Engagement Report 2021

METROPOLE Gestion

1. Purpose of the engagement report

As a company committed to Responsible Value Investing and an ESG pioneer since 2008, we attach great importance to companies taking ESG criteria into account. We firmly believe that engaging with companies promotes long-term value creation and is of benefit to all stakeholders (shareholders, employees, clients, suppliers, etc.).

Value creation is all the more significant and enduring when it offers capital providers a fair return and contributes to social utility. With this in mind, we engage with the companies in which we invest and encourage them to improve their extra-financial practices.

METROPOLE Gestion engages with the companies in which it invests whenever it identifies ESG risks or opportunities for improvement.

In concrete terms, this engagement may take one of three forms: individual engagement, thematic engagement and/or collective engagement.

Individual engagement involves initiatives broached directly by METROPOLE Gestion through ongoing dialogue with companies, dealing with controversies according to our procedure whenever events occur that might have a significant impact on companies and their stakeholders, and using our voting rights on ESG-related resolutions.

Thematic engagement, resulting from careful consideration carried out in-house and reviewed annually, on clearly defined themes.

Collective engagement is pursued jointly through investor groups or associations, with a view to increasing their influence over companies. METROPOLE Gestion reserves the option to take part in collective initiatives regarding ESG issues whenever it deems such action necessary, in the interests of investors and stakeholders.

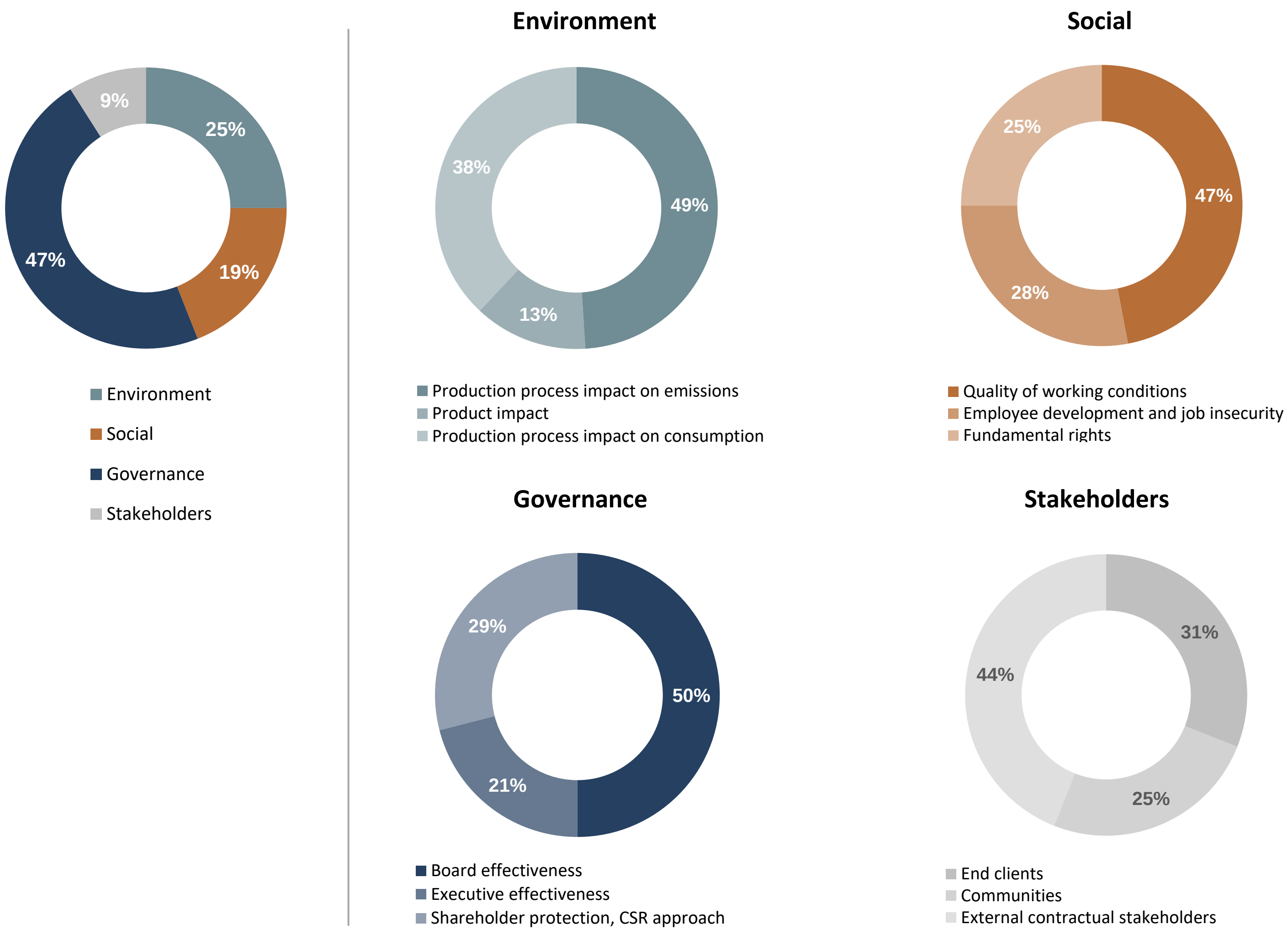
The purpose of this report is to present our interactions with the companies over the course of 2021 on our four pillars of extra-financial analysis: Environment, Social, Governance and Stakeholders.

2. Individual engagement

2.1 Dialogue with the companies

2.1.1 Our engagement in figures

Over the course of 2021, we conducted approximately 360 company interviews. We focus our ESG interviews on the issues specific to each company and to each business sector. We direct our questions primarily towards any weak points in the company, identified by means of our proprietary ESG rating model. In 2021, the issues discussed with companies were distributed as follows, by pillar and sub-pillar:



Governance and Environment related issues dominated our discussions with the companies in 2021.

