



# **Celeste Funds Management Limited**

## **Responsible Investment Framework Document**

**November 2008**

# Amendment History

Section	Amendment	Date
<b>Appendix D, Section 1, page 31</b>	Made amendment noting analyst to decide on appropriate form of engagement and who any issues ought to be addressed to. Also added comment that where a matter is not satisfactory, but not material in nature, CFM will abstain from meeting resolutions and explain the reason for doing so at the next company contact.	<b>01/05/2009</b>
<b>Entire Document</b>	Changed all references from “Souls” to “Celeste”	<b>25/01/2010</b>
<b>Responsible Investment Policy</b>	Removed reference to ESG service provider, as this ESG research is now undertaken by analysts in-house. Changed primary responsibility for ESG activity from CEO to Board. Changed review frequency of ESG program from bi-annual to annual, which is consistent with UN-PRI reporting cycle.	<b>24/01/2011</b>
<b>Section 1.4), page 11</b>	Removed reference to ESG service provider, as this ESG research is now undertaken by analysts in-house.	<b>24/01/2011</b>

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## Purpose

The purpose of this document is to detail the approach of Celeste Funds Management Limited (CFM) to implementing its Responsible Investment Policy. Furthermore, as a signatory to the “*United Nations – Principles for Responsible Investment*” (UN-PRI), CFM’s approach is closely aligned with the “Principles” articulated by the UN-PRI. Hence, this document is structured according to the six Principles of the UN-PRI (see **Appendix A**).

This document outlines the way in which CFM assess “*Environmental*”, “*Social*” and “*Governance*” issues, how this is then implemented in practice into the valuation, portfolio construction and company engagement process, and how it extends to its dealings with clients, service providers and the broader society.

## Introduction

CFM is, first and foremost, an ALPHA manager. We believe we can identify and understand the factors that drive shareholder value creation. Our primary motivation is to generate, over time, excess returns above those of the broader market, with an acceptable level of risk.

Historically CFM already placed significant emphasis on “*corporate governance*” and “*accounting quality*” when analysing and valuing stocks. This was due to the realisation that both of these issues can highlight exceptional management or alternatively unacceptable levels of risk as mentioned above, even though they are often overlooked by the broader investment market participants.

With the ever more compelling evidence of climate change came a realisation that while CFM already focussed on Governance or “G” issues, similar emphasis ought to be placed on the Environmental “E” and Social “S” issues, as they too have significant bearing on potential value accretion and/or destruction.

Out of this realisation grew a discussion which eventually led to a collegiate understanding as to how the CFM Investment Team thought best to implement ESG considerations into its investment process. CFM’s “*Responsible Investment Policy*” outlines CFM’s commitment to responsible investment, while this framework document outlines the practical implementation of this policy into CFM’s operations.

Since there is close alignment between the CFM philosophy and that articulated under the UN-PRI, we have taken the approach to outline the implementation of our Responsible Investment Policy in line with and in the context of the Principles of the UN-PRI.

# Celeste Funds Management Limited – Responsible Investment Policy

## **INTRODUCTION**

Celeste believe that environmental, social and corporate governance (ESG) issues impact on investment valuations and can affect the performance of portfolios. Managed poorly, ESG practices have the potential to destroy shareholder value. As an active investment manager we therefore have a duty to consider in our investment decision making the potential financial impacts of companies' exposure to, and management of these issues. We also believe that it is in the best interest of clients that we encourage high standards of corporate governance and corporate responsibility in the companies in which we invest.

Confidence in management integrity and quality is an essential ingredient in our investment process. Boards and Management who practice the highest standards of corporate governance and operate in a responsible and sustainable manner are likely to cultivate the capacity and transparency required to support success and enrich the position of shareholders, employees and broader society.

## **POLICY COMMITMENT**

Celeste' has made a policy commitment to manage all client funds according to responsible investment principles. We deliver on our commitment in four main ways:

1. Through our activism on **corporate governance**, by encouraging companies to follow the IFSA Corporate Governance Guidelines, by promoting best practice on remuneration policy, strategy and succession planning, and by exercising our clients' voting rights in all possible circumstances.
2. By integrating analysis of ESG issues into our **investment process**.
3. By **engaging** with companies and other stakeholders on material social, ethical and environmental issues, particularly climate change.
4. By participating in forums, conferences and policy consultations on responsible investment, and playing an **active role** in promoting corporate governance, corporate responsibility and responsible investment in collaboration with other like-minded investors.

Celeste will manage its business in keeping with emerging ESG standards in the finance sector.

## **RESOURCES**

Primary responsibility for Celeste ESG activities rests with the firms Board. All employees are aware of the Celeste ESG policies and are to varying degrees are actively involved in their assessment and implementation. Staff are informed and kept up to date with ESG practices and policies through attendance at conferences and seminars, research papers and briefings from external consultants.

Celeste recognises the need to build its knowledge and understanding on ESG issues. It does this through analyst attendance of ESG conferences and seminars as well as collaborative engagement processes. Until December 2010 Celeste engaged a specialized ESG research providers to enhance its own ESG research capacity. Celeste now does all ESG research in-house, but also encourages broker research on ESG issues.

## **REPORTING**

Celeste is committed to reporting to clients and other relevant stakeholders on the ways in which ESG criteria are integrated into the management of investment portfolios as well as ESG activities undertaken by the firm through the course of its normal business. To this end Celeste will produce an annual review of all ESG operations and activities.

Clients can be provided with specific ESG activity reports if required.

## **ASSOCIATION**

Celeste is committed to promote further awareness and action on ESG issues. The firm is a signatory to the ***United Nations Principles for Responsible Investment*** (June 2008) and follows the guidelines set out for integrating ESG considerations into investment decision-making. Celeste is also a member of the **Responsible Investment Association of Australasia** and the ***Investor Group on Climate Change***.

# 1) UN-PRI Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes

## 1.1) *Background*

The distinctly differentiating feature of CFM, as a manager, is the ability of the investment team to develop highly relevant knowledge of companies and the industries in which they operate, and to convert this in-depth understanding into unique insights that define share price performance.

The most valuable part of our investment process is the distillation – through our deep understanding of companies – of the few critical factors that drive share prices. To do this successfully, requires significant experience of each investment team member.

## 1.2) *Philosophy in Applying ESG in our Investment Process*

We do not negatively screen out prospective investee companies based on ESG considerations.

