MORROW SODALI

INSTITUTIONAL INVESTOR SURVEY 2019

INDEX

EXECUTIVE SUMMARY

Morrow Sodali's fourth annual Institutional Investor Survey confirms that 2019 will be another year of transformative change in relations between companies and their shareholders.

Survey results reveal that investors continue to dig deeper into the inner workings of portfolio companies. Investors aspire to engage with boards of directors regularly throughout the year, not just during the proxy season. At the same time, companies should not expect that every investor will respond to every outreach.

In our experience, responses vary from investor to investor and depend on many variables, including the perceived importance of the issue. Investors want more substantive information about board composition and business strategy. They want clearer explanations of the business rationale for governance and executive pay decisions. They want an integrated narrative that explains environmental, social and governance practices in terms of business risk and sustainable financial performance.

The good news for companies is that these survey results confirm a continuation of many investors' move away from reductive box-ticking and compliance checklists. Our more recent experience suggests that some investors have indeed progressed their approach, for example to be willing to nuance their voting decisions based on information gained via engagements. At the same time, a more rigid adherence to stated policies persists with others. Some investors are willing to give companies greater flexibility to explain policies in terms of their specific business conditions and strategic goals. However, a deeper dive into companies' strategic decisions increases demands on the time and attention of directors, requires much greater transparency and strains the limitations of regulated disclosure.

Investors are willing to give companies greater flexibility to explain policies in terms of their specific business conditions and strategic goals.

SOME OF THE INSTITUTIONAL INVESTOR KEY SURVEY FINDINGS

The quality of a company's governance policies and practices will play a pivotal role when investors make voting decisions say most respondents.

Question 1 asked investors to rank the importance of various factors that determine how they make voting decisions, summarizing this year's message to companies about the content of corporate reporting, disclosure and communication. **93%** of respondents selected "governance policies and practices;" **72%** selected "long-term business strategy;" **65%** selected "the quality and completeness of the company's communications;" **54%** selected "environmental and social policies and practices." Further, in **question 15**, **72%** of respondents agreed that "companies should adopt recommendations of the Task Force on Climate-related Financial Disclosures (TCFD)."

Investors say Quarterly Reporting promotes short-term behavior by companies (78%) and investors (72%), however 89% of respondents said that quarterly reporting leads to reliance on earnings guidance.

Only **22%** would admit that it affects their own behavior.
(For a more detailed analysis of quarterly reporting versus earnings guidance, see the ***Morrow Sodali Client Memo – Investor Relations – A Communications Clearinghouse****)*

Investor focus on board engagement continues to increase. A whopping 87% of respondents indicated that "proactive and regular engagement with the board of directors" helps in their evaluation of a company's culture, purpose and reputational risk.

In addition, **72%** selected "proactive and regular engagement with management." Thoughtfully planned engagements have become critical, strategic initiatives. They help secure favorable votes and minimize threats of activism. Additional context on proactive engagement can be found in the responses to **Question 3**: "What are your goals when engaging with listed companies and their directors?" **67%** are seeking to understand the company's business strategy and capital structure and to understand how the board oversees corporate culture and the tone at the top. Only **35%** see engagement as a way for investors to proactively inform companies about their voting policies and investment philosophy.

Companies can expect more focus on disclosure and increased dialogue around climate change strategy.

In **question 14**, **85%** of respondents said that they view climate change as the most important engagement topic. This result is slightly different than the response to **question 11** where, when asked to rank the importance of detailed disclosure on a list of topics, **83%** wanted more detailed information about human capital management, while **76%** wanted more detail on climate change, the 2nd most important answer. This result may indicate that currently more information is available on climate change than on human capital management. The challenge for both companies and institutional investors is to better understand and agree upon which metrics are relevant to a company's long-term performance and agree on standards that permit comparability with its peers and within a specific industry. In many ways, this is a debate that is taking part largely outside the bilateral connection between companies and their investors, with standard setting bodies, whether regulatory or voluntary taking the lead. The hurdles to progress here should not be understated as standardization and relevance could often conflict.

Investors will increase their focus on Board Composition and Accountability.

The spotlight will continue to be on director competence and boardroom transparency. In **question 5**, respondents made clear that the "skills" (**70%**) and "independence" (**67%**) of directors are critical factors in their evaluation of individual board members. These results are reinforced by their response to diversity. Gender and ethnicity scored much lower in importance than "skills and qualifications" (**89%**) and "professional experience" (**72%**) as criteria for judging the diversity of a board's composition. Investors also signaled their support for board evaluation, done either internally or with an external third-party assessment.

Many investors indicate that executive pay will frequently be the subject of collective engagement efforts.

This was to us an interesting point to observe. The perennial issue of executive pay continues to be viewed by investors as a window into the boardroom and even more deeply into the values and character of a business enterprise. For investors it is the ultimate issue for evaluating board accountability and independence. In the past however, it was very much the case that investors engaged on this issue separately with companies, expressing views that are based on their own distinct policies. Increasingly however, as some of the pay debate shifts to quantum and reputation (at least in some markets, notably the UK but also other European markets), investors find themselves able to work together to put forward certain points. This is clear from the response to **question 2**, where **67%** of investors ranked executive pay as the most important issue in their engagement with other investors in connection with an AGM. **Question 9** gives companies a useful guide to the elements of executive pay that matter most to investors: pay for performance (**65%**), rigour of performance targets (**56%**) and the inclusion of long-term performance targets (**41%**). Boards must continue to pay careful attention to explain their pay decisions in terms of performance – financial, operational and increasingly related to sustainability measures – and strategic goals.

Activist credible story focusing on long-term strategy, combined with poorly communicated business strategy by the company, is likely to attract investor support of activist campaigns.

Activism is on the increase both in the US and internationally. But even so, activists need the support of their fellow shareholders to leverage their influence. In 2017 we identified that **57%** of respondents would engage with activists when approached, and **43%** would proactively approach activists. This year we sought to find out what are the issues that might trigger such a discussion. Whilst historically activists tended to rest their cases on financial restructuring and operational improvements, these days more strategic issues become common – for example M&A, capital allocation and other aspects of corporate strategy. It is therefore interesting to observe that institutional investors are most likely to support an activist with a credible story focused on long-term strategy (**50%**) and in cases where the target company has unclear business strategy (**46%**), misallocated capital (**43%**) or a lack of board accountability to shareholder concerns (**41%**). Strategic shareholder activism is now defined as an asset class. Activism is here to stay. The debate over whether activism creates or destroys value is now mainly a topic of interest to academics and regulators, while companies must adapt to the realities of a marketplace that encourages activism.

LOOKING AHEAD

The trends of more company investor engagement as well as (separately) deeper integration of ESG to the investment process continue to both be at an important juncture for equity capital markets; our survey highlights this with increasing conviction year on year. Institutional investors now more than ever before play an influential role in setting the agenda on this, and in developing the proper tools. In our view, it is only a matter of time before this concept becomes near universally accepted and/or quasi legally binding in some markets.

As asset owners demand greater transparency on how investment managers exercise their stewardship duties, not merely to attract investment returns but also increasingly to integrate ESG considerations into the investment decision making process, it is encouraging to observe that each year more and more respondents indicate that they are progressing on this journey.

As recently as last month, a group of prominent institutional investors re-emphasized their commitments to the recommendations of the *Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD)* regarding climate risk and the transition to a low carbon economy. This is reflected in the results of our survey, which indicate that in 2019, investors will prioritize engagement around sustainability related topics and especially climate change.

The change of pace around ESG integration, the continued rise of activism and recent corporate scandals all combine to create an ever-growing necessity for issuers and their officers to keep abreast of the agenda and intentions of their Institutional Investors. Those who do this will observe that investors have shifted their focus from issuers' compliance with corporate governance codes, to sustainability related principles that have impact beyond proxy voting to engagement strategies and investment decisions.

Our 4th annual investor survey has only been made possible thanks to the participation of Institutional Investors.

We would like to thank them all for taking the time to respond to our survey.

ABOUT THE SURVEY

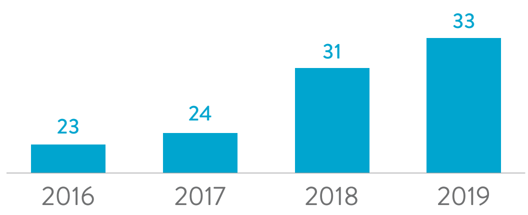
This is Morrow Sodali's 4th Annual Institutional Investor Survey. 46 global Institutional Investors – managing a combined $33 trillion in assets under management - took part. All Institutional Investors are PRI signatories and the individual participants are senior governance specialists with average experience of 12 years managing global voting and engagement responsibilities. The survey was conducted by a combination of online survey and one to one meetings.

Our survey includes some persistent questions from prior years along with several thematic questions on topics of near-term interest. We continue to monitor the views of Institutional Investors on a wide variety of global trends and emerging issues around the Annual Shareholder Meeting, ESG Integration, Board Practices, Executive Pay, Disclosure, Activism and Engagement Activities.

