



BUILDING
STRONGER
PORTFOLIOS

Environmental, Social and Governance report

Emerging Market and Asia Pacific Equities (EMAP)

Fourth Quarter 2020



ESG INTEGRATED FUND

J.P.Morgan
Asset Management

“

We believe effective investment stewardship
can materially contribute to helping build
stronger portfolios over the long term, for our clients.

”

George Gatch

CHIEF EXECUTIVE OFFICER
J.P. MORGAN ASSET MANAGEMENT



Our aspirations for engagement

When it comes to corporate engagement, being one of the world’s largest investment managers brings advantages but also challenges.

The starting point from which we engage with the companies in which we invest is strong. We are typically large shareholders, we have a reputation for being long term partners and our engagements are underpinned by the in depth research that comes with a large, well-resourced analyst team.

The challenge is to bring together our sizeable internal resources - from research to a specialist sustainability function - to ensure we pursue a coherent agenda based on consistent principles. In particular it is important that we understand the relationship between sustainable goals and financial outcomes, as it is engagement at this intersection which drives the greatest long term value for our clients.

The purpose of this report is to explain how we are setting about achieving these aspirations and to share examples of progress as we continue on our journey towards ever more productive and impactful corporate engagement.

Our frameworks for engagement

There are two frameworks that you will see referenced in this document:

- Our **Five Investment Stewardship Principles** are the highest level statement of universal priorities that we have. They are set by our Global Sustainable Investing Function and are principles we believe will have universal applicability and stand the test of time.



Governance



Strategy alignment with the long term



Human capital management



Stakeholder engagement



Climate risk

- Our **Research Frameworks** come entirely from the opposite, bottom up perspective. Across global equity we have a **40 question ESG Checklist** which ask the same questions of every company under global coverage to establish a baseline of their ESG credentials. In Emerging Markets and Asia Pacific we also have a **Materiality Framework**. This sees our specialist sector analysts determine which are the most important Environmental, Social and Governance issues within individual industries, and score companies on those in order to identify leaders and laggards.

We hope the case studies and data contained in the following pages help illustrate how these principles and frameworks work together to create a coherent and effective approach to corporate engagement.



Austin Forey, Head of GEM Fundamental Team



Pauline Ng, Head of ASEAN Chair of APAC AM ESG Leadership Team

Engagement: Environmental, Social & Governance

J.P. Morgan Asset Management believes that companies should act in a socially responsible manner. To this end, we are signatories to the United Nations-supported Principles of Responsible Investment (PRI), which commits participants to six Principles, with the aim of incorporating Environmental, Social and Governance (ESG) criteria into their processes when making stock selection decisions and promoting ESG disclosure. As a firm, we prefer to invest in companies that engage in social and environmental behaviours likely to enhance their reputations, rather than compromise them. We believe that such factors are key determinants of sustainability and, ultimately, can have a material impact on share prices over time.

J.P. Morgan Asset Management also recognises its wider stewardship responsibilities to its clients as a major asset owner. To this end, we support the UK Stewardship Code, which sets out the responsibilities of institutional shareholders in respect of investee companies. J.P. Morgan Asset Management endorses the Stewardship Code for its UK investments and supports the Principles as best practice elsewhere. We believe that regular contact with the companies in which we invest is central to our investment process, and we recognise the importance of being an 'active' owner on behalf of our clients.

We have significantly advanced our ESG and Sustainability research in Emerging Markets and Asia Pacific by establishing a materiality framework which now covers over 1,000 companies. The basis of "materiality" is to identify the Environmental, Social or Governance issues that are most likely to have a material negative financial impact on the company were they to be mismanaged, or potentially a material positive impact if they are managed well. Using the sector expertise of our global network of 100+ research analysts, we identified the five most material issues across 54 sub-industries and then scored each company 1-5 with the rating backed up by detailed research commentary. The implementation of this research framework has deepened our understanding of what best practice looks like for sustainability and we used this template to engage with companies.

Our materiality scores are of course a constantly evolving piece of research and this quarter there were upwards and downwards revisions.

Engagement: Environmental, Social & Governance

Sea

We held two engagements this quarter where we sat down with corporates in which we are invested to talk them through our ESG research and frameworks, share best practice and push the companies to improve on specific areas of weakness that we had identified.

Our analyst Sagar Rastogi met with Sea Ltd, the leading e-commerce player in ASEAN. Our materiality framework had identified several issues ranging from poor disclosure to the company having been flagged in third party reports for allowing counterfeit goods to be sold on platform. During the meeting we learnt of some initiatives of which we had been previously unaware, a reminder of the importance of engagement conversations; on environment, for example, the company allows buyers to opt for sea freight rather than air, has started a program of recycling consumer electronics and has introduced biodegradable packaging. It was also pleasing that the company was open to hearing our case studies of what best practice looks like elsewhere, and made commitments to adapt certain practices. We will continue to update our research and adjust our materiality scores if we see concrete evidence of change.



