

M&G Global Select Fund

Annual ESG review

FOR INVESTMENT PROFESSIONALS ONLY

November 2019



In the following report, we provide an overview of:

- The fund's sustainable ethos
- Our voting record over the previous year
- Our engagement activities over the previous year
- The ESG key performance indicators (KPIs) against which we compare the fund to its benchmark

The value and income from the fund's assets will go down as well as up. This will cause the value of your investment to fall as well as rise. There is no guarantee that the fund will achieve its objective and you may get back less than you originally invested.

Introduction

The M&G Global Select Fund invests in a concentrated portfolio of quality, sustainable companies, with the consideration of Environmental, Social and Governance (ESG) factors integrated throughout the investment process. We believe ESG awareness is a matter of good stewardship and a sensible part of any sustainable investment strategy aimed at maximising long-term economic returns.

Sustainability refers to the long-term durability of a business, determined by considerations including financial strength, competitive advantages and ESG factors. Such considerations include how a company is run, as well as how it treats its customers, its employees and the environment, for example.

We 'screen in' companies that meet these requirements, including them in our watchlist of stocks we would like to own when the timing and price are right. We perform deep fundamental research on this list, looking at all of the financial and non-financial elements affecting a business. We then wait patiently for behavioural episodes that allow us to invest in these companies at attractive valuations. In addition to 'screening in' we also formally 'screen out':

- Companies deemed to be in breach of the UN Global Compact Principles on human rights, labour, the environment and corruption; and
- Producers of tobacco and controversial weapons (comprising biological, chemical and nuclear weapons, cluster munitions, depleted uranium, anti-personnel mines and white phosphorous).

Finally, the fund does not invest in companies involved in gambling, adult entertainment, the extraction of thermal coal, oil shale and tar sands.



Voting

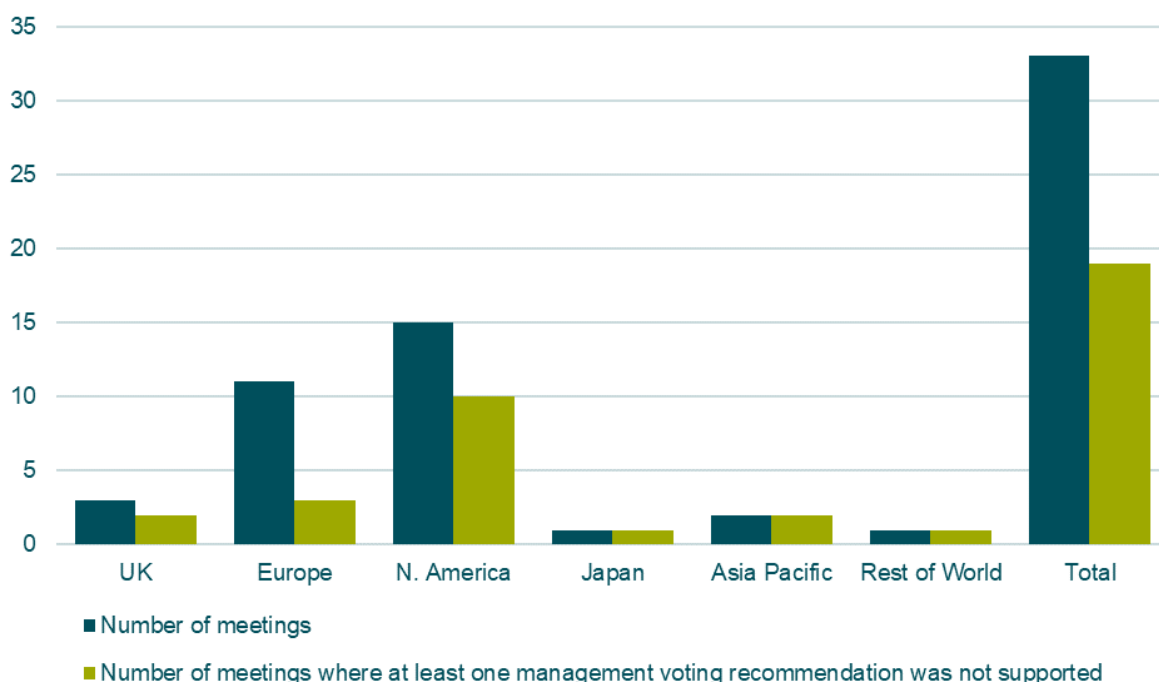
Between 30 September 2018 and 30 September 2019, we voted at 33 shareholder meetings (i.e. all of our holdings within the period).

