Responsible Investment

Quarterly Report
Q3 2014

Standard Life Investments

Contents

Introduction

Standard Life Investments is committed to being a responsible investor. This quarterly report details engagements our Responsible Investment Team has undertaken throughout the period with various companies specifically related to environmental, social and governance issues*.

While not an exhaustive list, this report is a comprehensive representation of the various steps we have taken to ensure we remain an active and responsible steward of our clients' assets.

In addition to details of specific corporate engagement, we have included recent reports written by members of our Responsible Investment Team. These research papers provide insight on issues such as water scarcity, stranded assets, freedom of speech in the telecoms industry and labour relations.

Standard Life Investments is one of the world's leading investment companies, offering global coverage of a broad range of investment instruments and markets. With global assets under management of £195.1 billion (as at 30/06/2014), our capabilities span equities, fixed income, real estate, private equity, multi-asset and absolute return solutions.

Headquartered in Edinburgh, Standard Life Investments employs more than 1,300 talented professionals. As a global investment manager, we maintain a presence throughout the world including offices in Boston, Hong Kong, Paris, London, Beijing, Montreal, Sydney, Dublin and Seoul.

*A separate Governance and Stewardship Team report on ESG activities will be produced in its end of year review.
See: http://www.standardlifeinvestments.com/governance_and_stewardship/index.html

Foreword

Amanda Young
Head of Responsible Investment

During the quarter, we witnessed the largest ever gathering of environmental, social and governance (ESG) professionals from around the world at the annual 'PRI in Person' event in Montreal. Around 600 global asset owners, investment managers and research providers came together to discuss and debate a range of ESG matters. This was an excellent event and I'm delighted to say that, as well as being in attendance, Standard Life Investments was one of its main sponsors.

It was clear that the key issue of the conference was climate change. While the risks associated with a changing climate and rising greenhouse gas emissions are nothing new, there was a renewed focus on this topic. This was no doubt due, in part, to the huge marches that took place around the world ahead of the UN climate change summit in September.

At the climate change summit, convened by Ban Ki-moon in New York, over 100 heads of state and government, including the world's biggest nations, joined together to make public commitments[1] to tackle climate change. These included ways to address and, more importantly, finance the measures needed to tackle climate change.

Numerous leaders highlighted the need to take action, including limiting global temperature increases to less than two degrees celsius. It is likely that world leaders will reach a universal climate agreement at the UN Climate Change Conference, to be held in Paris in 2015.

As I highlighted, the PRI in Person event also took place at the end of September and resulted in the launch of the Montreal Carbon Pledge. This commits its numerous signatories to measuring and publicly disclosing the carbon footprint of their investments on an annual basis. In my view, it also represents a new stage in responsible investing.

The conference, though, did not focus solely on climate change. It also covered issues such as corporate tax responsibility, green bonds, fracking and human rights in the extractive industries.

In addition, the annual Signatory General Meeting was held on the opening day of the event. This included in-depth discussions surrounding the governance of the PRI, as well as an update on the progress the PRI is making in consulting and improving its own governance. At Standard Life Investments, we have been engaged fully throughout this consultation process and we are pleased with the progress the PRI has made. We provided feedback at the conference and welcomed the open and constructive dialogue with the PRI[2].

On day two, we were delighted to participate in the active ownership session titled 'Managing Our Most Important Asset - How Good Human Capital Management Creates Long-Term Value'. At the session, an employee from a fast food chain provided a first-hand perspective on what life was like working in the industry. Employees should be viewed as an asset for any company; however, while firms are very good at articulating how important their employees are, they are very poor at disclosing how they manage their relationships with them.

This session coincided with the launch of Standard Life Investments' white paper on labour[3]. The paper outlines the issues we consider important regarding labour laws and employee relations, including how we approach these issues in our investment process.

On a personal note, I found the conference inspiring and it was a pleasure to spend time with so many enthusiastic delegates. It was also a great example of how times have changed, and how prominent a role responsible investing now plays in our industry. Indeed, 13 years ago it would have been a huge challenge to get fund managers to see the importance of an extractive company having an environmental policy and strategy. Today, ESG issues have reached the mainstream. PRI membership currently represents over $45 trillion of assets under management. Investors around the world now recognise that companies cannot operate in isolation. The way corporations manage issues like labour, human rights and climate change might influence their licence to operate, retain talented employees, innovate, protect reputation and enhance shareholder returns.

[1] Statements made at the climate summit can be found at: www.un.org/climatechange/summit

[2] A written submission to the PRI detailing our views can be found on our website : http://uk.standardlifeinvestments.com/CG_SLI_response_on_PRI_Governance/getLatest.pdf

[3] Details of our approach to labour issues can be found at : http://uk.standardlifeinvestments.com/RI_Labour_Relations/getLatest.pdf

The Responsible Investment Team

Who are we?

The Responsible Investment Team is dedicated to research and analysis of environmental and social issues that have a bearing on Standard Life Investments' client portfolios. We place specific focus on four key areas:

- employment issues
- human rights & community issues
- environmental matters
- anti-corruption.

The Team works closely with our separate Governance & Stewardship Team and seeks to ensure that environmental, social and governance (ESG) considerations are embedded throughout our investment process. Collectively, the team has over 30 years' experience in responsible finance. Further details on our approach and how we engage with investee companies can be found on our website.

The Team

Amanda Young
Head of Responsible Investment

Alix Chosson
Analyst, Responsible Investment

Rebecca Maclean
Analyst, Responsible Investment

Andrew Mason
Analyst, Responsible Investment

Thematic commentary

Standard Life Investments is committed to inform and lead debate on core issues affecting responsible investment, governance and stewardship.

As part of this commitment, we published several research papers throughout the quarter, providing insight into particular areas of concern to clients. In addition, we participated in numerous important initiatives within the spheres of responsible investment. In this section, we provide an overview of these articles and engagements.

Water - an increasingly scarce resource

Water is an essential – but increasingly scarce – resource. Water shortages, thanks to growing populations, rising middle classes and pollution, threaten the ability to grow vibrant, stable economies. For example, the World Bank estimates China's GDP is reduced by 2.3% every year owing to water scarcity and pollution. Even today, nearly a billion people do not have access to safe drinking water. Meanwhile, around 500,000 children die every year from illnesses caused by unsafe water and poor sanitation. By 2025, the United Nations estimates that 1.8 billion people will live in regions that have a severe lack of water. As populations and industries grow, the fight for water will no doubt increase.