Sagar Rastogi
Exp: 12/3



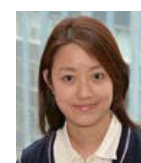
Stakeholder
engagement



Climate risk

President Chainstore

A similar case was an interaction between our analyst Catherine Moong and President Chainstore. We walked the company through our materiality scoring, and then had an in depth conversation about where the company might be able to improve. There were two areas which we highlighted, both of which the company committed to seriously consider. The first was on female board representation, where we indicated our view is that the current 15% level is too low. The second was to suggest the company consider removing adverts for tobacco from within its convenience stores, in order to be in line with best practice elsewhere in emerging markets.



Catherine Moong
Exp: 20/15



Governance



Human capital
management

Engagement: Environmental, Social & Governance

Xinyi Glass

Ensuring that our internal ESG scores are up to date is something we view as being of the utmost importance. This quarter we engaged with Xinyi Glass, a Chinese materials business, to ascertain its targets and strategies on greenhouse gas reduction. Historically we had raised a flag on this issue on our 40 question ESG checklist, due to a lack of clear plan, but our interaction with the company gave us confidence this would improve on a forward looking basis. In particular the company mentioned it plans to align its targets to its sister company, Xinyi Solar, which we do view as having a good enough approach.



Ada Gao
Exp: 7/1



Climate risk



Strategy alignment
with the long term

Shenzhou International

A final common interaction type is engaging with companies to better understand why they have been scored a particularly way by the third party ESG providers. During this quarter we had conversations with Shenzhou International, a textile manufacturer we have always viewed as an ESG leader, to try and understand why MSCI had given the stock a BBB score. Overall we came away reassured in the correctness of our judgement, which has been based on site visits and employee interviews as well as senior management interaction. Indeed we learnt of new impressive initiatives of which we were not previously aware, including plans to ensure no increase in future carbon emissions through the use of renewable power sources. The company did commit to disclose more on carbon footprint going forward, which was one of MSCI's criticisms and something we would also encourage.



Eva Wang
Exp: 16/4



Stakeholder
engagement

Globant

Finally it is interest to see how many companies in which we invest are using the ever higher prominence of ESG to drive business outcomes. The clearest example to date came this quarter when Globant, an Argentinean IT Services company, launched its Sustainable Business Studio which is designed at helping organizations transform themselves into more sustainable enterprises. Its offerings include data tools to measure carbon output, analysis of climate risk and C-Level strategy consulting on embedding a sustainable culture within an organization. We met with the founder of the company during the quarter who outlined his sustainable vision both for his own company and for Globant's clients.



Luis Carrillo
Exp: 28/22



**Sophie Bosch
de Hood**
Exp: 21/21



Strategy alignment
with the long term

Proxy Voting

J.P. Morgan Asset Management exercises the voting rights of shares held in client portfolios, where entrusted with this responsibility. We seek to vote in a prudent and diligent manner, based exclusively on our reasonable judgement of what will best serve the financial interests of our clients. So far as is practicable, we will vote at all of the meetings called by companies in which we are invested.

A summary of key voting statistics and activity for the period is detailed below:

Meetings voted	231	(95.9%)*
Votes with management	1,289	(89.8%)
Votes against management	138	(9.6%)
Abstentions	8	(0.6%)

**a further 10 meetings were not voted due to share blocking and/or conflicts of interest*

Source: JPMorgan Asset Management . Data is for fourth quarter 2020

The following examples should help illustrate the principles behind which we are casting our votes:

Bid Corp

We voted against two remuneration resolutions at the Bid Corp AGM. At the prior AGM we had voted in favour of a long term pay plan for senior management, and at this meeting the company's remuneration committee were looking to amend the targets in that plan to take account of the long term impact of the COVID-19 crisis on the company; Bid Corp is a foodservice company supplying to restaurants so has been particularly hard hit by the crisis. Although we understand the need to incentivize and retain senior management, JPMAM we felt unable to show support for changing an in-flight plan as it would go against our long held principles on this topic.



Piotr Drozd
Exp: 12/5



Governance



Human capital
management

Amoy Diagnostics

We voted in favour of a proposal on use of company funds at Amoy Diagnostics' AGM, which contrasted with ISS' recommendation to vote against the proposal. ISS stated that the company had not given sufficient disclosure on the sorts of products into which it would invest idle cash. However our analyst Vincent Yu held a meeting with the company and discovered that the disclosure had in fact been made, and based on our analysis of the disclosure we felt comfortable supporting management.