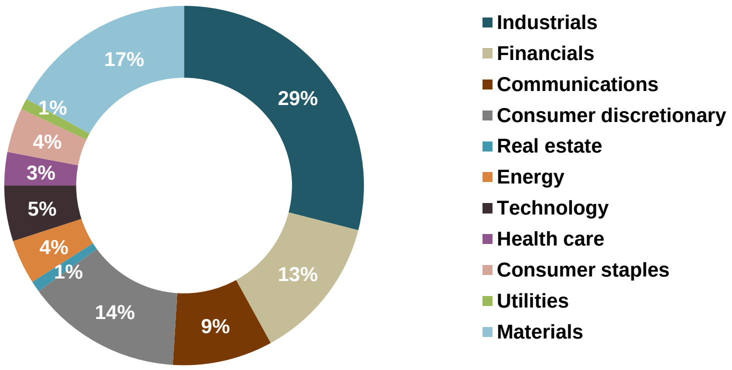
Governance features as one of the most discussed issues during our meetings with the companies. Firstly, because it covers every aspect of the organisation of corporate management and as such constitutes a prerequisite. Secondly, it is the pillar for which we have the largest number of measurement possibilities as it is subject to the highest level of regulation and also features among the most popular questions submitted to shareholder vote at general meetings. Lastly, because governance is subject to national regulations, it sheds light on specific local factors that need to be addressed with issuers. Examples include the significant level of employee representation on German Boards of Directors, or the practice common in Sweden of different classes of share entitling holders to different voting rights.

The issue of the Environment unsurprisingly took centre stage during our meetings, for two main reasons. Firstly, questions relating to energy transition and climate risks are highly likely to constitute the main issue over the coming decade. On this point, it is noteworthy that the pandemic crisis has added momentum to the movement already under way in recent years and has definitively placed climate issues at the heart of corporate strategies. Elsewhere, our thematic engagement for 2021, which is set out in detail in section 3 of this report addressed the financing of this energy transition by the banking sector. We discussed the issue specifically with most of the banks featuring in our portfolio.

The Social pillar, which is also strictly regulated in Western countries, is rarely subject to breaches and gives rise to fewer discussions. Dialogue is initiated, however, when controversy emerges surrounding working conditions and, especially, when fundamental rights are not being respected. We double down on such matters during our meetings with the companies operating in many regions of the world with less comprehensive protection of workers' rights, or with industrial companies, which are much more exposed to security risks.

Lastly, the Stakeholder pillar, which covers all the relations between the company, its customers, suppliers, public authorities and wider civil society, concerns issues that are frequently external to the company, which they may struggle to tackle. We systematically hold discussions with companies, however, whenever major controversies emerge (see section 2.1.3 Dialogue around controversies).

By sector, our interviews were distributed as follows:

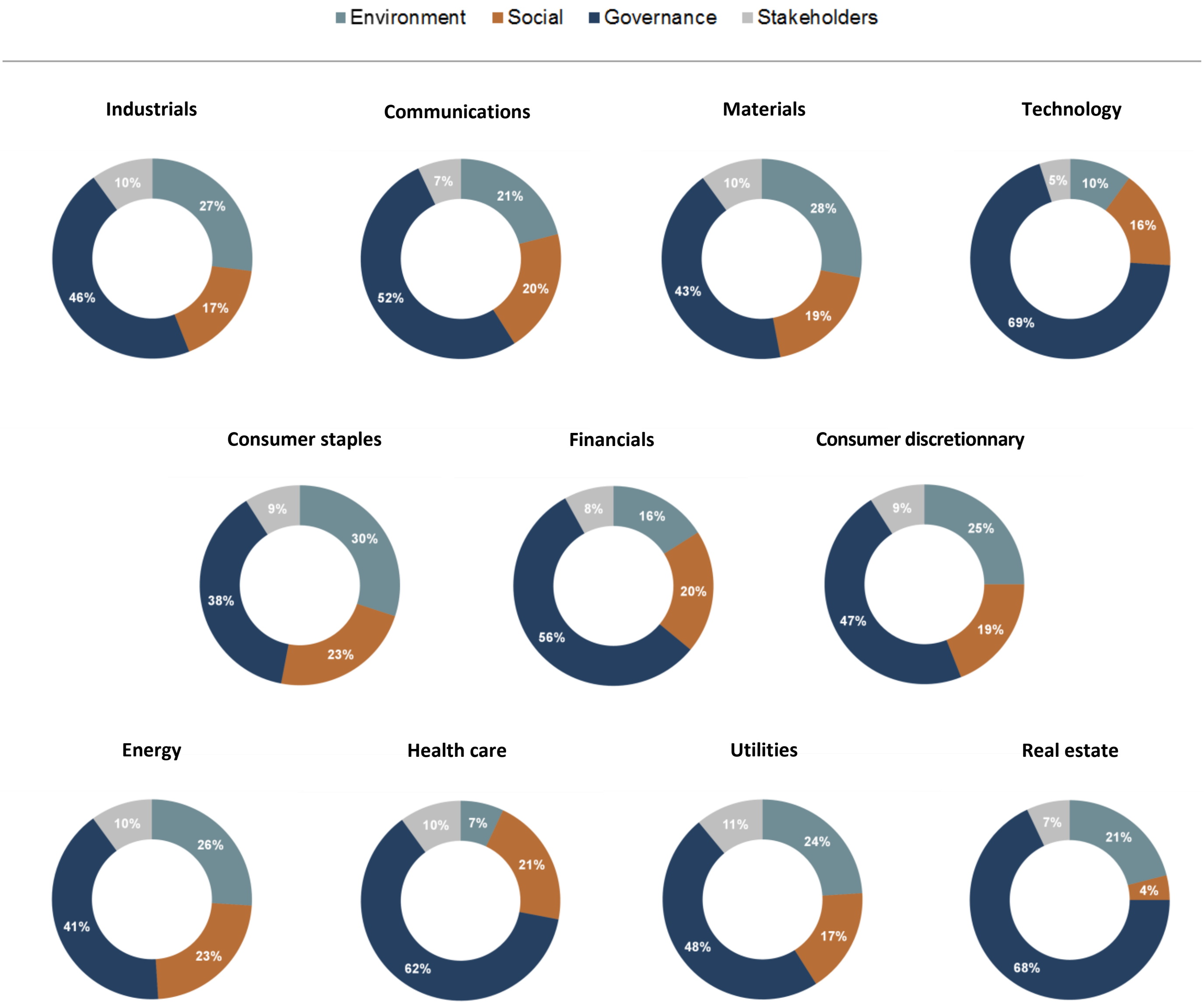


Within each sector (see figures below), the breakdown of issues by pillar generally follows the same trend, although with differences by sector.