Water conflict has risen over the past few decades and this is likely to continue. Once a free resource, water is being transformed into a commodity. This commodification has grown in parallel with fears over water scarcity and environmental degradation. Challenges for local communities have increased as a result. Many companies will therefore need to consider effective water resource management from both an operational and reputational perspective. This means firms will have to ensure they can access water without negatively affecting the local communities that rely on it for their day-to-day needs.

Globally, agriculture is the biggest drain on water supplies, accounting for 70% of all consumption. Second comes industry (mining, manufacturing, etc.), which uses 20%, with the remaining 10% consumed domestically. Further, agricultural commodities, like cotton, wheat and sugar, are used by companies in the food & beverage, retail and apparel sectors to produce their goods. As such, the likes of General Mills, Nestle, Danone and Coca-Cola, are also affected – directly and indirectly – by issues surrounding agriculture and water availability.

To remain competitive, companies have begun to invest significant sums to ensure good water stewardship. Since 2011, it is estimated that more than $84 billion has been spent worldwide on water management. While this figure is difficult to corroborate given the different ways companies disclose capital and operating costs, it is evident that the cost of accessing and managing water is increasing for businesses.

However, several companies are already seeing positive results from this outlay. For example, MillerCoors (a joint venture between SABMiller and Molson Coors) has been leading the brewing industry in water efficiency. Thanks to its innovative methods, it only uses an average of 3.5 barrels of water to brew one barrel of its beer; this compares to the US industry average of six barrels. MillerCoors also holds the world efficiency record for brewing, creating a barrel of beer from only 2.8 barrels of water.

There are numerous other market opportunities for businesses active in the water industry. Pioneering companies are developing technologies and processes that provide solutions to some of the world's water challenges. These technologies include leak detection, water reuse and desalination processes. Over the past five years, desalination capacity has increased by 57% to nearly 20 billion gallons a day, benefiting companies like GE and Veolia Environment. In addition, companies like Dow Chemical have developed technologies for water treatment and water purification that bring clean, affordable water to more people around the world.

At Standard Life Investments, we encourage the companies in which we invest to practice better water stewardship. By doing so, firms can deliver greater operational security in an environmentally sound manner while simultaneously benefiting the local communities in which they operate.

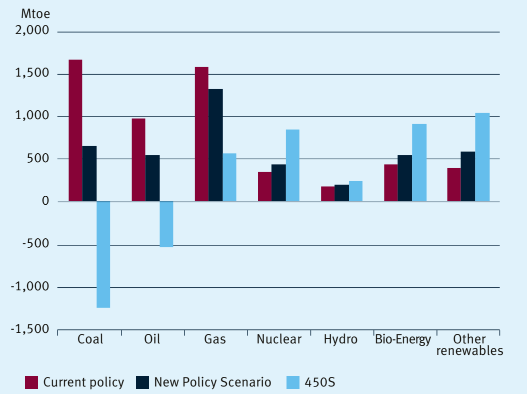
Stranded assets, climate change and coal

Stranded assets are those assets that suffer from unexpected devaluations or writedowns. The current industry debate focuses on the risks to fossil fuel reserves as a result of increasing carbon regulation. In 2011, the Carbon Tracker Initiative published a report titled 'Unburnable Carbon', which looked closely at this issue.

In order to avoid serious climate change, the UNFCCC (United Nations Framework Convention on Climate Change) states that the global mean temperature cannot rise by more than two degrees celsius above pre-industrial levels. However, the International Energy Agency (IEA) has estimated that to stay within this scenario, only one third of proven fossil fuel reserves can be consumed by 2050. Non-governmental agencies (NGOs), asset owners and asset managers have started to debate the topic and are engaging with fossil fuel companies in order to understand how they are integrating low carbon scenarios into their business models. In late 2013, 70 investors wrote to 40 oil, gas and coal businesses asking them to review their exposure to carbon regulation and outline their approach to managing risk.

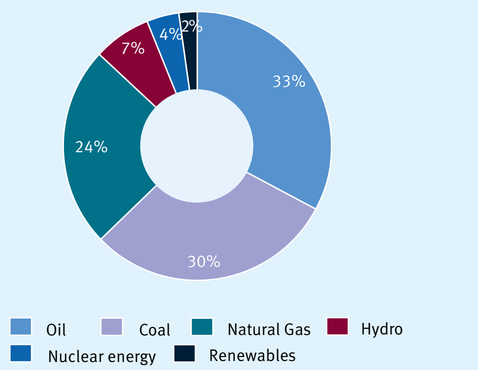
We have conducted two pieces of analysis on the topic of stranded assets. In the first report, we examined the outlook for coal demand growth in the context of climate and environmental regulation. The paper also outlines a methodology with which to analyse companies' exposure to changes in coal demand. In our view, thermal coal is the fossil fuel most vulnerable to stranding owing to its inextricable link to energy demand and the fact that it is easily substituted by other fuels.

Chart 1: Global energy demand by fuel under three scenarios, 2011 to 2035



Source: IEA, 2013 World Energy Outlook

Chart 2: Breakdown of global primary energy consumption (mtoe) 2013



Source: IEA, 2013 World Energy Outlook

Coal makes up 30% of global energy consumption and remains the cheapest form of energy in several countries. Thermal coal demand is driven by growing energy needs and coal's contribution to the energy mix. In many nations, coal is an important driver of economic growth, fuelling infrastructure and energy projects. It is unsurprising that coal consumption is correlated with GDP in many countries. It also explains why many of these nations are reluctant to limit their coal consumption. This makes environmental goals more difficult to achieve.

However, even in the absence of a global climate deal, it is our view that environmental pollution concerns can change sentiment towards coal and make alternatives increasingly attractive. Therefore, since the average reserve life of coal companies we analysed is around 30 years, long-term structural trends are important for company valuations.

Three factors are changing the outlook for coal's contribution to the global energy mix.

