SDG Engagement Equity

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2023 H1 Report

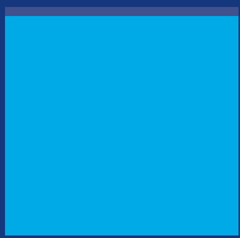
Federated Hermes Limited

www.hermes-investment.com
For professional investors only

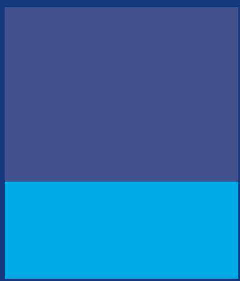
Federated Hermes SDG Engagement Equity H1 2023 highlights

108 **Engagement actions** carried out in H1 2023

94% of portfolio companies were engaged



36% of companies made progress with objectives



The investment backdrop is more constructive for us now than it has been for some time, driven by more normal volatility levels… and a greater focus on stock fundamentals.

In H1 2023, the proportion of our engagements were focused on:

19% environmental issues and objectives

48% social issues and objectives

22% governance issues and objectives

11% other strategic issues and objectives

The most intensively engaged Sustainable Development Goals (SDGs) were:

1 NO POVERTY — **44%** of engagement actions

3 GOOD HEALTH AND WELL-BEING — **13%** of engagement actions

5 GENDER EQUALITY — **20%** of engagement actions

8 DECENT WORK AND ECONOMIC GROWTH — **44%** of engagement actions

10 REDUCED INEQUALITIES — **48%** of engagement actions

The question of who a company employs, and how it treats its employees, both direct and indirect, is a matter over which company management have direct control.

Completed objectives: **10**

Total meetings voted: **45**

Number of meetings voted against management on at least one resolution: **42%**

Source: Federated Hermes, as at 30 June 2023.

Contents

Engagement introduction H1 2023

Will Pomroy Lead Engager

As we have moved into 2023, we are very aware that the ambitious agenda set forth by the UN Sustainable Development Goals (SDGs) is one that the world is off-track to meet.

June this year was the warmest yet since global temperate record-keeping began in 1850[1] and July was the world's warmest month on record[2]. As I write this report, nearly 200 million people in the United States, or 60% of the US population are under heat advisory or flood warning or watch as high temperatures spread[3]. The era of global warming has ended and "the era of global boiling has arrived", according to the UN Secretary General.

Suffice to say, while the question of environmental, social, and corporate governance (ESG) continues to be a hot-button topic in the United States, real-world events are making the severity of the issues hard to ignore.

Through this report we provide colour on the ongoing, mostly constructive, dialogues we are having with our investee companies. In many cases the direction of travel is positive. However, as the context illustrates, the pace of change invariably needs to accelerate.

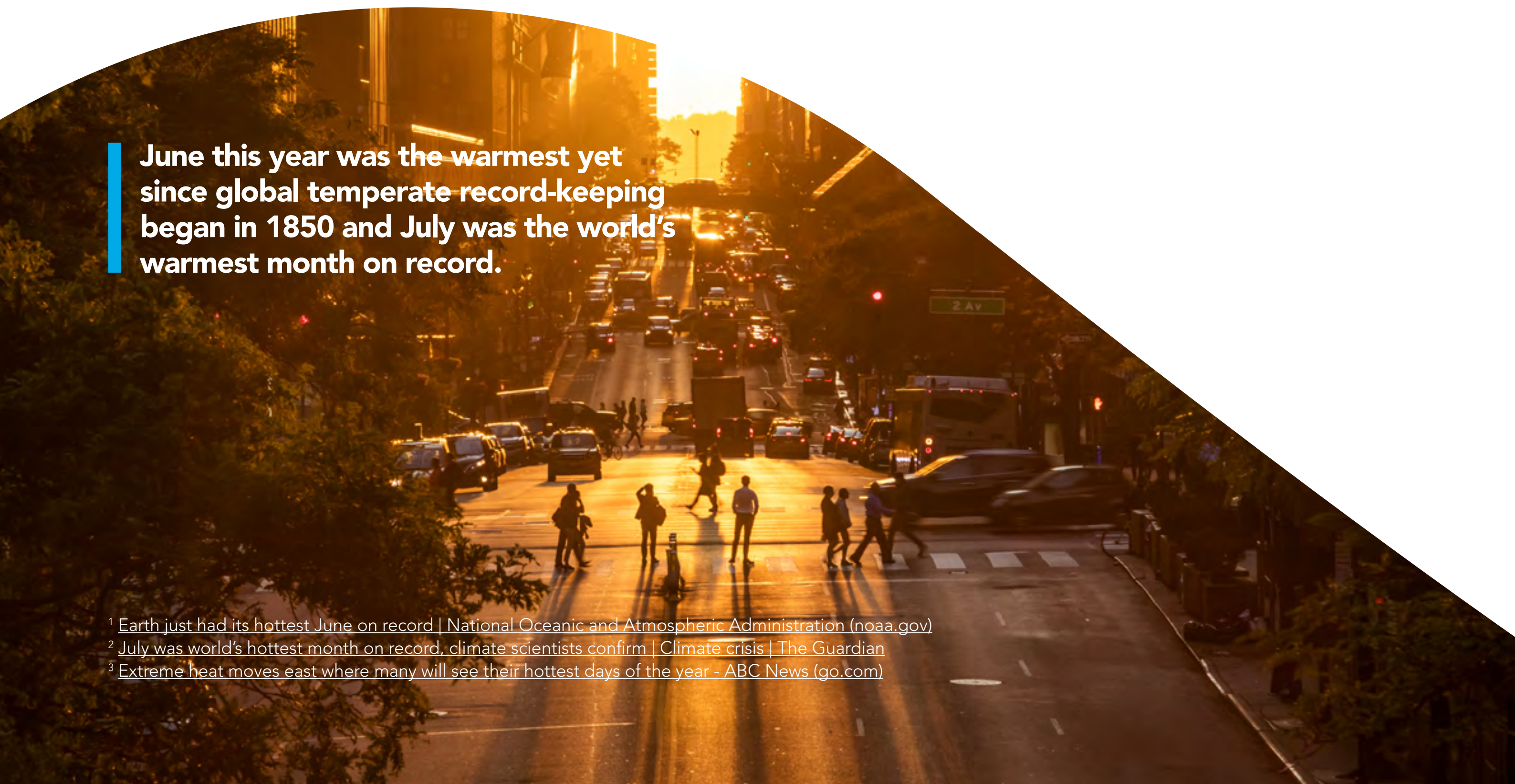
While rates of inflation are beginning to decline, they nonetheless remain elevated in many countries – and the real rates often remain higher for those on lower incomes.

We strongly believe in the benefits of active investment, both in the sense of actively choosing where to invest but also in the sense of being actively engaged with those companies in which we invest.

During this period, we have once again given particular emphasis in our engagements to the role that companies can, and should, play in supporting their employees. The question of who a company employs, and how it treats its employees, both direct and indirect, is a matter over which company management have direct control.

While rates of inflation are beginning to decline, they nonetheless remain elevated in many countries – and the real rates often remain higher for those on lower incomes. As a result, we continue to question and challenge companies' support for lower-paid employees. On a related theme, we also explore corporates' support for their employees' mental well-being – a matter which has grown in importance.

We thank our investors for entrusting us with their capital. We strongly believe in the benefits of active investment, both in the sense of actively choosing where to invest but also in the sense of being actively engaged with those companies in which we invest. To re-orientate our economies to enable the attainment of the SDGs, we believe it is necessary to work with a wide range of companies. Change is not straightforward; it takes time, and it is rarely linear. However, through ambition and perseverance, we are confident we can collectively play our part. To that end, we hope you enjoy reading our activity report on the first six months of 2023.



June this year was the warmest yet since global temperate record-keeping began in 1850 and July was the world's warmest month on record.

[1] Earth just had its hottest June on record | National Oceanic and Atmospheric Administration (noaa.gov)
[2] July was world's hottest month on record, climate scientists confirm | Climate crisis | The Guardian
[3] Extreme heat moves east where many will see their hottest days of the year - ABC News (go.com)

Federated Hermes SDG Engagement Equity Strategy overview

The Federated Hermes SDG Engagement Equity Strategy has the dual purpose of generating investment returns for clients (in excess of its reference benchmark) *and* creating real-world impact through purposeful engagement with investee companies.

Engagement seeks to be beneficial for both companies held in the portfolio and society at large – supporting efforts to attain the UN Sustainable Development Goals (SDGs).

What are the SDGs?

The SDGs, created by the United Nations, are a universal set of goals, targets and indicators for global development. By 2030 they aim to end global poverty, safeguard the planet and create prosperity for all.

There are 17 goals, 169 targets and 230 indicators, providing a 'sustainability roadmap' for the world.

The UN estimates that, if current trends persist, by the end of this decade,

575 million people will remain trapped in extreme poverty

Every company is affected by, or can contribute to, at least some of these goals – and can often benefit society and its own business by doing so. Attaining these goals means reducing harm and finding ways to generate positive impacts. It requires company boards and management teams to be bold, imaginative, and ambitious.