We found that discussions on the theme of the environment played a predominant role in dialogues with consumer staples, energy and materials companies. While outwardly surprising in the case of the consumer staples sector, this result reflects the fact that most of our discussions within this sector were with brewery firms, where environmental issues are actually of considerable importance, particularly as regards water consumption and waste management. The energy and materials sectors are naturally concerned, as energy transition is an unavoidable issue in their case.

Matters of governance were central in discussions with the technology, health and finance sectors. These results reflect in particular the frequency of our discussions with tech sector firm Atos in the light of the anomalies identified in its publication of its annual financial statements and the reorganisations taking place within the group.

Finally, the consumer staples sector also emerged as the most significantly affected by social matters. We had a number of discussions with AB InBev on the issue of working conditions, which attract recurrent criticism and negatively affect the group's ESG rating.



2.1.2 Impact of dialogue with the companies

In accordance with our ESG approach, our dialogue with the companies enables us to discuss and influence the companies' activities in the areas of the Environment, Social, Governance and Stakeholders. For each pillar, we therefore raised with companies the most relevant elements of our engagement approach.

Governance forms the bedrock of all implementation policies within a given company. Through dedicated quantitative and qualitative means, the company is able to establish the credibility and effectiveness of such policies, both internally and externally. The CSR policy is no exception to this rule. Its impact is therefore all the greater when it is made the responsibility of corporate executives and also involves a wider range of functions. From this standpoint, the unparalleled pandemic crisis the world has undergone over the past two years has accelerated awareness of the importance of ESG issues and propelled them to the very heart of corporate strategies. Also, most strategic plans announced nowadays include extra-financial targets among corporate priorities. The majority of companies are rethinking their governance accordingly and assigning responsibility for these issues to their executive or non-executive directors.

This shift has naturally led to a growing proportion of companies incorporating extra-financial criteria into their remuneration packages, one case in point being HeidelbergCement. The German cement manufacturer has introduced a multiplier system based on CO2 emissions levels and applied to financial results, ensuring that good financial performance is not rewarded if it comes at the expense of extra-financial performance. In the wake of our dialogue with companies, we note with satisfaction that similar practices are increasingly spreading to small-cap companies, despite their more limited resources. Construction materials group Wienerberger also introduced extra-financial criteria into the variable pay of its executives over the course of the year, following our opposing vote and discussions with the company over the course of the previous financial year. Rexel, too, has undertaken to include environmental criteria in its executive pay policy with effect from 2022.

We maintain dialogue with companies that have not yet implemented such measures or only imperfectly. This seems to be particularly the case with companies that have recently changed structure, such as Siemens Energy, created by Siemens' spin-off of its energy business at the end of 2020, or Metso Outotec, product of the merger between the two Finnish mining equipment groups, Metso and Outotec. The main reason for this is that the companies concerned are still rebuilding their governance structures. As a general rule, issuers are receptive to the idea of aligning executive incentives with extra-financial issues.

At the same time, the inclusion of ESG issues at the heart of corporate strategies requires companies' operational teams to buy into these policies in order to implement them effectively. While dedicated CSR teams still exist, they now play a much wider role and are working alongside operational divisions to structure the deployment of CSR policies, these policies are now only rarely confined to a dedicated team. We see this as an encouraging change, attesting to the important role that ESG has come to play in corporate strategy.

The Environment pillar is, naturally, the subject of discussion with issuers that has gained the most ground in recent years. The advances that have been made also bear out our approach, one that advocates dialogue with companies wielding a significant environmental footprint rather than flying in the face of industrial and environmental realities by systematically excluding them.

While 2020 saw most of Europe's oil and gas turn an historic corner with the adoption of energy transition strategies, 2021 was the year for them to consolidate their ambitions. By putting their targets and target monitoring to shareholder vote, as TotalEnergies and Shell both did, the oil and gas groups continued to reinforce their commitment to and transparency in the pursuit of those targets. From now on, the aim of our dialogue is to encourage these companies to even greater efforts so as to underscore the credibility of their approach and seize the opportunities that energy transition has to offer.

While these key players have certainly become aware of the risks and opportunities involved, all are calling for greater visibility in regulatory and political terms if they are truly to accelerate these changes.

Finally, in illustration of our remarks on governance, these companies are employing structural measures to establish the credibility of their strategies. Most of these groups have allowed their renewables activities considerable freedom of manoeuvre in terms of development, and groups like Repsol and Eni are also looking to attract new investors to join them in exploiting these opportunities.

Other big CO2 emitters are increasing their investments with a view to meeting their target of carbon neutrality by 2050 at the latest. Europe's steel makers and cement manufacturers, in particular, are increasingly developing more new projects with an eye to the future. ArcelorMittal has announced massive investments in Germany and Spain designed to decarbonise its existing steel production and move towards green steel. Sweden's SSAB will also be producing green steel as from 2026. Italian cement group Buzzi Unicem has also announced it is aiming for carbon neutrality, with the details to be fleshed out in 2022.

Under the impetus of regulation and also the cost of European carbon credits, all the major players are picking up the pace of transformation, often in collaboration with governments ready and willing to provide massive subsidies for such projects. In doing so, they are setting up competitive advantages for the long term over mainly non-European players that are not working to acquire this kind of expertise. In the shorter term, however, they are calling for better visibility in terms of regulations to ensure they are not unfairly penalised by one-sided regulation that is currently undermining their competitiveness. The introduction of the Carbon Border Adjustment Mechanism at EU borders should serve to protect the balance here.

Fully aware that there is still a long way to go on energy transition, we are pursuing our dialogue with all concerned, to achieve a better understanding of where improvements can be made and to encourage companies to make those improvements. Over the course of 2021, we focused particularly on dialogue with banks on their approach to the financing of energy transition, since they will be the ones helping companies, via the lending they provide, to achieve their objectives (see the section on Thematic Engagement).

In terms of the Social pillar, we stress two fundamental factors in the responsible approach: safety and the abolition of all forms of discrimination.

