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Please read the important disclosure at the end of this article.

TAKING ACTION ON THE IMPLICATIONS OF CLIMATE CHANGE

At Newton, we have been actively incorporating the consideration of environmental, social and governance (ESG) issues since our inception 40 years ago. We have been conducting ESG reviews on recommended stocks since 2005 and have exercised our clients' voting rights in the UK since inception, and globally since 2000. We have also been a signatory to the Principles for Responsible Investment (PRI) since February 2007 and consistently achieve top ratings. Responsible investment is integral to our investment process and climate change remains a key consideration for us as a firm.

CLIMATE CHANGE: WHY ARE WE THINKING ABOUT IT?

Navigating the challenges associated with climate change on behalf of our clients is a significant task.

Given the multifaceted nature of climate change, it is vital to identify and analyse a number of key forces driving related opportunities and risks. As active thematic investors, we use three particular elements of our investment process in seeking to address climate change:

WHY SHOULD INVESTORS BE THINKING ABOUT IT?

The issue of climate change is here to stay. It presents a considerable risk to humanity, but it will also create opportunities, as new ways of doing things come to the fore.

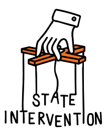
The industries and businesses which are well equipped to deal with these changes stand to prosper, whereas others which are less prepared are likely to fail.

1. OUR INVESTMENT THEMES

Our investment themes provide us with vital perspective on the investment landscape, allowing us to block out short-term market 'noise' and identify those powerful forces of fundamental change in the world around us, such as climate change. Three of our themes in particular help us to identify three highly interconnected ways in which climate change could have an impact on our clients' investments:

This theme helps us monitor the effects of greater societal and governmental awareness of climate change.

It also highlights the direct physical impact on companies as input costs increase while the world's economic resources become progressively depleted, as well as the indirect costs arising from extreme weather damage to assets.



With public awareness of climate change increasing, pressure is growing on policymakers to take action to mitigate the impact. This is likely to lead to increased regulation and policies, resulting in increased compliance costs for carbon-heavy businesses.

Meanwhile, public policy in the form of incentive schemes and tariffs has been vital in supporting renewable technologies, which we believe is creating attractive long-term investment opportunities.

An example of such a policy is the Renewable Obligation Certificate Scheme (ROCS) in the UK, which provides a floor to the return that is made from investing in new renewable assets.

This theme highlights innovation in renewable energy, and the associated opportunities for investors.

The sector offers bond-like investments, many of which benefit from government subsidies, and provide investors with significant diversification, a healthy dividend yield and potential for capital growth.

The key risk to investors is that, where incumbent companies do not make sufficient adjustments to their business models, assets will become 'stranded' (subject to premature devaluation as a result of regulatory or market changes).

How our themes help us identify the opportunities and risks of climate change

Identify drivers

Earth matters and *state intervention*

EU legislation requires reduction in carbon emissions by 2020; UK government needs to upgrade energy infrastructure.

Investment implications

Net effects

- Winners: Providers of renewable electricity.
- Losers: 'Dirtier' traditional sources of energy (e.g. coal, nuclear).

Investment opportunity evaluation

Renewable electricity company

- 6% dividend yield on offer
- Growth linked with Retail Price Index
- Dual income sources: Electricity imported to grid and ROCS subsidy

For illustrative purposes only.

Your capital may be at risk. The value of investments and the income from them can fall as well as rise and investors may not get back the original amount invested.

2. INTEGRATION OF RESPONSIBLE INVESTMENT (RI) CONSIDERATIONS

We believe responsible investment is better investment.

We mean this in an economic sense; we think that responsibly managed companies are better placed to achieve sustainable competitive advantage and provide strong long-term growth. In terms of climate change, we believe those companies which are adapting to the changing regulatory, economic and social backdrop offer the most attractive investment prospects.

RI considerations are an integral part of the investment decision-making process across all our strategies. We do not select securities simply for their RI or climate-change-related credentials, but seek investments which provide the optimum risk/return trade-off, backed by thematic drivers and solid fundamentals at an attractive valuation.

We also offer a number of sustainable strategies, which aim to achieve their objectives through investing for the long term in securities of companies that demonstrate attractive investment attributes and sustainable business practices, and that have no material unresolvable ESG issues:

- Embedding ESG analysis to look beyond the financial statements
- Investing in companies that positively manage the material impacts of their operations and products on the environment and society
- Sustainable 'red lines' ensure the poorest-performing companies are not eligible for investment, such as companies that violate the UN Global Compact Principles of sustainable corporate performance. Companies which we think are incompatible with the aim of limiting global warming to 2 °C are also excluded
- No investment in any company that derives more than 10% of its turnover from the production and sale of tobacco
- Avoidance of companies with material ESG risks which are likely to negatively affect future performance
- Engaging with companies where ESG issues are resolvable and can be improved, and reporting on that activity

We take three key steps to try to ensure our clients' portfolios are positioned for changes in the investment landscape brought about by climate change:

1. Integrated ESG research

We believe ESG factors can have a material impact on company value, and for a number of years our RI team have conducted ESG quality reviews of all the companies recommended by our sector analysts. We follow research from independent sources such as CDP (formerly the Carbon Disclosure Project), Institutional Investors Group on Climate Change (IIGCC) and Carbon Tracker in conjunction with our own proprietary research. Such research covers topics such as policy risk, long-term planning, emissions, use of natural resources and event risk.