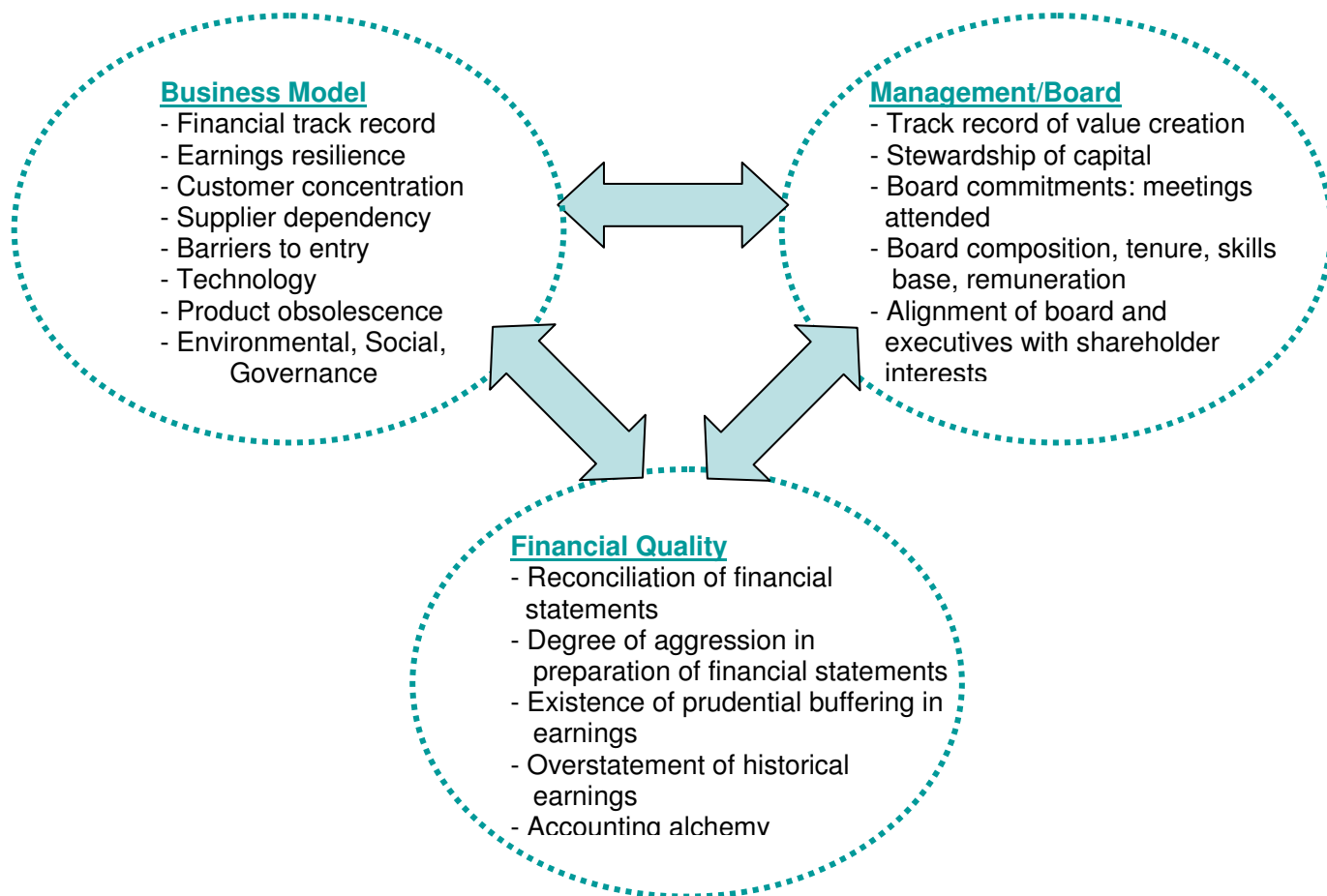
We can, and we do, invest in companies that in a broader sense could be described as ESG-unfriendly; for example, significant carbon emitters, companies that have less-than-exemplary governance standards, or companies that provide services or manufacture products that might be considered to be harmful to society, such as gambling and alcohol.

Instead, because we are driven by the pursuit of ALPHA, our ESG assessments are applied in determining the sustainability of businesses, and the returns to shareholders that they are able to generate.

While we do not assume any definitive moral positions, we do seek to engage with investee and prospective investee companies in helping to improve their ESG performance where we believe it to be materially significant in its potential impact on shareholder value.

However, it needs stressing that our principle focus in evaluating ESG issues relates to the impact they are likely to have on the value of our investments. As such, we seek to develop a clear understanding of the materiality of various ESG factors.

Our approach to ESG is therefore no different to our approach to any other parameters that impact, or have potential to impact, the value of our investments, such as illustrated in Figure1 below:



**Figure 1: Assessment Parameters for Uncovering ALPHA**

ESG considerations therefore constitute one of several subsets of drivers of shareholder value.

Because we believe certain E, S and G factors are potential sources of as well as threats to ALPHA, we believe firmly that ESG competence can not be exclusively procured from external parties, but predominantly needs to be part of CFM's intellectual capital.

### **1.3) Practical Application of ESG in the CFM Investment Process**

In essence, we apply ESG considerations in three ways:

1. By explicitly generating quantitative estimates of the value-at-risk should certain ESG driven events come to pass, for example, emissions trading legislation, environmental accidents, industrial unrest, fines or penalties, or misallocation of capital; and
2. As part of our direct assessment of ESG performance, which allows us to make cross-market and cross-sectoral comparisons for *benchmarking purposes*. In this context, we apply quantitative scores to E, S and G

factors, respectively, under a specific matrix of potential materiality or impact (High, Medium and Low) measured against company performance in each factor (A through D, in decreasing order of performance).

Each of these terms is classified on the basis of the definitions as outlined in **Appendix B**. The key output of this assessment process is a classification of the Impact of the ESG assessment on valuation. This is summarised in **Table 1** below:

<b>Materiality</b>	<b>Score</b>	<b>Impact</b>
<b>HIGH</b>	A & B	+VE
	C	NA
	D	-VE
<b>MEDIUM</b>	A	+VE
	B & C	NA
	D	-VE
<b>LOW</b>	A, B & C	NA
	D	-VE

**Table 1: Impact of ESG Evaluation Process on Rel Determination**

For specific definitions of “*Materiality*” and “*Score*”, refer to **Appendix B**. In the above, **Table 1** highlights the instances where ESG performance can have a positive or negative “*Impact*” on our assessment of the stock rel. A poor Score, as designated by a “*D*” rating will always have a negative Impact. This is due to our view that it is a wider reflection on poor management quality, while a +ve Score only has a positive Impact where Materiality is rated “*High*” or “*Medium*”.