We held in-depth discussions with Metso Outotec on the subject of safety, having noted an upturn in the number of occupational accidents to employees after several years of declining accident rates. The negative performance on this indicator is attributable to the merger between the two companies, Metso and Outotec. Integrating the two entities has required the teams on each side to take on board the safety procedures of the other, especially since so many operations are conducted on customer sites, making it harder to ensure compliance with safety rules. Teams are also having to get to grips with the specific characteristics of customers encountered for the first time as a result of the merger. The company is setting up in-house training campaigns to ensure uniform familiarity with safety procedures, for customers and suppliers as well as for their own workforce.

Generally speaking, we note an overall improvement in companies' accident rates. Many companies have achieved significant reductions in their accident rates over recent years, one example being engineering company Sandvik. Any marginal gains still to be made will come from adopting different approaches from those established over the past. In addition to the safety procedures and tools made available to teams for their own protection, the company is also introducing preventive measures: automation of 80% of the tasks at the highest risk of accident by digitising industrial equipment, psychological monitoring to identify conditions conducive to possible accidents, etc.

Regarding discrimination, we encourage the companies to promote equality of opportunity and gender parity, especially as regards women's access to managerial positions. The proportion of women in management roles averages 28%, an increase of 3% over the previous year. This percentage is rising significantly in the case of Board membership, which is more susceptible to rapid change.

While significant disparities persist between the industrial and services sectors, industrial firms have made major progress on gender diversity in management roles, increasing the percentage of women managers from 15% to 21% in 2021. This marked increase reflects not only recruitment and promotion policies introduced by companies several years ago, but also partnerships and university courses designed to attract women into industry. BP and Repsol lead the way with over 30% women managers. In contrast, the proportion of women managers in the service sector is on average twice as high at 40%. The media sector still holds the top slot, however, not far short of parity with 49% of women managers for the companies in our portfolio.

We also note the impact that cultural and regulatory approaches have on the introduction of non-discrimination policies. UK and US companies, WPP being a case in point, adopt inclusion criteria based on ethnic origin, something that is illegal in France and other European countries.

Stakeholders are playing an increasingly important role for companies, in that they can have a significant impact on a company's activities. We systematically discuss with companies the risks, opportunities and means they deploy to tackle issues relating to their value chain, in order to evaluate the degree of their control over externalities.

Any controversy arising from the poor practices of a supplier generally spills over onto the company itself, which means it is vital to involve the entire supply chain in adopting good practices. As a result, growing numbers of companies are calling on the services of Ecovadis, a specialist in sustainability assessment of global supply chains.

Another way for companies to reduce their CO2 emissions is by redesigning products and processes. The earlier this issue is addressed with suppliers, and the more consideration given to the reality of customer requirements, the greater the impact it will have. We are also seeing closer cooperation between different components of the value chain, as witnessed by Carrefour or Signify which are working with their suppliers to reduce the quantity of product packaging.

On a wider scale, the difficulties encountered by supply chains in the post-Covid economic recovery have underscored the fragility of these highly fragmented and globalised chains. It is more important than ever for a company to have full control over its value chain. It is against this background that companies such as Schneider Electric, Signify or Saint-Gobain, notwithstanding their global presence, are now putting much more emphasis on their regional presence, with shorter and easier to manage value chains.

2.1.3 Dialogue around controversies

We can include under the term "controversy" all allegations or disputes that affect companies, all types of events that impact their reputation or legal security and events generated within the company or affecting stakeholders or the environment.

As investors are bombarded with a permanent flow of information, and in order not to succumb to unproven claims, for many years now our approach has consisted of scrupulously analysing every controversy and producing a detailed assessment.

Each week the fund management team analyses the alerts generated by our internal system. Based on Eikon, this system identifies all media articles reporting potential controversies involving the portfolio securities. The alerts are presented during the weekly fund management committee meeting, then analysed by the management team, which assesses their pertinence according to our internal analysis matrix and decides on whatever action may be required.

The following are types of controversy considered to be major (non-exhaustive list):

- Collusion.
- Health or environmental scandal.
- Breaches of human rights.
- Corruption scandals.

Controversies with a high or very high risk systematically lead to discussions being held with the company. Controversies are then reviewed during subsequent meetings covering ESG issues.

In 2021, we analysed 98 alerts within our portfolios. 92 of these proved to be of only minor importance, and 6 of them were classified as major controversies.

The five companies affected by these controversies were Crédit Suisse, Siemens Energy, Publicis, Philips and Allianz.

❖ **Credit Suisse**: The stock, which we held at the beginning of the year, was the subject of two controversies:
  - The collapse of financial company Greensill Capital at the start of 2021 affected Crédit Suisse at several levels. Firstly, the Swiss bank had made a loan of USD140 million to the supply chain finance specialist. In addition, as part of its Asset Management business, Crédit Suisse had invested in debt originated and structured by Greensill Capital, via four supply chain and finance funds. On 1 March 2021, in the wake of Greensill's collapse, Crédit Suisse suspended subscriptions and redemptions for these four funds and then set about liquidating the portfolios. The funds had been marketed to institutional investors and represented outstandings in excess of USD10 billion. The financial risk to Crédit Suisse was low to non-existent, given that clients were aware of the risks they were taking. The reputational risk to the bank, on the other hand, was difficult to quantify but no doubt much more significant, with a high risk of the bank losing clients. Our analysis of this first controversy prompted us to keep a monitoring watch on the bank.
  - A few weeks later, Crédit Suisse was implicated in another scandal, the default of Archegos Capital Management. As a result of adverse market movements, financier Bill

Hwang's family office, which had built up positions worth tens of billions of dollars with high leverage in a certain number of stocks, found itself unable to meet margin calls from its banks. This triggered a massive fire-sale of the fund's positions resulting in huge losses. Crédit Suisse, acting as a prime broker to Archegos alongside banks like Goldman Sachs, Morgan Stanley and Nomura, suffered a loss of USD4.4 billion. This second incident highlighted inadequacies in risk management and poor governance. We decided to sell out of the position in March 2021.

