective.

[5] The SDGs are a set of 17 interconnected goals that were adopted by all UN member states in 2015. They are a universal call to action to end poverty, protect the planet and improve the lives and prospects of everyone, everywhere, by 2030.

[6] Engagement: Engaging with companies on business strategy and performance, including ESG concerns and using shareholder power to positively influence corporate behaviour.

[7] Leverage refers to an environment where companies have high levels of debt.

[8] Hard currency refers to money that is issued by a nation that is seen as politically and economically stable.

SECTION 2

Engagement review

Aaron Hay
Director, Engagement & Strategy, Sustainable Fixed Income (SFI)

Jake Goodman, CFA[9]
Engagement Manager, SFI

Bertie Nicholson
Engagement & ESG Associate, SFI

Sophie Demaré
Engagement & ESG Associate, SFI

In the first half of 2022, we continued to deepen and extend a wider range of engagements across the strategy. In the six months to 30 June 2022, we carried out 297 total engagements with 111 of 128 companies in our strategy.

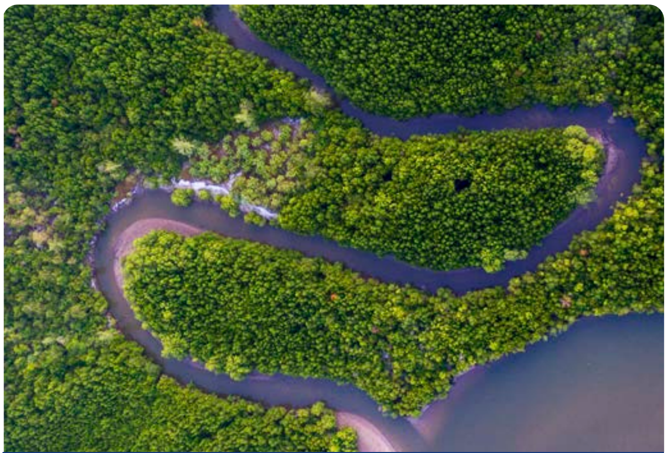
This represents continuing ample growth in the engagement we are driving, compared to our half-year mark in 2020 (205 engagements) and 2021 (263 actions).

Our mandate of 100% engagement of issuers annually is almost complete, having reached 87% as at 30 June 2022. Our success, almost three years on, is a result of deepened relationships, engagement learning and capabilities for driving more effective and timely dialogue with companies. We achieved engagement with 78% of the portfolio and 82 companies in H1 2020; this grew to 83% in H1 2021, making our 87% result in H1 2022 the most complete midyear accomplishment since our 2019 inception. Our success at delivering this mandate has continued to increase, despite our portfolio also growing from 82 to 128 investments since H1 of 2020.

We engaged with 111 companies in H1 2022 – representing 87% of our 100% annual engagement mandate

Our lead engagers dedicated to this strategy, Aaron Hay, Jake Goodman and Bertie Nicholson, collectively drove 156 engagements in H1 2022. As in previous years, our success in influencing and advising through engagement dialogue is multiplied by continued stewardship from senior engagement colleagues in EOS. Collectively, a further 141 engagements were driven by 27 EOS lead engagers, in addition to our dedicated SDGHY strategy team.

Our three dedicated lead engagers delivered 156 engagements, with 141 additional engagements driven by 27 lead engagers in EOS.



In our H1 2020 report, we described the relationship and trust-building work required to drive effective engagement.

In those stages, we sought to establish credibility and engage on ESG and SDG impact issues that really matter to companies, in addition to our SDG impact hypotheses. Since then, our robust engagement access, as exhibited by H1 2022 progress, proves that engagement works best when we are empowered to foster genuine, frank two-way dialogue with companies over years, not in single instances.

A stable and programmatic approach to engager-company relationships and dialogue contributes to the ease and proactivity of access we now enjoy with management teams and boards, almost three years into SDGHY engagement. As the rest of this section outlines, we believe that strong rapport and our informed, bespoke approach to risks and opportunities unique to each company leads to influence, which we think contributes to the outcomes companies later realise.

[9] CFA® is a trademark owned by the CFA Institute.

Figure 4. EOS senior professionals continued to make strong contributions to the influence we seek

Bruce Duguid,
Director, head of stewardship, EOS

14 engagements

Michael Yamoah,
Sectors: Technology hardware, software, mining and materials, energy and financial services

17 engagements

Owen Tutt,
Sectors: Oil and gas, chemicals, utilities

14 engagements

Joanne Beatty,
Sectors: Lead – chemicals, financial services, industrial and capital goods, transportation

12 engagements

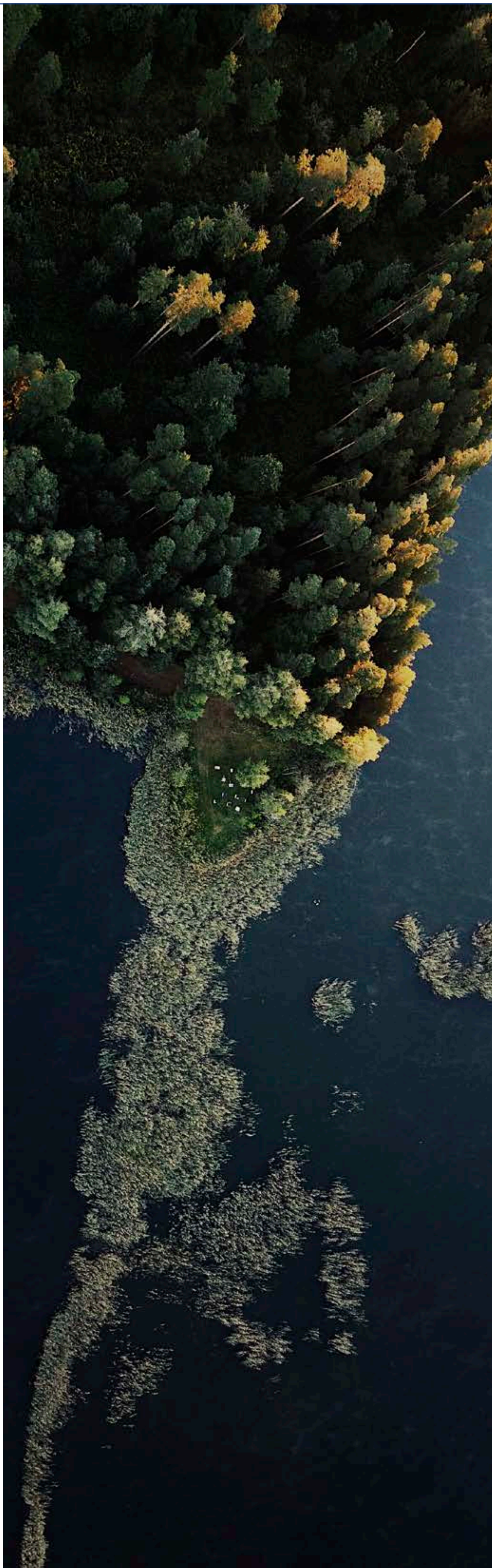
Jaime Gornsztejn,
Sectors: Lead – industrials and capital goods, financial services, mining and materials, oil and gas

10 engagements

Emily DeMasi,
Sectors: Co-lead, financial services, consumer goods and retail, pharmaceuticals and healthcare

