Signatory of:

PRI Principles for Responsible Investment

Sparinvest

Sparinvest Responsible Investment Review

August 2015

In this edition:

- High Scores in UN PRI Assessment Report 2015
- Highlights of our UN PRI Transparency Report
- Climate Change – the Burning Issue
- Climate Change and Ethical Funds
- ESG in a Quant Fund – a Closer Look
- Voting Season 2015
- PRI in Person

Dear Investor

Reviewing the progress of our RI journey is something that we do at regular intervals at Sparinvest, looking for areas of strength and weakness and setting ourselves goals to maintain momentum and improve processes. In addition, we complete an annual UN PRI Transparency Report. This is a requirement for any UN PRI signatory, but we find it to be a useful marker along the way, helping us to establish how far we have come in implementing the Principles (ESG integration/exclusions/active ownership) across all asset classes.

The structured and uniform nature of the reporting questionnaire also enables UN PRI to give feedback to each company about its progress relative to peers, in an Assessment Report. In March 2015 we submitted our 2014/15 Transparency Report, and UN PRI has just issued its Assessment Report based on that. We are delighted to report that Sparinvest achieved A/A+ grades in all relevant UN PRI scoring modules.

You will find full versions of both the Transparency Report and the resulting Assessment Report on Sparinvest's websites, but the 'Score Card', top right, gives a brief overview.

Sparinvest 'Score Card' from UN PRI Assessment Report 2015

PRI Scoring Modules	Sparinvest 2014	Sparinvest 2015	Peer Group
Overarching Approach	A	A+	B
Listed Equity Incorporation	A	A+	A
Listed Equity Active Ownership	B	A	B
Fixed Income Corporates	A	A+	C
Fixed Income Gov't Bonds	A	A+	E
Property (Indirect SAM)		A+	D

Source Sparinvest: The 2015 PRI Assessment Results shown above are extracted from the full UN PRI Assessment Report 2015 for Sparinvest Group and are based on the responses given in Sparinvest's 2014 Transparency Report, both of which are available at Sparinvest.eu.

We are particularly proud that we score so highly across all asset classes. This applies to equity and fixed income, where we manage investments directly, and to property, where our investments are via funds of funds. Here, the UN PRI assesses the extent to which ESG factors are taken into consideration during the process of selecting, appointing and monitoring external managers.

Transparency Report Highlights

On ESG Integration we reported that we continued to incorporate ESG issues into all investment decisions on our actively-managed funds, with responsibility for assessing ESG firmly embedded with the portfolio management teams as part of the analysis and monitoring phases of the investment process. Sparinvest considers ESG risks and opportunities as potential drivers of a company's long term intrinsic value and therefore it is of fundamental importance to the success of our strategies that our Portfolio Managers assess the materiality of these risks.

On Active Ownership we were able to report that Sparinvest's Value Equities team was highly active in individual engagement activities during 2014. We doubled the number of engagements from the previous year, and that is also a key factor behind our 'A' score for Active Ownership. Whilst we are happy with that, we would stress that our 'engagement with impact' strategy means that we are more focused on qualitative than quantitative outcomes. Numbers of engagements alone are not a particularly useful guide to efficacy. Our selection of ESG engagement candidates will continue to be on a case by case basis, led by the consideration of whether or not there is potential for us to effect material change.

Another thing to note is that at Sparinvest, discussions with portfolio companies about ESG issues are carried out by the Portfolio Managers, not by some separate division within the company. This is because we see ESG as an inherent part of corporate fundamentals. To us it is important that opportunities or risks which affect long term corporate value (or a company's ability to pay its coupon and principal) are evaluated by the people most familiar with the investment case.

	Number of Companies Engaged in 2013	Number of Companies Engaged in 2014
Individual/Internal staff engagements	10	21
Collaborative engagements	2	35
Service Provider engagements	125	111

Sparinvest believes in picking its engagements carefully and is always looking for the opportunity to be a constructive partner in dialogue with portfolio companies. One rewarding example from the past 2 years has been our lead role in a UN PRI–coordinated engagement on anti-corruption. This major collaborative initiative targeted 33 companies identified as having room for improvement in their policies - or disclosure of policies - relating to anti-corruption and bribery.