- **Divestment campaigns** are causing reputational damage to fossil fuel companies.
- **Environmental and carbon regulation** is becoming more stringent in many countries, with the associated compliance costs for coal consumers. Meanwhile, the additional lack of regulatory clarity in many nations also acts to stymie investment in thermal coal power plants.
- **Renewable energy** costs are falling, particularly when it comes to making the all-important energy storage batteries. Increasingly this removes the price-advantage coal has over so-called green technologies.

Recently, we conducted analysis on the outlook for thermal coal demand in the top eight coal-consuming countries. The model included drivers of energy demand growth, competition from alternatives and environmental standards for coal consumers.

The results indicated that growth rates in future coal demand are uncertain. Unsurprisingly, in this context, those high-cost producers that derive the majority of their profits from thermal coal will be most susceptible over the coming years.

Our second report on stranded assets focuses on oil. The key findings from both these reports will be published this year and will be found on our website at: http://www.standardlifeinvestments.com/sustainable_and_responsible_investing/index.html.

Telecoms industry dialogue on freedom of speech and privacy

In last quarter's report we highlighted our approach to evaluating and promoting human rights. During this quarter, we have applied this process within the telecoms industry.

In 2011, several telecoms operators came together to form the Telecom Industry Dialogue. This is a platform to promote multi-stakeholder dialogue between telecoms companies, governments and civil society bodies in order to advance freedom of expression and privacy rights within telecommunication services.

The initiative was launched immediately following the Arab Spring. At this time, several telecoms companies were criticised widely for allowing governments to censor communications, conduct mass surveillance and promote propaganda in an effort to contain the uprising. Although this sort of state intervention is authorised by license agreements, it highlights how challenging it is for companies to 'respect' human rights, when a state fails to do so (as stated in the Ruggie Principles). Specifically, these events proved the need for clearer guidelines and greater transparency regarding the relationship between telecoms operators and governments.

In March 2013, the Telecom Industry Dialogue published its Guiding Principles to assist telecoms companies in managing their human rights risks. Influenced by the UN Guiding Principles on Business and Human Rights, these ten principles address the issues of privacy and freedom of expression, specifically exploring the interaction and boundaries between a government's duty to protect human rights and the corporate responsibility of telecoms companies to respect human rights. In particular, the Guiding Principles offer guidance on how to address the human rights challenges relating to handling government requests. The publication of these principles was timely. In June 2013, Edward Snowden's revelations on the massive phone and internet surveillance programme conducted by the US government demonstrated that human rights issues relating to telecoms were not solely confined to countries with weak democratic rule.

In July, we participated in a call organised by the Global Network Initiative on the implementation of the Telecom Industry Dialogue on Freedom of Speech and Privacy Principles. We welcomed the steps taken to provide greater accountability and transparency on how telecoms firms deal with government requests. Furthermore, we believe the initiative constitutes a powerful platform to push for greater transparency from governments. Such a move would not only benefit the telecoms industry, but also civil society as a whole.

We believe the Guiding Principles constitute good common foundations from which to address these issues. In the future, companies should report on how they have implemented these principles (or equivalent policies) and how they monitor compliance.

However, the implementation of these principles requires member states to fulfil their duty to protect their citizens against human rights abuses, in the first place. As such, we believe telecoms firms operating in countries with weak institutional capabilities and where freedom of speech and privacy rights are not enshrined and enforced by law will struggle to initiate these principles.

We plan to engage with telecoms groups, including both members and non-members of the initiative, to assess their approach to freedom of speech and privacy issues. One of the major remaining issues is around the implementation of the third pillar of the Ruggie Principles, 'access to remedy'. This topic is likely to be high on the agenda when the Telecom Industry Dialogue meets in future. The issue promises to be quite challenging, but we will maintain our involvement throughout the process.

Labour relations white paper

During the quarter, we published our second white paper, on labour relations. The four strands of the UN Global Compact – human rights, labour relations, the environment and bribery & corruption – form the foundation of the work of our Responsible Investment Team. These issues are integral to our engagement with investee companies and we plan to produce a white paper on each.

The key set of global laws governing labour relations was formed in 1998 by the International Labour Organisation (ILO). This world-recognised body enshrines its core labour principles in its Declaration on Fundamental Principles and Rights at Work. The work of the ILO forms four of the ten principles of the United Nations Global Compact. These state that businesses should:

- uphold the freedom of association and the effective recognition of the right to collective bargaining (Principle 3)
- eliminate all forms of forced and compulsory labour (Principle 4)
- ensure the effective abolition of child labour (Principle 5)
- eliminate discrimination in respect of employment (Principle 6).

There is undoubtedly a growing focus on how companies treat their employees. We strongly believe that labour relations are a key issue for corporate management. While significant progress has been made in improving employment issues over time, labour relations remains a complex issue. In an increasingly globalised world, where companies of all sizes operate across numerous borders, labour relations now extend beyond a company's own operations to its entire supply chain. Corporations require robust strategies and processes to mitigate any potential reputational and operational risks arising from both direct (their own), and indirect (their suppliers') work practices. Failure to manage a workforce, as well as influence the practices and behaviours of suppliers, can lead to significant operational and reputational risks for companies.

The issues we highlight are considerable and include forced or bonded labour, discrimination, health, wages and employee engagement. We assess the risks of the companies in which we invest against these various aspects of labour laws. We also take into consideration the risks of the various sectors, both in respect to their direct and indirect work forces. Alongside this analysis, we engage with a number of stakeholders on a variety of labour-related matters to gain a broad understanding of the risks and challenges firms may face in the various regions of the world.

Collaborative engagement and events

Global statement on climate change

Standard Life Investments, in collaboration with almost 350 global institutional investors representing over $24 trillion in assets, has lent its support to a statement calling on governments to provide reliable and economically meaningful carbon pricing that helps redirect investment commensurate with the scale of the climate change challenge. The statement was released ahead of the United Nations Climate Summit, convened by the UN Secretary-General at the United Nations. Further information and details of the statement can be found on our website at:

http://www.standardlifeinvestments.com/sustainable_and_responsible_investing/documents.html

CDP climate change oil & gas working group

Standard Life Investments has been asked to participate in a working group organised by the Carbon Disclosure Project (CDP) to review its climate change questionnaire for the oil & gas sector. The CDP is a non-profit organisation that provides questionnaires for companies to disclose information on their approach to climate change issues and, in certain cases, water and forestry management.