9 engagements

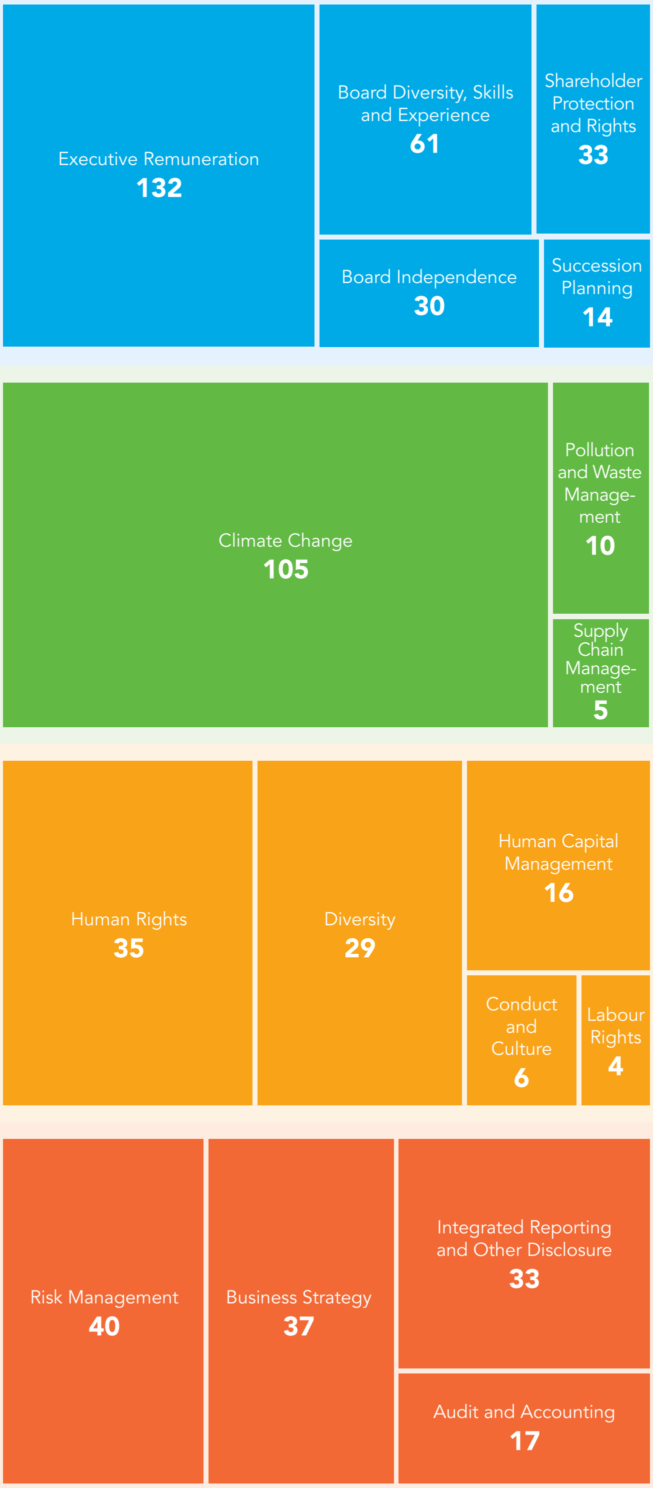
Source: Federated Hermes, as at 30 June 2022.



H1 2022: ESG Engagement Highlights

The foundation of our approach is based on the EOS model of engagement across material ESG issues, and we continue to find strength in the EOS 2021-23 plan and subthemes (see Appendix). Even as SDGs inform engagement focal points for companies, our wider, holistic approach also drives dialogue on ESG risks and opportunities unique to each issuer, and remains a bedrock for our strategy. We outline our overall H1 2022 engagement focus areas and state of our objectives for change below:

Figure 5. Engagements by theme and subtheme, H1 2022[10]



- **Governance** subthemes were most intensively engaged on in H1, our customary season for proxy, voting and AGM-related engagement.
- This is again guided by our approach, and planning for influencing on strengthened governance practices across the strategy, to the benefit of credit and equity investors alike. This featured in **173 engagements in H1**.
- **Executive remuneration** for transparent, accountable pay and **board diversity and skills** needed to supervise complex, evolving risks and opportunities were among our most-engaged subthemes during H1.

- **Environmental** themes formed part of **117 engagements** over the first six months of 2022.
- It is no surprise that H1 2022 continued to feature intensive **climate change** engagement, and has informed **105 engagements**.
- This is down to the all-encompassing nature of climate-related challenges and greenhouse gas emissions for companies that employ carbon-intensive assets, processes, or value chains.

- **Social and ethical**-related dialogue in H1 2022 formed part of **83 engagements**.
- **Human rights,** particularly within expansive company supply chains that reach into emerging economies, remain a focal point, in terms of transparency and in influencing human rights due diligence and management for the benefit of workers across value chains.
- Similarly, gender and ethnic **diversity** in management teams and workforces remains important in engagement where we believe corporate action can address specific inequalities.

- Given the potential for real-world environmental or social impact through a company's core strategy, we had immersive dialogue on **strategy, risk and communication** in **90 engagements**.
- Besides core strategy, our engagements on **integrated reporting** are important for surfacing the kinds of transparency we seek on material ESG and impact data, and this featured in **33 engagements** alongside widely-engaged topics in **business strategy** and **risk management.**

[10] Source: Federated Hermes as on 30 June 2022. Bold numbers denote number of engagements. Each engagement usually touches on multiple issues and sub-themes, so the sum of sub-theme engagement is higher than total unique engagements carried out. Sub-themes with less than two engagements are not pictured. For instance, we drove two water, one forestry and land use, one cyber security, and two bribery and corruption-related engagements which are not shown on this table.

H1 2022: Progression highlights in our objectives for change

The rest of this section focuses on thematic SDG engagement and progression of SDG-linked objectives. Before that, it is worthwhile to highlight the growth in objectives we pursue across our strategy. Compared to H1 2021, we have grown from **199 to 268 active objectives across holdings**. On average, this represents a little over two objectives per company across our portfolio of 128 holdings; this is the kind of increase we expect as lead engagers aim to introduce new topics or move into new areas of engagement in ongoing, shifting dialogue at companies.

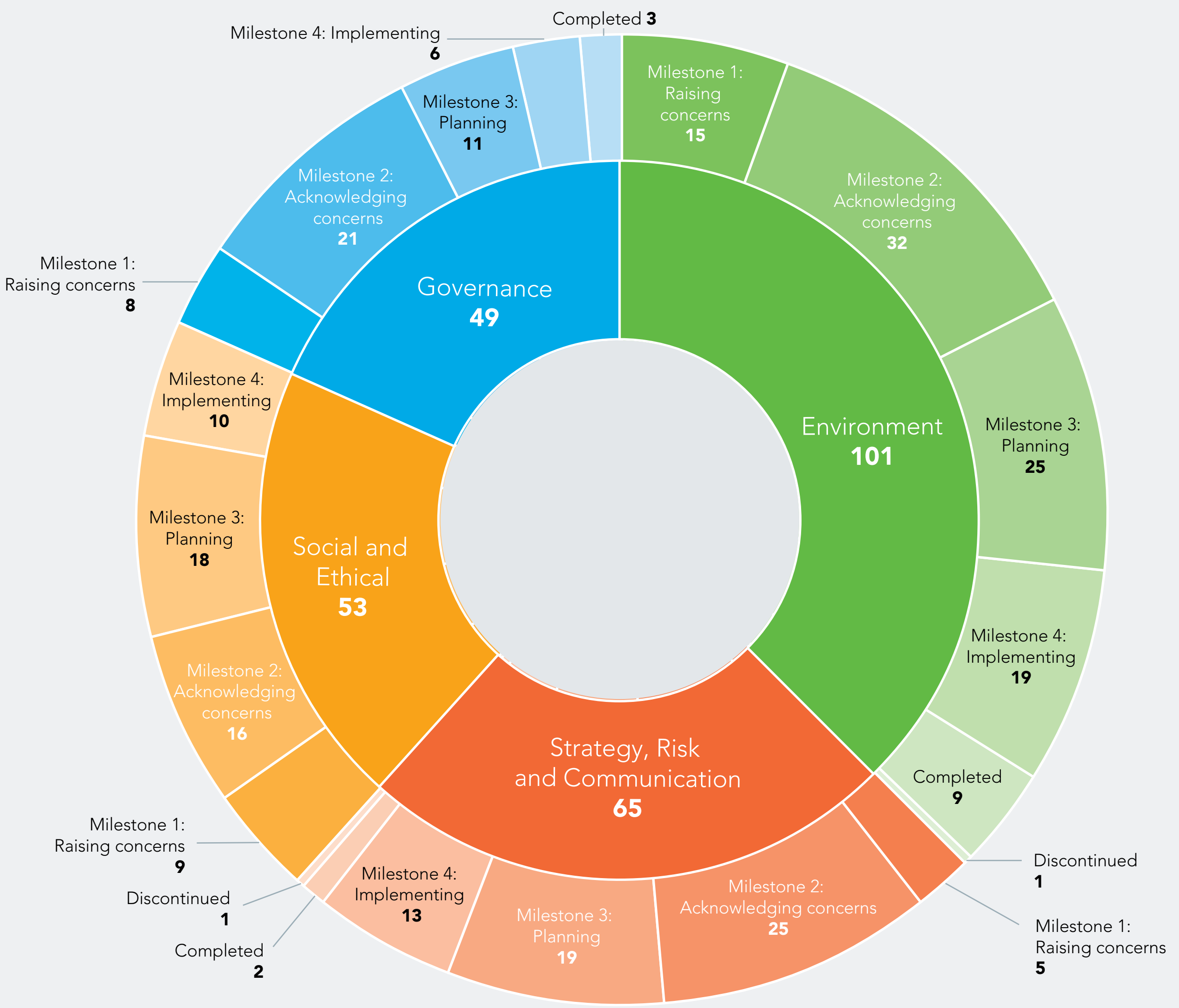
> **At the end of H1 2022, we were pursuing 268 objectives for change, across 128 companies**