3. As proxy clues into the quality of individual investment opportunities. In this regard, this is no different to the way we evaluate companies by taking into account any other parameters that impact, or have potential to impact, the value of our investments. For a listing of some of these factors, refer to **Appendix C**.

Collectively, it is our understanding and assessment of all of these considerations that are distilled into such valuation inputs as:

- earnings forecasts,
- the selection of valuation methodologies,
- the discount rate or capitalization multiples, and

- the strength of the analyst's conviction

Thus ESG analysis forms an integral part of our investment process and ultimately is reflected in stock valuations and stock return conviction levels.

#### **1.4) Use of Third Party ESG Research Capabilities**

The Investment Team very early on decided that complete integration of ESG assessment into CFM's fundamental research approach was necessary to maintain the integrity of our investment process.

CFM can access third party ESG research from a number of different sources, including:

- Through contributing membership of the UN-PRI, the "*Responsible Investment Association of Australasia*" (RIAA), and the "*Investor Group for Climate Change*" (IGCC) CFM analysts have access to a broad range of studies, conferences, discussion forums, webinars, etc.
- Brokers who have specialist ESG capabilities (e.g. Citigroup and GS JBWere)
- Subscription to specialist publications such as "*Ethical Investor*"

CFM will use third party ESG research as a starting point and to augment the internal research effort, but will not rely on it exclusively to decide on stock valuations. This is consistent with CFM's general approach to any third party research. For example, CFM analysts refer to broker research to gain a sense of market perception of a stock or see where consensus expectation lies. However, the ultimate investment decision is driven by bottom-up fundamental research by the analyst.

#### **1.5) Documentation of ESG Assessment**

Like all other fundamental research, there are three main ways in which ESG assessment is documented and captured by CFM:

##### **1.5.1) File Notes**

Firstly, all fundamental research is documented in File Notes by the analyst who has a specific stock responsibility. All File Notes are circulated within the Investment Team and hence all team members become aware of the relevant issues and what the analyst's assessment of the company's performance on these key issues is. File Notes are an essential element of CFM's investment process. It is considered essential that ESG issues are captured in exactly the same fashion as all other fundamental research is recorded in these File Notes.

##### **1.5.2) Stock Reviews**

Secondly, for all portfolio stocks a Stock Review document will be prepared. This is a process whereby the analyst with a specific stock responsibility will generate a Stock Review document and present the investment case for the stock to the Investment Team. His analysis is subjected to a thorough peer review process. The ESG rating and impact on valuation is recorded in the Stock Review and hence the analysts' assessment of these issues also undergoes peer review.

### **1.5.3) “Data And Ranking Table” (DART)**

Finally, the distillation of the investment process is the assignment of stock specific earnings growth rates and valuation rels. These are captured in the CFM “*Data And Ranking Table*” (DART). It is the analyst’s responsibility to ensure that his assessment of a stock is reflected in the most current DART inputs. The rationale for assignment of a particular earnings growth and rel should usually be obvious for other persons on the Investment Team by reference to the relevant Stock Review (which is a comprehensive snapshot for a stock at some point in time) and File Note (which is a “*live*” document which usually is more current than the Stock Review, but usually reflects incremental insights into a particular stock).

It is fundamental to CFM’s approach, that ESG issues are seamlessly integrated into the CFM investment process and do not sit outside of or as an addendum to this process.

### **1.6) *Encouragement of Third Party Research Providers to Integrate ESG Factors into Analysis***

Although CFM does its own fundamental research, CFM does not believe in reinventing the wheel either. It would be of benefit for CFM analysts if say broker research also seriously addressed ESG considerations – which at present it mostly does not. This would serve to improve the efficiency of CFM’s internally generated fundamental research. Hence CFM will encourage third party providers to improve the integration of ESG into their research and analysis.

### **1.7) *Advocating ESG Training for Investment Professionals***

As noted previously, CFM is aware that it is on a learning curve with respect to its ESG research effort. Through membership of RIAA, it supports the establishment of the “*Responsible Investment Academy*”, which will globally be the first of its kind. The specific mission of the Academy is to provide ESG training for investment professionals.

Again acknowledging the early stage of this effort, CFM has also sent analysts to various ESG seminars and conferences in order to develop a deeper understanding of the ESG thematic and to gain further insights about the practical application of ESG issues into our investment process.

This is an ongoing commitment by the company.

## 2) UN-PRI Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices

### 2.1) Background

The CFM policy at the beginning of this document spells out what approach CFM has adopted with respect to Responsible Investment. This section outlines systems and processes that have been developed to effectively implement this policy into day to day activities – i.e. to make the policy come alive, particularly with respect to engagement with companies on ESG issues.

As mentioned before, traditionally CFM has placed great emphasis on Governance. While over time CFM has developed its own unique set of criteria that analysts will consider with respect to the “G” performance of companies, these considerations are consistent with and are to a significant extent captured in the guidelines provided by the “*IFSA Blue Book – Corporate Governance A Guide for Fund Managers and Corporations (October 2004)*” (<http://www.ifsa.com.au/documents/IFSA%20Guidance%20Note%20No%202.pdf>).

With respect to “E” and “S”, analysts are guided by the assessment process highlighted in **Section 1.3** above. Failure of companies to comply with CFM’s expectations with respect to E, S & G issues, besides leading to a potential de-rating of the stock valuation, might call for engagement with the company in order to address and hopefully resolve these issues.

### 2.2) Engagement

The practical implementation of engagement is an outworking of CFM’s close integration of ESG into its investment process. CFM analysts will always endeavour to focus on the key issues that determine potential value accretion or destruction for a particular stock. The same holds true for our ESG assessment. Although initially there are many issues to consider, in the end it is likely that only a few key factors will be considered most relevant in terms of their potential impact on value. However, there are subtle differences in how this then develops into engagement with companies with respect to CFM’s Small Cap and Large Cap stocks.

#### 2.2.1) Direct Engagement

For Small Cap stocks, management contact is an essential part of our fundamental research. Given our relatively large size in the Small Cap market, in general CFM has no difficulty in gaining access to senior management for companies we invest in. In terms of engagement any ESG issues or concerns can be discussed directly with the Managing Director, Chief Executive Officer, Chief Financial Officers or where appropriate the company Chairman.

For large Cap stocks, in general intimate access to senior management is not available to the same extent that it is with Small Cap stocks. In some instances it might only be possible to have group access to senior management and one-on-one access to Investor Relations personnel or Company Secretaries.