Institutional Investors responding to this year's survey also have the following characteristics:

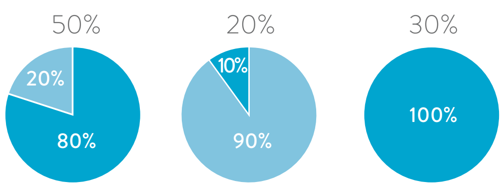
ASSETS UNDER MANAGEMENT

2019 $33 Trillion of assets under management
2018 $31 Trillion of assets under management
2017 $24 Trillion of assets under management
2016 $23 Trillion of assets under management



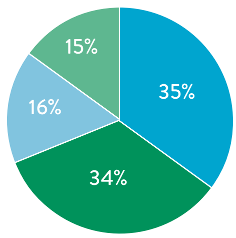
INVESTMENT STRATEGY: ACTIVE VS PASSIVE

Active $19.5 Trillion / **Passive $13.5 Trillion**
50% of respondents manage 80% Active / 20% Passive
20% of respondents manage 90% Passive / 10% Active
30% of respondents manage 100% Active / 0% Passive



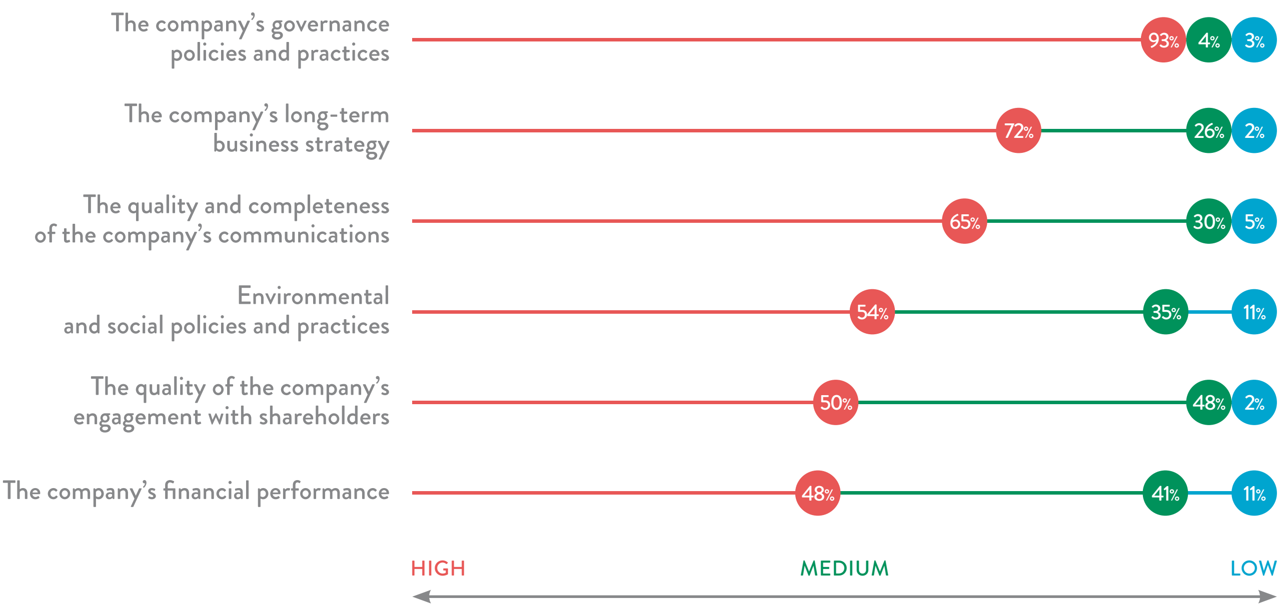
ROLE OF RESPONDENTS

- Head of Corporate Governance **35%**
- ESG Analysts **34%**
- Corporate Governance Specialists **16%**
- Head of Investment Stewardship **15%**



Q1

Please indicate how important the following factors will be when taking your voting decisions:



A NUMBER OF INVESTORS ALSO POINTED OUT

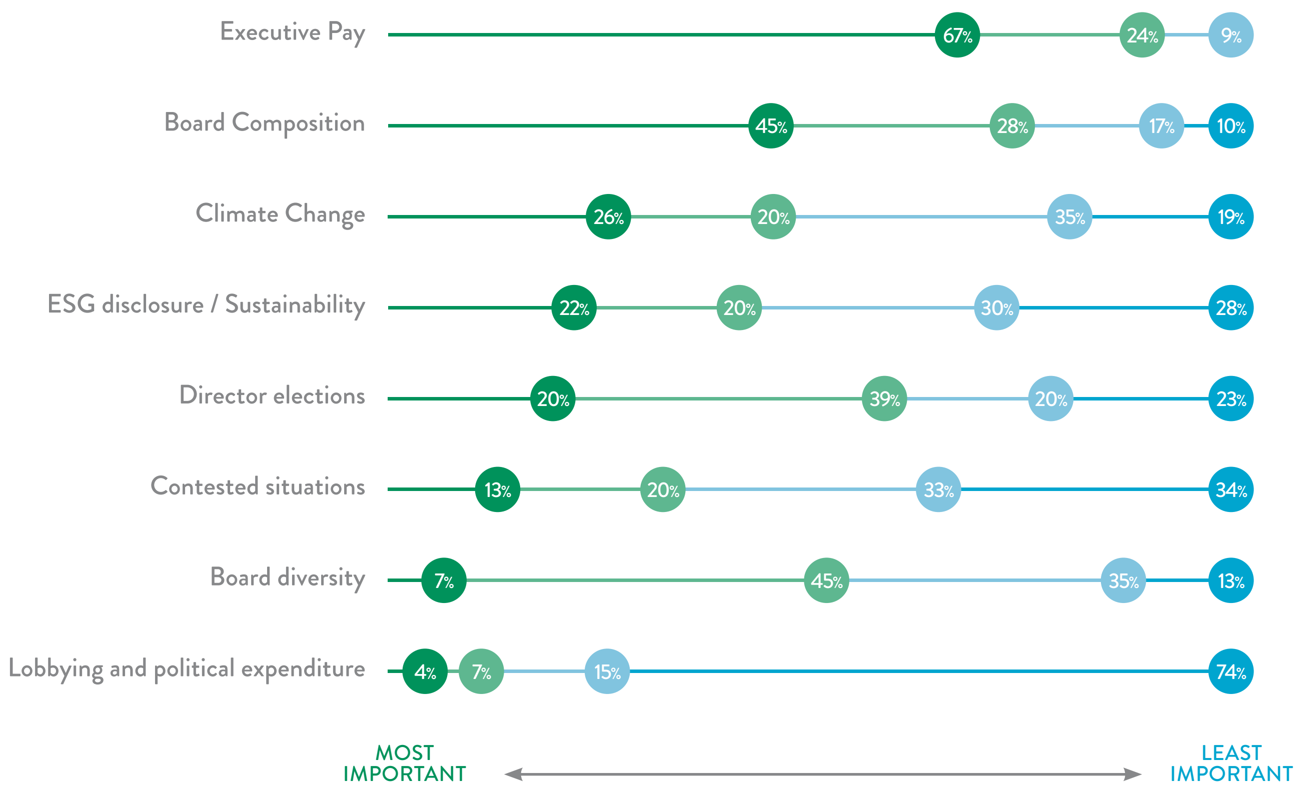
"They will focus more on company's decisions and outcomes around M&A activity when determining their vote decisions."

Asking investors to rank the importance of various factors that determine how they make voting decisions, a near consensus emerged, according to which "governance policies and practices" are the most important consideration (**93%**). This follows our finding from last year that increasingly it is the governance teams that are responsible for voting decision, either exclusively or in consultation with portfolio managers (**71%**). The second most important consideration was "long-term business strategy" followed by "the quality and completeness of the company's communications". Financial performance comes last, with only **48%** of respondents considering it important when voting.

This result highlights the growing importance for companies to ensure they discuss issues around governance with their investors. Those companies who believe that by having strong financial performance they are insulating themselves from negative votes may be surprised when it comes to their shareholder meetings.

At the same time, with investors increasingly focusing on the company's long-term business strategy, and thus shifting away from what is sometimes referred to pejoratively as "box ticking", it certainly tallies with our experience that those discussions with investors can be quick, meaningful and not at all disconnected from the overall business context.

Q2 On what issues are you most frequently engaging with other investors in connection with the AGMs of portfolio companies?



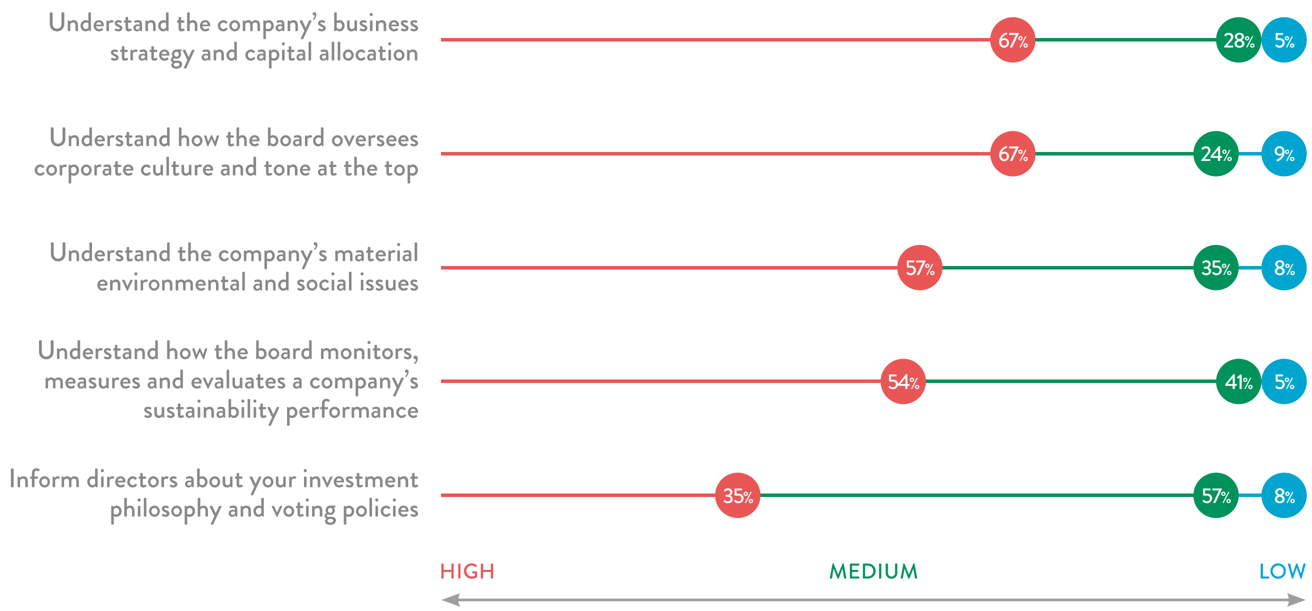
Formal investor networking groups such as the Council of Institutional Investors and the UK Investor Forum are increasingly the way that shareholders bring together multifaceted resources to agitate for change. Shareholders are utilising these mechanisms more frequently to escalate material and relevant issues, to amplify individual concerns, to gain momentum and seek change at companies. It's also not uncommon for companies to receive letters signed by a group of shareholders citing concerns around specific issues. Collective engagement around executive pay is on the rise as shareholders further align their interests and goals, as their individual engagements and robust policies prove unsuccessful.