> **We completed 14 objectives in H1 2022, growing from three in H1 2021**

Our mix of progression reflects considerable momentum in objectives since H1 2021, with many more milestones having now reached Milestone 3 (plan established) or Milestone 4 (plan being implemented). As we successfully progressed 28% of objectives during H1 2022, we are well on our way to meeting our expectation of at least 40% of objective progression annually.

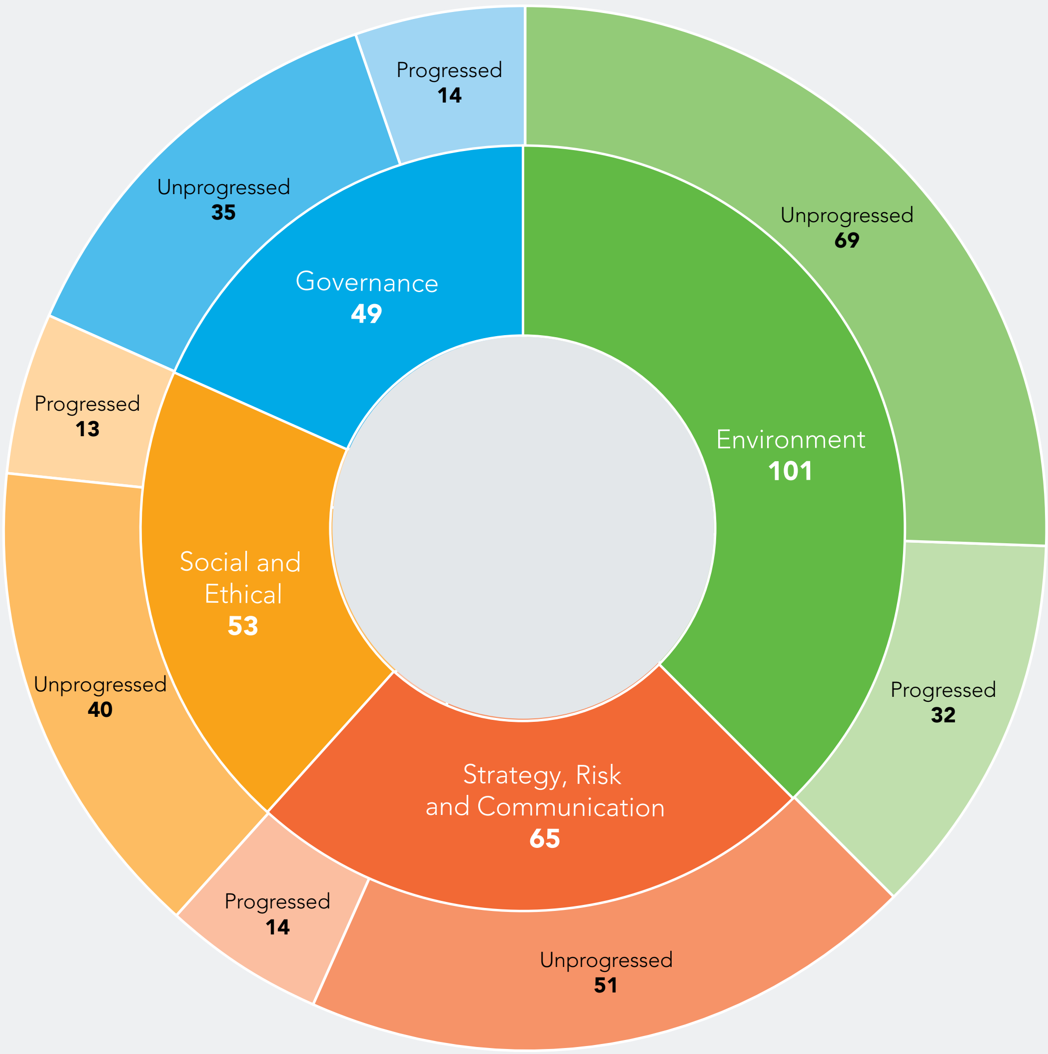
Notably, we completed 14 objectives in H1 2022, as detailed in SDG highlights at the end of this section. This is a considerable achievement relative to the three objectives completed during H1 2021, when the SDGHY engagement programme reached 18 months since inception.

Figure 6. Objectives by theme and current milestone, H1 2022



Source: Federated Hermes as at 30 June 2022.

Figure 7. Milestones progressed by theme, H1 2022



Source: Federated Hermes as at 30 June 2022.

SECTION 3

Connecting the SDGs

H1 2022: Our SDG impact focus

In our third year of SDGHY engagement, a picture of thematic SDG impact potential has become very clear.

Nowhere is this more apparent than in how SDG outcomes have been targeted through our objectives-based approach for influencing change. Although SDG hypotheses and resultant SDG scoring (see Appendix) for each investment is the starting point for engagement on impact and ESG challenges, it is in live engagement data that we see a clear picture emerge for the overall strategy. The Figure below describes the mix of material SDG impacts that objectives are focused on, while the subsequent table shows how SDGs featured across 297 engagements in H1 2022.

Figure 8. SDG-linked objectives with engagement actions in H1 2022

Source: EOS at Federated Hermes, Federated Hermes as at 30 June 2022.

The nature of our investable universe has led us to involvement with companies in the basic materials, capital goods, packaging, automotive, financial services and banking, telecommunications, and future-facing and legacy utilities and energy.

It is therefore no surprise that Climate Action (SDG 13), Responsible Consumption and Production (SDG 12), Industry, Innovation and Infrastructure (SDG 9), Clean and Affordable Energy (SDG 7) form an 'impact bedrock' for how we invest and engage. Companies in these sectors, which feature value chains with significant resource use and greenhouse gas emissions, have a powerful role in driving corporate and supply chain contributions to SDGs 7, 9, 12, and by extension, reducing emissions in the atmosphere, an 'outcome' focal point in SDG 13[11]. Similarly, customer or end-user enablement of resource efficiency and decarbonisation is, we believe, a major opportunity at banks and telecommunications peers[12].

> **It is no surprise that Climate Action, Responsible Consumption and Production, Industry, Innovation and Infrastructure, Clean and Affordable Energy form an 'impact bedrock' for how we invest and engage.**