In both instances, ESG issues can in the first instance be brought up directly with the company in these one-on-one meetings rather than during group presentations. Any such discussion are captured in File Notes and Stock Reviews as highlighted in **Section 1.5** above.

## 2.2.2) Collaborative Engagement

In instances where either CFM is not currently a shareholder or where access to management is limited (e.g. for Large Cap stocks), CFM may rely on collaborative engagement initiatives. This is facilitated through CFM's membership in three important organisations, namely:

- UN-PRI
- IGCC
- RIAA

Through membership of these bodies, CFM has the opportunity to collaborate both on a national and international level on ESG issues. Engagement through these organisations casts a wide net, with activities targeting not only specific companies but also governments at both state and federal level and international organisations such as the UN.

Participation in collaborative initiatives is mostly driven by the ESG Co-ordinator who will consult with Analysts, Portfolio Managers and the CEO on relevant issues. Alternatively, Analysts and Portfolio Managers will approach the ESG Co-ordinator to initiate a drive for collaborative engagement where this is deemed necessary.

## 2.2.3) Engagement Policy Implementation

The implementation of the engagement philosophy is achieved via the CFM "*ESG Engagement and Proxy Voting Policy*" which is attached in **Appendix D**. The policy details the exact process as to how CFM will approach engagement with a company where CFM analysts are not satisfied with the response they receive from a company on ESG issues.

An important aspect of this implementation is the recording of all such company engagements as well as Proxy Voting history. This is recorded in the "*Engagement and Proxy Voting Register*" as detailed in the "*ESG Engagement and Proxy Voting Policy*". This Register is maintained by the Office Manager in collaboration with the ESG Co-ordinator.

### **3) UN-PRI Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest**

#### **3.1) Background**

CFM is cognisant of the fact that standardised ESG reporting is essential for benchmarking of corporate performance. We support collaborative initiatives that work towards achieving more transparent and consistent ESG disclosure.

#### **3.2) Integration and standardisation of ESG disclosure in financial reporting**

##### **3.2.1) Large Cap Stock Universe**

In the Large Cap stock universe, due to its currently small size, CFM does not wield much direct influence. CFM believes that better leverage can be obtained through collaborative efforts. CFM will support collaborative efforts that are aimed at better standardisation of ESG disclosure and integration of this disclosure into annual financial reports.

##### **3.2.2) Small Cap Stock Universe**

Without being apologetic for companies with a poor ESG disclosure, in Small Caps CFM is cognisant of the fact that many small businesses are not as well resourced as its Large Cap counterparts. Hence ESG reporting systems and disclosure can not always be up to the same standard as for Large Cap companies. However, without wanting to create unnecessary administrative burdens for small companies we invest in, CFM does support more stringent ESG reporting standards particularly for stocks that have a High Impact on “E”, “S” or “G”, or which tend to be at the larger size end of the Small Cap universe.

#### **3.3) Requests for ESG information regarding adoption of and adherence to ESG reporting standards**

Consistent with our business philosophy, and in order to maximise best use of our valuable human resources, CFM will only focus on key ESG issues that we believe need to be addressed. Hence CFM analysts will only directly seek information on a company’s adoption of ESG practices to adherence to stated ESG policy, where this issue is thought to be of potentially negative impact (as defined in **Section 1.3**) in a valuation context.

In a broader context, CFM will support collaborative efforts that are aimed at encouraging companies to adopt or adhere to emerging norms and standards (e.g. the UN Global Compact – see **Appendix E**).

#### **3.4) Supporting ESG shareholder initiatives supporting ESG disclosure**

CFM will take an active role where it is not satisfied with the response it obtains to any ESG issue it has raised with a company. All CFM initiatives with respect to the above are captured in the “*Engagement and Proxy Voting Register*”. This register is reviewed [annually/bi-annually](#) by the CEO, Portfolio Managers and the ESG Co-ordinator to see if the level of engagement is appropriate and effective or if the process requires further improvement.

## **4) UN-PRI Principle 4: We will improve acceptance and implementation of the Principles within the investment industry**

### **4.1) Background**

As an allocator of capital and a small office-based operation, the impact CFM has in promoting the UN-PRI Principles into its investment process are far more significant than that of its immediate impact on the environment. However, CFM understands that it has to lead by example. In the context of the UN-PRI, this means that as a corporate body, CFM will need to apply the same standards that it applies to companies that we invest in to itself. This has implications on how CFM conducts its business and how it interacts with the world.

CFM only relatively recently has embraced the full integration of ESG considerations into its investment process, and is itself not yet fully living up to the highest ESG standards. It is therefore prudent for CFM to improve its own ESG performance while concurrently pushing for improved ESG performance of companies it invests in as well as its service providers. CFM will run these two processes in parallel – i.e. improving the in-house ESG performance as well as gradually seeking to have its service providers also integrate ESG considerations into their business operations.

### **4.2) Alignment of investment mandates and performance indicators with the Principles**

CFM manages funds on behalf of third party clients. The mission for CFM is to maximise investment returns or ALPHA for clients over a medium to long term time horizon. As mentioned above, CFM view ESG issues to be an integral part of achieving maximum ALPHA for clients.

All CFM analysts have remuneration structured so as to contain a significant incentive component that is based on the analyst's contribution to ALPHA generation. Due to CFM's seamless integration of ESG considerations into its investment process, analysts are not separately rated on their ESG performance. Rather, in assessing the analyst's contribution, CFM management will consider the overall quality of their research contribution, their input into peer reviews and discussion, and the portfolio performance which is an outworking of all of the above. By definition, this includes, but is not limited to the depth and skill with which they cover ESG issues in their work.

### **4.3) ESG performance of service providers**

As highlighted in Section 4.1) above, CFM is aiming to itself become a flag bearer of good corporate ESG performance and will also be pushing its service providers to meet similarly high ESG standards.

Where CFM does interact with service providers on their ESG performance, this interaction is noted in the "*Engagement and Proxy Voting Register*". Where service providers do not respond in a positive and constructive manner to this engagement, as with companies that CFM invests in, the intention is to continue the engagement process with the aim of bringing about change rather than simply switching providers. However, there may be circumstances where CFM might consider changing service providers due to ESG considerations.