We ran the engagement with a major Asian company – a holding where we already had a history of respectful interaction with management on various matters, having held shares for several years. We feel that important elements of this successful dialogue were the longstanding relationship, cultural and linguistic awareness from both sides, and a willingness not just to make demands, but to take an active role, helping the company through dialogue with other stakeholders such as NGOs. The company has now made bold steps to change its anticorruption policies (and disclosure) for the better. The engagement has only just concluded and we await the final assessment from UN PRI. Sparinvest's role in this engagement – and others – will be described more fully in the next RI review.

On Voting we reported that Sparinvest cast votes in over 90% of all available voting opportunities relating to holdings - a percentage that was in line with the industry average but which we aim to improve on.

Climate Change – The Burning Issue

Switching focus now to 2015, it has certainly been a busy year for the RI team to date. In the run-up to the Paris COP 21 Conference in December, one theme that has dominated headlines – not only within the RI industry but in society as a whole – is that of climate change. In particular, the focus is on the relationship between industrial carbon emissions caused by the burning of fossil fuels and dangerous levels of climate change. At the 2009 talks in Copenhagen, no global agreement on emissions reduction could be reached. Since then, however, China and the US have signed a joint emissions reduction agreement and promised to co-operate on green energy and environmental protection. There is momentum for Paris.

Seldom has an issue caught the imagination of both the investing public and student activists to such an extent. There have been high profile institutional fossil fuel divestments, divestment campaigns in traditional and social media and pronouncements from everyone from Barack Obama to the Pope about the need to transition from fossil fuel dependence to clean energy.

But of course, nothing is ever simple. If an asset manager is mindful of its fiduciary duty, can it wilfully avoid the potential income streams available from energy companies whose product is indispensable for several decades to come, especially if those income streams appear to be priced very cheaply? Is it right to adopt a blanket policy of divestment from a sector comprising a 'dirty-to-clean' spectrum of companies, where the 'dirtiest' companies can also be the incubators of the most innovative 'clean' solutions? Given that securities in energy companies will therefore be traded well into the future, every divestment – although made with the best intentions – will still result in an investment by a new buyer.

Many would argue that, if such companies will be around for some time to come, it is better for them to be owned by committed responsible investors who will take environmental risk factors into account during their investment analysis and then seek to influence companies towards better behaviour through voting and dialogue.

Sparinvest's overarching Responsible Investment Policy is built on an approach of inclusion and engagement for our mainstream investments. We do invest in energy companies and we engage with them on a variety of ESG issues. Indeed, we have recently joined another new UN PRI – coordinated engagement campaign that will focus on Human Rights in the Extractive Industries. Moving forward, we anticipate that our climate change engagement policy will be shaped by new information gained as a result of new developments within our ethical fund range.

Climate Change and Ethical Funds

In response to feedback from investors in our ethically-screened funds, and after discussion within Sparinvest's Investment Committee, two important decisions were taken:

1) To sign the Montreal Carbon Pledge on behalf of the two SICAV funds Sparinvest – Ethical Global Value and Sparinvest – Ethical Emerging Markets Value.
2) To extend sector-based ethical screening to include thermal coal and tar sands.

Signatory of:
PRI MontréalPLEDGE

Launched in September 2014, The Montreal Carbon Pledge is UN PRI's response to the challenge of working towards a 2°c compliant economy in order to contain the risk that 'dangerous' levels of climate change represent to a sustainable financial system. Signing the Pledge commits an asset manager to measuring and disclosing the carbon footprint of some or all equity portfolios on an annual basis. The aim is to use this information to develop an engagement strategy and/or identify and set carbon footprint reduction targets. The deadline for signing the Pledge is 1st September 2015 and carbon score disclosure must occur before 1st December.

Broadening of Ethical Exclusion criteria

With the 2°c goal for a sustainable economy firmly on the agenda, there has been much greater scrutiny of the business models and environmental impact of companies operating within the extractive sector. The majority of institutional divestment campaigns have focused exclusively on the most carbon-intensive of the fossil fuels – coal and tar sands – now widely accepted as being the worst offenders in the sector and increasingly regarded as being unethical investments for this reason.

After careful consideration, Sparinvest has also decided to implement the following sector-based exclusion criteria for actively-managed ethical funds as of June 2015.