We believe it is imperative that all parties – from the public and private sector, as well as providers and users of capital – heighten their ambitions and double their efforts. While the first period of the SDG agenda has hit significant headwinds, there remains scope for optimism.

At the halfway stage towards realising the ambitious 2030 Agenda for Sustainable Development, the world is a long way off-track. The UN estimates that, if current trends persist, by the end of this decade, 575 million people will remain trapped in extreme poverty and global temperatures will reach or exceed the critical 1.5°C tipping point soon thereafter[4].

We believe it is imperative that all parties – from the public and private sector, as well as providers and users of capital – heighten their ambitions and double their efforts. While the first period of the SDG agenda has hit significant headwinds, there remains scope for optimism. Strong partnerships are needed, and we intend to play our part.

Opportunities for impact

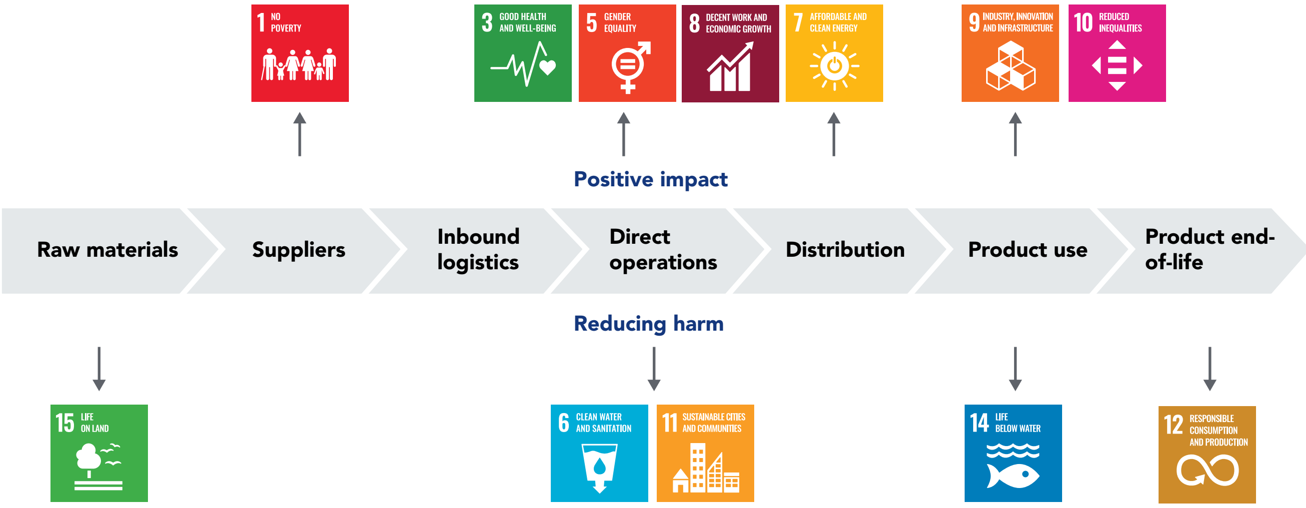
No company is an island. Every business is uniquely placed to impact real lives, due to its position within communities, direct relationships with employees, and connections with suppliers. Importantly, as investors, we can influence a company with regard to what business it does, and how it does it.

We have assessed that approximately

40% of the **169**

targets are relevant for dialogue between investors and corporates.

[4] Halfway there: 5 ways the UN is turbocharging the race to the SDGs | UN News



By engaging constructively and patiently with the company, we can play a critical role in bringing about positive changes. We can act as catalyst and convenor, play an important role in influencing capital allocation and hold management accountable for delivering on its promises.

We believe there are three characteristics required for genuinely impactful investor engagement:

- Be **purposeful**.

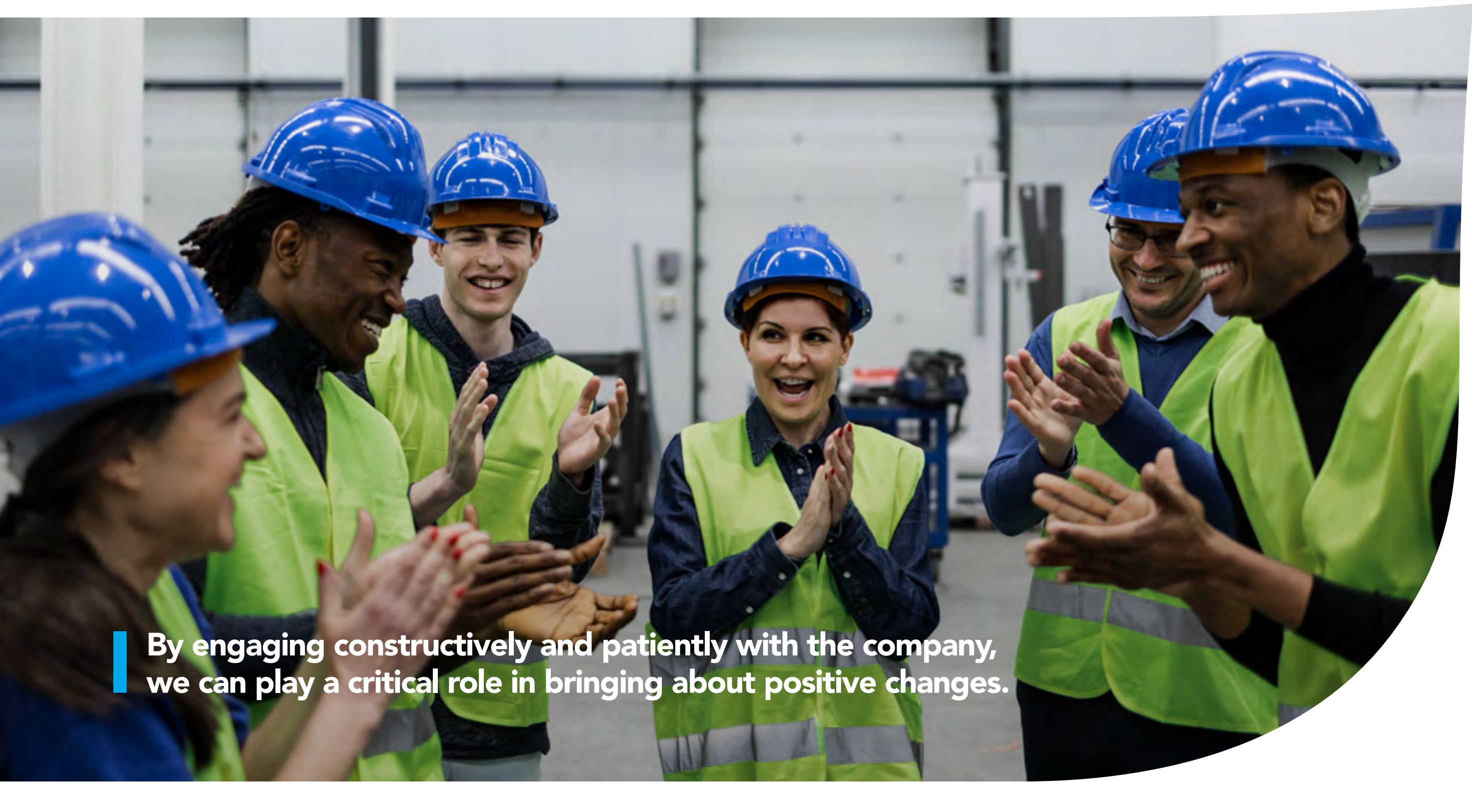
  Identifying an engagement thesis at the outset allows for an intentional dialogue with a clear purpose – namely realising positive outcomes that are beneficial for society and the business too.

- Be **informed and constructive.**

  Requests need to develop from a real understanding of a company's particular business model and geographic footprint, rather than being derived from one-size-fits-all frameworks.

- Be **persistent – successful engagement takes time**

  Meaningful results worth pursuing are those also worth waiting for.



Investment commentary H1 2023

Hamish Galpin Lead Manager

Positive returns for global equity markets as a whole was a welcome relief from the significant falls for both equities and bonds in 2022. On the face of it, stocks at the lower end of the market have not done as well in comparison to large caps (Our benchmark, the MSCI ACWI SMID Cap Index, was up 6.7% in H1 2023, compared to the S&P 500's 15.9%) but performance has once again been dominated by a small number of predominantly Information Technology stocks. However, during the period the S&P 500 Equal Weight Index – which weights all constituents the same, regardless of the size of the company or sector – returned 6.0% during H1 suggesting that small and mid-cap (SMID) stocks haven't done as badly after all, in comparison with most other segments[5].

To anyone kind enough to listen, I had postulated at the start of 2023 that it would be a good year for 'bottom-up' stock pickers like ourselves. This view was driven by the fact that the long period of artificially low interest rates had finally come to an end and the ensuing withdrawal of liquidity would result in a greater focus on fundamentals (as opposed to market themes and factor-driven investment). While this had not started to show through in any meaningful manner in the first few months of the year, it certainly did after the collapse of Silicon Valley Bank. We saw a 300bps boost to relative performance in the ensuing six weeks and maintained it through to the end of the quarter. Quality stocks were back in favour.