- **Siemens Energy**: In January 2021, US firm General Electric Co brought charges against a subsidiary of Siemens Energy for using fraudulently obtained information to gain unfair advantage during a bidding process launched by US power and energy company Dominion. In essence, a Dominion employee was alleged to have provided Siemens Energy employees with detailed information on the General Electric bid, to help Siemens Energy win the contracts. We held discussions with the company in an attempt to gain a better understanding of how this incident arose. Details were only made public after the company had completed its own internal enquiry. Rival bidders GE and also Mitsubishi were then informed. Internal sanctions were applied, and anyone who might have been privy to the information in question was reassigned to other duties. Management was kept informed. Ultimately, the project to which the Dominion bid related was cancelled. Regrettable though this incident was, Siemens Energy's reaction is evidence of robust procedures which served first to identify the incident internally and then to apply appropriate responses. Analysis of the controversy revealed low risk. In September 2021, the two companies announced that an amicable settlement had been reached, although no details were revealed.

- **Publicis**: On Thursday 6 May 2021, the State of Massachusetts filed suit against Publicis Health, accusing the Publicis subsidiary of having contributed to the opioid crisis by designing and deploying unfair and misleading marketing schemes to help the privately-owned firm of Purdue Pharma boost sales of OxyContin. The proceedings against Publicis followed on from other actions against the opioid manufacturers (Purdue Pharma, Johnson&Johnson, Mallinckrodt, Teva, etc.) and those filed by over 50 states against McKinsey, which had provided strategic consulting services to Purdue Pharma in particular. Publicis confirmed the existence of business relations with Purdue Pharma between 2010 and 2019 and the sums it had received in payment, with press articles suggesting payments of USD50 million over the period. Purdue Pharma was a small client by Publicis standards. The advertising group posted 2019 revenue of €12.3 billion, of which North America accounted for €6.7 billion. The services provided by Publicis consisted of producing advertising messages targeting doctors and media space buying. The medical representative business operated by Publicis in the past was not involved. We spoke with Publicis, who pointed out that the product concerned was FDA-approved and available only on medical prescription and that the advertising had been approved by the client as part of a strategy also determined by the client. Publicis would appear to be the only advertising agency drawn into this scandal, for which there is no precedent. Even when the tobacco industry was put on public trial, no proceedings were ever brought against advertising agencies. Our analysis of this controversy prompted us to place Publicis under monitoring watch.

- **Philips**: Along with its Q1 2021 earnings announcement, Philips also released details of the quality failing in the polyurethane foam used in some of the respirators and sleep aid devices in its DreamStation line. Under certain conditions of use/upkeep, this foam risked breaking down and creating particles that could potentially enter the air pathway of the device and from there reach patients' airways. No deaths were reported, but cases of respiratory difficulties, headaches, etc. were alleged. The group initially booked a provision of €250 million for improving product quality. On 14 June 2021, the company voluntarily launched a recall programme for the products concerned and announced a further provision of €250 million booked in Q2. Yet another provision for a further €225 million was set aside in Q4. This problem has affected the group in three ways. The first was a loss of revenue, since the product cannot be marketed until the problem is solved. The loss amounted to around €650 million, just over 3.5% of group sales. Secondly, the recall operation carried a cost to the company, which set aside a total of €725 million in provisions. The final and most uncertain factor is the legal risk. A number of patients and commercial partners have begun legal proceedings. The company is not in a position to estimate the risk involved. Our analysis of this controversy identified a high level of risk that prompted us to seek discussions with the group in September 2021.

- **Allianz**: In March 2020, as the Covid-19 pandemic sent markets into a tailspin, the Structured Alpha funds, a set of structured funds relying on complex options strategies managed by group subsidiary Allianz GI, suffered heavy losses. At its peak at end 2019, this range of funds held assets totalling USD13 billion out of total Allianz GI assets under management of USD357 billion (3.5% of AUM). Clients' losses amounted to USD6 billion. Many clients filed suit, prompting the US Department of Justice and the SEC to launch an investigation. Our analysis of the controversy, made as US federal agencies were just opening their investigations, led us to place Allianz on monitoring watch. Allianz annual results announced for 2021 included a charge of USD3.7 billion in anticipation of settlements being finalised with clients concerned. The DoJ and SEC investigations are still ongoing.

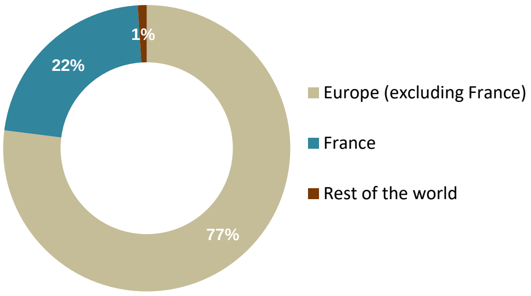
2.2 Engagement through voting

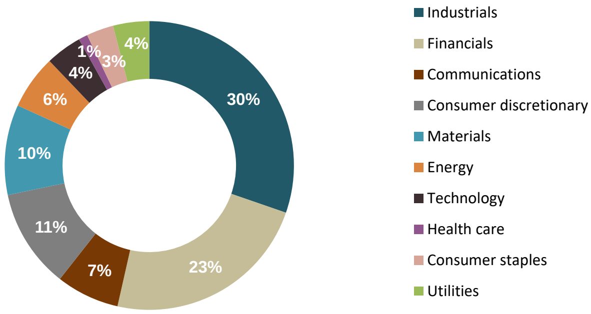
2.2.1 Our votes in 2021

Our individual engagement is also conducted through our voting process applied to the companies' general meetings. METROPOLE Gestion considers that the actual exercise of voting rights represents an essential element of the relationship between a company and its shareholders. METROPOLE Gestion therefore exercises its voting rights for all companies whose securities are held in the portfolios, in accordance with the voting policy. As a signatory of UNPRI (UN Principles for Responsible Investment), we ensure that our vote is cast in compliance with environmental, social and governance criteria as set out in the Code of Transparency and CSR Policy (Corporate Social Responsibility) implemented by METROPOLE Gestion, available on our website.

In 2021, the management company exercised its voting rights at **136** general meetings out of **138**, a participation rate of 98.7%.