Last year **59%** of investors told us that they expect to engage collectively with other shareholders, so this year we were interested to find out the key themes behind this. In line with the continued intense focus on executive pay, **67%** of respondents stated that executive pay will be the most frequent topic for collective dialogue and escalation. This is a significant change to last year when climate change and activism received more attention.

KEY TAKEAWAYS

Investors are most inclined
to engage collectively on executive pay.
67% of respondents stated that
executive pay will be the most frequent issue
that prompts collective engagement around the AGM.

Q3 What are your goals when engaging with listed companies and their directors?



Corporate engagement, now an established part of the relationship between investors and the companies they invest in, is progressing in quality. In the past few years we have observed that more markets are accepting investor engagement as an integral part of the responsibilities of the board. This means that rather than considering whether to engage, many companies are now focused on how to ensure the quality of engagement. The experience accumulated by companies and investors in several markets enables them to elevate the discussion from simply being an exchange of basic information to a more meaningful dialogue aimed at gaining a better understanding of some of the more important strategic issues.

It is against this backdrop that we were pleasantly surprised that the two engagement objectives rated as having the highest importance by investors are those connected to the key strategic aspects of the long-term management of the company. **67%** of investors indicated that both gaining a better understanding of the company's business strategy and capital allocation, and of how the board oversees corporate culture and the tone at the top are the most important objectives when engaging with listed companies and their directors.

57% of investors stated that the company's material environmental and social issues are of high importance. Investors are increasingly integrating the impact of E&S into their investment decision making processes and understanding how the board navigates the various discussions on this with management forms part of their internal analysis.

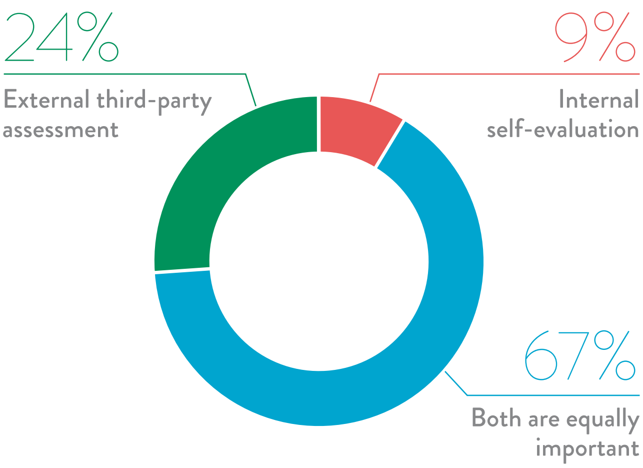
KEY TAKEAWAYS

67% of investors indicated that both gaining a better understanding of the company's business strategy and capital allocation, and of how the board oversees corporate culture and tone at the top are the most important objectives when engaging with listed companies and their directors.

WHAT RESPONDENTS SAID...

"We will focus our discussions on NED oversight of management, particularly communication between execs and non-execs and examples of how the board challenges management."

Q4 Please indicate what you believe to be the most effective form of board evaluation?



WHAT INVESTORS SAID...

"There is no single best process, but the process should be well articulated and justified in terms of how it adds value to ensuring right mix of skills, director accountability/attentiveness are assessed and how the process ensures adequate level of board refreshment."

Conducting Board evaluations has progressed to become a standard practice for public companies. In a comprehensive overview of international practices across 20 countries, the OECD concludes that board reviews are becoming the norm.[1] However, as with most recently evolved standards, details in methodology and disclosure vary greatly.

Following previous surveys where investors indicated that disclosure regarding the Board evaluation process plays a role in generating confidence in the Board refreshment process, with a preference for improving disclosure on the evaluation's findings, recommendations and follow-up actions for the Board,[2] the global debate has moved on from "if" to "how."

In the US, where **93%** of Fortune 100 companies included at least some disclosure on board evaluations in their proxy statements,[3] the Council of Institutional Investors' Research and Education Fund ("CII-REF") recently published an overview of existing disclosure practices with the aim of identifying best-practice examples, but expressly not to promote a universal standard. Instead, the CII-REF asks Boards to maintain an individual approach to Board evaluations which takes into account the particular context of their company.[4]

Typically, corporate issuers undertake annual self-assessments accompanied by less frequent evaluations conducted by an external provider. Institutional Investors endorse this complementary approach: **67%** agree that both external third-party assessments and internal self-evaluations are equally important, while **24%** consider external third-party assessments as most important.

In August 2018, the UK government asked the Institute of Chartered Secretaries and Administrators ("ICSA") to review the quality and effectiveness of external Board evaluations, to produce a code of practice for both companies and board evaluation providers. Two months later, Stephen Haddrill, Chief Executive of the Financial Reporting Council ("FRC") admitted in an ICGN meeting of the CII that he did not expect Board evaluations themselves to prevent Boards from failing. Instead, improved disclosure of the evaluations' conclusions would give investors the opportunity to act.[5] Corporate issuers should be mindful that conducting Board evaluations without providing meaningful disclosure may become a contentious issue for debate when engaging with investors.

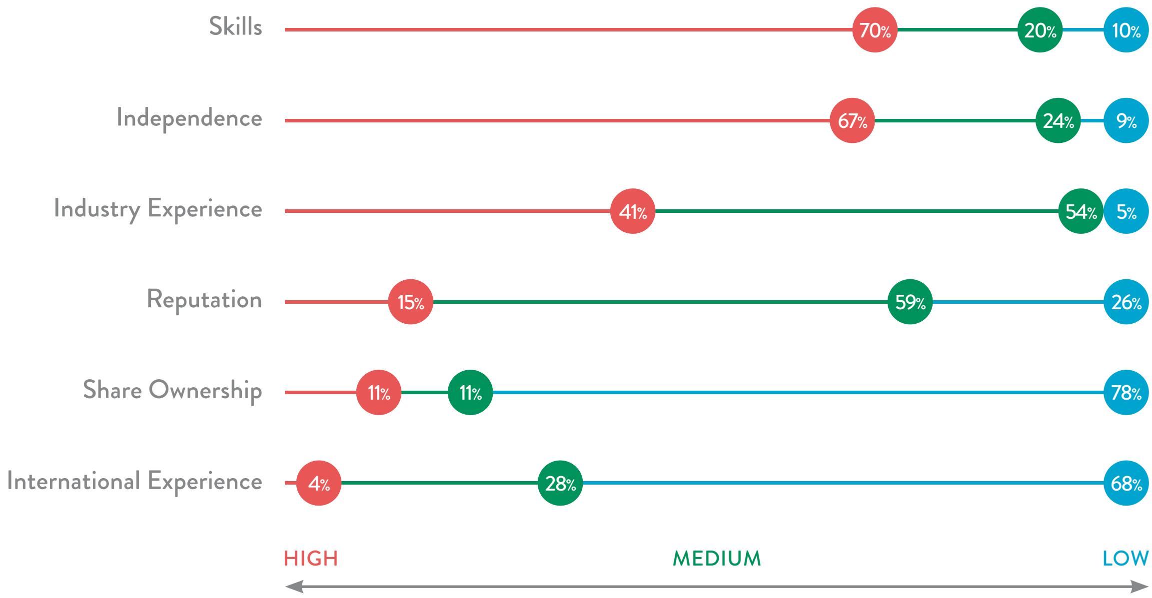
KEY TAKEAWAYS

67% of investors agree that both external third-party assessments and internal self-evaluations are equally important.

24% say external third-party assessments are most important.

1. OECD (2018), Board Evaluation: Overview of International Practices.
2. Morrow Sodali Investor Surveys 2017 & 2018.
3. "Improving Board Performance through Effective Evaluation," EY Center for Board Matters, October 2018.
4. "Board Evaluation Disclosure", CII Research and Education Fund, January 2019.
5. Global Proxy Watch – The Newsletter of International Corporate Governance and Stewardship, 26 October 2018.

Q5 How important are the following qualifications for you to take a decision on whether to support the election of individual directors?