We outperformed most noticeably in Health Care and Industrials; areas in which Federated Hermes' SMID strategies have often performed strongly. These sectors are ripe for finding high-quality differentiated businesses. Underperformance was most pronounced in Information Technology, where keeping up with the 20%+ rise in the sector over the period was always going to be a challenge – our IT stocks are more slow-burn industrial than whizzy consumer.

Geographically, almost all the positive performance was in the US where the Strategy's exposure to the better-than-expected economic backdrop in general, and the housing sector in particular, were beneficial to relative performance: Simpson Manufacturing, Eagle Materials and Fortune Brands Innovations, all building products companies, were top-five performers.

There was a predominance of interest-rate sensitive stocks among the underperformers, led by our only US bank, Chicago-based Wintrust Financial. Other stocks included Retail Opportunities Investment Corp (Real Estate), Molten Ventures (Venture Capital) and Reinsurance Group of America. That said, the Strategy is structurally underweight Financials – there is less SDG engagement to do – so the sector overall contributed 35bps to relative performance.

We did not buy any new stocks in H1, nor did we make any complete disposals. We increased the positions in three stocks which were new in 2022: PTC, Viscofan and Equifax. Techtronic Industries was also an addition after we had the chance to evaluate the short-seller report issued on it and talk to management. We also took advantage of a technical situation in Breedon, driven by its move from the AIM market to the main market in the UK, to add to the holding.

We trimmed positions where good share price performance made holdings too large (Simpson and Burkhardt Compression were examples of this). We also trimmed where the engagement case was seen to have weakened or where progress was not as good as we had hoped.

We maintain the view that the investment backdrop is more constructive for us now than it has been for some time, driven by more normal volatility levels (having been too low prior to Covid-19, limiting performance potential) and a greater focus on stock fundamentals. While economic growth is improving, it is nonetheless low, but this favours more nimble SMID stocks that can take market share from their larger cap peers. Altogether, a favourable backdrop, we think, save for the outlier scenario of a debt-driven recession.

Past performance is not a reliable indicator of future performance.

Positive returns for equity markets as a whole in the first half of 2023 are a welcome relief from significant falls for both equities and bonds in 2022.

[5] Bloomberg as at 30 June 2023

Engagement highlights – H1 2023

Engagement on pay equity

We have consistently prioritised engagement with investee companies on the question of Decent Work[6] for two reasons:

a) Management teams have control over who they employ and how they treat their workforce.

b) There is ample evidence to demonstrate that companies which value their employees (in financial and non-financial terms) out-perform[7].

The onset of the global pandemic during 2020 led us to step up our focus on Decent Work. For the first time in decades, progress on poverty alleviation and gender equality took a step back. In addition to creating huge uncertainty for millions of workers; the response to Covid exacerbated pre-existing health, gender and financial inequalities. These schisms have expanded further on the back of the rise in inflation since 2022. Lower-paid workers have been disproportionately affected by these headwinds.

Against the wider context of an ongoing tightness in the labour market and growing skills gaps across a multitude of industries, we're engaging with companies on both horizontal and vertical employee mobility.

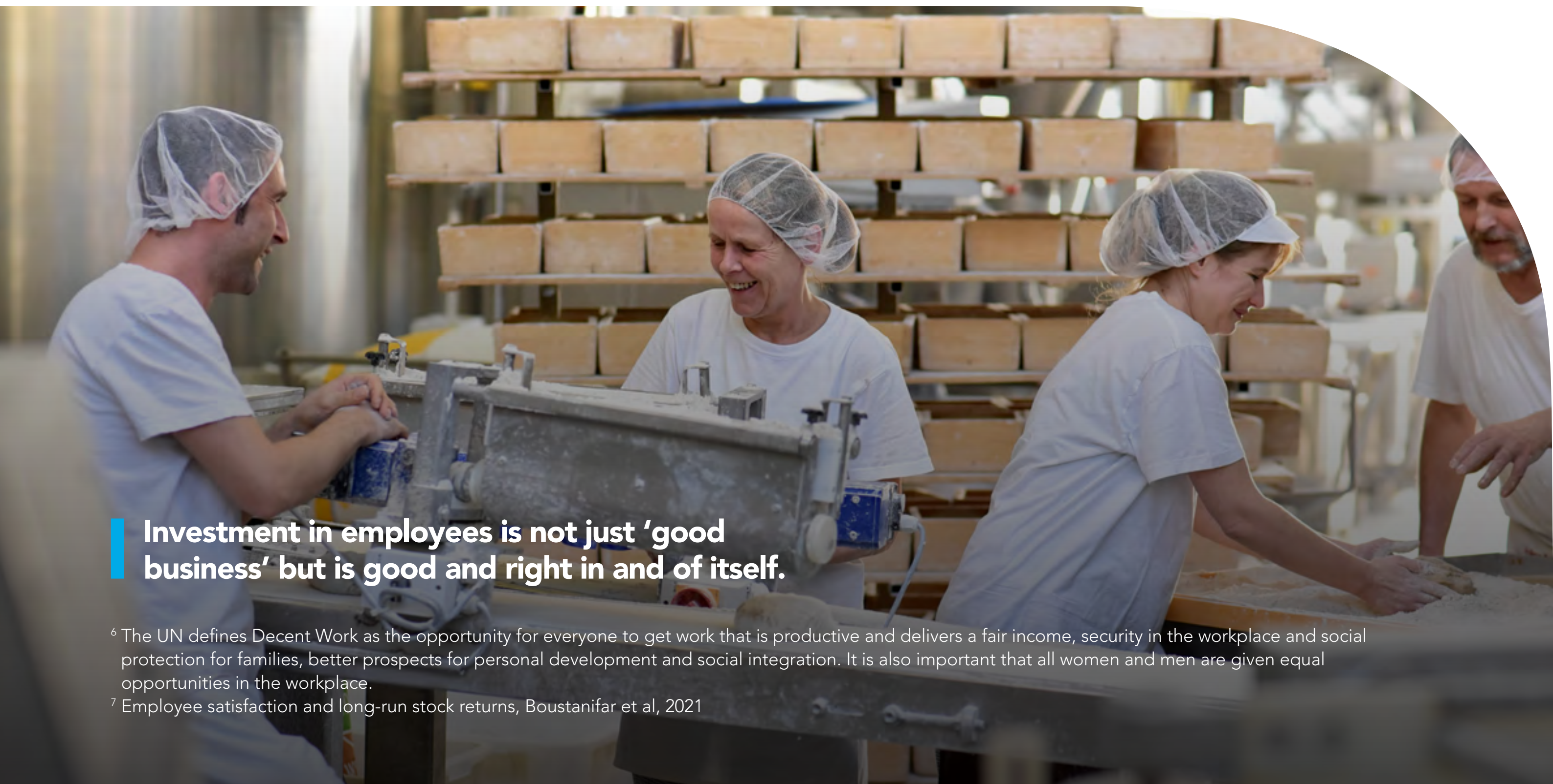
Our view is that a company should actively provide decent work opportunities by expanding its recruitment pools and ensuring a greater equality of opportunity for promotion within. It also should invest in training and development, enabling upskilling and redeployment. Fundamental to all of this is the recognition that a decent income, in the form of a living wage, is the foundational element to Decent Work.

In January 2023, we wrote to the CEOs of many our holdings to initiate or build upon existing engagements on compensation for their lowest-paid employees. We contended that viewing the workforce as a strategic asset which needs safeguarding, maintaining and developing is a key ingredient for sustained success. Furthermore, we argued that it is incumbent upon all businesses to ensure that its employees are, to the best extent practicable, provided a decent income which affords them a dignified standard of living.

As one investee company explained to us, its approach to recruitment and managing its workforce may cost more but they believe it has significant pay back because everyone is pulling in the same direction. We share this view.

Another holding, LKQ, which has upped its investments in its workforce, went so far as to cite in its earnings call a month after our letter that "companies with engaged employees are 23% more profitable… so from a business perspective, positive employee engagement is critical, but importantly, it's the right thing to do for our most important asset: our people!". Again, we wholeheartedly agree with this sentiment. Investment in employees is not just 'good business' but is good and right in and of itself.

We can point to specific examples of companies investing in their employees' salaries and benefits over the past few years. We have seen employee satisfaction increase, staff turnover decrease and operational savings realised as a result. We are also aware of other companies that have not made adequate investments. This in turn exacerbated their struggles with attraction and retention, creating unplanned additional costs. We will therefore continue to engage with these companies on this agenda and press for positive change.



Investment in employees is not just 'good business' but is good and right in and of itself.