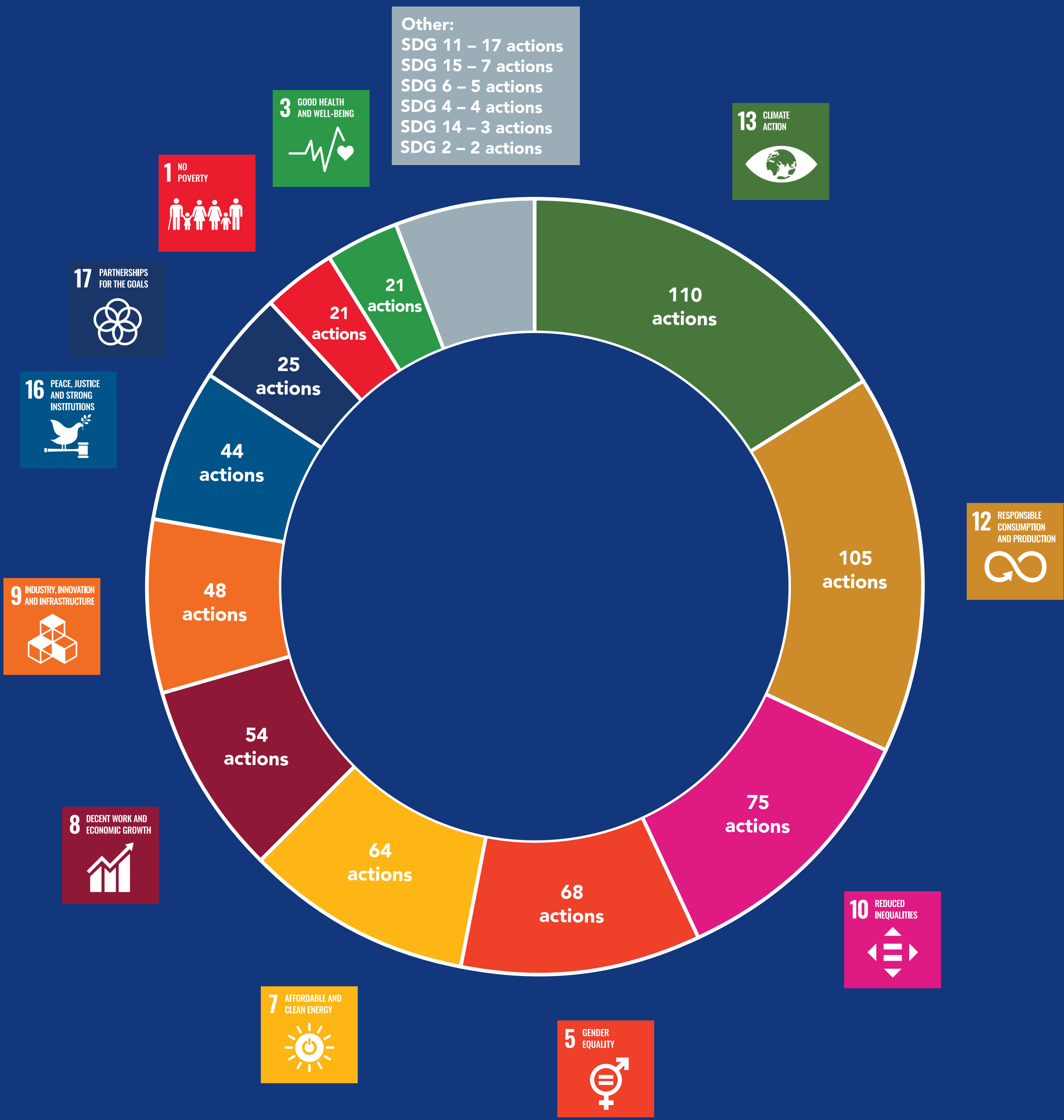
As in previous reports, we continue to witness highly active dialogue on social impact as we identify bottom-up potential in Decent Work and Economic Growth (SDG 8), Reduced Inequalities (SDG 10), Gender Equality (SDG 5), and No Poverty (SDG 1). Many companies we engage are major employers or indirectly fund employment of others in supply chains. They have a role in building future-focused, resilient supply chains and operations in line with the SDGs, thus giving rise to improved outcomes for the workforces, communities or customers involved in transformation, and on a more equitable and resilient basis.

This section concludes with highlights on how we have progressed our SDG-focussed objectives at companies during H1 2022.

[11] Climate Action.

[12] See our previous report: The sleeping giant: Unlocking sustainable finance | Federated Hermes Limited (hermes-investment.com)

Figure 9. Total actions with an SDG-linked objective or issue, H1 2022



Source: EOS at Federated Hermes, Federated Hermes as at 30 June 2022.

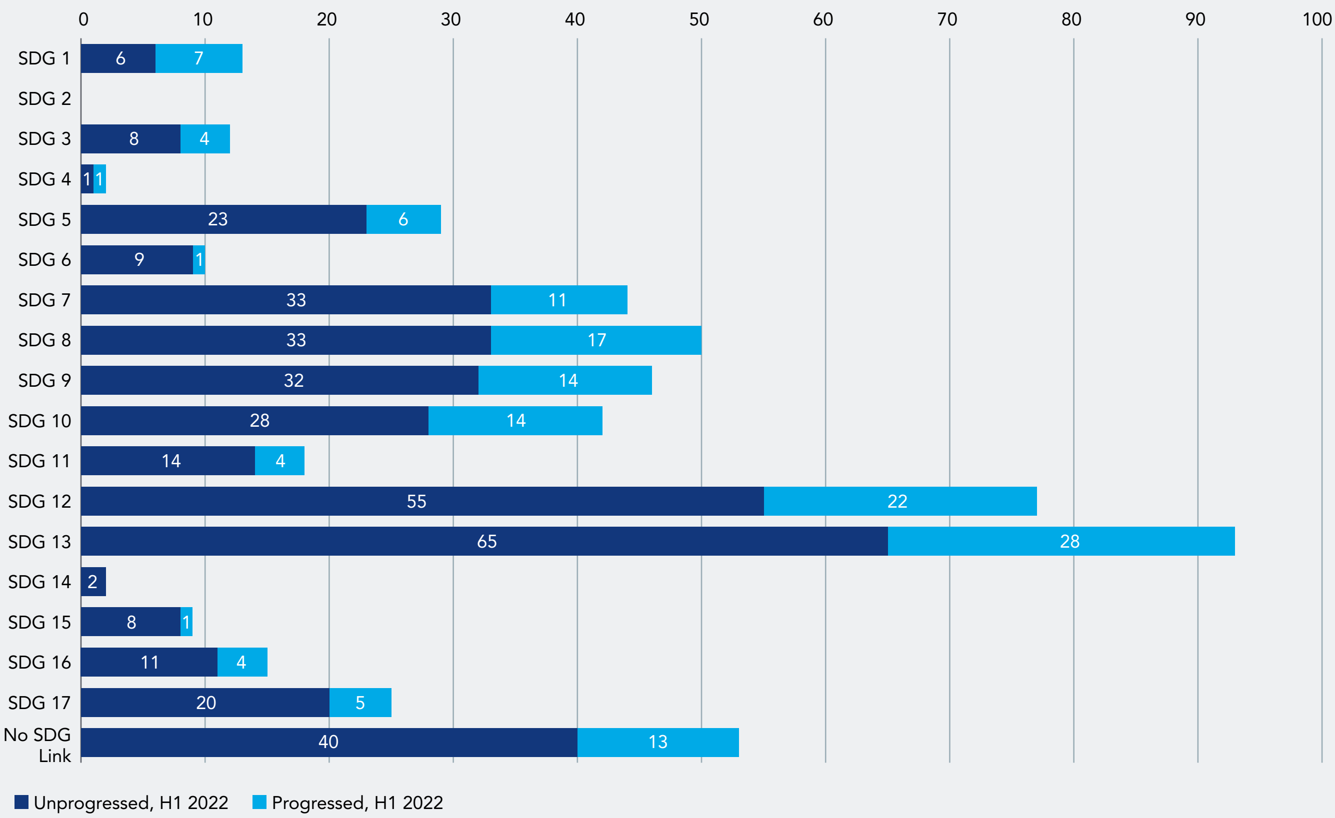
H1 2022: Progress in SDG engagement and objectives for impact

We are delighted with progression realised against acute areas of SDG focus after our first two years of establishing engagement dialogue and SDG impact hypotheses. As the figure below attests, H1 2022 featured progress on 28% of objectives linked to one or more SDGs, with momentum across SDGs in Climate Action (SDG 13), Responsible Consumption and Production (SDG 12), Industry, Innovation and Infrastructure (SDG 9), Clean and Affordable Energy (SDG 7), as well as socially-focused SDGs outlined on the last page.

Notably, we progressed 13 objectives which are not linked to SDGs. These are typically governance or remuneration-focused objectives for change which do not have meaningful links to an SDG, but remain material ESG risks and opportunities where we believe companies need to evolve. This aligns with our objective to ensure companies we invest in have strong and improving governance practices.

The remainder of this section provides a review of highlights from SDG-driven progression in H1 2022.

Figure 10. Total SDG-linked objectives progression, H1 2022



Source: Federated Hermes as at 30 June 2022. NB: No objectives have been set for SDG 2. NB: Total SDG-linked objectives in Figure 10 are greater than in Figure 8, because Figure 10 also includes objectives which did not have one or more engagement actions during H1 2022.