The group is made up of industry representatives and investors. Members will provide advice and recommendations for a sector-specific climate change questionnaire for the oil & gas industry. At present, there are several sustainability disclosing standards available to companies. We welcome these standards, although it is our view that disclosure needs to be focused on financial materiality and should not be overly burdensome. The collaboration with key industry representatives provides an opportunity for investors to identify the information that is most useful for ESG analysis. Additionally, it will enable companies to feed back on the issues related to questions in the current CDP questionnaire.

PRI steering committee on employee relations

As detailed in our labour relations white paper, we believe that the way companies treat their employees is a key issue and we continue to work with the PRI on employee relations. During the quarter, we spoke with major UK retailers J Sainsbury and Marks & Spencer as part of our involvement in the PRI-led collaborative engagement on employee relations. At the meetings, investors outlined the purpose of the engagement and the companies' disclosure against the relevant key performance indicators. Conversations with the sector are ongoing, with a number of companies indicating they would improve future disclosure as a result of these discussions.

PRI governance review

We joined a number of asset managers and asset owners to discuss a recent review of the PRI governance structure and what steps could be taken to improve the current process. The review detailed ten recommendations in total, which included the creation of a single governing body, an independent chair and fewer standing committees. We welcome this review. The issue of PRI governance has come under increasing scrutiny of late, including the delisting of several Danish signatories. For further details of our response to the issues raised during the review please see:

http://www.standardlifeinvestments.com/sustainable_and_responsible_investing/documents.html

Sector and asset class reports

Nick Kordowski
Investment Director

As a global investment manager with capabilities spanning the full breadth of asset classes, our active approach to responsible investment facilitates the provision of client insight across many sectors and areas of investment. Below we invite comments by our European telecoms sector analyst and our real estate team.

European telecoms sector

Within the European telecoms sector, Norway's Telenor and Sweden's TeliaSonera enjoy some of the strongest credit ratings and, consequently, some of the lowest credit spreads of any telecoms operator. These credit profiles are further supported by the fact that their respective governments have large ownership stakes in the firms, while both have relatively stable operations in a number of Scandinavian markets. However, both Telenor and TeliaSonera also have significant operations in emerging markets. Therefore, given the associated risks with such geographical diversity, credit investors need to conduct analysis on the strategies both companies use in these regions, as well as on the quality of their governance and risk management practices. In this context, we have worked closely with the Responsible Investment Team and have incorporated the analysis into the positioning of our funds.

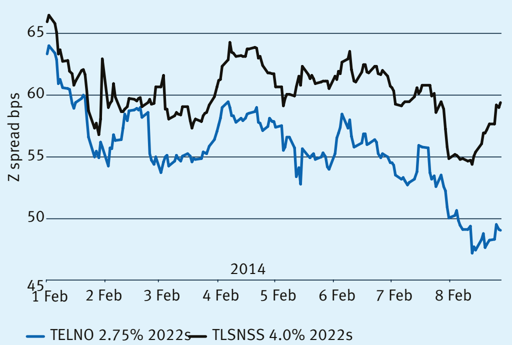
In late 2012, the Reponsible Investment Team reviewed TeliaSonera's human rights and bribery & corruption procedures. This followed allegations of wrongdoing in Uzbekistan. Subsequent to the meeting – and after further internal analysis – the Credit and Responsible Investment Teams remained unconvinced as to the suitability of the company's risk management framework given the potentially volatile conditions in its countries of operation. As such, all our corporate bond portfolios moved underweight in the stock relative to their benchmarks.

Meanwhile, the Reponsible Investment Team has also had steady contact with Telenor in the wake of it winning a contract to run two mobile licences in Myanmar. Given the risks and challenges of operating in this country, we concluded it would be useful to supplement our standard credit research with more active engagement with Telenor. While the company will need to adapt and improve its existing practices in many regards, it has shown ongoing improvement throughout the engagement, particularly relating to the transparency and market communications surrounding this new venture (this is in stark contrast to the other licence winner, Ooredoo).

Although not a singular reason for fund positioning, the views and analysis of the Reponsible Investment Team have proved useful when assessing the overall quality of risk management and the flexibility of strategies companies possess to meet new challenges. Since 2012, TeliaSonera has been investigated by the US Department of Justice over the Uzbekistan corruption allegations, and experienced significant management change. It has also come under the scrutiny of the Swedish government. This, in turn, has been a factor in TeliaSonera's credit-spread underperformance relative to Telenor (see chart).

We continue to work with the Reponsible Investment Team to further our understanding of how companies are implementing a variety of policies and strategies, many of which have the potential to influence the market's perception of valuation for a corporate bond issuer.

Corporate bond spread performance 2014 YTD



Source: Barclays Bank 2014

GRESB
Green Star 2014

GRESB
Sector Leader 2014

Sustaining reality…
Keeping it green..?

Standard Life Investments won the IPD 'Sustainability Data Award' this year. We also gained worldwide recognition for all the funds we submitted to the Global Real Estate Sustainability Benchmark (GRESB).

We put forward nine of our funds to GRESB this year and achieved 'Green Star' status for all of them, covering both sector-specific and diversified funds. With assets located throughout the UK, Europe, Canada and Australia, this is recognition that whatever the property type and in whichever geographical region we operate, we invest in real estate in a sustainable manner.

In addition, the Standard Life Investments Property Income Trust (a listed fund), achieved 'Green Star' status this year. It was also recognised as a 'Global Sector Leader' for the diversified office/industrial small lot sector.

For further information on our real estate capabilities please see:

http://www.standardlifeinvestments.com/our_investment_capabilities/property/index.html

Graham Baxter
Sustainable Engineering Manager

Sustainability engagement

During the third quarter of 2014, we engaged with a wide variety of companies regarding environmental and social issues. Below we outline further details of some of these interactions, in addition to a summary of all company meetings.