[6] The UN defines Decent Work as the opportunity for everyone to get work that is productive and delivers a fair income, security in the workplace and social protection for families, better prospects for personal development and social integration. It is also important that all women and men are given equal opportunities in the workplace.
[7] Employee satisfaction and long-run stock returns, Boustanifar et al, 2021

SSP Group: The largest employer in the Strategy is SSP Group – the world's second-largest travel food and beverage concessions operator. Effectively in hibernation during the initial period of the pandemic, SSP has been rapidly hiring in 2022 and 2023. As at the end of March 2023, the company employed about 37,000 people – an increase of 10,000 from 12 months earlier.

The company is in essence a people business. Its employees serve millions of customers each year in airports and railway stations around the world. Its ability to create and sustain long-term partnerships with clients and partner brands relies on its teams delivering a commercially viable and sustainable offer. To that end, retaining core talent in what can be a very seasonable business requires focus.

Employee turnover is high (c.40% when seasonally adjusted, or >100% in absolute terms) and average salaries are a modest £19,500. **Pay increases for the lowest paid in 2022 were up 6% vs. 3% for the wider workforce** and supportive benefits were expanded too. The company's labour costs are roughly 30% of sales.

Our conservative assumptions[8] for SSP's UK business (28% of sales in FY22) suggest that moving its approx. 8,800 UK employees to at least a living wage level (as per the Living Wage Foundation[9]) would cost about £15m (assuming 60% of employees are currently paid the UK minimum wage which is known as the UK National Living Wage). While this cost is immediate, we believe that there is scope to realise cost savings from turnover reductions and like-for-like revenue gains from more engaged and productive employees. If voluntary turnover were to reduce to 30% annually, then the saving from this change alone could be upwards of £5m each year. Recognising that many of the benefits are hard to quantify, we would suggest that over the medium term the potential benefits are greater.

Pleasingly, the company's management team, led by CEO Patrick Coveney (joined March 2022) recognises this correlation. During a meeting in Q2 2023, the **CEO committed to continue to raise pay for the company's lowest-paid employees at a higher rate than for the wider workforce in the coming years.** Costs will be passed on through pricing and absorbed through productivity enhancements achieved through deployment of further technological investments. We continue to engage with the company on this issue and the practical and short-term commercial challenges of moving to a Living Wage Plus model of employment[10].

Other notable actions:

- Breedon Group (UK building materials): made two *ad hoc* payments of £400 to approximately 3,000 employees (c.80% of the total workforce) during 2022.
- Eagle Materials (US building materials): Undertook a living-wage gap analysis during 2022, covering all its operations in every city and state. It indicated the company's average hourly pay is nearly 20% above independent living wage figures (using the MIT Living Wage calculator).
- RPM (US speciality chemicals): In 2022, salaries in the US for its bottom-quartile employees increased 13%, while the top three quartiles increased 7.4%. Included in the top three quartiles are executive/senior management, whose salaries increased 6.9%.
- Vistry (UK housebuilder): in April 2022 the company put in place a temporary cost-of-living allowance of up to 3.75%, ensuring that the lowest-paid employees received the most support. These allowances became a permanent part of all annual salaries under £60,000 from January 2023.

[8] We have assumed 60% of UK employees are paid a minimum wage and calculated wages using personnel expenses – executive director compensation / number of employees. For costs of turnover, we have used a 30% of average salary cost.
[9] The Living Wage Foundation is an NGO whose purpose is to encourage employers to play their part in tackling in-work and post-work poverty and provide a decent standard of living by paying the real Living Wage, adopting Living Hours and Living Pensions as well as wider good employment practices.
[10] The Living Wage Plus is basically a full bag of extras on top of the basic Living Wage. The extras will not be added to the Living Wage, but users can pick components, such as car ownership, expenses for cinema/culture, eating out, the provision of care.
[11] **The Science Based Targets initiative (SBTi)**: Established in 2015, the SBTi is designed to help companies to set greenhouse gas (GHG) emission reduction targets in line with climate science. The initiative defines and promotes best practices in emissions reductions and includes a team of experts to provide companies with independent assessment and validation of their targets.
[12] Company reports

Company engagement highlights

Below are some other specific highlights from our engagement activity during the first half of 2023.

Breedon

(UK building materials)

It was a positive first six months of the year for Breedon from an ESG perspective. In May, the company was admitted to the Premium Listing Segment of the UK Main Market and the company also made progress towards meeting its commitment to the Science-Based Targets initiative[11]. Most excitingly, the company is a key partner in the launch of the Peak Cluster initiative. This is an innovative collaboration to capture, transport and permanently store CO_2 emissions from the cement and lime industry in Derbyshire and Staffordshire and is expected to remove more than 3 million tonnes of CO_2 each year by 2030, a move that will reduce UK emissions from these industries by 40%[12].

On the topic of its cement business, the group managed to achieve a combined 50% fossil fuel replacement rate in the first six months of 2023 with its plant in Kinnegad, Ireland at times exceeding 90%. We visited its much older Hope cement plant in June this year – the oldest cement plant in Britain. This site is almost a century old and does not have the capability to achieve such high levels of alternative fuel usage. Nonetheless, we were highly impressed at the efforts that have been made to ensure the site operates as reliably and efficiently as is practicable – it has achieved plant mastery status for four years in a row. We were further impressed at on-site management's passion for restoring quarried land to nature as a way of achieving greater local biodiversity. While alternative fuel usage at Hope may have a ceiling, the company's trials of graphene-enhanced cement could create significant emissions savings. We view this as a positive when coupled with the impressive progress being made in adopting carbon capture and storage through the Peak Cluster initiative.

We applaud the progress being made and continue to engage on the company's human-capital management strategy in light of its aging workforce (43% of employees are aged over 50) and the mental health stresses in the construction industry.

Wintrust

(US regional bank)

We met with the new CEO and veteran COO of this Chicago bank not long after the collapse of Silicon Valley Bank (SVB).

On discussing the bank's commercial real estate exposure and deposit-flight risk following the collapse of SVB, we were reassured that that bank's long-term prudent approach to risk remains intact.

We reflected again on the bank's role in enabling financial inclusion in Chicago, where approximately 7% of residents remain unbanked[13]. Positively, 50% of its retail locations opened in the previous five years have been in lower-income communities. We will continue to explore this further – and are confident that the bank is more focused on actions, rather than words, with respect to this agenda.

Techtronic Industries

(Global power tools manufacturer)

It has been a busy six months for Techtronic – the self-styled Tesla of the power tools industry. The company was the subject of a short-seller report in February and latterly a congressional commission examining human rights issues in China.

On governance matters, we had a positive dialogue with an independent board member during which we encouraged improved board independence and diversity.

On the allegations of forced labour within its personal protective equipment (PPE) glove production supply chain, the company reiterated that it only partners with suppliers that commit to ethical labour practices throughout supply chains, and ensures no forced labour is used. They contend they have found no evidence to support the claims made to the contrary. Nonetheless, we will explore further what additional due diligence processes the company has put in place to provide itself with the greater levels of reassurance needed that these PPE products are indeed free of forced labour (and – beyond forced labour – are being produced within factories with which Techtronic and Milwaukee would be proud to be associated).

In May we had the pleasure again of visiting the company's Milwaukee Tool Innovation Centre (we last visited in 2018) where we spent the day with the long-tenured management team (together for 17 years). Overall, we were once again impressed by the company's culture and commitment towards innovation – the former evidenced by its Glassdoor rating continuing to exceed most of the more lauded US tech companies.

It is clear that Techtronic and Milwaukee products are generating energy and emissions savings and also contributing to fewer workplace injuries at construction sites. By sustaining the same battery interface (unique to its products), the company is avoiding unnecessary product obsolescence and, in so doing, enabling users to extend the life of existing products and batteries. Nonetheless, we continue to explore with the company the potential to expand (without cannibalising new product sales) its recycling, repair and remanufacturing proposition.

[13] BankON_Strategy_Final-082020.pdf (bankonchicago.com)

Progress of our engagements in H1 2023

2023 H1 engagement overview

% of companies at period-end engaged
94%

Total engagement actions
108

Total meetings voted
45

SDG specific engagement actions
98

Live objectives
149

Number of meetings voted against management on at least one resolution
19 (42%)

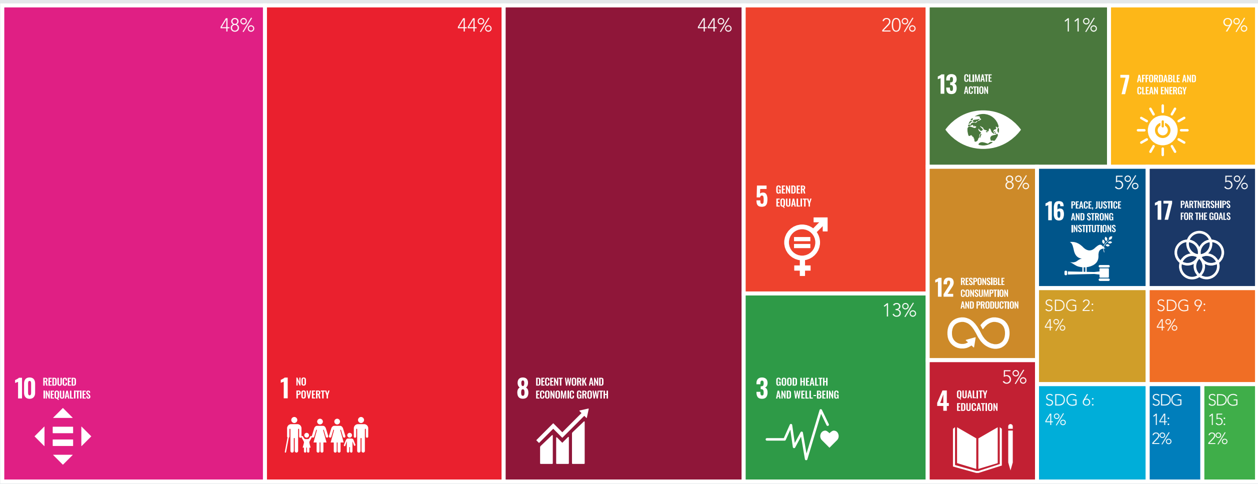
Total resolutions voted against
31 (6%)