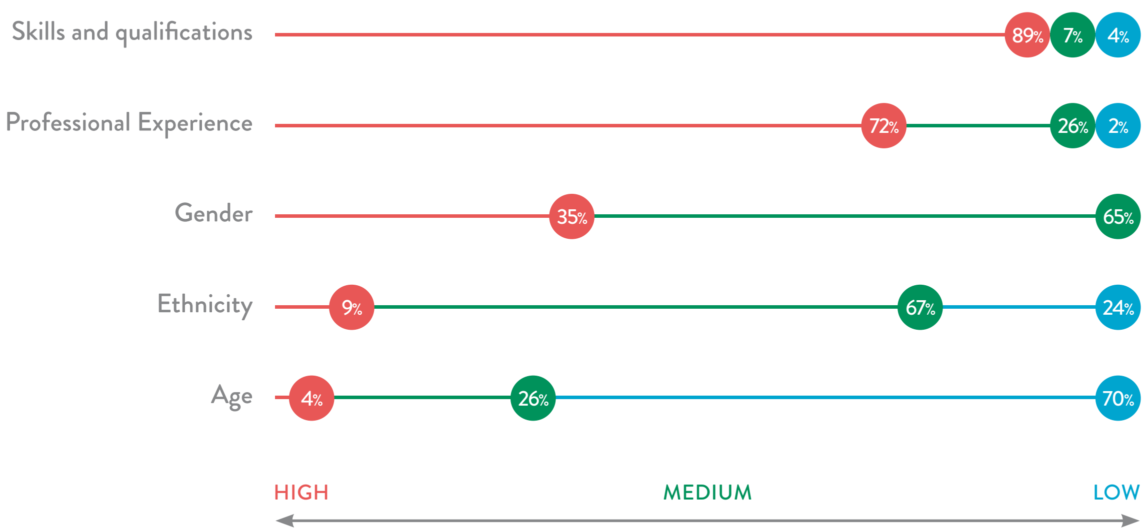


The 2019 survey identified that investors continue to focus on skills (**70%**) and independence (**67%**) as the most important factors when determining whether to support director elections. **41%** of investors believe industry experience to be the next most important factor. These top three factors were also the same as in the 2018 survey.

Directors are being heavily scrutinised for their contribution and the role they play on company boards. Increasingly, investors seek disclosure on their skills and experience and how this positively contributes to the overall effectiveness of the board. The objective of new appointments of directors should be to fill those gaps, identified using the board skills matrix, while at the same time maintaining or reinforcing the board's independence levels.

Reputation (**15%**), share ownership (**11%**) and international experience (**4%**) are considered important as well, however to a lesser extent.

Q6 What type of diversity do you find most important?



Diversity remains a major concern in the debate on effective Board composition. Scientific studies on how diverse viewpoints benefit decision making are plentiful, with much of public debate focussing on gender diversity. Regulators and corporate governance codes around the world have reacted and introduced quotas for female participation on Boards into hard and soft law.

Investors, on the other hand, consider a wide range of diversity criteria as important, which is also reflected in the demand for clearer and more comprehensive disclosure on Board profiles. Although none of the respondents to this year's survey see gender diversity as not relevant (**35%** most important, **65%** second most important), skills (**89%**) and experience (**72%**) remain the most important form of diversity for a significant majority. This clear investor preference is consistent with survey results in previous years.
Ethnicity is slightly more important than last year, with **9%** of investors considering it most important and only **24%** least important (compared to **8%** and **29%** in 2018, respectively).

Shareholders value gender diversity, and increasingly also the diversity of other demographic factors, with one exception: age remains at the bottom of investors' priority list for Board diversity, which may run contrary to the experience of corporate issuers in some countries, such as Germany or France, where age limits and composition requirements in local rules and regulations are a frequent cause for debate.

Nevertheless, investors widely agree that being strong on gender or ethnicity does not compensate for a well-rounded set of skills and professional experience. Recent studies even suggest that work experience-related diversity may not just improve the quality, but also the speed of Board decision making.[1] Demographic diversity is only complementary to diversity in qualifications.

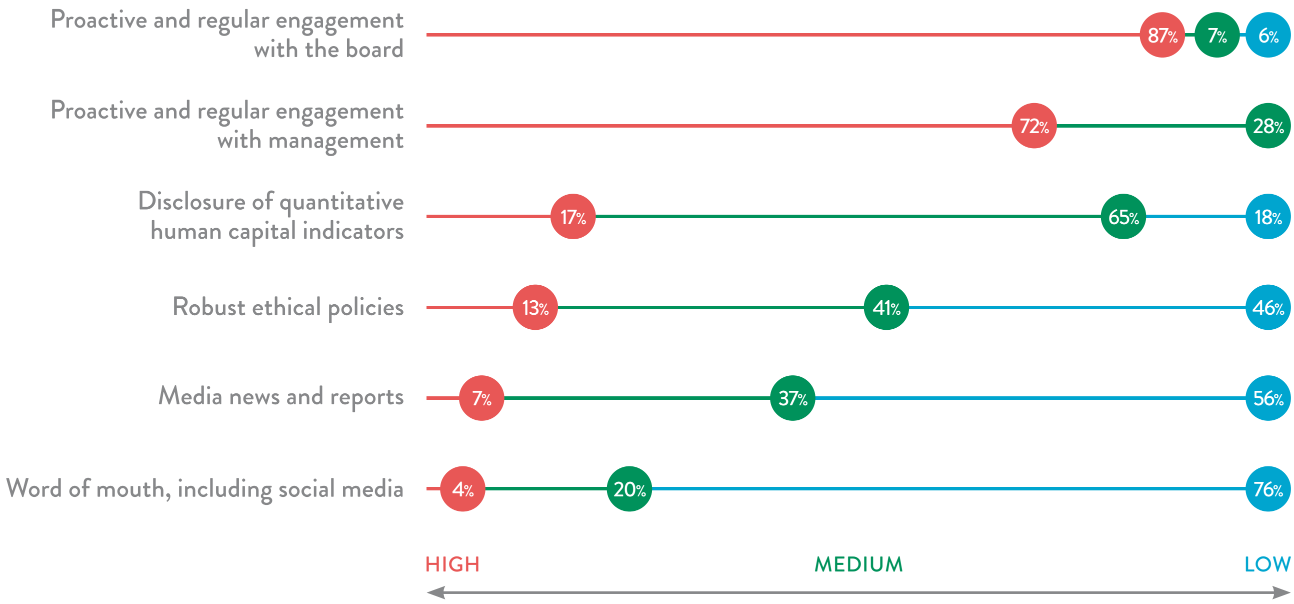
1. "Job-related diversity: the comprehensiveness and speed of board decision-making processes", Journal of Management and Governance, Knaadi, Benkewitz, Zhank, June 2018.

KEY TAKEAWAYS

In deciding whether to support board candidates, investors consider in order of importance the candidate's skills, independence and industry experience.

Skills and qualifications **(89%)**, as well as professional experience **(72%)**, are rated as more important than gender diversity **(35%)**.

Q7 Which of the following helps you evaluate a company's corporate culture, purpose and reputational risk?



The lessons learned from recent corporate scandals and organizational crises is that without an ethical and compliant culture, organizations will be at risk. How the Board interacts with management and reaches key decisions on strategic matters is of increasing importance to investors. Policies and codes of conduct are used as the first step, particularly to help how corporate culture is defined, measured and improved, however it's necessary that compliance with these is monitored constantly. Often, a policy approach does not ensure a healthy corporate culture; instead setting numerical targets and holding talks between the Board, management, staff and key stakeholders on a regular basis are the more robust methods for establishing a positive culture.

In our 2016 survey investors suggested that having no access to directors would lead to the request for engagement being escalated with companies. Furthermore, in our 2017 survey, when asked which company representatives investors prefer to engage on corporate governance issues, **72%** of investors suggested board members. In this year's survey we continue to see a significant rise in the demand for dialogue with the board; **87%** of investors say proactive and regular engagement with the board helps evaluate a company's corporate culture, purpose and reputational risk. A further **72%**, for the same question, say proactive and regular engagement with management is very helpful.

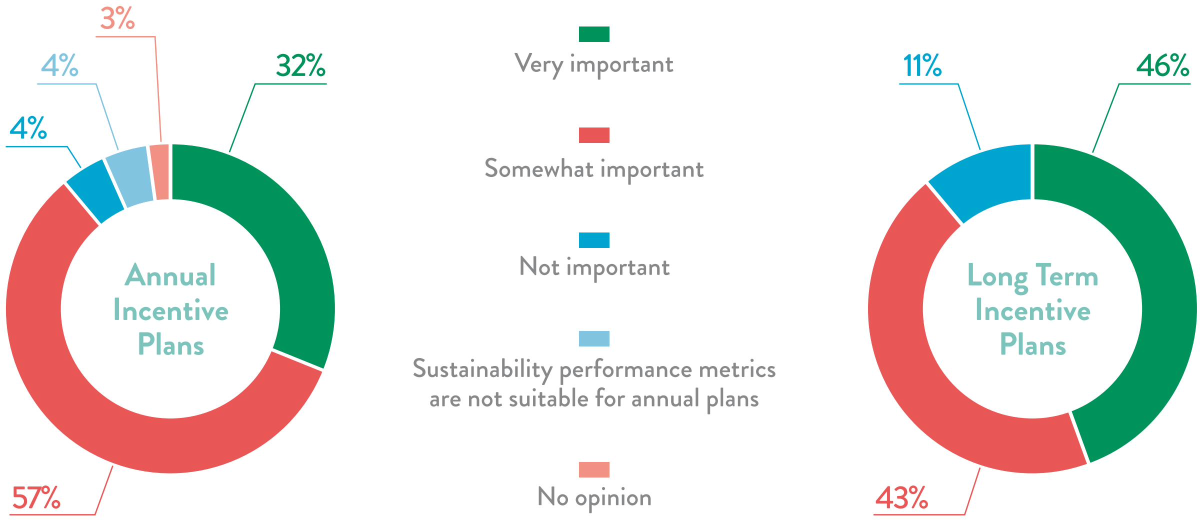
Disclosure of quantitative human capital indicators (**17%**), robust ethical policies (**13%**), media, news and reports (**7%**) and word of mouth and social media (**4%**) are other less frequently used methods to evaluate a company's culture.

KEY TAKEAWAYS

Proactive and regular engagement with the board helps evaluate a company's corporate culture, purpose and reputational risk say **87%** of respondents.

72% say proactive and regular engagement with management is very helpful.

Q8 How important is the inclusion of sustainability performance metrics and targets in the following executive pay plans?



WHAT RESPONDENTS SAID...