#### **4.4) Support development of tools for benchmarking ESG integration of the UN-PRI**

In its overall effort to integrate ESG considerations into its business processes, CFM will make use of benchmarking of performance of its service providers with respect to ESG integration. Any such benchmarking efforts will be documented in the “*Engagement and Proxy Voting Register*”. The rationale for this is that any suppliers of CFM will become aware of the fact that CFM is looking into their ESG performance as part of this benchmarking effort. Hence this effectively becomes another form of engagement and is therefore documented in the Register.

#### **4.5) Support regulatory or policy development to enable implementation of the UN-PRI**

The ultimate aim of the UN-PRI is to see no less than the universal adaptation of the Principles into the investment industry and by extension the entire market. CFM supports this concept and will lend its support and co-operation towards the development of regulatory systems and policy that aids the broader implementation of the Principles. Again, all such support is documented in the “*Engagement and Proxy Voting Register*” which is reviewed annually.

## **5) UN-PRI Principle 5: We will work together to enhance the effectiveness of implementing the Principles**

Through membership of the IGCC and RIAA and in fact through being a signatory to the UN-PRI, CFM is committed to collaboration to further enhance the implementation process of the Principles. While CFM faces some limitation as to how active it can be in this collaboration effort due to its size, it will endeavour to participate in collaborative efforts where appropriate and indeed initiate collaboration where this is deemed necessary. All such collaboration is recorded in the “*Engagement and Proxy Voting Register*” and reviewed annually.

## **6) UN-PRI Principle 6: We will each report on our activities and progress towards implementing the Principles**

### **6.1) *Disclose how ESG issues are integrated within investment practices***

As this document details how CFM has integrated ESG issues within its investment process, CFM will provide a copy of this document to its wholesale clients. In addition, over time CFM has the intention to post a copy of this document onto its Website where it will be available to all existing and potential clients. However, CFM believes that the appropriate time to do so will be when there has been at least one annual review of CFM's ESG performance and once CFM itself has implemented more ESG considerations into its business processes and not just merely into its investment process.

### **6.2) *Disclose active ownership activities***

After a period of 12 months following implementation of this policy framework CFM will post an annual summary of its ESG activities, as documented in the “*Engagement and Proxy Voting Register*” onto its Website. This Register contains all active ownership activities and hence provides a complete reference with respect to all active ownership initiatives by CFM.

### **6.3) *Disclose what is required from service providers in relation to the Principles***

CFM will document all communication on ESG issues with its suppliers in the “*Engagement and Proxy Voting Register*”. The aim of any contact or correspondence with our service providers is to be clear about what our motivation is and we will also state clearly what our expectations are in requesting certain levels of service or information from them.

### **6.4) *Report to clients about ESG issues and the Principles***

In its reporting to clients, CFM is very much driven by what particular information clients request from CFM. To the extent that clients only request reporting on portfolio transactions, portfolio weightings and performance data, this is what CFM will supply – no more and no less. However, consistent with our full integration of ESG issues into our investment process, where portfolio positions are adjusted, bought or sold due to ESG considerations, this will be reported to clients as being due to the ESG issues. The aim is to have full transparency for our clients as to how our ESG assessment translates into portfolio construction.

### **6.5) *Report on progress relating to the Principles***

CFM is committed to reporting its progress in further implementation of the Principles. This reporting will be done in accordance with the UN-PRI procedure. Likewise CFM will report progress on this to all clients who request this information.

### **6.6) Seek to determine the impact of the Principles**

CFM strongly believes in the principle of continuous improvement. It will support any studies that report on or measure the impact that the Principles have on ALPHA so as to allow further improvement of CFM's implementation of the Principles. To this end, there will be an annual review of CFM's ALPHA performance, its "*Engagement and Proxy Voting Register*", and its report to the UN-PRI on the implementation of the Principles as well as any further third party research on the matter.

### **6.7) Make use of reporting to raise awareness about the Principles among a broader group of stakeholders**

CFM will seek to raise the profile of the Principles through its interaction with all the stakeholders of the business. Any instances where CFM has had an interaction with stakeholders to do so will be recorded in the "*Engagement and Proxy Voting Register*". As mentioned previously, CFM will review the Register and seek to assess its performance with the intention of further improving its own performance in raising awareness about the Principles in the broader community.

## **Appendix A – United Nations Principles for Responsible Investment (UN-PRI)**

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

### ***1 We will incorporate ESG issues into investment analysis and decision-making processes.***

Possible actions:

- Address ESG issues in investment policy statements
- Support development of ESG-related tools, metrics, and analyses
- Assess the capabilities of internal investment managers to incorporate ESG issues
- Assess the capabilities of external investment managers to incorporate ESG issues
- Ask investment service providers (such as financial analysts, consultants, brokers, research firms, or rating companies) to integrate ESG factors into evolving research and analysis
- Encourage academic and other research on this theme
- Advocate ESG training for investment professionals

### ***2 We will be active owners and incorporate ESG issues into our ownership policies and practices.***

Possible actions:

- Develop and disclose an active ownership policy consistent with the Principles
- Exercise voting rights or monitor compliance with voting policy (if outsourced)
- Develop an engagement capability (either directly or through outsourcing)
- Participate in the development of policy, regulation, and standard setting (such as promoting and protecting shareholder rights)
- File shareholder resolutions consistent with long-term ESG considerations
- Engage with companies on ESG issues
- Participate in collaborative engagement initiatives
- Ask investment managers to undertake and report on ESG-related engagement

### ***3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.***

Possible actions:

- Ask for standardised reporting on ESG issues (using tools such as the Global Reporting Initiative)

- Ask for ESG issues to be integrated within annual financial reports
- Ask for information from companies regarding adoption of/adherence to relevant norms, standards, codes of conduct or international initiatives (such as the UN Global Compact)
- Support shareholder initiatives and resolutions promoting ESG disclosure

#### ***4 We will promote acceptance and implementation of the Principles within the investment industry.***

Possible actions:

- Include Principles-related requirements in requests for proposals (RFPs)
- Align investment mandates, monitoring procedures, performance indicators and incentive structures accordingly (for example, ensure investment management processes reflect long-term time horizons when appropriate)
- Communicate ESG expectations to investment service providers
- Revisit relationships with service providers that fail to meet ESG expectations
- Support the development of tools for benchmarking ESG integration
- Support regulatory or policy developments that enable implementation of the Principles

#### ***5 We will work together to enhance our effectiveness in implementing the Principles.***

Possible actions:

- Support/participate in networks and information platforms to share tools, pool resources, and make use of investor reporting as a source of learning
- Collectively address relevant emerging issues
- Develop or support appropriate collaborative initiatives

#### ***6 We will each report on our activities and progress towards implementing the Principles.***

Possible actions:

- Disclose how ESG issues are integrated within investment practices
- Disclose active ownership activities (voting, engagement, and/or policy dialogue)
- Disclose what is required from service providers in relation to the Principles
- Communicate with beneficiaries about ESG issues and the Principles
- Report on progress and/or achievements relating to the Principles using a 'Comply or Explain'<sup>1</sup> approach
- Seek to determine the impact of the Principles
- Make use of reporting to raise awareness among a broader group of stakeholders

<sup>1</sup>The Comply or Explain approach requires signatories to report on how they implement the Principles, or provide an explanation where they do not comply with them.