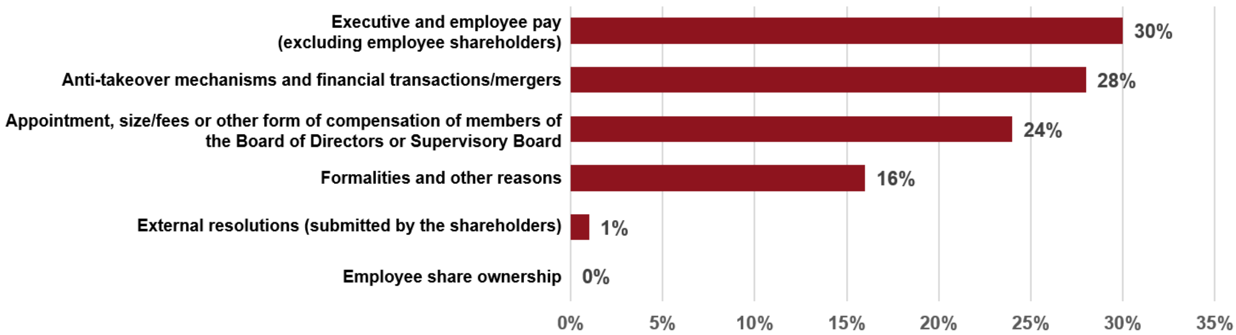
The general meetings we attended break down as follow:





Our engagement with the companies requires us to contest resolutions submitted to shareholder vote where we believe they do not meet best practice or do not appear to favour the interests of our clients. On behalf of the managed UCITS and AIFs during 2021, METROPOLE Gestion voted against 243 different resolutions (11% of total resolution votes) at 82 general meetings, i.e. 60.3% of the general meetings we attended.

These votes against break down into the following areas:



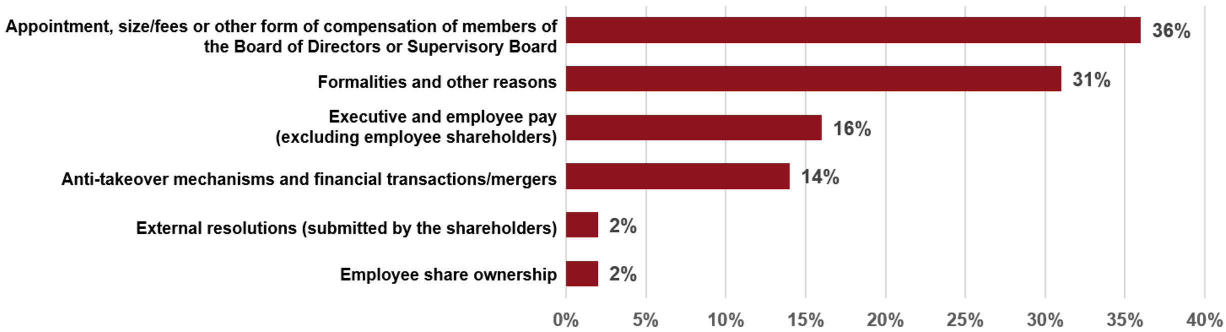
Resolutions on executive and employee pay (excluding employee share ownership schemes) made up the biggest component (30%) of our opposing votes, an increase on 2020 (27%). Our main sources of dissatisfaction continue to be a lack of transparency on details of the criteria for variable compensation awards (Bonus and Long-Term Incentive System) and the amounts of severance pay in the event of termination.

Resolutions on financial operations or mergers constituted the second most common grounds for opposing votes in 2021 (28%). This category of opposing votes saw an increase over 2020, when it accounted for 21%. Many of the resolutions involved provisions allowing for the possibility of significant capital increases without seeking prior approval from shareholders. In other instances, the source of our objections lay in a lack of transparency on possible recourse to certain financing instruments.

Resolutions relating to the Board of Directors or Supervisory Board, which had accounted for the majority of our opposing votes in 2020 (30%), triggered fewer opposing votes in 2021, down to 24%. The duration of Board members' terms of office, proposals for the re-election of members with poor attendance records, diversity and the degree of independence of certain members were once again the main grounds for opposition.

In terms of ESG pillars, it should be noted that most resolutions submitted to shareholder vote continue to relate to questions of governance. In 2021, 98.3% of resolutions put to the vote related to this pillar. A stable figure compared to 2020 (98.8%). Among the main issues submitted to the vote can therefore be found the composition of the board of directors (36% of resolutions), executive pay (16%) and financial transactions and M&A (14%).

Thematic breakdown of resolutions voted on:



In 2021, in accordance with our policy of engagement, we supported a resolution not recommended by the Board of Directors of Royal Dutch Shell. Follow This, an activist organisation that encourages oil and gas groups to accelerate their energy transition, had joined with a shareholder consortium to submit a resolution asking Shell to set targets in line with the Paris Climate Agreement.

Since climate and energy and ecological transition issues were once again under-represented among the resolutions put to shareholder vote, we also address these issues as part of our three-part engagement policy.

- Individual engagement with companies (through dialogue and exercising voting rights on ESG resolutions).
- Thematic engagement (focused since 2019 on climate change).
- Collective engagement: in 2020, METROPOLE Gestion has joined the « Non-Disclosure Campaign » aimed at improving information transparency relating to climate change provided by companies but also the « CDP SBT campaign », a campaign asking companies to commit to fight climate change by setting science-based targets through the Science Based Targets initiative's (SBTi). As part of the Climate Action 100+ initiative, we are committed to the goal of decarbonising the cement manufacturers.

A dedicated report on the exercise of voting rights and shareholder dialogue is available on our website.

2.2.2 Dialogue ahead of General Meetings

As our approach is designed to improve the practices employed by the companies, we also conduct engagement activities before general meetings to cover, and even influence, the content of the agenda items. We make every effort to ensure that it is in line with the interests of minority shareholders and complies with our principles of governance.

Among the more noteworthy discussions this year were those with Travis Perkins and UniCredit, which resulted in differing conclusion, with us supporting management in one instance and opposing in the other.

- **Travis Perkins** held an extraordinary general meeting to approve its spin-off of Wickes Group. The third resolution concerned the remuneration of the presumed executives of Wickes, a subject that had been discussed with the company. The proposed remuneration provided for the payment of an extraordinary bonus to the new executives, an issue open to criticism in itself. Following these discussions, we concluded that this payment was primarily intended as compensation for rights acquired by virtue of their status as executives of Travis Perkins and relinquished on taking up new positions at Wickes Group. Although initially opposed to the resolution, we ultimately voted in favour in the light of the additional information provided by the company.