H1 2022: Selected progress highlights in SDG-driven objectives

SDG 7: Affordable and Clean Energy

SDG 13: Climate Action

AES Corporation: Accelerate reduction of coal in generating mix

Completed

How we engaged: AES has a proactive approach to its risks linked to coal-fired power. It had committed to reducing exposure to coal to less than 10% of its generating mix by 2030. We engaged with executives on this in 2020 to understand how the company assesses divestment or retirement decisions for coal-fired power assets, and in 2021, we asked for clarification of how Chilean coal asset closures may be accelerated. In H1 2022, the company confirmed it would accelerate coal exits in its generating mix to below 10% by 2025, five years sooner than planned, as it continues to build renewables which outweigh coal capacity retirements by about 3 to 1 in Chile. We engaged in H1 2022 on implications for commercial strategy and asked how it will manage its coal phase-outs. The company plans to remain in all regions in which it operates while transitioning from coal. This includes Vietnam where the company will replace coal capacity with lower-emissions assets, but couldn't yet comment on a pipeline. We completed our objective, and this new timetable enhances AES's contributions to SDG 7.

Next Steps: With the Chilean picture now quite clear, we will continue to engage on how other regions will be decarbonised, including in Asia. Furthermore, we believe the company has significant experience in managing the impact on communities reliant on coal assets, and believe it should showcase its just transition approaches to other utilities. This has led to us setting a new objective from August 2021 on the company showcasing a highly transparent accounting of how it is applying a just transition policy to asset sales or retirements.

Brookfield Renewables: Decarbonisation of carbon-intensive assets

Progressed to Milestone 2: Acknowledging concerns

How we engaged: Brookfield Renewables is an ambitious renewables developer; it provides comprehensive decarbonisation strategy guidance for renewables assets but less dialogue on carbon-intensive assets which, while less significant in capacity, drive greater contributions to greenhouse gas emissions. It therefore needs to provide greater transparency and a strategy for how these assets are set to shift for investors. We set this objective and raised it in H1 2022 with management, when we learned that carbon-intensive assets fall within the wider Brookfield Asset Management net-zero-by-2050 target.

Next Steps: To progress to Milestone 3 (Planning), we would like to see greater disclosure on how its carbon-intensive assets will be managed, regardless of what strategy they fall under, to provide greater certainty to investors and wider stakeholders on the decarbonisation approach.

SDG 1: No Poverty

SDG 3: Good Health and Well-being

SDG 8: Decent Work and Economic Growth

SDG 10: Reduced Inequality

AES Corporation: Just transition policy and transparent outcomes

Progressed to Milestone 3: Planning

How we engaged: The company's remaining hydrocarbon-based assets may face complicated transition risks. These could include choices to retire or sell high-carbon assets and viability of reliant communities and workers. Although the company has sought to integrate just transition considerations, we believe this should be articulated in a full policy or strategy, and that it should account for how the policy is applied to benefit stakeholders of key assets. We raised this in 2021 and the company asked us for feedback on its current climate-related reporting and transparency. We provided more feedback in May 2022 and suggested that transparency in detail and examples of just transition policy usage could be helpful models of good practice for utilities peers to consider in managing stakeholders through socially-challenging asset rotations.

Next Steps: To move to Milestone 4 (Implementing), we need to see and engage on a fully articulated just transition policy in a standalone, public format. To complete the objective, we would like to see annual accounting or similar disclosure on how its policy has been effectively applied to hydrocarbon asset retirements or sales.

AK Bank: Best-in-class sustainable finance strategy and key exclusions

Progressed to Milestone 2: Acknowledging concerns

How we engaged: We believe AK Bank should have a world-class sustainable finance framework, strategy and targets, and show how it is executing this over time. It should also ensure exclusions and risk policies continue to evolve in line with stakeholder expectations and needs. We engaged with management on this four times since 2021; in H1 2022, we provided written feedback on how it can account for its sustainability-driven lending and financing externally as this grows as a proportion of total business, and subsequently discussed long-term strategy for sustainable finance with the head of this unit. We were pleased to learn that the bank shares our opportunistic view of unique social and environmental financing needs of the Turkish economy and the potential in solving for lending needs of individuals and SMEs to have a real impact.

Next Steps: To move to Milestone 3 (Planning), we will engage on how the bank may further evolve and publish lending restrictions, to account for decisions where there is considerable environmental or social risk, and to complement the positive 'impact' opportunity. To move to Milestone 4 (Implementing), we would like to see some evidence of positive, non-financial outcomes for customers, resulting from sustainable financing.

Alpha Bank: Develop sustainable finance strategy, targets and disclosure

Progressed to Milestone 2: Acknowledging concerns

How we engaged: The bank is working on a robust strategy to finance key environmental, decarbonisation and social outcomes in the Greek economy. We want to see the bank publish a sustainable finance framework with relevant targeted areas of lending which speaks to the needs of the country. Moreover, the strategy must provide targets and subsequent disclosures which are set relative to all lending and asset management activity, and which defines areas of lending and financing it will pursue. In our H1 2022 engagement, we were pleased to learn that the sustainable finance framework is under development and relative targets for sustainable financing are being considered, and we followed up with a letter providing feedback on reporting sustainable finance outcomes and broader ESG disclosure based on its current disclosures.

Next Steps: We committed to providing the bank with more feedback based on future iterations of its sustainable finance strategy, and to move to Milestone 3 (Planning), we would like to see published sustainable finance targets with clear indications of major categories of social and environmental impact driven use-of-proceeds, adapted to Greek consumers and businesses' needs.

General Motors: Increase transparency on supply chain social and human rights performance

Progressed to Milestone 3: Planning

How we engaged: The company has introduced saliency assessments and a revised human rights policy. Additional enhancements are also underway due to the changing nature of risks within supply chains related to the sourcing of raw materials. The company is moving to a different mix of materials for electric vehicles – such as rare earth minerals and EV powertrain components which may be sourced from or manufactured in higher-risk locations. In H1 2022, we met with the CEO and senior management on two occasions, partly to discuss enhancing social and human rights due diligence audit and remediation disclosure. We then provided written feedback using peer examples.

Next Steps: To move to Milestone 4 (Implementing) we would like to see an indication that enhanced human rights transparency and due diligence in supply chains may be offered to investors, and we plan to engage on progress in human rights management in H2 2022.

SDG 9: Industry, Innovation and Infrastructure

SDG 13: Climate Action

Cemex: Science-based emissions targets

Completed

How we engaged: We started engaging with Cemex on the development of science-based carbon emissions reduction targets in 2018, given the profile of the cement industry as one of the highest emitters of carbon dioxide due to the nature of its manufacturing process. Although the company expressed its commitment to climate action, there was no clarity on the alignment of its emissions intensity reduction target of 35% by 2030, compared to 1990, to the goals of the Paris Agreement. In subsequent engagements, the company sought to assure us about the internal methodology used to develop targets, however, we explained that we expected an external validation. In 2021, the CEO confirmed that Cemex would submit its revised 2030 target of 20.3% Scope 1 intensity reduction and 42.4% Scope 2 intensity reduction by 2030, compared to 2020, to validation by the Science-Based Targets initiative (SBTi). The 2030 target was validated by the SBTi under the "well below 2°C" category.

Next Steps: Cemex now has all the paper commitments in place that show it is sincerely aiming to achieve ambitious emissions reduction. The next step is for the company to demonstrate real greenhouse gas reductions that put it on a path to achieving those targets. In time we would also like to see how the company can increase its ambition and align with a 1.5°C pathway.

DCP Midstream: Set emissions targets and verify emissions data

Progressed to Milestone 3: Planning

How we engaged: The company is unlikely to diversify from oil and gas midstream operations in the short to medium term, and it may also be difficult to set a science-based target given the relative lack of control the company has over its upstream and downstream partners as a mover of fuels. However, we believe the company needs to set Scope 1 and 2 emissions, even if it is not able to set a Scope 3 target at this time. The company has now set a Scope 1 and 2 emissions intensity reduction target of 30% by 2030 against the 2018 level and announced a net zero 2050 target for Scopes 1 and 2. It has also linked ESG factors to compensation for a range of employees. In H1 we met with senior management to discuss the challenges of achieving the new target.