The Principles for Responsible Investment were developed by an international group of institutional investors reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The process was convened by the United Nations Secretary-General.

In signing the Principles, we as investors publicly commit to adopt and implement them, where consistent with our fiduciary responsibilities. We also commit to evaluate the effectiveness and improve the content of the Principles over time. We believe this will improve our ability to meet commitments to beneficiaries as well as better align our investment activities with the broader interests of society.

We encourage other investors to adopt the Principles.

# Appendix B – Materiality and ESG Score Definitions

## ESG Definitions

In terms of Score

- A = Distinction/best practice
- B = Credit/doing well/improving performance
- C = Pass/contemplating the issue/doing basics
- D = Fail/not contemplating the issue/not doing basics

## Environment

### Score

#### A

- Company has an environmental policy.
- Company has good disclosure of environmental performance.
- Company measures current performance and has targets for improved performance.
- Company has shown evidence of improved performance moving towards targets.
- Company has independent auditors verifying the data.

#### B

- Company has an environmental policy.
- Company has good disclosure of environmental performance.
- Company measures current performance and has targets for improved performance.

#### C

- Company has an environmental policy and acknowledges improving environmental performance as an issue.
- Company has minimal disclosure as to current performance or targets.

#### D

- Company does not acknowledge or is paying lip service to the environment as an issue.
- Company has minimal/no policy, minimal/no measurement and no reporting structures.

## Materiality

### Low - *'Environment issues to have a low impact on valuation/ alpha creation'*

- Where the companies operations have a minimal impact on the environment.
- Any financial impost for carbon emissions would not be material to earnings and/or valuation.
- Typically would apply to service companies, IP companies etc eg Insurers, Banks, CPU, COH

### Medium- *'Environment issues to have a medium impact on valuation/ alpha creation'*

- Where the companies operations have a medium impact on the environment.
- Any financial impost for carbon emissions would be material to earnings/valuation.
- Typically would apply to light manufacturing companies, retailers etc. eg CCL, REH, SHL

### High - *'Environment issues to have a high impact on valuation/ alpha creation.'*

- Where the companies operations have a high impact on the environment.
- Any financial impost for carbon emissions would be very material to earnings/valuation.
- Typically would apply to miners, heavy manufacturing companies etc. eg BHP, OST, TOL,ABC

## Social

### Score

#### A

- Staff recognised as being critical to the ongoing success of the business.
- The continued development, performance management and rewarding of staff is a high focus as evidenced by such things as staff training, staff surveys, staff development, succession planning, flexible workplaces, health and safety management etc.
- The company exhibits a strong culture, high staff engagement and low staff turnover. Data is published verifying the above.
- Pay and incentives of senior management linked to staff management and also customer satisfaction.
- Broad equal opportunity policy which expands beyond gender and race (includes factors such as age, religion, sexual orientation, disabilities, political beliefs etc). Evidence of policy in action and improvement over time eg percentage of staff, managers and board that are women.
- Product or service provided is highly beneficial to society.
- Company provides support to communities in which it conducts business through partnerships, sponsorships or donations.

#### B

- Staff recognised as being important to the ongoing success of the business.
- Development of staff is a focus as evidenced by such things as staff training, staff surveys, staff development, succession planning, flexible workplaces, health and safety management etc.
- The company has high staff engagement and low staff turnover.
- Broad equal opportunity policy which expands beyond gender and race (includes factors such as age, religion, sexual orientation, disabilities, political beliefs etc). Evidence of policy in action eg percentage of staff, managers and board that are women.
- Company provides support to communities in which it conducts business through partnerships, sponsorships or donations.

#### C

- Company recognises the importance of people. Conduct staff surveys, training etc but no data released.
- Equal opportunity policy with reference to at least gender and race.
- Company recognises the importance of contributing to society through charitable support.

#### D

- Company is indifferent to staff and this is evident through poor staff morale, poor staff engagement statistics and rising staff turnover.
- Company is involved in human rights abuses and/or potentially exposed to or involved in corruption..

## Materiality

### Low - *'Social issues to have a low impact on valuation/alpha creation'*

- Where the company is a capital intensive business as against a people intensive business.
- Typically would apply to heavy manufacturing industries, Infrastructure etc eg ABC, TCL, BLD.

### Medium- *'Social issues to have a medium impact on valuation/alpha creation'*

- Where the company has a balance between people intensity and capital intensity.
- Typically would apply to light manufacturing industries, retailers, service companies eg FGL, CCL, REH, CPU etc

### High - *'Social issues to have a high impact on valuation/alpha creation.'*

- Where the company is essentially a people business.
- Where people are the key Intellectual Property of the business and the key value drivers.
- Where the company is a relatively large employer of people.
- Where the company is a fast growing businesses and attracting and retaining staff is difficult.
- Typically would apply to Financials, IP companies, resource companies eg QBE, COH, BHP, MQG, PPT, LEI etc

## Governance

### Score

#### A

- Compliance with key Governance elements.
- Published code of ethics/conduct dealing with issues such as compliance with laws and regulations, bribery and corruption, fairness and honesty, giving and receiving gifts, conflicts of interest, employee requirements.
- Good board balance with breadth of board skills.
- High board and committee attendance
- Alignment of interest between management and SH through significant at risk performance pay with appropriate and disclosed hurdles.
- Strong history of management performance creating wealth for shareholders.

## **B**

- Compliance with key Governance elements.
- Published code of ethics/conduct dealing with issues such as compliance with laws and regulations, bribery and corruption, fairness and honesty, giving and receiving gifts, conflicts of interest, employee requirements.
- Good board balance.
- High board and committee attendance
- Alignment of interest between management and SH through significant at risk performance pay.