"The inclusion of ESG metrics in executive pay is a good practice whenever the company has a clear sustainability strategy. The crux is the alignment of the metrics with the company's strategy."

The focus on environmental and social matters has captured the attention of investors and other stakeholders (as well as the public), as evidenced by our findings in the Institutional Investor Survey results this year and for previous years. When coupled with the on-going, intense scrutiny on executive pay packages and the fact that a well-designed executive pay program supports a company's long-term strategy, it is no surprise that investors are keen to understand how the executive leadership team is being evaluated to ensure a successful – and sustainable – future for long-term value creation.

Investor expectations for companies to supplement – not replace – core executive pay metrics with sustainability performance measures that are relevant to the company's business and that are aligned with its short, medium and long-term strategy, continue to gain traction. Although we broadened the question this year beyond the CEO, our findings indicate that an aggregate **89%** of investors believe that it is "very important" or "somewhat important" to partly tie an executive's long-term incentive awards to performance on sustainability measures. This represents a slight upward trend from the **84%** aggregate figure we reported last year, which focused on the CEO. We note a similar upturn on investor expectations with regard to the inclusion of sustainability performance metrics in short-term, annual incentive programs. This year, **32%** of survey respondents reported that it is "very important" – vs. **29%** in the previous year.

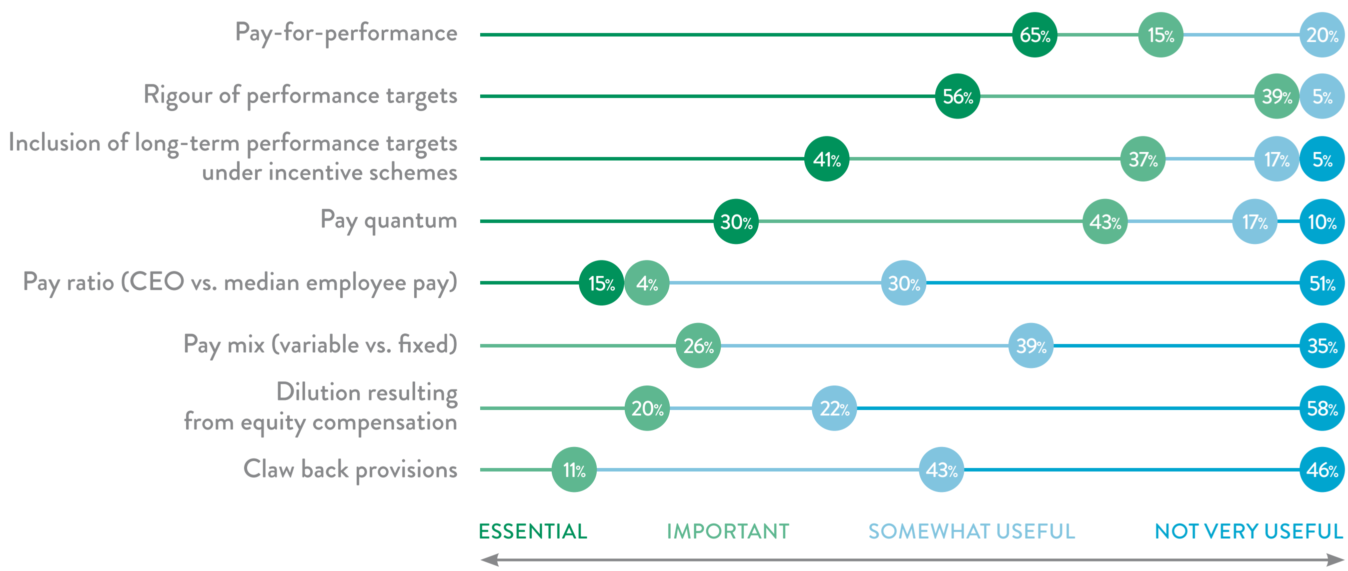
These results provide new challenges for boards and executive pay committees. Sustainability concerns are now firmly part of executive pay evaluations, although these types of metrics do not supersede traditional measures. The metrics and targets must remain within a company's risk/reward framework while adequately incentivizing executives, particularly to create additional opportunities for the company.

KEY TAKEAWAYS

89% of investors agree the inclusion of sustainability performance metrics and targets in executive long-term incentive plans is either "very important" or "somewhat important".

Only **4%** say its "not important" for annual or long-term incentive plans.

Q9 How important are the following considerations in your evaluation of executive pay?



65% of investors say Pay-for-performance remains the most important consideration when evaluating executive pay although this is down **23 percentage points** from last year. On the other hand, the importance of companies applying rigorous performance targets increased **10 percentage points** from **46%** to **56%**.

Investor concerns and attention on executive pay has not waned – spanning all markets. It remains a critical area for engagement between investors and their portfolio companies as investors seek to better understand a company's pay philosophy and how this helps create a true pay-for-performance culture. This being demonstrated with sound pay structures and practices and appropriate pay-related decisions that confirm the board's understanding of the long-term strategy set out by management.

In our Institutional Investor Survey 2017, we reported that **23%** of respondents considered pay quantum to be the most important executive pay issue. While that figure marginally declined to **20%** in 2018, since 2017 it has jumped two places to be the fourth most important executive pay topic this year. Also the fact that **30%** of survey respondents this year find it to be the most significant consideration in executive pay is noteworthy. Special one-time grants that are typically outsized in nature may have put additional spotlight on the matter. Moreover, pay disparity has become a mainstream discussion point in society.

KEY TAKEAWAYS

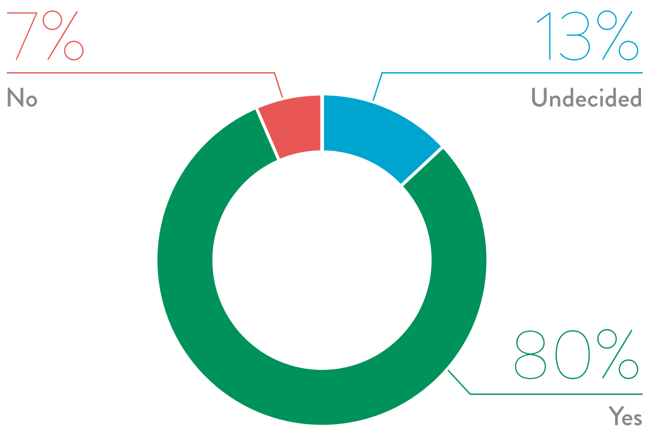
The importance of company's applying rigorous performance targets increased **10% points** from **46%** to **56%**.

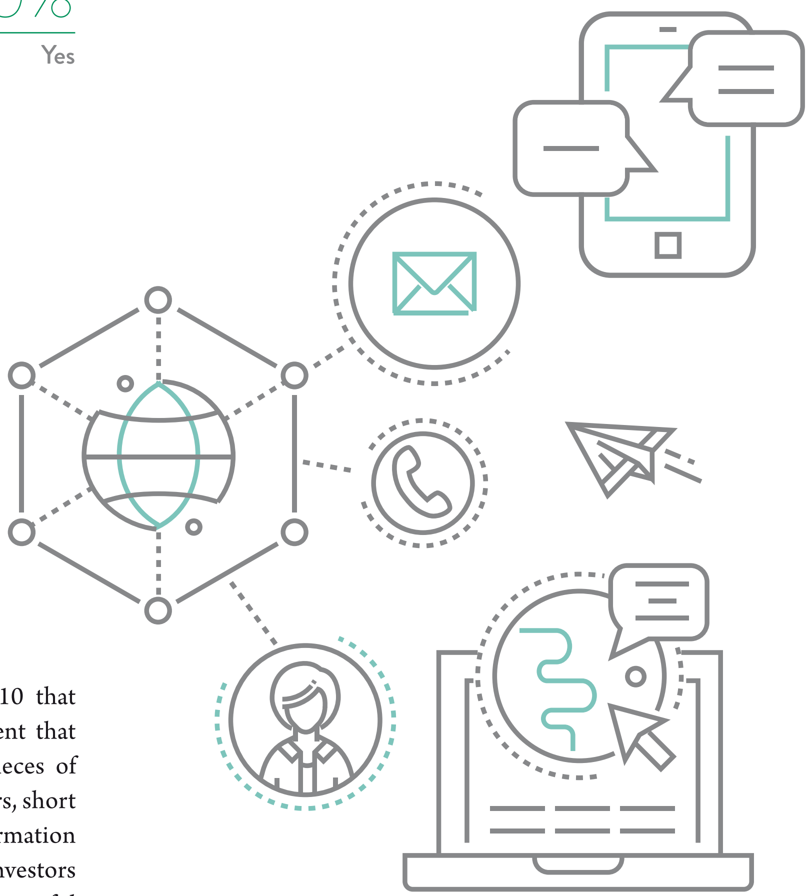
Investors are increasing their attention towards pay quantum, say **30%** of respondents, up **10% points** from last year.

Our findings on the importance for investors of the rigor of performance targets – the second most important pay consideration for three consecutive years, but a ten point jump from the previous year – coincides with investor concerns over pay quantum. If executive pay is substantial and growing, then investors expect a strong correlation with the achievement of challenging and rigorous targets – and for compensation committees to set these goals appropriately to justify the higher pay.

With regards to pay-for-performance, as in previous years, it remains the primary concern among investors when evaluating executive pay. We believe the decline in the percentage of respondents who consider the topic to be the most important is due to the enhanced and improved dialogue between investors and their portfolio companies. The engagements have allowed companies to better articulate their compensation stories for the year, providing investors with a lens into a company's approach to executive pay and the ultimate pay decisions. Additionally, in many markets, companies continue to dramatically improve their disclosure on executive pay and the link between pay and performance.

Q10 Do you support integrated reporting?