Vincent Yu
Exp: 13/8



Governance

Proxy Voting (2)

Kepeco

We voted against the proposed director for the company's audit committee. It was an interesting case as the third party advisors were split with ISS recommending a vote Against the proposal and Glass Lewis recommending a vote in favour. JPMAM's view is that audit committees should be comprised solely of independent directors. While the candidate in question had not had a direct relationship with the company, the individual had been nominated by the Ministry of Economic and Finance. Given Kepeco is a state owned company, our view was that any government recommended appointee could ultimately not be seen as independent.



Seol Kim
Exp: 15/4



Governance

CNOOC

We voted in favour of a proposal to amend the terms of a non-compete agreement between the listed company and the parent company, to allow for asset transfers between the groups with the caveat that such a transaction would have to be approved by independent directors and only take place in special circumstances. Although we would usually be biased against proposals making asset shuffling between different parts of a group easier, in this instance we felt it protected minority shareholders by ensuring that if an asset owned by the company came under sanctions as part of US-China tensions, there would be a buyer for that asset who would pay a fair price. Our analyst Andrew Tan held a meeting with the company which gave us comfort on this point.



Andrew Tan
Exp: 26/13



Governance



Stakeholder
engagement



**Sandro
Apostolico**
Exp: 24/24



**Veronika
Lysogorskaya**
Exp: 15/10



Andrew Tan
Exp: 26/13

Spotlight on

In this quarter's report we asked our three natural resources analysts on the Emerging Markets and Asia Pacific Team to come together to discuss the outlook for the Oil & Gas sector from a sustainability perspective. We hope it gives some insight on the industry and also on how our research process works. The participants were Sandro Apostolico (SA), Veronika Lysogorskaya (VL) and Andrew Tan (AT) who cover commodity stocks in Latam, EMEA and Asia respectively.

1. You recently build the materiality framework for the oil & gas sector. What were the key issues identified and what, if anything, surprised you?

AT: The main issue to overcome was finding the right information. Most of the financially material ESG issues we identified were environmental issues which lent themselves to being quantitatively measured. However it was challenging to score some companies where data disclosure was limited, so in those cases we had to engage to get the companies to publish more.

VL: In EMEA we certainly found disclosure an issue, although it was also a surprise as one discovery was that a lack of information does not always mean the company is an offender. We were concerned that Novatek had no reporting on workplace fatalities in 2019, but after speaking to the company we discovered that was because there had been no fatalities; this represents best in class safety performance on fatalities even compared with global peers. The other challenging aspect of disclosure is consistency, for example scope 1 vs 2 for emissions or LTIFR vs TRCFR for safety records.

SA: The good news is that I do definitely see disclosure starting to improve, and in some ways seeing the extent to which companies are embracing this change has been the biggest surprise. The oil & gas companies I look at have assembled teams, developed systems and established procedures to map, quantify, and set goals on all key issues. Moreover, they now openly and systematically publish the results and the historical data for investors to track how they were doing, what they have done, and where they want to go.

2. How has adding further ESG research to the investment process shaped how you think about investing in the oil & gas sector?

SA: I think here at JPMAM, ESG has never been a separate analysis that is detached from the investment thesis. For example we have always had a preference for companies which employees well and avoided any names that have been documented as having engaged in corruption.

What is new is how much stronger the toolkit is with which we have to make these assessments, especially now all research is globally consistent and on a single software platform. The 40 ESG questions, materiality work and structured engagement have bought an important discipline to our interactions with and analysis of companies.

Spotlight on

AT: To give an example of how the new information impacts our business analysis, we recently had a dialogue with a company who stated that with policy efforts on energy transition global oil demand would only reach 90 million barrels per day (mbd) in 15 years compared to prior projections of 120 mbd.

This understanding can then inform how we think about the right strategy for oil and gas businesses. In this case the company said its strategy is to avoid owning assets that are part of the 30 mbd that will go out of business and then find greener sources of income to offset. This will mean divesting marginal fields, cutting cost and increasing efficiency. On the other hand companies which are already very low on the cost curve will have a superior duration and we can reflect this in our research outputs.

A more sophisticated understanding of supply can help other parts of our analysis. For example because of the energy transition, it is very likely that we will see underinvestments which can cause cyclical spikes in oil price even if temporary in nature.

VL: I agree. ESG has always been an integrated part of our approach in EMEA, however deeper understanding of ESG issues and climate change challenge in particular has helped us to look further out and focus on what will be the winning longer term strategies for the next 10-20 years.

3. As climate change becomes a bigger issue globally, is it one way negativity for the sector or do you see and opportunities? What is required to be a successful oil & gas company in the modern world?