Investors should note that the fund holds a small number of investments, and therefore a fall in the value of a single investment may have a greater impact than if it held a larger number of investments. The fund can be exposed to different currencies. Movements in currency exchange rates may adversely affect the value of your investment.

Details of M&G's voting, together with our published voting policy, are on the M&G corporate website within the Responsible Investment section.

Our starting position is to be supportive of the management of the companies in which we invest. However, there are occasions when company boards or shareholders put forward resolutions that we feel unable to support, especially if they are not in line with our public voting policy.

Meetings where at least one management recommendation was not supported



Votes cast as against, abstain or withhold by category and region

	UK	Europe	N. America	Japan	Asia Pacific	RoW
Directors-related	0%	40%	46%	0%	0%	100%
Remuneration	50%	60%	4%	100%	33%	0%
Capital-related	50%	0%	0%	0%	67%	0%
Corporate activity	0%	0%	0%	0%	0%	0%
Anti-takeover	0%	0%	14%	0%	0%	0%
Routine other business	0%	0%	0%	0%	0%	0%
Shareholder resolutions	0%	0%	36%	0%	0%	0%
	100%	100%	100%	100%	100%	100%

Engagement

Meeting management teams is an integral part of our investment process. This is not to gain an 'information edge' on the financial development of a company, but rather to get a good grip on the business model, become comfortable with the company's long-term strategy and, not least, to get a sense of how aligned the management is with our values. We look for:

- Alignment of values and time horizons
- Track record of integrity and responsibility
- Cultural strength
- Trustworthiness and transparency.

M&G Investments generally, and the Select team specifically, seeks and promotes long-term thinking from management teams. We place a great deal of emphasis on establishing if a company is run in a responsible manner by trustworthy people with the stakeholders' best interests in mind. Discussions with management and a deep look into the company's history, disclosure and incentive schemes, can normally provide valuable information.

If we have identified specific corporate responsibility issues, we will present these to the management team. We also offer our help on how to think about targets, disclosure and incentive structures. However, because of our bias towards responsibly run businesses, we do not consider ourselves to be 'ESG-activists'. In most cases, our engagement will not be aimed at solving problems, but rather at getting a good sense of the business culture – we believe that conversations with management teams about corporate responsibility can reveal much more about the business culture than any sustainability report or newspaper headline. We believe that active asset managers can have a significant impact on corporate behaviour, and we hope that, alongside like-minded investors, we will be able to strengthen the corporate responsibility, culture and long-term performance of the companies in which we invest.

Engagement case studies

Microsoft – technology

Microsoft provides technology services, software and hardware for both public and private customers, and is currently the world's largest company by market capitalisation. During the period we met Microsoft's then recently appointed chief environmental officer. The creation of the role signalled the beginning of co-ordinated and group-wide environmental efforts by the company. Microsoft is a pioneer in implementing an internal carbon fee that actually charges business units for their emissions. Microsoft stated that sustainability was front and centre of the business and core to everything it does. It has made significant investment in its Artificial Intelligence For Earth (AI4E) project and has put in place strategies to reduce emissions from data centres and policies on cobalt sourcing, among others. We were also invited to join an investor call to discuss raw material sourcing with specific guidance from the OECD and UN Principles on Human Rights, the key materials being cobalt, magnesium, aluminium and copper.