Next Steps: To complete the objective we want the company to set targets to at least 2025, and ideally to 2030 in line with Paris Agreement aligned pathways. Further, the company should consider whether it can achieve more than its 30% intensity reduction during the 2018-2030 period, given that it has already achieved substantive reductions in emissions intensity since 2018.

Anglo American: Value chain emissions ambition and strategy

Completed

How we engaged: When we first set an objective for Anglo American to develop a plan for reducing steel value chain emissions we felt the company was being left behind by peers. Productive conversations, including as part of the CA100+, over the past two years have seen the company increase its ambition in this regard. The company has now set a Scope 3 value chain emissions reduction target of 50% by 2040, based on use of high grade iron ore pellets in lower carbon steel production such as hydrogen reduction. This has been agreed by the Board and is being put to shareholders as part of its 'say on climate' vote.

Next Steps: Setting Scope 3 targets is a positive step forward and provides an opportunity for further engagement to increase the ambition of the target to one that is clearly aligned to 1.5°C pathways.

SDG 9: Industry, Innovation and Infrastructure

SDG 12: Responsible Consumption and Production

Berry Global Group: Minimum recycled content volume target

Completed

How we engaged: In 2020, the company set a goal of using at least 10% recycled materials as a proportion of total raw materials volume by the mid-2020s. We noted that the company's peers had set more ambitious targets for recycled content at 25% by 2025, and downstream consumer goods buyers had set targets much higher than this. Our expectation was that the company should set a 25% recycled content goal by 2025 for its total materials volume in line with peers. We conveyed our expectations to the company in a 2020 mid-year engagement, comparing the company's goal with those set by its peer competitors. During an investor-led collaborative engagement on plastics, the company said it was examining how to set more ambitious targets. In 2021, we welcomed significant investment by the company towards innovation and sustainability-related initiatives to drive improved operational efficiency in recycled content. The company has since announced its new 30% by 2030 circularity goal for its fast-moving consumer goods which represent approximately two-thirds of total revenue for the company.

We appreciated that the company was prioritising a move away from its reliance on virgin fossil-fuel plastics and that the new 2030 goal surpasses its previous target of using 10% post-consumer recycled resin by 2025. Going forward, we will continue to engage the company on circularity.

Ford Motor Company: EV sales objective success

Progressed to Milestone 2: Acknowledging concerns

How we engaged: Ford expects 40% of its global product mix to be electric by 2030, setting targets for all of its passenger vehicles in Europe to be fully electric, and two-thirds of commercial vehicles to be all-electric or plug-in hybrid, by 2030. It now needs to demonstrate nearer-term progress towards these objectives. We believe genuine progress towards targets within the next three years is required to validate the company's growth hypothesis and subsequent go-to-market success. At the beginning of 2021 we set an objective for the company to report that it has shifted a minimum level of EV sales in the 2023 model year and how this shift has impacted its fleet emissions intensity. During a meeting with the company we raised this idea and explained why this information is important to outside stakeholders.

Next Steps: The company has listened to our request and responded positively. However, although it has demonstrated a direction of travel on sales, we need to engage to understand how it can follow this with indicative fleet emissions reduction impacts.

Solvay: Improve ChemScore

Progressed to Milestone 3: Planning

How we engaged: Solvay has an advanced sustainability strategy and high quality reporting, as is warranted by a company in a sector such as chemicals with many material ESG risks. When we initiated engagement with the company in Q4 2021 we were surprised by its low score on the ChemScore benchmark. At the start of 2022 we set an objective for the company to improve its score and signed a joint investor letter to the company outlining our expectations. The company responded to the letter highlighting the many areas where it has made progress and its robust product stewardship policy that manages the risks throughout the product's entire life cycle, from the design stage to its end of life. In March 2022 we met the company as part of a collaborative engagement where it acknowledged the poor ChemScore result and explained it was due to lack of disclosure. It is engaging with the initiative to improve the result.

Next Steps: The company has acknowledged its low score. Now we need to see what actions it will take to improve the score in the short and medium term. Once we have this information the objective can move to Milestone 4.

SDG 5: Gender Equality

SDG 10: Reduced Inequality

AES Corporation: Diversity strategy and workforce reporting

Progressed to Milestone 4: Implementing

How we engaged: Compared to US utilities peers, the company has historically emphasised greater levels of diversity at senior levels, which it is partly due to CEO leadership on the issue, and partly to the company's diverse 15 operating countries across the developed and developing world. However, it was missing goals related to ethnic and racial diversity. We want the company to enhance its targets and begin to disclose workforce composition data. We have engaged on this issue five times since 2020 and had a breakthrough in Q2 2022 when the company updated us that our concerns around diversity and related disclosures have been considered and will be reflected in future reporting. This was part of a wide-ranging meeting where we also covered its just transition strategy and recruitment procedures.

Next Steps: The final stage to complete this objective will be to review the disclosure once released. Will assess whether it meets our expectations or requires further improvement before we consider the objective complete.

IQVIA: Publish workforce composition data

Completed

How we engaged: When we spoke with the investor relations team in August of 2021, we encouraged the publication of the company's EEO-1[13] data and then again in February 2022, when we met with a board director. During our conversation, we learned the company was planning to publish its EEO-1 data and other workforce composition metrics in its next ESG report. When asked what drove the decision to publish workforce composition data, the company said it had heard this request from multiple investors and that it was something the board had been discussing for some time. We were pleased to see the publication of this data soon thereafter in the company's 2021 ESG report and that, in addition to the EEO-1 data, the company provided more granular disclosures on the gender, racial/ethnic diversity profile of its workforce.

We value this increased transparency and encourage the company to include more dimensions of diversity in its reporting going forward, including more data and reporting on attraction, retention and promotion rates of IQVIA's workforce.

[13] The EEO-1 Component 1 report is a mandatory annual data collection that requires all US private sector employers with 100 or more employees, and federal contractors with 50 or more employees meeting certain criteria, to submit demographic workforce data, including data by race/ethnicity, sex and job categories.

SDG 8: Decent Work and Economic Growth

LKQ: Living wages and decent employment

Progressed to Milestone 4: Implementation

How we engaged: The company has over 44,000 employees across 1,600 locations worldwide. Of the employees, approximately 40% are in North America and 80% are hourly workers (on $14-16 as of FY20). We have been engaging the company on moving towards the payment of a living wage to its hourly workers. Over the course of two engagements in H1 2022 we were able to make substantial progress on this objective. The company acknowledged that in the competitive labour market in which it is recruiting that they need to have a socially responsible floor for wages. We had further exchanges with the company to again seek clarification around how it thinks about the investment case for investing in the workforce; its targets for employee turnover and the read across between employee engagement to turnover levels; accident rates and ultimately cost savings and productivity increases. The company confirmed that it maintains an employee turnover target for its North American hourly workers and cited again several initiatives in place to drive higher employee engagement and retention.

Next Steps: LKQ now seems to have most of the pieces in place to introduce a living wage for its hourly workers. We will continue to press the company for implementing this practice based on all the evidence it has collected supporting the business case.

Ford Motor Company: Employee engagement and retention

Progressed to Milestone 2: Acknowledging concerns

How we engaged: Ford is deploying a wide-ranging restructuring programme to eliminate persistent losses in its overseas operations. This involves reducing its European workforce by 25% and its Latin American workforce by 80%. As long as the company continues to shut down plants in order to improve its financial profile, it will continue to face the risk of workforce unrest, lower productivity, or shortages in labour and talent. We believe that engagement and retention strategies must focus on retaining and engaging employees as it restructures for an EV-centric future and started engaging on this in H1 2022. We asked about the company's employee satisfaction and turnover in its legacy and future businesses and suggested it should start disclosing turnover rates for both.

Next Steps: Now that we have raised our initial concern with the company the next step is to provide additional feedback and to engage on the long-term strategy for human capital in greater depth.