- Italian bank **UniCredit** appointed a new CEO in April 2021. Prior to his arrival, the Board of Directors submitted an amendment to its remuneration policy for the approval of shareholders. The proposal met with a number of obstacles, however. The amendment sought to guarantee the new CEO, as yet unknown, a fixed bonus of 200% of basic fixed salary for 2021. We considered this to be absolutely contrary to good governance practice. After taking note of the company's arguments in favour of its proposal, we decided to oppose the bonus award.

3. Thematic engagement

3.1 Presentation of the theme chosen for 2021

For 2021, the management team chose the theme of "financing energy transition".

Signed in 2015, the Paris Climate Agreement breathed fresh life into the fight against climate change. Numerous initiatives therefore emerged or gained momentum designed to deal with the actual and transitional risks, in addition to the opportunities presented by climate change and energy transition. Although by no means the only issue, CO_2 emission reduction is a central issue with the target specified in the Paris agreement of limiting global warming by 2050 to a maximum of 2°C compared to the pre-industrial era. The consequences of the agreement have led to new regulations encouraging companies along this path. This especially applies to the European Union, which in 2019 announced its objective of carbon neutrality by 2050.

As a responsible investor, we also contribute to the attainment of this objective through our process of engagement with our companies. We also hold dialogue with issuers regarding their strategies in this area in order to address climate risks and grasp any opportunities that energy transition might have to offer. We have therefore dedicated the last three rounds of our thematic engagement to combating climate change.

In 2019, we took the initiative of raising awareness and developing accountability among the companies represented in our portfolios in terms of setting ambitious targets for reducing their CO2 emissions (relative or absolute reduction in emissions by a given deadline), in line with the 2° trajectory of the Paris Climate Agreement, and of having their plans approved by the Science Based Target initiative.

In 2020, we encouraged companies to publish a climate report in accordance with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), firstly to ensure that their performance could be assessed on a reliable and level playing field and, ultimately, to encourage greater awareness of the issues associated with climate risk.

In 2021, we pursued our engagement on behalf of the climate with a campaign aimed at financial institutions, which we see as an essential link in the fight against global warming. Banks, in particular, have been slow to realise the impact that their corporate lending can have on greenhouse gas emissions, and not all of them have implemented effective policies in this particular area. We therefore held discussions with the banks in our portfolio to ensure that they could identify and accurately measure the climate risks to which they were exposed and, more importantly, to which they contributed. We also called on them to overhaul their governance, to adapt it to climate issues and make it a basis for the deployment of ambitious policies designed to finance energy transition.

3.2 Summary of our interviews

On the basis of these interviews, we concluded that the risks associated with climate change, as far as banks are concerned, are primarily macroeconomic. A failure to achieve energy transition at the national or international level would result in lower GDP growth and thus in reduced corporate lending, an increase in provisions for risk, an increase in capital requirements (regulatory capital) and hence an increase in the cost of capital.

By the very nature of the banking business, “physical” climate risks would appear to be very limited, confined mainly to the risk of impairment of real estate assets located close to areas liable to flooding or exposed to natural disasters. The risks identified relate for the most part to so-called “transition” risks, when banks retain high levels of exposure to financing sectors presenting energy transition risks. Some businesses might eventually encounter difficulties financing their activities or face their profitability being curtailed by new regulations. The Italian economy, for example, has a high exposure to industry, a sector made up of large numbers of SMEs. There is a real risk that these companies will face stricter environmental regulations in the years ahead, and might have difficulty in complying in view of their smaller size and thus more limited resources. Retail banking is also concerned, with risk concentrated on mortgage loan portfolios, i.e. the risk of households defaulting on mortgage repayments should a major physical climate event occur.

Above all, we find that the banks carry a considerable degree of climate liability through their corporate lending. UK retail bank Lloyds, for example, estimates that its loan portfolio contributed to the emission of 25.4 million tonnes of CO2 in 2019, equivalent to 5.6% of the country’s total emissions, even though the bank has little exposure to the oil and mining sectors, which account for less than 0.3% of total loans outstanding.

Above all else, managing climate risk in banking requires a complex assessment that the sector has not yet succeeded in perfecting. European banks are only just beginning to measure the carbon footprint of their credit portfolios, but using different methodologies that make it difficult to compare the respective levels of progress being made. BNP Paribas, Société Générale and ING have started work on aligning their credit portfolios with the Paris Climate Agreement targets using the PACTA (Paris Agreement Capital Transition Alignment) method, which defines standardised indicators and sets targets by sector of activity. For maximum effectiveness, the PACTA method prioritises aligning the five biggest greenhouse gas-emitting sectors (fossil fuel extraction, power generation, transport, steel and cement). These five sectors account for 75% of global emissions and 30% of loans outstanding in the case of ING, the bank with the relatively highest exposure to the raw materials sector. Lloyds, which has so far analysed 70% of its balance sheet, applies the PCAF (Partnership for Carbon Accounting Financials) method, which measures the CO2 emissions of its lending activity in absolute terms but cannot be used to determine the temperature of a portfolio, unlike the PACTA method more widely adopted in the banking sector. In the next stage, the bank will begin measuring the temperature of its assets in partnership with the Bank of England, as part of the BoE Climate Biennial Exploratory Scenario. The aim of this exercise, amounting to a resilience test, is to determine the cost of risk for the banking system in three different climate scenarios.

If they are to reduce their climate impact and truly contribute to combating climate change, banks will need to adapt their governance and practices to factor in this issue at every level of their operations. In our 2018 engagement campaign, we encouraged the companies in which we invested to incorporate ESG criteria into determining the variable remuneration of their executives. A number of banks, including Lloyds, ING and Société Générale have introduced remuneration schemes linked to the achievement of climate targets. This practice is nevertheless not sufficiently widespread in the European banking sector. At the operational level, adopting climate strategies generally takes the form of implementing exclusion policies, prohibiting the financing of the most harmful activities such as coal mining, or refusing consumer credit to an individual to buy a second-hand car deemed too old and therefore too polluting. Preferring a more constructive approach, some banks are setting up specialist teams to support corporate clients through their energy transition. The intention is also to influence clients' investment decisions by adopting pricing that reflects climate factors, such as cheaper loans for electric vehicles or, in contrast, a penalty hike if the loan carries climate risk. Ultimately, the shared objective of the banking sector is to reduce its lending to the highest-emitting activities along a trajectory aligned with the Paris Climate Agreement.