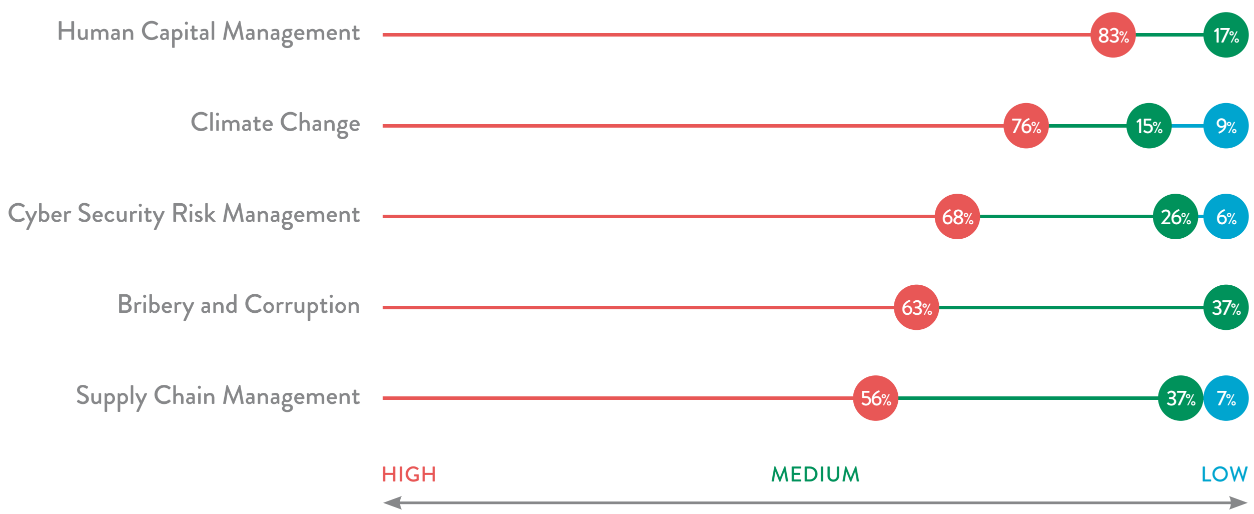
Remarkably, **80%** of respondents said in Question 10 that they support "integrated reporting," a global movement that addresses how companies can fit all these diverse pieces of performance data, financial and non-financial risk factors, short and long-term strategy and other strands of relevant information into a coherent whole to "tell the company's story." Investors want companies to provide a clear, concise and meaningful narrative rather than lengthy, piecemeal disclosures.

We would certainly welcome this, in light of our finding (Q1) that the long-term strategy of the company is an important voting consideration for many investors (**72%** of respondents). Integrated reporting is one of the ways companies can make it easier for investors to understand their strategy and as such, should be welcomed.

KEY TAKEAWAYS

A whopping **80%** of respondents support integrated reporting.

Q11 How important is more detailed disclosure for your evaluation of the following sustainability topics?



Disclosure quality is essential in any decision-making process investors carry out. Indeed, corporate governance developments not only cover the implementation of certain practices but also increasing the scope of the information reported. As the latter consolidates across several relatively new sustainability fields, it is crucial to find the balance between reporting what is material and satisfying investors' appetite for information.

In 2017 we asked investors which topics they would like to see more disclosure around corporate governance and sustainability, with "material sustainable issues" ranking 3rd with **71%** importance. This year we focused the question on key sustainability related topics. Significantly but maybe unsurprisingly **83%** of investors say human capital management is the most important topic when asking companies for more detailed disclosure. With an increasing volume of research demonstrating the link between levels of employee engagement and share-price performance of public companies, human capital management is becoming an important indicator for long-term investors when evaluating sustainable factors that could impact a company's long term value.

WHAT RESPONDENTS SAID...

"We recognise the Importance of individual factors will vary by sector and by company but if it's material to the business we would like to see more detailed disclosure."

Information on environmental-related matters was considered the second most important disclosure for investors to have when carrying out their sustainability evaluations, as disclosure on climate change was highlighted as a crucial element by **76%** of them. Consistently, only **7%** of the investors flag it as inconsequential.

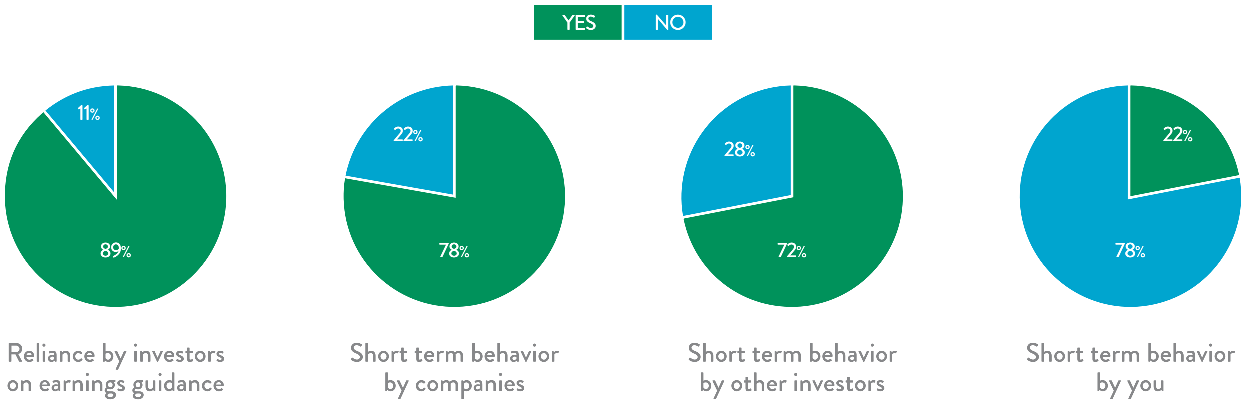
Finally, according to investors **(68%)** cyber security risk management is the 3rd most important topic when pushing for more sustainability disclosure in 2019. Conversely, only **9%** of the investors find it unimportant.

KEY TAKEAWAYS

83% of investors say human capital management is the most important topic when asking company's for more detailed disclosure.

Disclosure on climate change is also of great importance, say **76%** of respondents.

Q12 Do you believe quarterly reporting promotes the following?



INVESTORS SAID...

"We should not confuse quarterly reporting and quarterly guidance. Only the latter might drive short term behavior by companies."

While public companies in Australia, Europe, Spain, the UK and other countries are not obligated to file quarterly reports (though some companies do so voluntarily), companies in the U.S. are still required to do so. But that may be changing. The U.S. Securities and Exchange Commission is seeking public comment on "…how the existing periodic reporting system, earnings releases, and earnings guidance, alone or in combination with other factors, may foster an overly short-term focus by managers and other market participants."

The elimination of quarterly reporting is championed by many companies as well as the US Chamber of Commerce, which argue that quarterly reporting undermines a long-term focus among public companies. The Chamber has stated that they would "welcome an overhaul of a 1930s-era disclosure system that is not user-friendly and no longer meets the needs of a 21st century economy." Even a well-known activist, Nelson Peltz of Trian Fund Management, LLC, is in favor of eliminating quarterly reporting, stating that, "A company's management team will be able to use the additional time that would otherwise be spent on preparing quarterly earnings releases… on running the business."

Our survey echoes the concern amongst investors about quarterly reporting causing a short-term focus with **78%** of respondents saying that quarterly reporting promotes short-term behavior by companies. It is also of note that **72%** of respondents thought that quarterly reporting also promotes short-term behavior by investors. Curiously though, only **22%** of investors in the survey thought that quarterly reporting promoted their own short-term behavior.

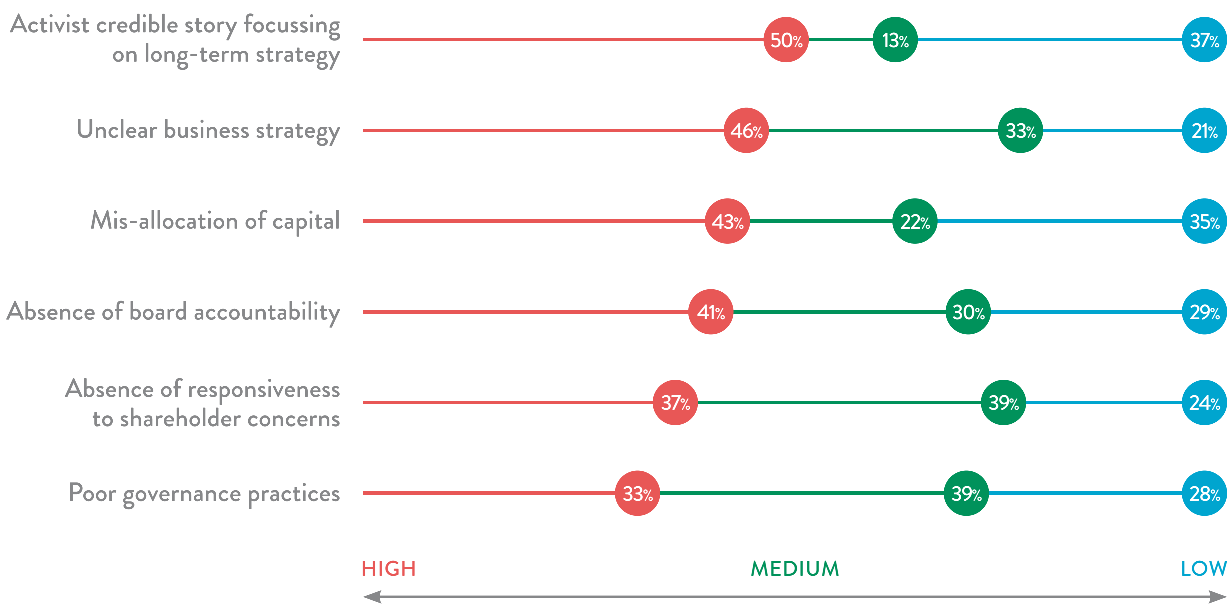
We also received an interesting comment from one investor who said, "We should not confuse quarterly reporting and quarterly guidance. Only the latter might drive short term behavior by companies. The quarterly reports provide investors with information on how companies are performing against the 'baseline ECG' of their long-term plan for value creation."