Teva – pharmaceuticals

Teva is an Israeli pharmaceuticals company producing generic medications based on existing drugs that have gone off-patent, as well as producing some of its own specialised products. We closely followed a US states-filed antitrust case, in which the states involved said a number of generic pharmaceutical companies had been involved in collusion and price fixing, including Teva. Teva denied the allegations, and we engaged with the company to understand the processes it had in place to eliminate such risks, and improvements that could be made to those processes. Naturally the company was limited in the information it was able to share, being involved in open investigations, and ultimately we lost faith in the investment case for the business and sold our shares.

Barry Callebaut – cocoa producer

While we maintain ongoing dialogue with our investee companies, we also engage with companies on our watch-list of stocks that we would like to own when the timing and price are right. One such engagement of note involved one of the world's largest cocoa producers, Barry Callebaut. We met the company's chief financial officer and remuneration committee chairman to ask, among other things, how the company expects to lift 500,000 farmers out of poverty.

The company explained that the average cocoa farm yields 300kg of beans per hectare. A good farm (without automation) should achieve 1,000kg per hectare through the use of farm education, basic equipment, pesticides, additional farmer

training programmes and similar, all of which are provided by Barry Callebaut. The company believes a farmer should be lifted from poverty at 750kg, and the company will monitor how the average yield per hectare is progressing for its farmers. We also discussed more general sustainability issues with the company, which has done a lot of work with African governments to help ensure the sustainable sourcing of beans. This includes a programme of farm mapping, using drones and satellite images to ensure forested areas are not being converted into cocoa farms. It has currently mapped around 150,000 of the most critical farms in its supply chain. The company also explained how it helps to diversify crops within given regions, and how women cocoa farmers are empowered, meaning more money flows back into the farms and families.

Key ESG Performance Indicators

When researching stocks for the portfolio, we consider the materiality of ESG factors relative to a given company or industry. We also undertake ongoing ESG analysis on individual holdings within the portfolio, building an evolving picture of sustainability issues relevant to that company. For example, while raw material sourcing represents a significant risk for the fashion industry, the same does not apply to the financial sector (where responsible lending might be considered), or for an IT company (where cyber security might be a much larger risk). We internally score the holdings in our portfolio, rating them against these issues of materiality.

Resources deployed to monitor the ESG impact of the funds are mainly internal to M&G. They comprise the Select team's three embedded analysts, as well as the team's investment specialist – we believe in the importance of conducting our own research and forming independent views. To assist with the decision-making process, we will however scrutinise research and indicators from several third-party providers and get support from M&G's Corporate Finance and Stewardship team for our engagement efforts.

In order to consider key ESG performance indicators at a fund level, we have focused on factors that are relevant across the entire portfolio:

KPIs at a glance

KPI	Environmental			Social		Governance		Human Rights
	Total Co2 Eq Emissions to Revenue USD	Total Water Use to Revenue MIn USD	Waste Reduction	Employee Satisfaction	Women Managers	Board Gender Diversity, Percent	Average Board Tenure	Global Compact BMK
M&G Global Select	80	417	83.0%	79.0%	34.0%	24.0%	8.4	40.0%
MSCI World	210	12,375	87.0%	78.0%	31.0%	25.0%	8.1	60.0%

Source: Eikon Reuters, 25 November 2019

These are by no means the only ESG factors that we consider at a company level, but we feel they are the most practical at a portfolio level. These factors are regularly reported by the majority of companies, they are transparent and reliable and work across sectors, allowing us to report consistently. These KPIs are not intended to represent a comprehensive overview of the many factors that are analysed as part of our ESG assessment, nor our ongoing monitoring of, and engagement with, investee companies.

Indicators are sourced from Eikon Reuters to facilitate updating and consistency of data. For a full explanation of each KPI, please see our KPI report on the M&G website.

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The fund invests mainly in company shares and is therefore likely to experience larger price fluctuations than funds that invest in bonds and/or cash.

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