## **C**

- Compliance with key Governance elements.
- Published code of ethics/conduct dealing with issues such as compliance with laws and regulations, bribery and corruption, fairness and honesty, giving and receiving gifts, conflicts of interest, employee requirements.
- Good board and committee attendance

## **D**

- Non compliance with key Governance elements.
- Failure of board to provide adequate stewardship.
- Management and board history of destroying wealth for shareholders.
- Material conflicts between Mgt, Board and shareholders.
- Poor board and committee attendance.

## **Materiality**

**Low** - *'Governance issues to have a low impact on valuation/ alpha creation'*

- Where governance issues are not deemed to have a material impact on value creation.
- Given our investment process, it will be rare that Governance will ever be considered Low materiality.

**Medium-** *'Governance issues to have a medium impact on valuation/ alpha creation'*

- Base premise

**High** - *'Governance issues to have a high impact on valuation/ alpha creation.'*

- Where there are concerns about the people running the business or on the board (eg SEV) .
- Where the company is underperforming and the board is intransigent (eg FGL or AGK).
- Where there is a majority shareholder and there is potential for abuse of minorities (eg AXA, LEI).

## **Impact of ESG Evaluation Process on Rel Determination**

<b>Materiality</b>	<b>Score</b>	<b>Impact</b>
<b>HIGH</b>	A & B	+VE
	C	NA
	D	-VE
<b>MEDIUM</b>	A	+VE
	B & C	NA
	D	-VE
<b>LOW</b>	A, B & C	NA
	D	-VE

## **Appendix C – Parameters that Impact Valuation**

### **Industry Structure**

- Underlying System Growth
- Geographical Distribution
- Degree of Consolidation
- Participant Discipline

### **Competitive Landscape**

- Competitor Distribution
- Competitor Size
- Price Leadership

### **Customer Type and Concentration**

- Balance of Power
- Revenue Segmentation
- Customer Relationships

### **Barriers to Entry**

- Intellectual Property
- Legislative
- Capital

### **Technological Obsolescence**

#### **Financial Pedigree**

- Financial Track Record
- Quality of Financial Statements
- Returns to Shareholders

#### **Governance**

- Board Practices, Composition and Tenure
- Bribery and Corruption
- Ethical Codes
- Stakeholder Responsibility
- Risk Management
- Executive Remuneration
- Alignment of Executive Interests with Those of Shareholders

#### **Environmental**

- Impact
- Management
- Reporting
- Performance
- Auditing
- Green House Gas Emissions and Energy Usage
- Climate Change
- Biodiversity

#### **Social**

- Human Rights
- Stakeholder Issues – Policy, Systems, Engagement, Reporting
- Employee Issues – Equal Opportunities, Health and Safety, Minority Representation, Job Creation and Security, Training, Trade Unions and Employee Participation, Whistleblower Policies
- Customer/Supplier Relations
- Community Involvement



# Appendix D - Celeste Funds Management ESG Engagement and Proxy Voting Policy

## Celeste Funds Management ESG Engagement and Proxy Voting Policy

### **Purpose:**

The purpose of this document is to lay out the process and systems used by Celeste Funds Management (“Celeste”) to implement its ESG engagement and proxy voting.

Since Analysts’ time is scarce, it is desired that implementation of this policy does not place undue demands on Analysts’ time, and that they do not get burdened with unnecessary administrative tasks.

In addition to recording engagement and proxy voting for companies Celeste invests in, this register is also used to record ALL forms of other engagement activities. This includes engagement with service providers as well as industry peers where collaborative projects are undertaken.

In essence this policy serves to ensure that Celeste’ activities related to the UN-PRI are documented, so that our performance in relation to the Principles can be measured, reviewed and hopefully improved.

In many respects this document follows on from the fundamental research and assessment of ESG performance of companies by the Celeste analysts.

### **Engagement with Portfolio Companies:**

Through their fundamental research, Celeste analysts identify what ESG issues have material impact on the valuation of the company being analysed.

#### **1. Portfolio Stocks**

For companies where we see valuation upside, but this is being impaired negatively by ESG issues, analysts will raise the issue with the company during regular company contacts wherever possible. The Analyst decides on the appropriate form of the engagement and who to address the issue to on a case by case basis.

**Action:** **Analysts** document all such company contacts and issues raised in their **File Notes**.

Where the Analyst remains dissatisfied with the company’s response to the issues raised, Celeste will either vote “Against” or “Abstain” from the relevant AGM resolutions. In such instances, a letter will be sent to the company prior to the meeting to explain the reasoning of our vote.

In instances where the Analyst is not satisfied with a company's action or proposed meeting resolution, but this is not material to valuation, Celeste will vote to "Abstain" from the resolution. Our position will be brought to the company's attention during the next company contact.

## a. For Large Cap Stocks

### Action:

1. The **Office Manager** will maintain and update a "*Company Meetings Register*" on a weekly basis.
2. The **Office Manager** will advise the **Analyst** responsible for the stock of upcoming meetings and Custodian instruction deadlines.
3. The **Analyst** will inform the **Office Manager** of their intention to vote prior to the Custodian instruction deadline.
4. Where the **Analyst** intends to vote "*Against*" or "*Abstain*" from a resolution, he will inform the **Portfolio Manager** accordingly. Depending on the situation and the issue at hand, a group discussion between the entire **Investment Team** might be convened.
5. Where the issue is material, the **Analyst** will send a formal letter to the company (using the "*Celeste Funds Management Engagement Letter Template*" where appropriate) informing the company as to why Celeste Funds Management is voting "Against" on a particular issue.
6. If a matter is deemed unsatisfactory but not material, Celeste Funds Management will "Abstain" from the appropriate resolution. In this instance, the reason for abstaining from the vote is explained to company management during the next company contact.
7. The **Office Manager** sends the instruction to the custodian[s].
8. The **Office Manager** updates the "*Engagement and Proxy Voting Register*".
9. In some circumstances, an issue might warrant seeking a collaborative engagement via the UN-PRI, RIAA or IGCC. Where the **Analyst** deems this appropriate, he informs the **ESG Co-ordinator** and **Portfolio Manager** or in special circumstances the entire **Investment Team**.
10. Where a collaborative engagement is agreed upon, the **ESG Co-ordinator** or the **Analyst/Portfolio Manager** will implement this action.
11. The **ESG Co-ordinator** enters such engagement into the "*Engagement and Proxy Voting Register*".
12. Where an unsatisfactory response is received from the company regarding the engagement letter, a decision must be taken by the **Analyst**, as to whether or not the fund should continue to invest in the stock.