% companies with progress on objectives
36%

Completed objectives
10

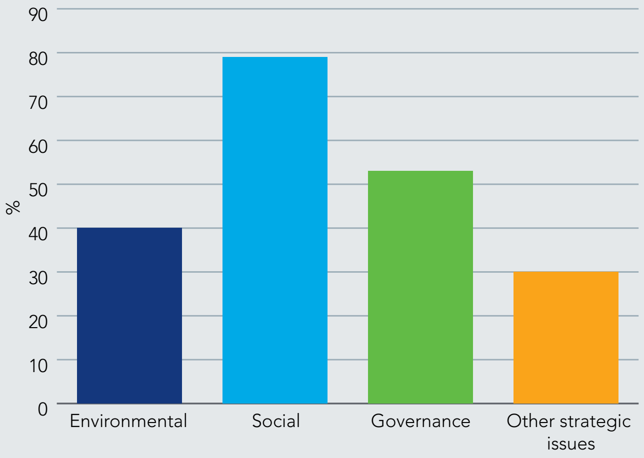
Source: Federated Hermes, as at 30 June 2023.

Figure 1: H1 2023 engagement actions per SDG



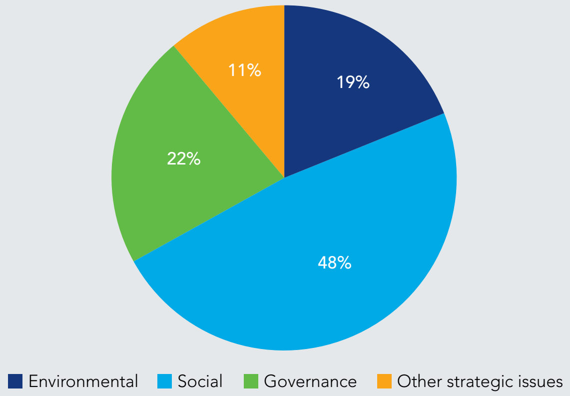
Source: Federated Hermes, as at 30 June 2023.

Figure 2. Relative thematic focus for engaged companies (percentage of companies engaged per theme)



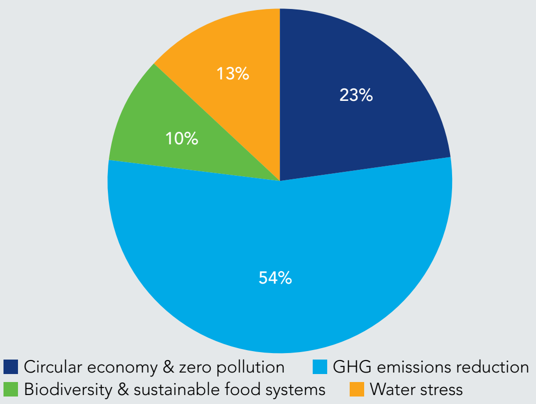
Source: Federated Hermes, as at 30 June 2023.

Figure 3: Relative focus for engaged companies (proportion of total engaged issues/objectives)



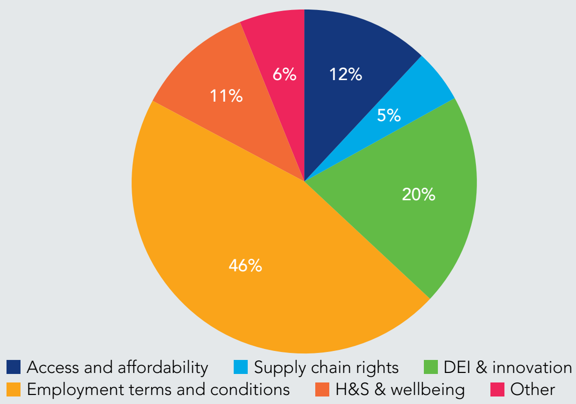
Source: Federated Hermes, as at 30 June 2023.

Figure 4: Relative focus of environmental engagement during H1 2023 (proportion of total environmental issues/objectives engaged)



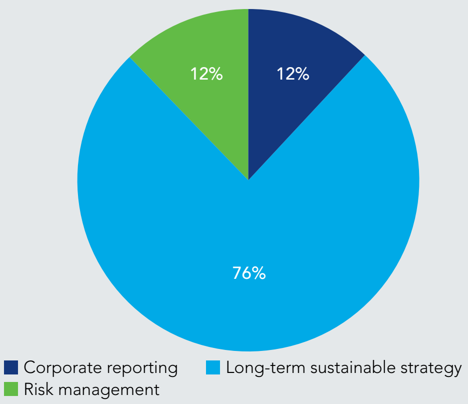
Source: Federated Hermes, as at 30 June 2023.

Figure 5: Relative focus of social engagement during H1 2023 (proportion of total social issues/objectives engaged)



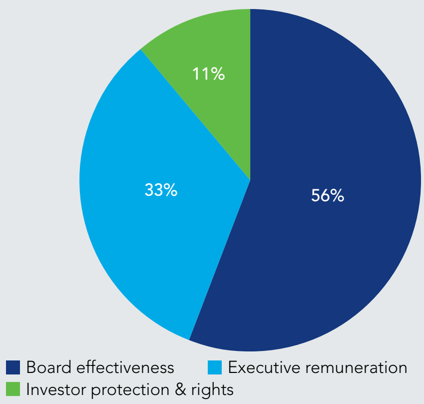
Source: Federated Hermes, as at 30 June 2023.

Figure 6: Relative focus of strategy, risk and communications engagement during H1 2023 (proportion of total strategy, risk and communications issues/objectives engaged)

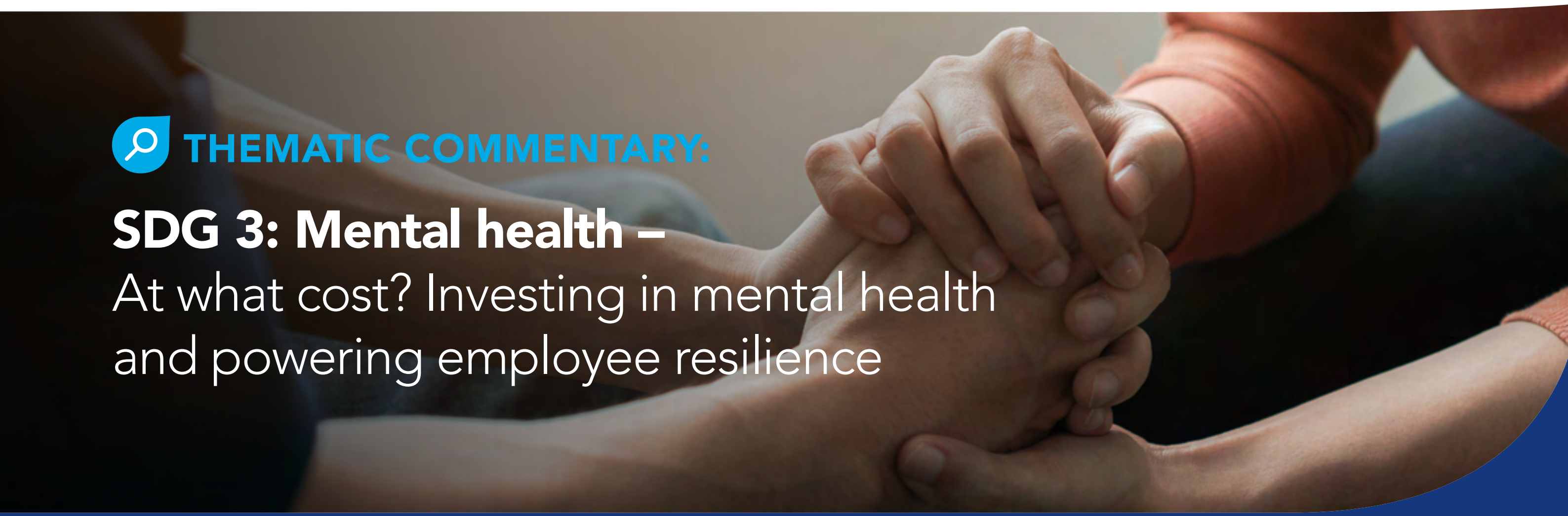


Source: Federated Hermes, as at 30 June 2023.