SDG 12.6: Disclosure

Banco BTG Pactual: Consistent ESG disclosures and targets

Progressed to Milestone 3: Planning

How we engaged: Although the company has considerably evolved its approach and strategy for material ESG issues in recent years, it has produced ESG disclosures which are of low quality. It therefore remains difficult to assess the bank's approach to issues including climate change finance and the bank's own environmental impacts. We want to see the company publish at least two years of consistent ESG disclosures at a group level which meaningfully disclose and quantify (where possible) year-over-year performance on the material issues identified. In Q1 2022 we were pleased to discuss the company's significantly enhanced ESG disclosure based on its 2020 financial year. This disclosure sought to address many of the initial concerns we had around a lack of financial reporting. The report has been produced in English and includes targets for some of the material social and environmental opportunities available to the bank.

Next Steps: Further engagement is required to discuss the company's sustainability strategy and targets. This will take us beyond our early 2022 engagement dialogue. Key among these future engagements will be the bank's rapidly-evolving impact and sustainable financing opportunities.

Brookfield Renewables: Implement climate scenario analysis in line with all TCFD recommendations

Progressed to Milestone 3: Planning

How we engaged: The company has diversified operations across a range of renewables technologies and four continents. This infrastructure may be exposed to increasing acute and chronic physical risk, including fires, floods and greater volatility in water supplies for its significant hydroelectricity footprint. We believe executing comprehensive and scenario-relevant physical and transition risk analysis will help the business mitigate climate change risks to its assets. We met with senior management and questioned the role of carbon intensive assets, which are briefly mentioned in the sustainability report. We also sent feedback on its inaugural TCFD report, which we viewed as a very credible first attempt.

Next Steps: We believe the company's TCFD report can be improved further. In future versions it should aim for full Paris alignment by expanding the scope of its targets to include carbon-intensive investments.

Canpack: Disclose full scope emissions and set medium-term emissions targets

Progressed to Milestone 3: Planning

How we engaged: We want the company to provide full disclosure of all scopes of greenhouse gas emissions. Once this is in place, it should set emissions reductions targets that are science-based and reaching to at least 2025 and, ideally, to 2030. We met with the company in Q2 2022 and were pleased to learn it has made good progress with collecting Scope 3 data. It has gained full approval on its target data figures from the Science-Based Targets initiative (SBTi) for well-below two degrees science-based targets, with a consideration to upgrade to 1.5-degrees Celsius. We provided feedback on managing supplier emissions, suggesting that encouraging suppliers to commit to the SBTi and ultimately aiming for a certain percentage of them to do so is an effective way to achieve its Scope 3 emissions reduction target.

Next Steps: Canpack now has the processes in place to collect the required data and set science-based targets. The next step is to make this a reality which we expect will be evident in its next sustainability report.

SECTION 4

Appendix

Appendix A. Summary of six-factor heuristic framework for SDG *ex-ante* scoring

Factors to assess	Some evidence of SDG *ex-ante* potential, but requires deeper engagement…	… to more certain SDG *ex-ante* potential, and requires less intensive engagement
1. Business purpose & strategy How are SDG-related opportunities reflected in the company's purpose and the strategy it articulates to investors and society?	There may be articulation of how the company benefits society, but this is not central to its vision or strategy. The company may mention contributions to the SDGs but does not yet illustrate how it may deliver such benefits, nor how they guide culture, strategy or execution.	The company is focused on how its actions benefit society, and this is part of its core strategy. The company articulates how it will contribute to achieving the SDGs in its corporate purpose and through its culture.
2. SDG-related benefits of products & services How are SDG-related benefits provided through products or services? Are these key to the value proposition for customers or society?	Little articulation of the social or environmental benefits of products or services. Products or services with SDG-related benefits may not generate significant revenues today but might in the future. Engagement may be required to validate potential benefits.	Strong articulation of the social and/or environmental benefits of products or services. Value propositions are intended to deliver SDG-related outcomes. These may already generate substantial revenue.
3. SDG-related impact of operations How is the company driving SDG-related benefits through its operations, across the environmental and social dimensions within its control, or through its influence over its value chain?	Weak articulation of how the company's operations have a positive or negative impact. Intensive engagement may be required to determine the future potential for greater positive impact.	Material operational impacts are disclosed in positive and negative terms and how these may be improving over time. The company may exhibit leadership on some impacts relative to peers or has time-bound targets for a range of social and environmental risks and opportunities.
4. SDG-related capital allocation Is the company allocating capital to invest in growing products or services with SDG-related benefits? Has the company disclosed or quantified this?	Less disclosure of capital allocations to products or services with SDG-related benefit, or to investments which deliver impact through operations. Future opportunities are difficult to identify prior to engagement.	Disclosed capital allocation includes clear priorities for products and services with SDG-related benefits, or delivery of positive SDG impact through its operations.
5. Evidence & disclosure of SDG outcomes What SDG-related outcomes has the company, its customers or society realised? Have ESG or SDG impacts been quantified and disclosed?	Little evidence to demonstrate how the company is contributing to SDG-related outcomes for customers or society in quantified or qualitative terms. Disclosure may be a key area for engagement.	Ample evidence to demonstrate contributions to SDG-related outcomes for customers or society. Some quantification for incremental or total impact over time. The company explains its methodology for measuring such outcomes.
6. Engagement insight What have we learned from engagement in the past, and what is our engager's assessment of the company's future potential for impacting SDGs?	Demonstrates interest in engaging on SDG-related matters or opportunities, but this is unlikely to influence the business in the short term. Longer-term potential may exist, but significant barriers are apparent through engagement. More engagement is required to develop insight here.	Open to engagement dialogue and constructively acts on feedback and advice. The company actively applies the SDGs as a framework for informing its strategy, and will continue to build on opportunities for sustainable development.

Appendix B. Clarifying Our Approach

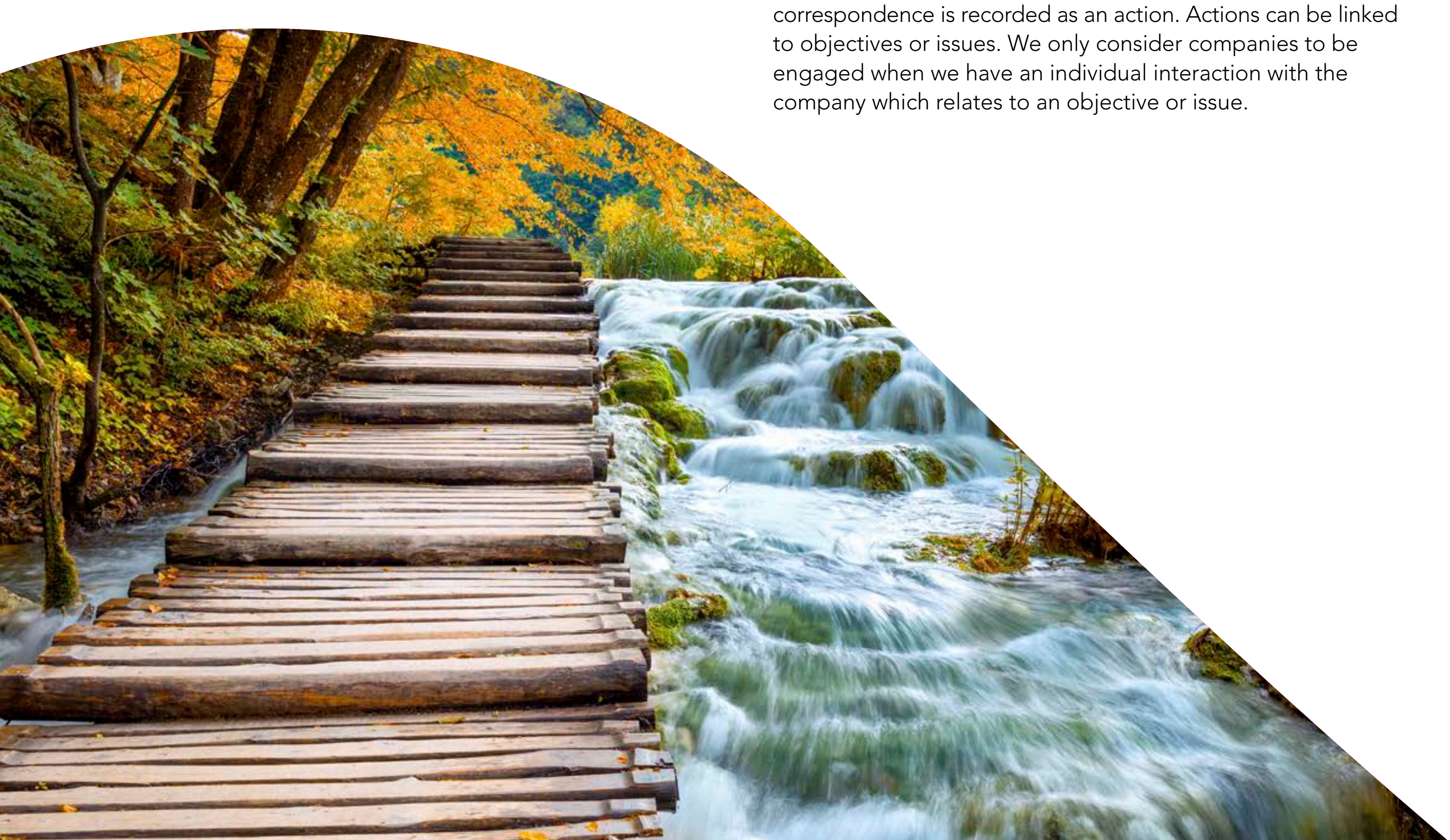
Our engagement approach is systematic and transparent. Our proprietary milestone system allows us to track the progress of our engagements relative to the objectives set for each company.