Sector Screening – Ethical Funds

- Alcohol
- Tobacco
- Gambling
- Pornography
- Weapons and other military equipment and services
- Thermal Coal & Tar Sands* NEW

*(added as an exclusion factor in June 2015 with a 5% maximum tolerance on production of – and revenues derived from – thermal coal, zero tolerance for tar sands)

This new Coal and Tar Sands screening, along with the carbon footprinting exercise required for the Montreal Pledge disclosure, will give us better perspective when engaging with holding companies on climate change issues.

Other UN PRI Initiatives:

CAC 40 – One Share, One Vote

Sparinvest added its signature to a letter sent to the Presidents of those CAC 40 companies affected by a new French Law that threatens the principle of 'one share, one vote' and potentially also threatens Board neutrality during takeover bids. The only CAC holding of ours that was affected by this was Renault where we voted with management at the AGM to support the concept of one share, one vote. However, the motion was defeated due to a majority shareholding by the French Government.

UN Guiding Principles Reporting Framework

Sparinvest has also supported an investor-led human rights engagement initiative that seeks to promote a standard Reporting Framework for companies to disclose their progress in implementing the UN Guiding Principles. It is believed that the UNGP Reporting Framework will help companies to meet evolving expectations for more robust disclosure of human rights risks and remedial actions.

Improving the ESG Profile of a Quant. Fund

As stated in our Responsible Investment Policy, when investing using quantitative strategies, emphasis is on overall portfolio characteristics rather than on the individual holdings. Accordingly, consideration of ESG-factors is integrated in the investment process at the total portfolio level.

With this in mind, we thought it would be useful to describe how we influence the ESG profile of the only quantitatively managed equity fund in our SICAV.

The SICAV sub-fund Sparinvest - Equitas seeks to generate alpha through factor investing, using the established 'smart' factors of value, small cap and momentum. All other things being equal, where the fund's strategy throws up a choice of shares to invest in, the Portfolio Managers will choose the one with the highest (best) ESG score.

Using MSCI ESG ratings, a numerical score is applied to every member of the investment universe, to the extent that such scores are available in a universe of around 6,000 stocks.

One thing to bear in mind here is that these scores are not static. Not only does MSCI continuously update its ESG ratings based on its latest ESG research information. But the composition of the individual MSCI Benchmarks that make up our quant. investment universe also changes semi-annually when these are rebalanced as a result of market developments. When this happens, index weights change and new constituent companies can enter the benchmark universe – potentially with very different ESG scores to those companies leaving it. Both of these effects can impact the overall portfolio ESG score of our quant. portfolio – negatively or positively – without any action on our part.

It is only when rebalancing or adjusting the portfolio that our managers can – with due consideration of the general investment strategy – select holdings that improve the overall portfolio ESG score. In practice, this means that the ESG score of the portfolio is calculated before and after each portfolio rebalancing exercise, with the constant aim that the post rebalancing portfolio ESG score will be an improvement relative to the starting point. Over time this results in a gradual and consistent improvement in ESG score relative to the current universe and ratings.

2015 Voting Season

With the 2015 voting season pretty much over, we can report that Sparinvest cast votes in 87.5% of the 226 votable meetings within portfolio companies. This figure is somewhat below where we would like it to be as a result of operational factors that we hope to have resolved by next year. (We changed custodian during the year and this made it difficult to get the Powers of Attorney in place for some of the countries where they are needed for voting.) The proportion of votes cast against management recommendations increased to 10% from 7% last year. However, a simple percentage of 'votes against' is not very informative. In reality, we believe that voting is most powerful when used in conjunction with constructive dialogue with companies. When potentially voting against management recommendations, we contact the company to discuss the situation – when time permits, before the voting deadline. That dialogue may, for example, lead to management adjusting proposals, or to us supporting the proposal while working with the company to bring about change in future years.

New RI Analysts

At the beginning of 2015 we welcomed two new trainee RI analysts to the Sparinvest team. Their intensive training period has included – amongst other things – working very closely with our Portfolio Managers over the voting season to ensure that 2419 individual votes were cast.

Marco Schwennesen Orland

Firat Kucukavci

If you would like to hear more about Sparinvest's engagement activities, please come along and listen to Senior Portfolio Manager, David Orr speaking with his dialogue partner from the UN PRI anti-corruption initiative on Day 2 (9th September) at the 'PRI in Person' event at London's ExCel Centre.

Yours faithfully

Nichola Marshall
Head of Responsible Investment