Reducing lending to the industries causing the most climate harm, a constraint for the banking sector, is not the only lever available for effective climate policy, however. Energy transition also offers a real development opportunity for the banking sector, such is the scale of the financing required to build a carbon-free economy. At this stage, the banks we have spoken with have not yet quantified this potential, but initial estimates suggest that the investment needed for energy transition, whether it be construction of infrastructure to produce renewable energy, replacing the existing fleet of ICE vehicles or renovating buildings, will be substantial, far outstripping levels of lending to fossil-fuel related activities that are soon to be phased out.

4. Collective engagement

As a signatory of the CDP, METROPOLE Gestion has joined the Non-Disclosure Campaign, a collective engagement campaign targeting companies failing to respond to information requests from the CDP. This form of engagement aims to improve transparency of information, notably relating to climate change data communicated by companies by following the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Such contributions of information to the CDP are vital for measuring companies' impact on climate change in a complete and uniform manner and for assessing the effectiveness of the mitigation measures taken by companies.

In the 2020 campaign, we targeted 10 companies in our role as Lead Investor on the CDP themes of climate change, forests and water security. 20% of the companies targeted responded positively to the campaign. Encouraging as this favourable response rate already is, we naturally hope to convince even more issuers of the validity of our requests.

We are delighted to have received a favourable response rate of 31% from the 13 companies we targeted in 2021.

Company	**Business sector**
BP	Energy
Total	Energy
Accor	Consumer discretionary
Bouygues	Materials
ANDRITZ	Industrials
Meggitt	Industrials
LISI	Industrials
Construcciones & Auxiliar de Ferrocarriles	Industrials
Buzzi Unicem	Materials
Covestro	Chemicals
SSAB	Commodities
Wienerberger	Materials
Saint-Gobain	Materials

This exceeds the average response rate for the campaign as a whole, which was 25%.

The rate actually rises to 38% for the favourable response rate to the theme of climate change. We also note that these responses came from high-emissions industries such as oil and gas (BP) or chemicals (Covestro). The fact that hotel group Accor and aerospace equipment manufacturer Meggitt also responded favourably to our engagement goes to show that every sector of the economy now considers itself affected by these issues.

Our only regret is the absence of favourable responses on the theme of deforestation, which is almost certainly due to the overriding attention being focused on climate change issues.

As part of the CDP, we are also associated with the CDP Science Based Targets initiative (SBTi) campaign, founded on the same principle of shareholders joining forces to call on target companies to adopt scientifically validated targets for reducing their CO2 emissions. This new campaign offers yet another and somewhat different way to encourage companies to decarbonise their activities and align with trajectory 2 of the Paris Climate Agreement. A total of 194 European companies have been targeted, 37% of which have undertaken to set targets or whose targets are in the process of validation.

Lastly, we pursued our engagement with Climate Action 100+ over 2021 to participate in collective dialogue with HeidelbergCement. The cement sector is massively exposed to the problem of CO2 emissions due to the high emissions generated by its production process. HeidelbergCement, a world leader in the industry, has a fundamental role to play in decarbonising its industry, as much by its power to set new standards for the industry as a whole as by reducing its own emissions. Although we already engage individually with the company, our collective engagement as part of an institution as widely known as Climate Action 100+ allows us to activate new levers to encourage the company to improve its practices. In this context, we are pleased that this dialogue has already proved fruitful on the following points:

- Implementation of extra-financial criteria in the remuneration of managers with a bonus/malus mechanism on variable remuneration linked to financial performance. With this innovative approach, HeidelbergCement's financial and extra-financial performance can no longer be separated.
- Appointment of a Director in charge of ESG issues.
- SBTi membership.
- Improvement of the company's reporting in accordance with the TCfD guidelines on risk and opportunity assessment: acquisition of a risk assessment tool for each of the group's sites.
- Publication of a lobbying report by the group which obliges it to position itself on the environmental policies of the business groups to which it belongs.

These elements are of course only steps, but they lay the foundations for the objective that the group has set itself to achieve carbon neutrality by 2050 at the latest. We will continue this collective dialogue so that the group increases its efforts in the years to come.

5. Conclusion

In the aftermath of an historic year in 2020, marked by the outbreak of a pandemic that paralysed the entire planet, 2021 was a year of spectacular recovery and marked the start of a new cycle that puts ESG issues front and centre, and foremost amongst them the issue of energy transition, now associated with every aspect of corporate strategic development. Companies are being called upon from all sides to introduce development models compatible with the Paris Climate Agreement. The impetus come from government authorities, which are ramping up their investments in this area; from regulations, aiming for greater insistence on these criteria; from end customers, who increasingly value virtuous companies; and, of course, from investors, who play a vital role in financing and supporting companies in their sustainable development.

Companies, for their part, all now claim to be concerned by these issues and some are already well positioned in the process of revolution. Most industries, however, have yet to define the trajectories and how to pursue them, given the prevailing regulatory uncertainties, the disparate nature of the measures adopted, the often high costs of implementation, short term issues of competitiveness, etc. Bearing this in mind, our engagement with issuers sets out to work with them to assess the risks they face and identify the opportunities this transformation presents, so as to build on the efforts already made. This ongoing dialogue is now essential since companies that have chosen the right positioning will obviously reap the competitive advantages and emerge from this transition as winners. The lead that European companies have taken in this area offers them highly favourable prospects for the medium term.

While environmental aspects currently occupy the foreground by virtue of their sheer urgency, the current crisis also highlights the importance of the other ESG pillars. We cannot afford to overlook them, because other transformations are already at work. The technological disruption affecting every sector of the economy, the changes in society, the instability of global geopolitical and economic balances are also creating problems in terms of social relations, governance or the relations between stakeholders. Our role as a Responsible Value investor is to engage with companies on all of these fronts so as to arrive at the best possible analysis of the risks and opportunities they face, and to make responsible investment decisions.

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