We use a matrix approach to identify the companies with which we engage. This approach considers a number of criteria, including internal mandates, specific client mandates and company performance. The key below offers details of the drivers for engagement with individual companies. We outlined this in more detail in our quarterly report during the first quarter. Additionally, further information on our approach to engagement can be found at:

http://www.standardlifeinvestments.com/sustainable_and_responsible_investing/engagement.html

Key

- Internal mandate
- Client mandate
- Performance based engagement

Associated British Foods	Associated British Foods (ABF) is a diversified international food, ingredients and retail group operating in 47 countries. We spoke with the ABF to gain further insight into its corporate responsibility strategy. The company has a decentralised approach to sustainability. It has five main operations: sugar, agriculture, grocery, ingredients and Primark (the retail outlet). This quarter, each business is submitting measurable sustainability priorities. Once they are collated, they will be presented to the board and be the basis for the group's priorities. ABF confirmed that it has no intention to issue group-wide sustainability targets. We welcomed ABF's plans to promote knowledge-sharing of sustainability best practices between its divisions. For example, the ethical sourcing team from Primark has been working closely with ABF's grocery division, helping improve its supply-chain ethical audits. Following the 2013 Rana Plaza disaster in which 1,127 people died after a building collapsed, Primark has introduced a series of measures to manage the aftermath and mitigate the future risk of such events. These include signing the Bangladesh Accord on Building & Fire Safety, contributing $12 million into the Rana Plaza Donors Trust Fund and conducting structural integrity assessment of all its factories in Bangladesh. At Standard Life Investments, we are encouraged to learn that Primark is enforcing more stringent health & safety standards for suppliers and has terminated contracts with factories unwilling to make the necessary improvements. Meanwhile, ABF is drawing on expertise from different segments of its business to trace the source of cotton thread using DNA-matching technology. Although the project is challenging, it presents a potential business opportunity if successful. It is also in keeping with the wider market. Given the water and social issues relating to cotton production in many countries, such as Uzbekistan, many apparel manufacturers and retailers now identify the source of all the cotton they use in their products. Elsewhere, ABF agreed that health trends and the World Health Organisation's guidance to decrease sugar consumption present some challenges for the sugar segment of its business. In response, ABF has launched a website 'Making sense of sugar', which outlines the benefits sugar can play as part of a healthy and balanced diet. The company has also started to produce its own natural sweetener, Stevia. This is a welcome development, providing protection against falling sugar demand in a number of countries. We will continue to track the progress of ABF's various sustainability initiatives.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

BNP Paribas	We questioned the French bank BNP Paribas on the $8.9 billion fine it received in the US after it breached sanctions against Sudan, Cuba and Iran. The bank advised that these breaches were not reflective of its overall approach and that it has invested £200 million in new compliance mechanisms. Recently, 40 employees (mainly from the Swiss unit) including the head of compliance and chairman of the Swiss unit faced disciplinary proceedings. In response, the bank has restructured its risk oversight. This involves audit, group compliance, group legal and group risk functions reporting on a monthly basis to a group supervisory committee, which is chaired by the CEO. The committee works in collaboration with a group conduct committee and reports to the board. To add additional oversight, all US dollar flows are now controlled via operations in New York. We encouraged the bank's compliance functions to focus on high-risk business areas and geographies. We also encouraged greater disclosure of the risks subsequently identified and the actions taken to address them. BNP has had well-established sustainability practices since 2002, and has taken a number of steps to bolster its economic, social and civic responsibilities. The bank may face further conduct costs as a result of potential investigations by FINMA (Swiss financial regulator) and greater demands from the European Banking Authority. However, we will continue to monitor the progress of BNP Paribas' risk functions and any potential future fines.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

British American Tobacco	British American Tobacco (BAT) is the world's most international tobacco group, operating in more countries than any other. We questioned the steps BAT is taking to reduce the negative health impacts of its products. The company stated that it had invested £167 million in R&D last year, focused primarily on reducing the harmfulness of tobacco-based products. This included the development of new products for the e-cigarette market. However, e-cigarettes currently make-up less than 1% of the total tobacco market, while it is still unclear what regulations will be applied in the future. We highlighted the various steps being taken by the World Health Organisation (WHO), several governments and the EU to reduce the number of people that smoke. The WHO's Framework on Tobacco Control is having its sixth meeting in Russia later this year. Among the proposals are the promotion of alternative crops to tobacco and the divestment of government funds from tobacco stocks. The use of plain packaging has taken effect in Australia, and may spread to geographies including the UK and Ireland. Upcoming EU regulation includes the EU Tobacco Products Directive, scheduled to come on line in 2016, with a further two to three years for it to be applied among member nations. BAT highlighted that it would work with governments regarding these measures but cautioned that certain steps, such as the introduction of plain packaging, could lead to an increase in the number of illicit cigarettes produced. We will continue to engage with the company regarding the various regulatory measures imposed on the sector, the rise of tobacco substitutes such as e-cigarettes and its work on reducing the harmfulness of tobacco-based products.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

Britvic	We met with Britvic, the British soft drinks company. We welcomed Britvic's new health strategy, which consists of four pillars: providing a wide choice, supporting a more transparent labelling system, driving calorie reduction and a responsible approach to marketing. As a leader in health-conscious beverage manufacturing, these measures should give Britvic additional business opportunities. It should also help the firm with its self-stated aim of being trusted by both its customers and the communities in which it operates. We encouraged Britvic to consider integrating the communication of health objectives into the business strategy and hope to see more on this in the 2014 annual report. For our part, we highlighted the prospect, and subsequent challenges, of a sugar tax in the UK and the ongoing transition of consumers towards 'healthier' diets. In March this year, the World Health Organisation downgraded guidance for daily sugar intake from 10% to 5% of energy requirements, equivalent to 25 grams of sugar per day. Since 2010, Britvic has reduced the calorie content of its own brands in the UK by 37%, and has also signed-up to the government's Responsibility Deal. Recently, Britvic committed to front-of-pack labelling across all products. We welcome these moves. Britvic's responsible sourcing programme entails conducting ethical risk assessments of all it direct suppliers. At Standard Life Investments, we encouraged greater disclosure of the methodology and results of this analysis. Meanwhile, the company is in the early stages of conducting analysis of its water risk exposure in areas most at threat. Britvic agreed to disclose details of the results when the work is complete. Finally, we encouraged Britvic to provide more disclosure on product safety, following the Fruit Shoot recall in 2012.
Cineworld	We met with Cineworld, a leading European cinema group, to discuss employee relations. We discussed how the company addressed labour-related issues, including the management of a workforce predominantly on zero-hour contracts. We also discussed the company's position on the issue of the living wage. We were reassured to learn about the various mechanisms the company has in place to engage with its employees. Cineworld highlighted the advantages that come with zero-hour contracts, including flexibility and other social benefits. We encouraged the company to provide greater disclosure on the structure of its workforce, the social benefits it provides to its employees and the training and career development programmes is has in place. We also encouraged Cineworld to report on employee turnover and health & safety metrics. We will continue to monitor the company's future disclosure practices in these areas.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