## b. For Small Cap Stocks

### Action:

1. As the custodian notifies the **Portfolio Manager** of all upcoming corporate actions in a reliable and efficient manner, the **Portfolio Manager** will advise the **Office Manager** of his intention to vote prior to the Custodian instruction deadline.
2. Where the **Portfolio Manager** intends to vote “*Against*” or “*Abstain*” from a resolution, he will inform the **Analyst** accordingly. Depending on the situation and the issue at hand, a group discussion between the entire **Investment Team** might be convened
3. Follow steps 5 to 11 as per the above.

## **2. Non-portfolio stocks**

As a general rule, given constraints of time, Celeste will collaborate with third parties with respect to engagement with companies that we do not invest in (like UN PRI, RIAA or IGCC).

**Action:** Any engagement of this kind will be documented and advised to the **Office Manager**, who will maintain the “*Engagement and Proxy Voting Register*”.

## **3. Service Providers**

Where Celeste engages on ESG issues with services providers (e.g. brokers, IT provider, building services, etc), this is also recorded in the “*Engagement and Proxy Voting Register*”. The register is reviewed on an annual basis. The review process will determine if further engagement will be sought, if benchmarking studies of the service provider against industry peers should be undertaken, and in some circumstances if an alternative provider ought to be selected.

## **4. Policy and Regulatory Collaboration**

From time to time Celeste will participate in or initiate collaborative work aimed at implanting the UN-PRI Principles in a policy and regulatory framework. An important aspect of this is to work towards standardisation of ESG reporting and disclosure of ESG issues in annual financial reports. Any such collaboration is also recorded in the “*Engagement and Proxy Voting Register*”. The register is reviewed on an annual basis. The review process will determine if previous collaboration has been effective and what areas of policy and regulatory systems might be in need of further improvement.

## **5. Broader Stakeholder Engagement**

Where Celeste engages with any type of stakeholder that are not already mentioned above on ESG or UN-PRI related issues, this contact will be recorded in the “*Engagement and Proxy Voting Register*”. The register is reviewed on an annual basis. The review process will determine if any stakeholders require particular attention or which group of stakeholders has responded poorly to the engagement initiative and what can be done to improve that situation.

## Appendix E – United Nations Global Compact

### ***Overview of the UN Global Compact***

The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with [ten universally accepted principles](#) in the areas of [human rights](#), [labour](#), [environment](#) and [anti-corruption](#). By doing so, business, as a primary agent driving globalization, can help ensure that markets, commerce, technology and finance advance in ways that benefit economies and societies everywhere.

Never before have the objectives of the international community and the business world been so aligned. Common goals, such as building markets, combating corruption, safeguarding the environment and ensuring social inclusion, have resulted in unprecedented partnerships and openness among business, government, civil society, labour and the United Nations. Many businesses recognize the need to collaborate with international actors in the current global context where social, political and economic challenges (and opportunities) – whether occurring at home or in other regions – affect companies as never before.

This ever-increasing understanding is reflected in the growth of the Global Compact, which today stands as the largest corporate citizenship and sustainability initiative in the world -- with over 4700 corporate participants and stakeholders from over 130 countries.

The Global Compact is a leadership platform, endorsed by Chief Executive Officers, and offering a unique strategic platform for participants to advance their commitments to sustainability and corporate citizenship. Structured as a public-private initiative, the Global Compact is policy framework for the development, implementation, and disclosure of sustainability principles and practices and offering participants a wide spectrum of specialized workstreams, management tools and resources, and topical programs and projects -- all designed to help advance sustainable business models and markets in order to contribute to the initiative's overarching mission of helping to build a more sustainable and inclusive global economy. (See [How to Participate](#).)

The UN Global Compact has two objectives:

1. Mainstream the ten principles in business activities around the world
2. Catalyze actions in support of broader UN goals, including the Millennium Development Goals (MDGs)

With these twin and complementary objectives in mind, the Global Compact has shaped an initiative that provides collaborative solutions to the most fundamental challenges facing both business and society. The Global Compact seeks to combine the best properties of the UN, such as moral authority and convening power, with the private sector's solution-finding strengths, and the expertise and capacities of a range of key stakeholders. The initiative is global and local; private and public; voluntary yet accountable. The Global Compact's has a unique constellation of participants and stakeholders -- bringing companies together with governments, civil society, labour, the United Nations, and other key interests.

The benefits of engagement include the following:

Adopting an established and globally recognized policy framework for the development, implementation, and disclosure of environmental, social, and governance policies and practices.  
Sharing best and emerging practices to advance practical solutions and strategies to common challenges.  
Advancing sustainability solutions in partnership with a range of stakeholders, including UN agencies, governments, civil society, labour, and other non-business interests.  
Linking business units and subsidiaries across the value chain with the Global Compact's Local Networks around the world -- many of these in developing and emerging markets.  
Accessing the United Nations' extensive knowledge of and experience with sustainability and development issues.  
Utilizing UN Global Compact management tools and resources, and the opportunity to engage in specialized workstreams in the environmental, social and governance realms.

In summary, the Global Compact exists to assist the private sector in the management of increasingly complex risks and opportunities in the environmental, social and governance realms. By partnering with companies in this way, and leveraging the expertise and capacities of a range of other stakeholders, the Global Compact seeks to embed markets and societies with universal principles and values for the benefit of all.

## ***The Ten Principles***

The UN Global Compact's ten principles in the areas of human rights, labour, the environment and anti-corruption enjoy universal consensus and are derived from:

[The Universal Declaration of Human Rights](#)

[The International Labour Organization's Declaration on Fundamental Principles and Rights at Work](#)

[The Rio Declaration on Environment and Development](#)

[The United Nations Convention Against Corruption](#)

The Global Compact asks companies to embrace, support and enact, within their sphere of influence, a set of core values in the areas of human rights, labour standards, the environment, and anti-corruption:

### [Human Rights](#)

[Principle 1](#): Businesses should support and respect the protection of internationally proclaimed human rights; and

[Principle 2](#): make sure that they are not complicit in human rights abuses.

### [Labour Standards](#)

[Principle 3](#): Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;

[Principle 4](#): the elimination of all forms of forced and compulsory labour;

[Principle 5](#): the effective abolition of child labour; and

[Principle 6](#): the elimination of discrimination in respect of employment and occupation.

### [Environment](#)

[Principle 7](#): Businesses should support a precautionary approach to environmental challenges;  
[Principle 8](#): undertake initiatives to promote greater environmental responsibility; and  
[Principle 9](#): encourage the development and diffusion of environmentally friendly technologies.

### Anti-Corruption

[Principle 10](#): Businesses should work against corruption in all its forms, including extortion and bribery.