Figure 7: Relative focus of governance engagement during H1 2023 (proportion of total governance issues/objectives engaged)



Source: Federated Hermes, as at 30 June 2023.



THEMATIC COMMENTARY:

SDG 3: Mental health –

At what cost? Investing in mental health and powering employee resilience

SDG 3: Ensure healthy lives and promote well-being for all at all ages

Target 3.4 aims to reduce by one-third premature mortality from non-communicable diseases through prevention and treatment and promote mental health and well-being.

3 GOOD HEALTH AND WELL-BEING

What does SDG 3: the global goal focused on health, first bring to mind? It's time to take a broader view.

We've heard the adage 'mental health is as important as physical health'. Yet living free from overwhelming stress, anxiety or depression can be thought of as a 'nice-to-have' at work, not a necessity to optimise business resilience and growth. Worse, it may not be thought about at all.

The cost of poor mental health to the private sector in the UK is estimated to be £43-46bn in 2020-21, an increase of 25% since pre-pandemic estimates in 2019[14].

Deloitte suggests employers can expect a return of £5.30 on average for every £1 spent, through benefits such as improved worker engagement, enhanced productivity, increased innovation, and sustainability[15].

Only around 40% of companies in the SDG Engagement Equity Strategy explicitly mention mental health as an important concern within corporate disclosures.

But for some sectors declining mental health is particularly acute. Here, we explore the companies that are uplifting more than just the bottom line.

AMN Healthcare wanted to better understand the impact that depleted mental health had on the nursing sector as a whole, so in 2022/23 it undertook a survey of

18,000 nurses

Key workers, such as those in the nursing and construction sector, are fighting on the frontlines of mental ill health.

Tragically, on 18 January 2022, Michael Odell, a 27-year-old intensive-care nurse committed suicide. His death was attributed in part to the emotional fallout from the gruelling two years of working through the pandemic[16]. Unfortunately, his story is not unusual[17].

US-based AMN Healthcare wanted to better understand the impact that depleted mental health had on the nursing sector as a whole, so in 2022/23 it undertook a survey of 18,000 nurses[18]. It revealed, among other factors, that career satisfaction, intention to leave roles, and mental health and well-being issues have become significantly worse since the height of the pandemic.

CEO Cary Grace spoke out about the company's leadership commitment to mental health in the workplace and faced up to the problems facing the sector. "This really underscores the continued mental health and well-being challenges the nursing workforce experiences post pandemic[19]."

Building on the comprehensive support it provides to its corporate employees which spans mental, emotional, physical and financial wellbeing, the company has upped the support available to its frontline healthcare professionals.

AMN has provided access to employee assistance programmes, on-demand mental health resources through non-profit partners, and guaranteed sick pay while quarantined.

[14] Deloitte (2022) 'Mental Health and Employers: The Case for Investment – Pandemic and Beyond.' Online at http://www2.deloitte.com/content/dam/Deloitte/uk/Documentas/consultancy/deloitte-uk-mental-health-report-2022.pdf.
[15] Deloitte, ibid.
[16] Chatterjee, R, 'A nurse's death raises the alarm about the profession's mental health crisis' (2022), https://www.npr.org/sections/health-shots/2022/03/31/1088672446/a-nurses-death-raises-the-alarm-about-the-professions-mental-health-crisis, retrieved July 2023.
[17] The Office for National Statistics (ONS) in the UK identified female nurses as having a risk of suicide 23% above the risk of women in other occupation, and this number has no doubt likely risen since reported in 2017, https://www.ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/deaths/adhocs/009209suicidedeathsamongnursesaged20to64yearsdeathsregisteredinenglandandwalesbetween2011and2017, retrieved July 2023.
[18] AMN Healthcare, 2023 AMN Healthcare Survey of Registered Nurses The Pandemic's Consequence (1 May 2023), https://www.amnhealthcare.com/amn-insights/nursing/surveys/2023/, retrieved July 2023.
[19] Para 4, Mandowara, Khushi and Leo, Leroy, 'One-third of US nurses plan to quit profession, survey shows', 1 May 2023, Reuters, https://www.reuters.com/world/us/one-third-us-nurses-plan-quit-profession-report-2023-05-01/, retrieved July 2023.

Tellingly, the company's clinician team placed more than 14,000 care calls to its healthcare professionals during 2022 to ensure they had the necessary support.

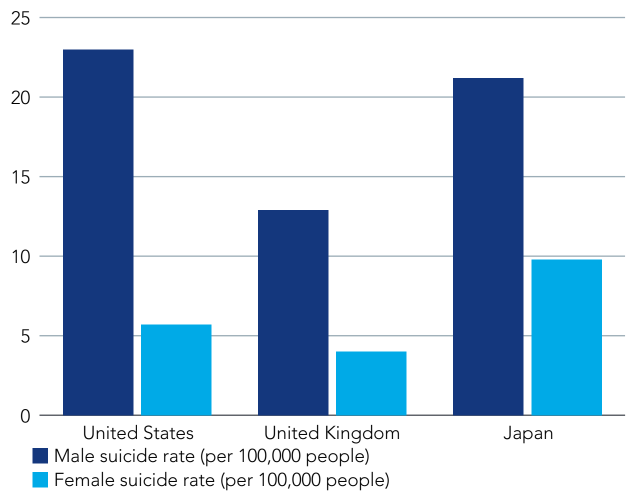
AMN also directed financial support to those in need through its AMN Caring for Caregivers Fund which seeks to ensure healthcare professionals receive financial support for certain events such as life-threatening or serious illnesses, natural disasters, funeral costs, or other events causing financial strain.

AMN's leadership – led by a clear stance from the CEO – demonstrates best practice and shows what committed mental health support can look like at work.

Under pressure

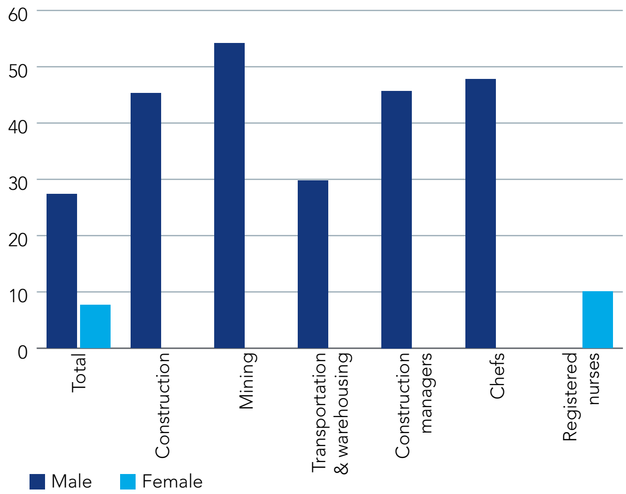
It is unfortunately common knowledge that men are far more likely to die by suicide than women – four times as likely in the United States. Indeed, suicide is the leading cause of death in England in adults below the age of 50.

Figure 8: Suicide rates (per 100,000 people)



Source: OECD

Figure 9: Suicide rates by industry (per 100,000 people)



Source: US Centers for Disease Control and Prevention (2016 data)