General Motors	
● ●	US auto manufacturer General Motors (GM) is facing significant challenges following an ignition-switch recall that has been linked to 32 crashes and 13 deaths. Globally, the auto industry is facing increased scrutiny for product safety. For example, the number of automotive recalls in China doubled in 2013. At Standard Life Investments, we contacted GM to receive an update on the policy and procedural changes it enacted to mitigate the risks and financial implications of the recall. GM has reacted seriously to the recent recalls and implemented a range of initiatives to improve accountability and safety rigour within the organisation. Two-thirds of the models recalled are no longer in production, which has served to reduce the impact across current product lines. Safety decisions have been elevated to the highest level in the company following the ignition-switch recall. We welcomed this step-change in accountability and responsibility. In other matters, we questioned the company about the prospect for growth in alternative fuel and electric cars. GM has a broad portfolio of alternative fuel cars to meet demands in different geographies, from flexible fuels to electric cars. We welcomed and encouraged GM's investments in product development and see this as an opportunity for the company globally. We noted that in 2013, GM decreased spend on R&D. The company assured us that it was focusing spend but could not identify the areas to lose funding. The five strategy areas are: 1) automotive cleantech, 2) connected vehicles, 3) advanced materials, 4) sensory, processors and memory, and 5) manufacturing technologies.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

Glencore	
	Glencore is UK-listed diversified global mining company, with a focus on metals and minerals, energy products and agricultural goods. We spoke with the company in order to gain a better understanding of how it was managing its anti-corruption mechanisms. Following the merger between Glencore and Xstrata, the firm has been working to develop its corporate responsibility practices. Glencore provided an overview of the governance mechanisms that oversee both policy and implementation of anti-bribery and corruption. As part of this, sanctions are managed and monitored. The company also provided an overview of how it screens its counterparts and external partners. In addition, Glencore provided details of how it manages business ethics in the different parts of its trading and mining operations, including training the right people and ensuring the right type of training is given in key areas of risk. While we received some assurance over its procedures, we noted that there was little information regarding this in the public domain. We therefore encouraged the company to make more detail available generally regarding its risk assessments and training processes. We also questioned Glencore on its lack of an independent whistleblowing hotline. The group confirmed that it had chosen not to have a third-party overseeing its whistleblowing mechanisms, citing confidentiality reasons. That said, Glencore confirmed that it had anonymous whistleblowing apparatus in place through email and telephone lines. As a result of earlier conversations with the company, Glencore has now taken third-party advice. In addition, following our last meeting it has introduced a local language call-line. We welcomed these moves but encouraged better disclosure on how it manages its whistleblowing mechanisms, including disclosure of governance, processes and audit. We also encouraged Glencore to consider how it would encourage employees to use these reporting mechanisms, given that they were not independent. There is evidence to suggest that fear of reprisal discourages individuals from using call-lines that are not run by independent agencies. We discussed the company's follow-up processes to its reporting mechanisms and questioned how they are overseen by the business ethics committee. Elsewhere, we questioned the company over how it ensures high standards of trading activity and compliance with laws and regulations. Glencore provided us with an update on its improved health & safety mechanisms. There are still some countries where the company faces cultural challenges and a slow change in attitudes towards better safety standards. However, the number of fatalities in the first half of the year was lower than in previous years and Glencore is starting to see the results of its enhanced health & safety standards. While recognising the improvements Glencore is making, we encouraged it to continue to focus on changing the culture at a number of its mines, particularly those that were previously nationalised.

Sustainability engagement

Key

- Internal mandate
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- Performance based engagement

Hammerson	Hammerson is a major UK property development and investment company that is currently developing new sustainability targets. The main focus of this activity is to reduce environmental impacts/costs, while also assessing the effects the company is having at a social level. As part of this process, the company requested we share our views on its proposed strategies. We welcomed the steps already taken to reduce emissions and energy use per sales, which has continued to drop since 2007. We also noted that this included rapid reductions between 2007 and 2010. Technological changes, particularly reductions in the cost of lighting, provided the initial rapid reductions. Savings are now more difficult to find, but costs continue to gradually fall. We were additionally encouraged by the group's risk management practices, which appear robust, particularly regarding legislative risk. After all, the sector is subject to numerous regulations, which can vary in different geographies. As part of its long-term strategy, we encouraged Hammerson to consider energy security and demand, water use/waste, and techniques to adapt to the effects of climate change, such as flooding, subsidence and weather damage. We will offer Hammerson additional commentary after it has drafted its sustainability strategy.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

International Personal Finance

We were invited to attend a stakeholder roundtable event with International Personal Finance (IPF) to discuss the company's approach to business ethics. IPF offers small cash-loans that are made and collected by agents to its customers. It operates in central and eastern Europe and Mexico.

The company provided an overview of how it applies its business ethics standards to its operations. The brand awareness in its eastern European markets is significant, which highlights the importance of protecting the company's reputation. IPF outlined how it worked to ensure a 'cycle of debt' is not created for its customers. The company places a strong rewards culture for its regular customers, introducing preferred lending rates. The challenge it faces, however, is that many of its markets are unregulated. As such, IPF has worked to develop a minimum set of standards for all its operations. While keen to grow its business, IPF is determined this should be done in the right way, with high standards of business ethics in place.