2. Engagement and active proxy voting

We have a rigorous approach to corporate governance and proxy voting, and we engage proactively with companies to bring climate-change related issues to the forefront of their thinking and to push for better practices. Examples of issues on which we have engaged recently with companies include climate resilience and stranded assets among heavy greenhouse gas emitters, reactions to COP 21, and investment in renewables.

3. Monitoring of policy and regulation

We follow developments in the policy and regulation landscape closely, and attend climate negotiations and conferences. Our team members are members of key bodies, such as the CDP.

We think that responsibly managed companies are better placed to achieve sustainable competitive advantage and provide strong long-term growth

RESPONSIBLE INVESTMENT ENGAGEMENT CASE STUDY

Child labour and cobalt mining

We worked with a large Korean battery manufacturer, of which we are one of the largest shareholders, after concerns were raised over the use of child labour in its supply chains (for mining the cobalt used in the batteries). After visiting China and South Korea to look at the supply chain in person, we realised that an issue with child labour existed – linked to the poor economic situation in the Democratic Republic of Congo (DRC) – and that it needed to be raised with management.

After a number of emails, calls and meetings with management, we were able to get an internal report published that assessed the company's involvement with child labour in cobalt mining and raised the profile of the issue internally. The company also explained that it was working with the Responsible Cobalt Initiative (RCI) as the best way to drive real change.

We then went to engage with other companies on this issue and support the RCI, as it was clear that this was an ESG issue that many companies were involved with. We continue to work with the battery manufacturer to monitor progress on the initiatives created to address the problem and push for a full supply chain audit. Overall, we believe the response has been positive and will improve lives in the DRC.

For illustrative purposes only.

3. OUR ETHICAL INVESTMENT KNOWLEDGE AND EXPERIENCE

The movement towards fossil-fuel divestment – the removal of stocks, bonds and other instruments from portfolios – is a young, rapid and fast-evolving trend. An increasing number of institutions and charities are seeking to align their capital with their mission and objectives, and implement a form of fossil-fuel restriction. We believe all investors, those who do implement a screen and those who do not, could benefit from experience and knowledge in this field.

Experience

In trying to strike an appropriate balance between delivering attractive investment returns and avoiding key areas of concern, experience is key.

At Newton, we manage £2.9 billion in assets covered by ethical criteria (as at 30 June 2018), and we have run ex-fossil-fuel portfolios for over 14 years.

We have worked with clients to create and implement ethical policies ranging from full sector-wide exclusions of extractives through to targeted restrictions on companies deriving significant revenues from the most carbon-intensive fossil fuels, thermal coal, tar sand and oil shale.

Knowledge

We pay close attention to the changing ethical investment landscape to ensure we are aware of the latest developments and trends.

For investors who are considering an ethical policy, it is vital they are aware of the potential effect it could have on their portfolio, and as such, in 2015 we commissioned two academics from Warwick Business School to publish independent research on the topic

Conclusion

As we have outlined above, climate change is a multifaceted issue for the investment community. However, we believe our active, thematic approach, integration of responsible investment considerations and extensive experience in the field of fossil-fuel divestment stands us in good stead as we manage our clients' portfolios amid the changes inherent in climate change.

OUR ETHICAL INVESTING RESEARCH
THE IMPACT OF ETHICAL INVESTING ON RETURNS, VOLATILITY AND INCOME

Despite the growing number of institutions adopting ethical investment approaches, there have been few studies of the impact of these on an investment portfolio.

Against this backdrop of minimal research, we commissioned Dr Chendi Zhang of Warwick Business School to analyse the impacts of commonly applied ethical screens, including fossil fuels.

Dr Zhang's research, which covers a sample period from 2004 to 2015, evaluates the impact of exclusions in terms of performance, yield and volatility. 10,000 stocks in 28 developed and emerging markets, and 1,283 US corporate bonds, were included in the scope of the paper.

The key impacts of fossil-fuel restrictions were that:

- Overall returns increased by 0.02% p.a.
- Volatility was lowered by 0.02% p.a.
- Dividend yield was reduced by 0.03% p.a. The *de minimis* impact on yield is perhaps surprising given that oil & gas has historically been heralded as one of the best-yielding sectors
- During periods of sustained fossil-fuel price weakness, the enhancement to return of fossil-fuel avoidance was as much as 0.86% between 2012 and 2014
- Impact of exclusion of equities and bonds domiciled in different countries on returns varies over time (see illustration)

Range in impact on portfolio returns of exclusion per annum (%)

DEVELOPED MARKETS	US	UK	EMERGING MARKETS
-0.3% ↔ 0.9%	-0.5% ↔ 0.5%	-0.9% ↔ 1.8%	Increases returns all time periods max 2.6% p.a. 2008 - 2010

Source: The Impact of ethical investing on returns volatility and income, Newton, 2015.

To find out more and read the full paper, visit: www.newtonim.com/info/impact-of-ethical-investing

For illustrative purposes only. The research and data contained in this document was commissioned by Newton in 2015.
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Responsible investment policies and principles

Here we lay out our approach in detail, how it works in practice and how it adds value.

Quarterly responsible investment report

We fully disclose our voting activity and company engagement for each quarter in this quarterly report.

Thought leadership

We publish articles and blogs on a wide range of topics related to responsible investment.

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