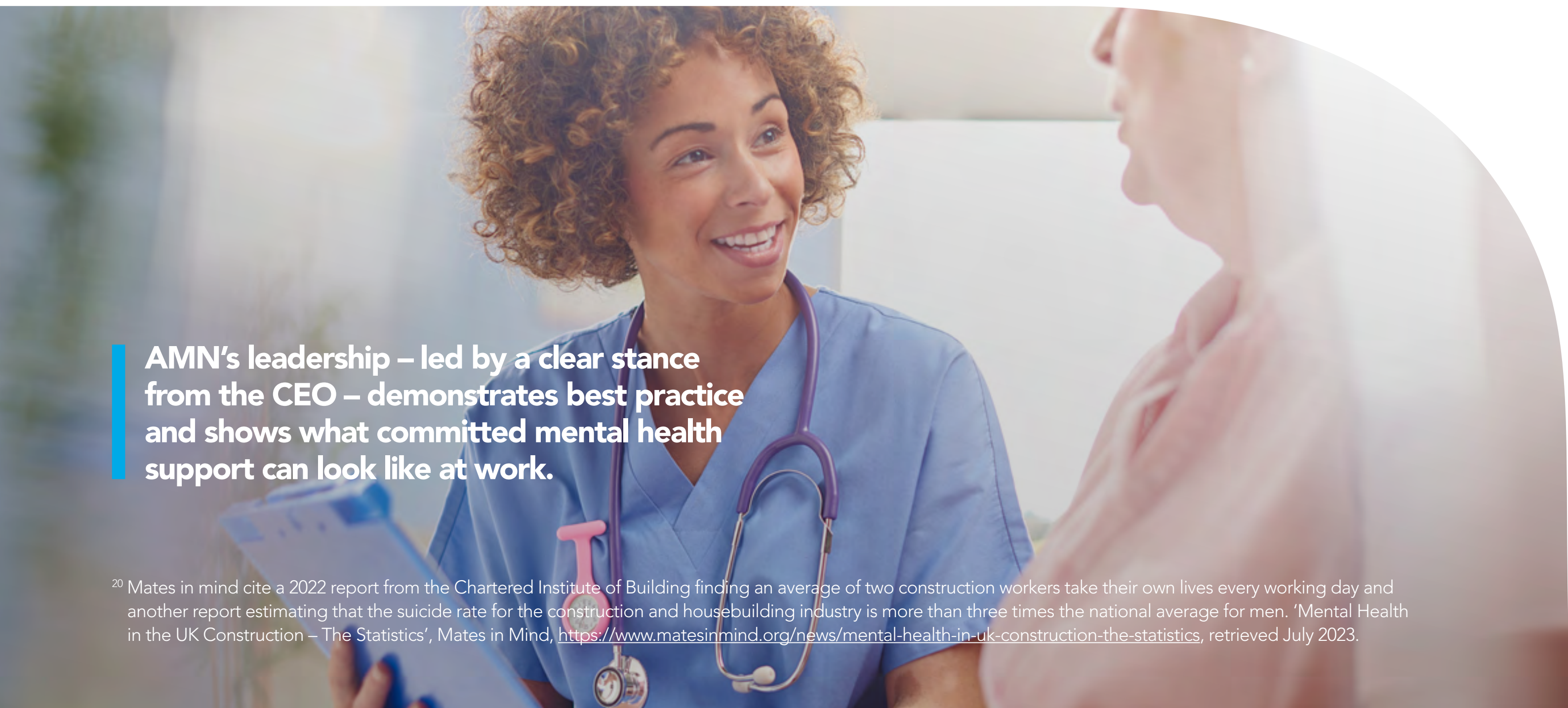
Less commonly known is that in construction – a male dominated industry – men are three times more likely to die by suicide than the national average. In reality, two people employed in construction in the UK die by suicide every working day – 700 men a year[20].

Similar to nursing, construction work has a variety of pressures from tight contracts to long hours, time away from loved-ones and managing budgets, not to mention the added stresses of the pandemic and now the rising costs of supplies.

However, additionally, within construction lies a 'macho' culture which prevents many workers from seeking help. Instead, many turn towards alcohol, drugs or gambling to numb their feelings.

Charities like Mates in Mind are raising awareness of the issue – and, consequentially, construction firms are finally talking.

For example, trained mental health first aider, Manchester-based Rob Muldoon, recalls thinking he was 'failing' when a rainy day stole away a day of work on the building site nine years ago.



AMN's leadership – led by a clear stance from the CEO – demonstrates best practice and shows what committed mental health support can look like at work.

[20] Mates in mind cite a 2022 report from the Chartered Institute of Building finding an average of two construction workers take their own lives every working day and another report estimating that the suicide rate for the construction and housebuilding industry is more than three times the national average for men. 'Mental Health in the UK Construction – The Statistics', Mates in Mind, https://www.matesinmind.org/news/mental-health-in-uk-construction-the-statistics, retrieved July 2023.

In our Strategy, Breedon has started raising the topic of mental health at work, delivering a Health and Wellbeing event and Wellbeing Framework.

"You've just got to switch yourself off," said the previously self-employed bricklayer.

"And all you're thinking is 'I've got to do this, I've got to do this, I've got to do this'. And then when you do get to the end of the day… you're in absolute pieces, and you've got to get home, get yourself sorted. And then try and do it all again tomorrow. And do it again the day after... and it's miserable, absolutely miserable.[21]"

In our Strategy, Breedon has started raising the topic of mental health at work, delivering a Health and Wellbeing event and Wellbeing Framework. In 2022 it trained eight Mental Health First Aiders at its Hope cement site and has trained a further three based at each of its' depots. Breedon does not yet explicitly acknowledge the higher risk that employees in the construction sector face in its disclosures. This is something we'd like to see in the future.

Possibly further along the journey is UK housebuilder Vistry which has scaled its mental health efforts significantly in the last few years.

It has a cohort of 204 mental health first aiders to support employees. They in turn are supported in quarterly mental health first aid meetings and all feedback is passed on and acted upon by its national mental health committee (each of Vistry's business units has a mental health committee, which feeds into the national committee).

Vistry also has internal digital resources and links to organisations, plus an employee assistance programme. Managers receive mental health awareness training and are expected to regularly check that team members feel comfortable with their workload.

Deconstructing macho culture in the construction sector, and normalising conversations about mental health, is no easy task. However, it is vital for leaders – particularly male leaders – to be the change they want to see and make it clear that it's time to talk.

We're asking for more

Health and wellbeing is affected not only by disease but also by social and economic factors such as housing, poverty and education – and these are all impacted in turn by mental health. Beyond the examples cited above, action is necessary across all sectors – both white and blue collar – to promote change.

Managers receive mental health awareness training and are expected to regularly check that team members feel comfortable with their workload.

In practice, fully integrating mental health into business strategies and reporting cycles takes time. Each company is at a different stage of the journey.

However, adopting a mental health workplace policy, and fostering a culture that encourages openness and dialogue on mental health, is an important step towards improving our collective mental health.

We will be asking for:

- All leadership teams to take visual ownership, fostering and building a caring culture.
- The promotion of employee assistance programmes (own and those offered by third parties).
- The training of line managers and supervisors in what to do when they spot an issue.
- The training of mental health first aiders.

There is clearly scope for companies to develop robust systems and step up their supportive practices to tackle mental health. We urge them to do so.

[21] Thomas-Alexander, Tiya, 'Like drawing blood from a stone' – construction's mental health struggle | Construction News, October 2021, https://www.constructionnews.co.uk/long-reads/like-drawing-blood-from-a-stone-constructions-mental-health-struggle-25-10-2021/, retrieved July 2023.

ENGAGEMENT COMMENTARY: LKQ

In a nutshell

LKQ is a global distributor of vehicle products, including replacement parts, used in the repair and maintenance of vehicles.

US$14.3bn
Market capitalisation (Aug 2023)

US$12.7bn
Revenue (FY22)

45,000
employees (FY22) of which 19.5% are female

Carbon intensity:
27.8 MT
Scope 1 and 2 greenhouse gas emissions per US$m of revenue (FY22)

Most pertinently for this note, LKQ is the largest recycler of automobiles in the world. Circularity is at the heart of its business model. In North America, its salvage operations recycle more than 90% of the materials from end-of-life vehicles.

LKQ's recycling activities intrinsically generate a positive environmental impact; and it is well positioned to sustain its commitment to automotive circularity as the proportion of electric vehicles (EVs) around the world increases.

Furthermore, the company has made meaningful steps to reduce its operational emissions footprint and enhance the livelihoods of the 45,000 people it employs.

Investment case

- Secular trend favouring alternative collision parts, in North America in particular.
- Long track record of execution by experienced management team.
- Scale enables superior part availability, ensuring improved reliability for customers.
- European alternative part utilisation under 10% suggests opportunity for LKQ to grow and penetrate the market through partnerships with key European insurers.

Theory of change

12 RESPONSIBLE CONSUMPTION AND PRODUCTION

Enterprise impact

In 2023, LKQ celebrated its 25th anniversary. The company has, through its salvage and recycling operations, generated significant positive environmental impacts over the course of its history to date.

The next 25 years, however, will see a fundamental change in the automobile market and vehicle population. EVs will slowly replace traditional internal combustion engine (ICE) vehicles and technology should further reduce the frequency of collisions.

As the total number of vehicles in operation shifts towards EVs, recycling and remanufacturing priorities will change. The battery is – by some distance – the most expensive component of an EV vehicle. This shift presents challenges.

Lithium-ion batteries, for example, need careful end-of-life management to avoid leaching of dangerous chemicals. Furthermore, the mining of the various metals needed for such batteries requires vast resources. So while EVs can reduce CO_2 emissions over a vehicle's lifetime (depending on the electricity used to power them); the batteries they require mean they start life with a large environmental footprint.

As the world's largest vehicle recycler, LKQ has shown a commitment to the circularity of materials for ICE engines. It is well positioned to expand these capabilities to cover EVs as well.

Operational impact

LKQ is a large operation, spanning 26 countries and about 45,000 employees. A large proportion of workers are paid by the hour and on modest incomes; many doing dangerous work.

As a result, there is significant scope for the company to reduce its own operational emissions footprint, and to address social inequalities by investing in its employees.

Practice of change

Since investing in LKQ we have had multiple interactions with management, including site visits, and have discussed a range of sustainability topics.

While the company has a track record of positive environmental impact, it is only recently that it has begun to formalise its sustainability strategy.

To that end, we welcomed the appointment in 2021 of the company's first Sustainability Director. Since this appointment, along with the appointment of a new Senior Vice President of Human Resources, the company has accelerated its commitments towards both its people and its operational impacts.