The company has provided significant training for its senior managers to ensure the organisation's culture is set from the top. IPF has also taken advice from the Institute of Business Ethics. Areas addressed by the company include understanding customer needs, life/work balance for agents, collection practices, health & safety and adopting a high set of business standards. IPF has outlined its standards in its Code of Conduct, which has been communicated to the wider business. The second stage is to ensure adequate training so that these practices are thoroughly embedded throughout IPF. The final stage will be monitoring and accountability, of which customer feedback is an essential component. In order to enhance this process, the company is also keen to gather views of a wide range of stakeholders.

We were encouraged by the company's approach and welcomed the detailed examples of how it was putting its principles into practice.

We questioned the company on preferential pricing and how this worked in practice. We were also keen to understand how customers were treated with respect. This fed into a conversation about how agents were rewarded and the pay mechanisms that fostered high standards of corporate behaviour.

For our part, we recommended that the company enhance its education programmes for its customers. This should increase customer awareness of money management and promote better economic welfare among its clients. We also encouraged IPF to increase transparency around these issues and some of the core metrics relating to its business, including customer retention, customers that become agents, holiday loans, financial incentives and broad business ethics monitoring. We were encouraged by the company's approach to these matters. IPF believes that its business has the ability to be socially enhancing, despite the challenges the industry faces in the wider marketplace.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

John Lewis Partnerships	We were asked to provide comment on John Lewis Partnership's (JLP), the UK food and department store retailer, sustainability stakeholder engagement. We provided feedback on the structure and contents of the JLP Sustainability Review 2014. In general, we are encouraged by the company's level of sustainability reporting and feel that it has been successfully integrated into the core of its business strategy. The Sustainability Review focuses on the material environment, as well as social and governance issues relevant for John Lewis and Waitrose. We welcome the Partnership's work to provide quantitative targets and performance metrics in the report. We suggested several recommendations to improve transparency, including management of business ethics, performance indicators for employee turnover and direct supplier audits.
Lloyds Banking Group	Lloyds Banking Group (LBG) is one of the UK's largest retail banks and is currently carrying out an assessment of its new 'Helping Britain Prosper' plan. This is a set of seven commitments, with independently verified metrics, that aim to support its business, its customers and the British economy. We welcomed the seven metrics used and highlighted that, in addition to corresponding key performance indicators, they offered a robust way to measure how well LBG was doing in its goal to become a sustainable bank. We questioned the company about its current lending to small- and medium-sized enterprises (SME) and retail customers. We also asked about the reward and remuneration mechanisms that are in place for its employees. LBG stated that it is committed to supporting its retail and SME customers. It also said that employee's remuneration was not solely focused on level of sales but also focused on customer satisfaction. We believe that LBG's commitments are a good step towards focusing and conveying its 'social utility'. However, we still have concerns regarding the bank's conduct in other areas, notably allegations around manipulation of the UK government's special liquidity scheme and Libor fixing. LBG has stated that these are predominantly legacy issues. We will continue to engage with the bank and monitor the progress of its 'Helping Britain Prosper' plan.

Sustainability engagement

Key

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Lockheed Martin	Lockheed Martin (LMT), the US defence company, has been hit by cuts to the US defence budget. As a result, it is seeking to expand into non-domestic markets through Lockheed Martin International. It aims to achieve 20% of overall sales in these markets in the next year, with a 60/40 split between foreign military sales and direct customer sales (DCS). We met with the company to share our concerns regarding DCS in areas that have a high risk of bribery & corruption. We encouraged LMT to conduct bribery & corruption risk assessments of each country in which it does business. We also recommended implementing more robust anti-bribery and corruption measures in these geographies. The company is highly dependent on suppliers to provide its products and services. Sound supply-chain measures are in place and a partnership approach is taken with most large suppliers. We highlighted that LMT has exposure to conflict minerals (predominantly those sourced in the Democratic Republic of Congo) and is subject to Section 1502 of the Dodd Frank Act. The company provided details of the systems it has in place to monitor and avoid breaches of the Act. Given the heightened bribery & corruption risks inherent in non-domestic markets, we will continue to monitor LMT's progress closely.
Novartis	Novartis, a Swiss based healthcare company, recently made its first presentation on environmental, social and governance (ESG) issues. The company is seeking to take a more proactive approach to investor engagement and to enhance dialogue on ESG issues. Novartis has streamlined its oversight of sustainability issues and its board of directors now has oversight for this strategy and governance. These steps – to improve disclosures on ESG issues, to identify material ESG issues and to ensure that the appropriate governance of these matters is in place – are to be welcomed. After reviewing all non-financial issues that have an impact on its business and are relevant to stakeholders, the company identified 25 key issues. These can be grouped into eight clusters, three of which Novartis believes are of particular importance: • access to healthcare (i.e. lower income patients, intellectual property) • governance and ethical business practices (i.e. clinical trials, bribery & corruption, marketing, board structure and independence) • research and development (i.e. R&D pipeline, R&D in neglected diseases, adaptive research). We welcome the steps taken by Novartis to identify material ESG, to improve its disclosure on these issues and to ensure that the appropriate governance of these matters is in place. However, concerns remain regarding the application of the company's employee code of conduct and ongoing investigations into its operations in Japan. We will continue to engage with the Novartis as it takes steps to become more transparent.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

Orange	Orange is a French multinational telecommunications company with operations in over 30 countries. We engaged with the company to discuss its approach to two significant challenges for the telecoms sector: human capital management and data privacy and protection. We asked Orange how it was adapting its workforce to the shift of its business towards digital services. We questioned the company on its recruitment and training strategy, and were encouraged to learn about the measures Orange is implementing regarding internal training. We highlighted some of the labour challenges resulting from its former status as a public national operator, including the management of a workforce composed of both civil servants and private contracts. The company is taking various steps to manage this transition. On the issues of data protection and privacy, we believe Orange has laid down solid foundations with adequate policies and commitments. However, it now has to rollout the relevant monitoring systems in its various markets. We encouraged the company to clarify and reinforce its governance around those issues and show more clearly the steps taken to anticipate regulation and increasing expectations from stakeholders. We welcomed that Orange is an active member of the Telecom Industry Dialogue on Freedom of Expression and Privacy and were encouraged by some of the steps taken to increase transparency around the handling of government data requests. Orange operates in a number of countries lacking due process of law and where the state may infringe on individual freedoms, including privacy and freedom of expression. We believe that all telecoms companies, including Orange, still have some way to go to fully implement the UN Guiding Principles on Business and Human Rights in the context of telecommunication services. Orange appears to be taking positive steps in this direction. We will continue to engage with Orange and other companies in the sector on these issues.