Objectives

We set clear and specific objectives within our company engagements to ensure we achieve positive outcomes. An objective is a specific, measurable change defined at the company – an outcome we are seeking to achieve. Each objective is tracked using milestones. Objectives are regularly reviewed until they are completed – when the company has demonstrably implemented the change requested – or discontinued. Objectives may be discontinued if the objective is no longer relevant, or because the engagement is no longer feasible or material.

We only consider companies to be engaged when we have an individual interaction with the company which relates to an objective or issue.

We may engage with a company on multiple objectives at any one time, covering a variety of material ESG issues. An example of an objective could be: "Development of a strategy consistent with the goals of the Paris Agreement, including setting science-based emissions reduction targets for operating emissions (Scope 1, 2 emissions)." Each objective relates to a single theme and sub-theme.



Issues

How does an objective differ from an issue, another term we use within our engagement? An issue is a topic we have raised with a company in engagement, but where we do not precisely define the outcome that we are seeking to achieve. This can be more appropriate if the issue is of lower materiality and so we do not anticipate engaging with the frequency required to pursue an objective. Or perhaps we are still in the process of identifying what type of change we may want to see at a company and so are not yet able to set a precise objective. Issues are frequently used for companies outside our continuous engagement programme, for example those where we typically engage only around the annual shareholder meeting and our voting recommendation.

We set clear and specific objectives within our company engagements to ensure we achieve positive outcomes.

Milestones

To measure our progress and the achievement of engagement objectives, we use a four-stage milestone strategy. When we set an objective at the start of an engagement, we will also identify recognisable milestones that need to be achieved. Progress against these objectives is assessed regularly and evaluated against the original engagement proposal.

Actions

These are the interactions that take place between our engagement professionals and the companies or public-policy bodies with whom they are engaging. Every call, meeting or correspondence is recorded as an action. Actions can be linked to objectives or issues. We only consider companies to be engaged when we have an individual interaction with the company which relates to an objective or issue.

Engagement themes for 2021-23

Appendix C. SDG Engagement High Yield Credit Hedged to USD GIPS® Composite

GIPS® Composite

Composite: **Federated Hermes SDG Engagement High Yield Credit Hedged to USD**

Index: **ICE BofA Global High Yield Constrained (USD Hdgd)**

Periods ending: **30 June 2022**

All information is quoted in USD

Annualised Returns (%)

	Composite Gross Return	Index	Composite Net Return (Assuming Maximum Fee)
Q2 22	(9.99)	(9.93)	(10.14)
YTD	(15.19)	(14.88)	(15.47)
1 Year	(14.67)	(14.98)	(15.22)
Oct-19 – Jun 22 (Annualised)^^	(0.74)	(1.44)	(1.39)

Annual Returns (%)

Year	Composite Gross Return	Composite Net Return	Benchmark Return	*Composite 3-Yr St Dev	*Benchmark 3-Yr St Dev	No of Portfolios	**Dispersion	Composite Assets (Million)	Firm Assets (Billion)
2019	4.04	3.87	2.90	N/A	N/A	<5	N/A	276.3	40.2
2020	7.94	7.23	6.48	N/A	N/A	<5	N/A	680.6	585.7
2021	2.87	2.20	3.04	N/A	N/A	<5	N/A	1,855.3	634.2

^^Represents composite inception period. See below for additional notes to the schedule of rates of return and statistics.

* Represents the 3-year annualized standard deviation for both the gross composite and the index returns. Statistic is used to measure the volatility of composite returns.

** Standard deviation is calculated using gross returns. Dispersion is not applicable ("N/A") for any period if fewer than five accounts are in the composite for that period.

The composite includes all discretionary portfolios following the SDG Engagement Global High Yield Credit Hedged to USD strategy run by the Federated Hermes Global Credit team (London Office) and has an inception date of 1 October 2019. The objective of the strategy is to exceed the return of the benchmark over a rolling five-year period whilst delivering positive societal impact aligned to the United Nations Sustainable Development Goals ("UN SDGs"). The strategy may invest in a broad range of assets, either directly or through the use of derivatives, (including, but not limited to, equities, equity-related securities, Eligible CIS and/or financial indices, futures, options, swaps, debt, fx and money markets). The strategy through its investments in FDIs may be leveraged. The composite's benchmark is the ICE BofA Global High Yield Constrained Hedged to USD Index, which is designed to measure the debt market performance of global high yield debt. The benchmark contains primarily USD and EUR issues. The Index is rebalanced on the last calendar day of the month and the return is calculated on a total return basis. This composite was created in November 2019. Performance shown for 2019 is for a partial period starting 1 October 2019. Federated Hermes claims compliance with the Global Investment Performance Standards ("GIPS®") and has prepared and presented this report in compliance with the GIPS® standards. Federated Hermes has been independently verified for the period of January 1, 1992, through March 31, 2022. The verification report is available upon request. A firm that claims compliance with the GIPS® standards must establish policies and procedures for complying with all the applicable requirements of the GIPS® standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS® standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report. The management fee schedule for this strategy is 0.65% per annum. Gross of fees returns have been calculated gross of management/custodial fees and net of reclaimable withholding taxes, but after all trading commissions.

Federated Hermes is a global, independent, multi-strategy investment management firm. For GIPS® purposes, Federated Hermes is defined to include the assets of registered investment companies that are advised or sub-advised by the various Federated Hermes advisory companies. Effective September 30, 2020, for GIPS® purposes the name of the firm was officially changed to Federated Hermes. Firm assets on this report exclude assets affiliated with Hermes GPE and the advisory-only, model-based assets that may be included in other reports providing total firm assets. Interest income and dividends are recognized on an accrual basis. Returns include the reinvestment of all income. All market values and performance information are valued in USD unless currency is denoted in composite description. Annual composite dispersion is measured and presented using the asset weighted standard deviation of the gross returns of all of the portfolios included in the composite over the entire year. See the composite description language for a discussion on appropriate fees currently applied to calculate composite performance. Net composite results are based off model fees using the stated fee schedule. In addition, further fee information can be obtained from the firm's respective Forms ADV Part 2 Brochure Item 5. Additional information regarding the policies for valuing investments, calculating performance, and preparing GIPS® reports, as well as a complete list and description of the firm's composites and pooled funds is available upon request. Past performance is not indicative of future results. GIPS® is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. See disclosures on the Schedule of Rates of Return and Statistics Reports for additional information.

Where the strategy invests in debt instruments (such as bonds) there is a risk that the entity who issues the contract will not be able to repay the debt or to pay the interest on the debt. If this happens then the value of the strategy may vary sharply and may result in loss. The strategy makes extensive use of Financial Derivative Instruments (FDIs), the value of which depends on the performance of an underlying asset. Small changes in the price of that asset may cause larger changes in the value of the FDIs, increasing either potential gain or loss.

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. Any investments overseas may be affected by currency exchange rates. Past performance is not a reliable indicator of future results and targets are not guaranteed.

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