EV circularity

The average life span of an automobile today is in the region of 12 years, suggesting the transition to EVs will take decades. ICE vehicles are still forecast to hold about two-thirds of total global auto market share in 2030[22]. The emergence of EVs as a mass-market product is a recent phenomenon. One reason recycling capacity has lagged battery production is because an EV can run for years before its battery pack requires disposal. As a result, a non-closed battery loop is commonplace, leading to material waste and costly disposal. Nonetheless, 1.3 million batteries are expected to need repair or replacement in Europe by 2030 – and this figure is forecast to increase by 30% annually[23].

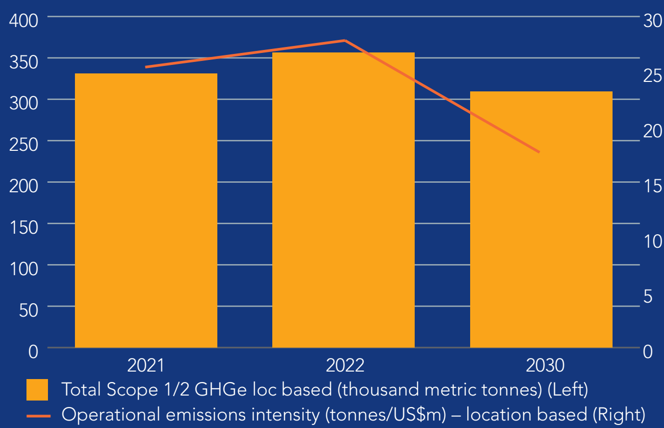
LKQ has made a number of strategic acquisitions in anticipation of this shift. The company has acquired hybrid battery remanufacturers GreenBean and Bumblebee, both of which specialise in repairing faulty battery cells and extending a battery's useful life. Over the longer-term, the company has signed a memorandum of understanding (MoU) with Korea Zinc to pursue the recycling of lithium-ion batteries in the US.

An EV battery's life span is typically seven to nine years. Replacement costs can be between US$8,000 and US$20,000, which poses a significant challenge to developing a second-hand EV market. However, LKQ's investment in remanufacturing hybrid batteries should help reduce this cost barrier – and there is potential to develop similar solutions to remanufacture EV batteries.

Operational carbon footprint

Despite a year-on-year increase in reported emissions in FY22, the company is making strides forward. LKQ has committed to a 30% emissions intensity reduction by 2030 vs. 2021 and a roadmap towards this target will be established by 2025. The company has set a target to become net zero by 2050. LKQ began measuring its Scope 3 emissions in 2023 (in addition to Scopes 1 and 2)[24].

Figure 10: 30% operational emissions intensity reduction by 2030 (vs. 2021)



Source: Company reports.

A large contributor to the company's operational emissions is its 14,000 vehicle fleet. It has begun to procure electric and bio-fuel vehicles – for example, 100 electric vans and 30 compressed biomethane trucks in the UK – which should help address this. However, we believe the company has the capacity to accelerate this transition. With current emissions reduction targets only set to modestly reduce absolute emissions by the end of the decade, we believe the company should heighten its ambition.

Workforce

The CEO has described the workforce as 'the heart and soul' of the company, and we have been struck by the vocal commitment of management towards its workforce.

[22] 'Explosive' growth means one in three new cars will be electric by 2030, IEA says - Carbon Brief
[23] LKQ Expects Major Savings in Cost and CO_2 from Traction Battery Repair and Remanufacturing - LKQ Corp
[24] **Scope emissions:** Scope 1, Scope 2, and Scope 3 is a classification system for greenhouse gas (GHG) emissions a firm creates through its operations, energy usage, and the wider value chain.

- Scope 1 emissions – All direct emissions from the activities of an organisation or under their control. Including fuel combustion on site such as gas boilers, fleet vehicles and air-conditioning leaks.
- Scope 2 emissions – Indirect emissions from electricity purchased and used by the organisation. Emissions are created during the production of the energy and eventually used by the organisation.
- Scope 3 emissions – All other indirect emissions from activities of the organisation, occurring from sources that they do not own or control. These are usually the greatest share of the carbon footprint, covering emissions associated with business travel, procurement, waste and water.

Of course, these words need to be supported by actions. **Reassuringly LKQ has raised its wage floor the last few years**, to US$14 in early 2021 and US$15 by the end of 2021. Its **average hourly starting wage in early 2023 was above US$18.** Wage increases for its hourly employees have outpaced the wider workforce in each of the last two years and US$1,000 was deposited in every United States employee's 401k pension plan during 2022.

Beyond basic pay, the company has introduced a number of meaningful benefits to help address any financial insecurities its employees may face. For example, it began to rollout an income advance scheme in the United States during 2023 – a benefit which evidence suggests has a meaningfully positive impact on reducing financial stress.

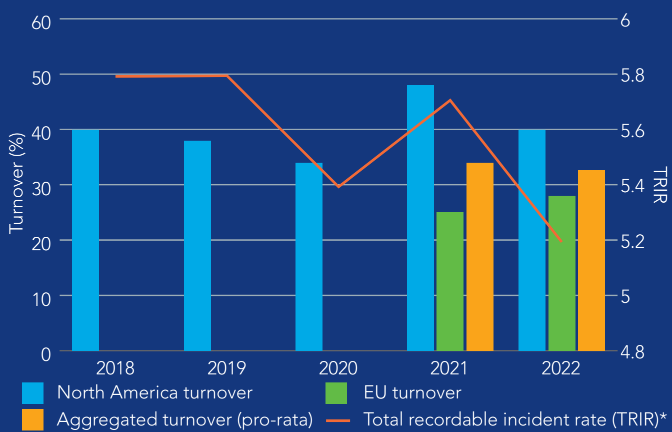
We believe LKQ's management team is genuinely committed to directing workforce investments in a such a way as to break inter-generational poverty – a common feature in many of the communities in which its sites are located.

The company's Joseph M. Holsten Scholarship fund for children of employees has been around for a number of years. In the past, however, the scholarship fund's outreach was modest. In 2023, the fund grew to US$1m and should support 400 beneficiaries per year (1% of the total employee population). The company has also reinforced its commitment towards US employees who wish to further enhance their own educational and career advancement journeys by increasing annual tuition reimbursement to US$5,000 per employee.

We were further heartened by the CEO publicly noting on a February 2023 earnings call that "positive employee engagement is critical, but importantly, it's the right thing to do for our most important asset, our people". We very much agree with this view and are sympathetic to the fact that cultural change takes time and results longer still.

Nonetheless, we observe that the company does operate with very high levels of staff turnover and accident rates – the two are typically highly correlated. Our view is that there remains much scope for improvement here: both as the management team continues to develop its genuine commitment in this regard and with substantive actions and investments. The results should be beneficial for staff but also for business: unnecessary turnover is costly; stressed employees are unproductive, and accidents incur insurance claims.

Figure 11: Turnover and accident rates

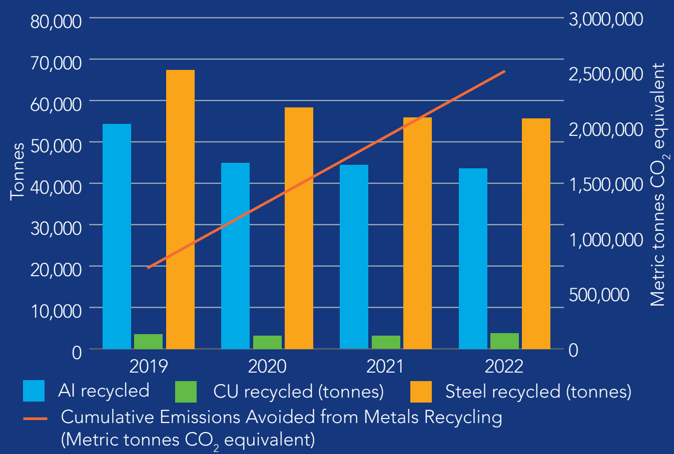


***incidents per 200,000 hours worked**
Source: Company reports.

Enterprise impact – avoided emissions

As the world's largest recycler of vehicles, the company's positive environmental impact is central to its business. LKQ procured 768,000 vehicles in 2022. From these vehicles it salvaged 90% or more of the materials. In terms of the metals alone, this process results in significant avoided emissions – displacing demand for primary production. But this reduction is only part of the story as fluids (fuel, motor oil to windshield washer) from the salvaged vehicles are reused, including in its own vehicles, and tyres are similarly sold or repurposed.

Figure 12: Emissions avoided from metal recycling (metric tonnes CO_2 equivalent)



Source: Company reports and Federated Hermes estimations.

Next steps

We have been pleased by LKQ management's commitment towards expanding its positive impact in emissions reduction, not least as the automotive industry evolves from ICEs to EVs. Nonetheless, **we wish to see additional change:**

- **Accelerated fleet transition with heightened (absolute) operational emissions-reduction goals.**
- **Ongoing investment in people (including pay) to aim for a Living Wage Plus employment model with expanded internal career development paths and an ongoing commitment to breaking the cycle of intergenerational poverty.**
- **A further concerted focus on health and safety with senior management accountability to drive down accident rates.**

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