AT: It is an existential threat but one which is accompanied by new opportunities. And we have to be realistic: an oil and gas company cannot stop producing oil and gas overnight. What they need to do is to have long term plans to evolve their output mix towards greener fuel in a multi-stage fashion. It makes sense for companies to tilt the output towards gas first. Even though gas is fossil fuel, it is a transition fuel that is affordable enough to displace coal first.

The new opportunities come from R&D and incumbency. Companies with deep pockets such as Aramco are in a prime position to fund breakthrough technologies; recall that the big oil companies played a large role in helping to pioneer solar technology. Aside from capital, there are other incumbency benefits; E&P companies that are integrated into downstream distribution already have a ready network to sell electricity or hydrogen in the future.

VL: We have a good example of a company reinventing itself through its distribution arm in Russia. Novatek is rolling out a network of LNG refueling stations to incentivize the usage of LNG-fuelled trucks as well as running a pilot project with MMK, a large steel producer, to convert some of its truck fleet to LNG. All of these create new sources of demand for gas and prolong longevity of gas as a fuel.

Capital allocation also plays an important role. For producers at the bottom of the cost curve, the best strategy for all stakeholders may be to continue focusing on fossil fuel production in the least pollutive and most efficient way possible. This will allow them to harvest the reserves they own while maximizing the returns to shareholders.

Spotlight on

SA: One other debate we have had internally is the extent to which we should reward companies in our ESG scoring for diversifying towards renewables. There are different perspectives, and clearly US companies with access to gas and capital are better positioned to do this. However, as Nika alluded to, it is just as important to focus on the ESG practices within the existing oil operations of a company. Are they extracting oil in the most environmentally friendly and efficient way? What is their safety record? Are they returning excess capital to shareholders for them to decide how to best reallocate it from an ESG perspective? These are as important questions to ask as simply whether or not a company is changing its mix.

4. In the developed world we hear a lot about carbon transition. Is this also topic for emerging market oil & gas companies, and what are the other difference between EM and DM majors?

SA: The urgency in emerging markets has perhaps lagged on transition, although this is starting to change, but on the other hand we do see some cases of leadership when it comes to ESG practices within companies' existing operations.

VL: This sounds right to me. In Russia there are examples of companies moving in step with DM peers in some aspects. For example Lukoil was among 41 other oil companies including BP, Shell and Total that endorsed the World Bank's "Zero Routine Flaring by 2030" initiative.

However in other cases the approach is a bit different. For example Russian oil & gas companies tend to be more focused on setting achievable medium term targets rather than grander long term plans. Although these represent smaller steps, nearer term milestones do give much greater accountability. External parties seem to be recognizing the merits of this approach, for example Novatek has targets out to 2030 and was recently upgraded to A rank by MSCI.

AT: In Asia, all countries have signed the Paris Agreement and made their respective commitments so companies are starting to put frameworks in place. For example China has a stated target to be net zero by 2060 and Petrochina said it will be "near-zero" by 2050. We can debate on the seriousness of their intent, but it is a good start and direction of travel.

5. How central is ESG to your engagements with companies? Can you share some recent conversations you have been having?

SA: As I said earlier, it has always been core to our research efforts and conversations. A typical recent example was with a copper company. After analyzing its 2019 sustainability report we were disappointed on the health and safety performance. We engaged with management and because their responses were not specific enough we requested a meeting with the ESG team. We met the team responsible for ESG and the engineer responsible for mining safety and hygiene. It was an incredibly productive meeting in which they went through all the specificities we asked, explained the performance for 2019, and quantified 2020 (until December) indicating quite an improvement in the specific metrics.

VL: As Sandro indicates, it is the depth of the conversations we have that is changing. So take the safety example; we noted that beyond companies' own employees, a common theme is accidents among contractors. We bought this up in several interactions and found out some useful information. For instance Rosneft has started to involve HR in tenders to ensure that potential contractors comply and operate within all the safety standards as well as including safety terms into contracts. Being the largest producer in Russia, this improves the standards for the whole industry.

Spotlight on

AT: As well as these detailed examples, there are also a couple of common high level themes I would mention. One is conversations around more transparency: clearer target, better data and more disclosure. Another is more strategic discussions. One example is that we recently expressed our reservations to an oil & gas business which said it wanted to branch into vaccines and pharmaceuticals as part of its carbon transition strategy.



Source: J.P. Morgan Asset Management; data as of December 31, 2020.

BUILDING STRONGER PORTFOLIOS

At J.P. Morgan Asset Management, collaborating with our clients in an effort to build stronger portfolios drives everything we do.

We are committed to sharing our expertise, insights and solutions to help make better investment decisions. Whatever you are looking to achieve, together we can solve it.



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