KEY TAKEAWAYS

78% of respondents say that quarterly reporting promotes short-term behavior by companies.

72% of respondents thought that quarterly reporting also promotes short-term behavior by investors.

Q13 In addition to poor financial performance, what factors lead you to support activist initiatives?



Activism continues unabated. According to Lazard, in 2018 activists targeted a record 226 companies, up from 188 in 2017. And campaigns were global, with the most active being in the US (**57%**), Europe (**23%**) and APAC (**12%**). Reflecting the rise of activism is that of the 131 activists that ran campaigns in 2018, about **30%** were first time activists. In large measure, the rise in activism can be ascribed to some macro factors.

For example, the last decade has seen an inflow of $1.5 trillion to index funds and ETFs and an outflow of $1.4 trillion from active managers. As a result, traditional, long-only active managers are turning to activism in an effort to distinguish themselves from passive funds and to justify to their clients the higher fees they charge.

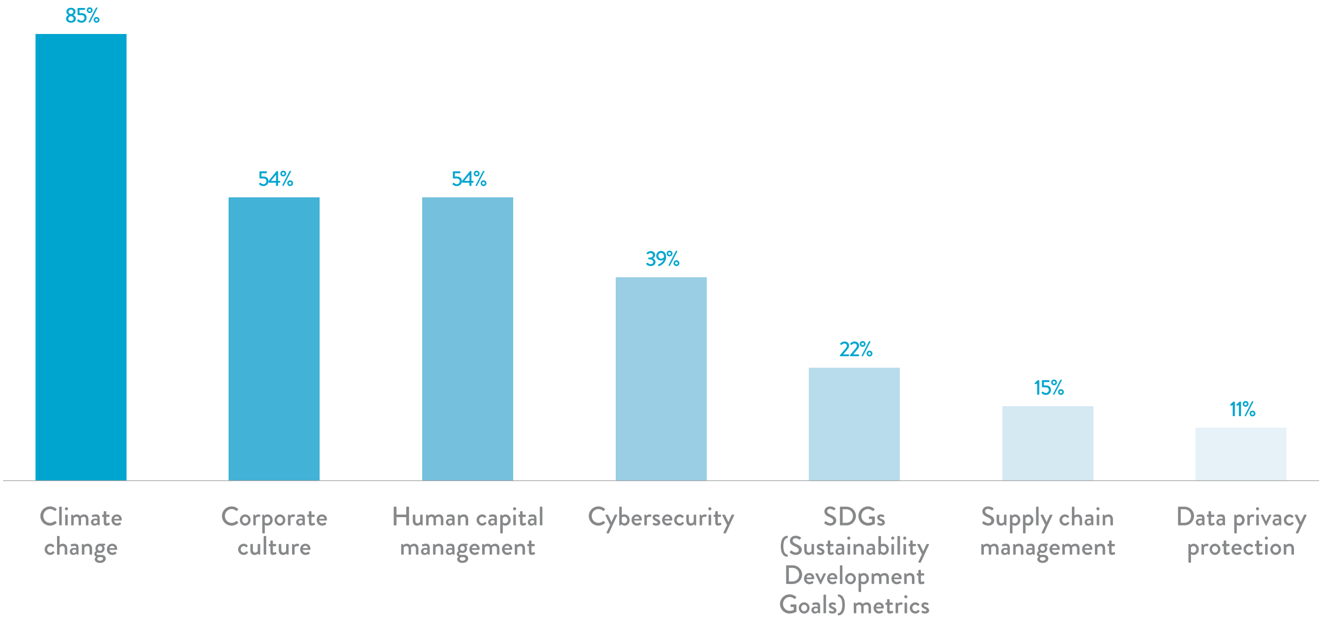
Even traditional, long-only investors are using activist engagement and advocating for strategic change at portfolio companies, either on their own or in conjunction with known shareholder activists. These investors are looking to analyze issues related to long-term strategy, capital allocation and, increasingly, risks associated with E&S issues and the board's assessment of risk and plans to deal with risk on many fronts.

We have also seen index funds more willing to flex their muscle. And with Vanguard, BlackRock and State Street alone controlling close to **20%** of most large US companies; companies will feel the heat. While index managers may not have the capacity to analyze individual companies, they are increasingly receptive to campaigns by activists. Especially as activists craft campaigns that are well thought out, steeped in detail and lay out a plan for long-term growth at targeted companies.

Our survey confirms that a focus on the long-term is critical for investors. In fact, this was the primary factor cited by investors as a reason to support an activist; with **50%** of respondents indicating that it was "most important" that an activist have a credible story focussing on long-term strategy.

Focus on the long-term as a reason to support an activist was followed by **46%** of investors that felt support for an activist was warranted if a company had an unclear business strategy. This was closely followed by **43%** of investors that believe mis-allocation of capital could result in support of activist initiatives, **37%** that said the reason to support an activist was an absence of responsiveness to shareholder concerns and **33%** suggest poor governance practices could also lead to supporting activist proposals/initiatives.

Q14 Which three sustainability topics will you focus on most when engaging with companies in 2019?



In recent years Institutional Investors have invested heavily in stewardship to drive corporate decisions and influence their ESG and sustainability policies and practices. Key stakeholders including Governments, NGOs and Asset Owners, and the endorsement of key initiatives such as Climate Action 100+ and the TCFD recommendations have propelled companies and shareholders to intensify their engagement focus.

85% of survey respondents indicated that climate change will be the most prioritised sustainability topic of their corporate engagements in 2019, this is up **31 percentage points** from last year, a significant increase, and **35 percentage points** since 2017.

54% of investors agreed that human capital management, up **30 percentage points** from 2018 and corporate culture will be the other key engagement topics in 2019.

As identified in the results, investors will increase their engagement efforts and focus on companies' alignment between their internal allocation of capital and business strategies to help move towards a low carbon economy. As ESG integration gradually impacts investment decisions, Institutional Investors will escalate their stewardship obligations as they look to impact capital allocation investment decisions.

It is also worth noting that **22%** of respondents identified the United Nations Sustainability Development Goals (UN SDGs) as a key focus area. The UN SDGs are a set of 17 global goals established by the United Nations in 2015 aiming to "end poverty, protect the planet and ensure prosperity for all" by 2030.

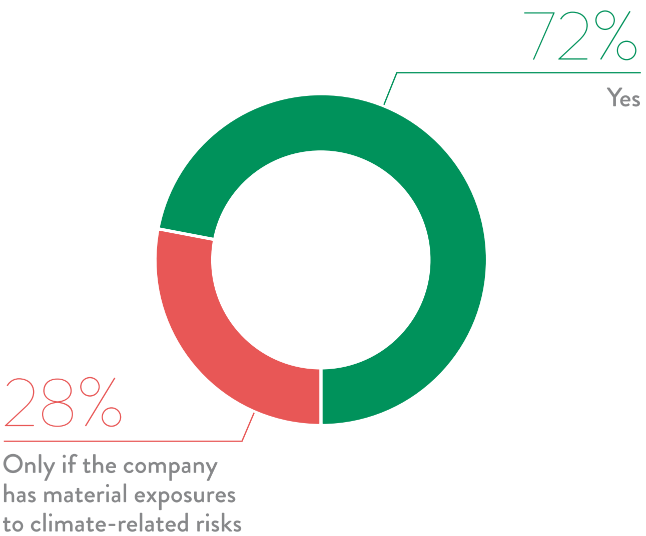
According to a report jointly published in July 2018 by the Global Reporting Initiative, the Principles for Responsible Investment and the UN Global Compact, investors are increasingly expecting companies to report on the SDGs relevant to their operations and their impact on company strategy and financial performance.

KEY TAKEAWAYS

85% of survey respondents indicated that climate change will be the most prioritised sustainability topic of their corporate engagements in 2019.

54% of investors equally agreed that human capital management and corporate culture will be the other key engagement topics in 2019.

Q15 Do you believe that companies should adopt the recommendations of the task force on climate-related financial disclosures?



WHAT RESPONDENTS SAID...

"All companies should review the TCFD recommendations when thinking of how to improve their reporting on climate risk."

In June 2017, the Task Force for Climate Related Disclosures (TCFD), a Financial Stability Board initiative, published a set of recommendations which aim "to provide a foundation to improve investors' and others' ability to appropriately assess and price climate-related risk and opportunities." Under these voluntary recommendations, companies are encouraged to disclose information on their climate related-risks, climate-related opportunities as well as the financial impacts of climate change on their business.

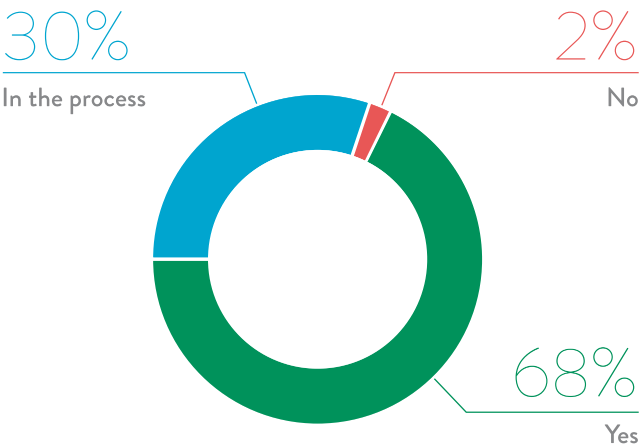
Market support for the TCFD recommendations appears to be on the rise. As of December 2018, more than 500 organisations globally have officially expressed their support for the TCFD and its recommendations including listed companies, institutional investors and other organisations.

KEY TAKEAWAYS

72% of respondents agree that companies should adopt the TCFD recommendations.

While **28%** of respondents indicated that companies should adopt the TCFD recommendations only if they have material exposures to climate-related risks, more significantly, **72%** of respondents agree that companies should adopt the recommendations regardless.

Q16 Are ESG, non-financial risk factors and sustainability now integrated into your investment/divestment decision-making processes for all asset classes?



ENVIRONMENTAL

SOCIAL

GOVERNANCE

Issuers' sustainability and ability to manage risk and inform the market of non-financial performance indicators that might impact company performance is becoming an increasingly important element for investors. Indeed, the attention given to how ESG impacts investees' company's share price and business development is considered for some investors as important as the usual assessment of investees' economic and financial performance. Nonetheless, there is some scepticism within the investor community as they grapple with linking ESG considerations with positive financial returns. As Institutional Investors frequently inform us that clients/asset owners ask more questions about how they consider ESG, we followed up with the same question from last year to gauge appetite for ESG integration and investment strategies.

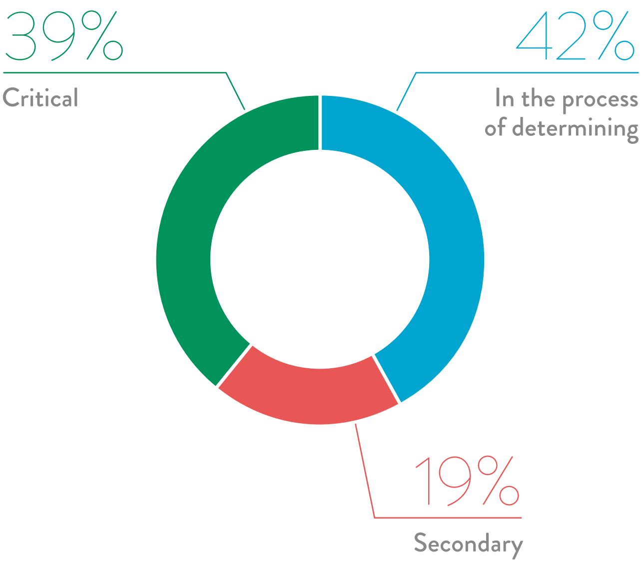
We found a marked increase compared to last year as **68%** of investors, a rise of **19 percentage points**, confirm they integrate non-financial factors across all asset classes. **30%** of respondents suggest they are still in the process and only **2%** of investors said that the assessment of non-financial, ESG factors are not integrated in their investment decisions, down **5 percentage points** from 2018.

KEY TAKEAWAYS

68% of investors say ESG factors are now fully integrated across all asset classes.

Interestingly only **2%** say non-financial, ESG factors are not integrated into their investment decisions.

Q17 When making fixed income investment decisions, how important is a company's ESG disclosure?



For several years now, many mainstream investors have been working on integrating ESG considerations in their fixed income investment decision making. This progress is evidenced by the fact that **39%** of our respondents stated the quality of ESG disclosure is becoming critical when making fixed income investment decisions, this is an increase of **24 percentage points** from 2017. A further **19%** agree it is at least viable but a secondary consideration. Furthermore, the number of respondents still "in the process of determining" is down **15%** points from 2017 with only **42%** of investors admitting they are still "in the process of determining" this year. Interestingly, like 2017, no investor (**0%**) considered it not critical.

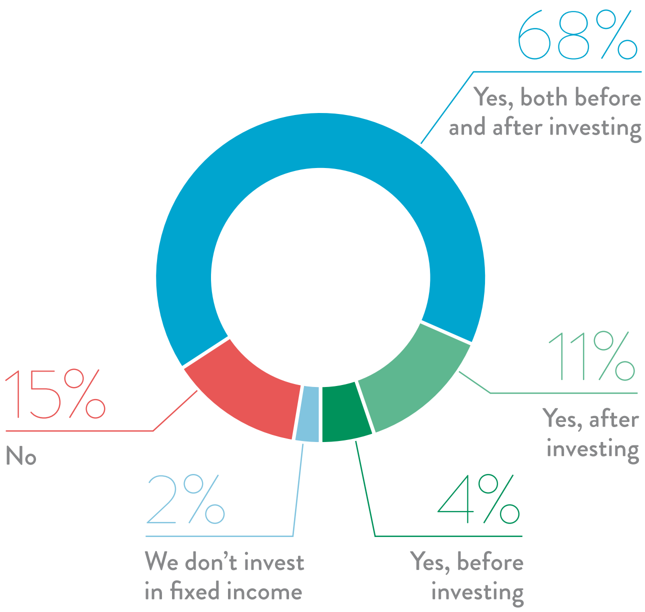
From a corporate perspective, the current status of ESG integration in fixed income can be confusing. Unlike equity, where shareholder meetings provide a natural point of contact for such interaction, the investment cycle in fixed income means that the interaction with fixed income investors, unless proactively triggered, could only happen around the time of issuance. From our experience, a growing number of investors tend to involve fixed income team members in existing ESG engagements but initiating a stand alone fixed income engagement is still an unusual occurance. However compared with our 2017 results, the 2019 survey outcomes provide further evidence that investors are increasingly assessing non financial, ESG factors to help mitiage risk.

KEY TAKEAWAYS

39% of our respondents stating the quality of ESG disclosure is becoming critical, up **24% points** from 2017.

Interestingly, no investor (**0%**) considered it "not important", the same outcome as 2017.

Q18 When making fixed income investment decisions, do your portfolio managers or your stewardship team engage with companies on ESG issues?



There is a strong perception that focus on ESG will contribute to the overall performance of funds over time. An increasing number of the respondents we surveyed have adapted their understanding of ESG and now see ESG assessment as an integral part of their risk management exercises. Fund managers are asking more questions about ESG topics and Investment Stewardship Analysts are feeding them with additional intelligence around non financial factors that might impact risks and opportunities.

As discussed in the previous fixed income question, for several years now, investors are integrating ESG considerations in their fixed income investment decision making. Here we asked at what stage are investors assessesing ESG risks. **68%** of respondents will assess ESG factors both before and after investing, this is an increase of **12 percentage points** from 2017.

Only **15%** of respondents reveal they do not consider ESG as a key issue when making investment decisions, this is down **10 percentage points** from 2018 when we asked investors the same question related to green bonds.

Credit managers are increasingly working to assess materiality of specific ESG considerations before making investment decisions. While explicit ESG data is increasingly available for the fixed income market, the market still lacks a common practice in ESG integration. Understanding how money managers integrate ESG factors into their investment decisions is an important component to evaluating their security selection and portfolio construction processes.

KEY TAKEAWAYS

68% of respondents will assess ESG factors both before and after investing, this is an increase of **12 percentage points** from 2017.

Only **15%** of respondents reveal they do not consider ESG as a key issue when taking investment decisions.

COMPANY OVERVIEW

Morrow Sodali is the leading global consultancy specializing in **shareholder and bondholder services, corporate governance, proxy solicitation and capital markets transactions**.
The firm provides corporate boards and executives with strategic advice and services relating to a broad range of activities, including: mergers and acquisitions, annual and special meetings, shareholder activist initiatives, multinational cross-border equity transactions and debt restructuring services.

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AUTHORS

KIRAN VASANTHAM
Director
Investor Engagement
k.vasantham@morrowsodali.com

DAVID SHAMMAI
Corporate Governance Director
Cross Border
d.shammai@morrowsodali.com

NEW YORK

CHARLES A. KOONS
Managing Director
Activism & Contested Situations
c.koons@morrowsodali.com

LONDON

CHARLES NELSON
Director
Head of UK
c.nelson@morrowsodali.com

SYDNEY

CHRISTIAN SEALEY
Chief Operating Officer
Australia
c.sealey@morrowsodali.com

FRANKFURT

ANDREA BISCHOFF
Senior Director
a.bischoff@morrowsodali.com

MADRID

BORJA MIRANDA
Managing Director
b.miranda@morrowsodali.com

PARIS

JEAN-FLORENT RÉROLLE
Managing Director
jf.rerolle@morrowsodali.com

ROME

ANDREA DI SEGNI
Managing Director
a.disegni@morrowsodali.com

SAO PAULO

AGNES L. BLANCO QUERIDO
Director
a.blanco@morrowsodali.com

STAMFORD

WILLIAM ULTAN
Managing Director, Corporate Governance
w.ultan@morrowsodali.com

OFFICES

NEW YORK
509 Madison Avenue
Suite 1206
New York, NY 10022
P. +1 212 825 1600

LONDON
103 Wigmore St
Marylebone, W1U 1QS
London, United Kingdom
P. +44 207 355 0921

SYDNEY
135 King Street
Suite 25.02, Level 25
Sydney NSW 2000
P. +61 2 80 22 79 35

FRANKFURT
Mainzer Landstrasse 50
60325
Frankfurt am Main, Germany
M. +49 176 6366 7485

MADRID
Calle de Almagro 3
28010
Madrid, Spain
P. +34 9142 91 412

PARIS
29-31 Rue de Courcelles
75008
Paris, France
P. +33 1 79 97 13 66

ROME
Via XXIV Maggio, 43
00184
Rome, Italy
P. +39 06 45212800

SAO PAULO
Rua Prof. Atílio Innocenti 165, 4º Andar
Vila Nova Conceição
São Paulo - SP, 04538-000, Brazil
M. +55 11 972 783 858

STAMFORD
470 West Avenue
Suite 3000
Stamford, CT 06902
P. +1 203 658 9400

Local Partnerships:
MEXICO CITY • BEIJING • JOHANNESBURG

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