Sustainability engagement

Key

- Internal mandate
- Client mandate
- Performance based engagement

Petrofac	Petrofac operates in 29 countries providing facility support to the oil & gas production and processing industry. The company's operations include designing and building oil & gas facilities, operating and managing facilities, and training personnel. We requested a more in-depth meeting with the company following Petrofac's presentation to Standard life Investments and a number of other investors during the last quarter. Petrofac intends to increase its workforce from 18,000 to 25,000 in the next five years. We questioned how the company would manage this expansion and if there are enough skills within the marketplace to fill these positions. The company acknowledged that while there was a skills shortage within the industry, it has established training systems to support the development of new employees. We welcomed these steps and the company's positive health & safety record. Petrofac advised that its health & safety track record and training facilities are helping it to win new business. We questioned the company about its appetite to service unconventional extractive projects, such as deep-water drilling and oil sands, areas in which a number of its clients are beginning to operate. Over the next five years, Petrofac said it intended to focus on conventional and relatively low risk onshore and offshore projects. We welcome these steps, particularly around employee safety and training. We note that the company is developing deep-water capabilities and we will continue to monitor its progress, particularly if it begins to service unconventional extractive projects. We also agreed to provide the company with feedback on its upcoming sustainability report.
Soco	We have had continued engagement with Soco, the UK oil & gas operator, throughout the year, with a particular focus on its operations in the Democratic Republic of Congo (DRC) and its potential operations in Virunga National Park. The company announced that it will not undertake or commission any exploratory or other drilling within Virunga National Park unless UNESCO and the DRC government agree. Further details of this issue and our engagement with Soco can be found in our reports during the first and second quarters of this year. We welcomed the progress made within the Park, although we have concerns regarding further allegations against the group. These include links to human rights abuses and incidents of bribery & corruption. We continue to engage with the company and encourage best environmental, social and governance practices.

Sustainability engagement

Key

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Telenor	We attended Telenor's webinar update concerning sustainability issues in Myanmar. Telenor, a European telecommunications group, is one of the two companies that won mobile licenses for the country and will start operations in September. The company provided further details on how it was addressing the six main ESG challenges identified in its operations in Burma/Myanmar: institutional capacity in development, legal framework, corruption, land issues, health & safety, and conflict areas. In particular, the lack of institutional capacity has direct operational consequences as it slows down the network rollout, and is therefore going to be one of the main challenges for Telenor. We welcomed the significant efforts made by Telenor to provide more transparency on the challenges it faces in Myanmar and the subsequent steps taken to address these hurdles. We were encouraged by Telenor's level of transparency with regard to the difficulties it encounters in operating in this very challenging environment. However, it reinforces our view that the significant human rights challenges specific to the situation in Myanmar will be difficult to overcome, including the lack of institutional capacity, land rights and the role of the military. The legal framework is still under construction and it is difficult to know what assurances will be given to basic rights, such as freedom of expression and privacy. Telenor's reliance on local business partners has the potential to be a catalyst for local socioeconomic development. However, it could also produce significant operational and reputational risks. The company has put in place relevant policies and processes to address this, but the monitoring of suppliers and contractors promises to be a practical challenge. We will continue to monitor these issues closely, particularly after the official launch of activities in September.

Sustainability engagement

Key

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UBS	UBS, the Swiss investment bank, is currently facing a number of issues regarding tax compliance, including a recent settlement with the German authorities and ongoing investigations in France concerning its cross-border wealth management services. The company may also face further conduct costs as result of FX market manipulation and its activities within the US mortgage market. We questioned the group regarding its current oversight and risk mechanisms and the provisions that have been put in place to meet potential conduct costs. UBS highlighted that there is currently a group executive board that oversees corporate responsibility; a board of directors that acts as a corporate responsibility advisory panel; and a global environmental and social risk committee chaired by the group chief risk officer. We have asked for greater public disclosure on how these various boards interact, something the company has said it will consider in future communications. UBS also detailed provisions it had made for future conduct costs and highlighted that its quarterly reporting process offers transparency on potential risks and how such costs will be met. UBS claims that the US no longer presents a significant risk regarding the tax services it provides and that the 'non-target letter programme' is not relevant to its business. However, UBS offered a fairly weak response regarding its risk and compliance operations in different geographies and business units. It claimed that there was a clear escalation process to central risk functions, but had little to offer on the independence of compliance in the different regions or information on who had ultimate responsibility to escalate issues. More positively, however, UBS did state that RMs have the ultimate responsibility for any risks incurred. We will continue to monitor the company's approach to sustainability and the various conduct risks it is facing.

Sustainability engagement

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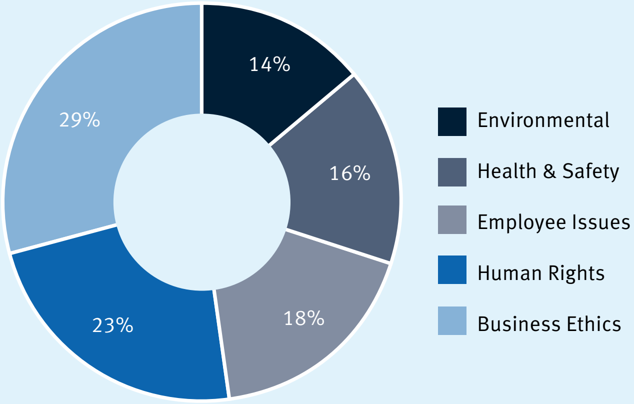
Vinci	Vinci is a French listed global construction company, employing over 180,000 people in some 100 countries. The company's activities include building, civil engineering, hydraulic engineering and construction-related specialities. We engaged with Vinci after it won the public tender for the extension of a motorway in Russia, a project that has faced several human rights, environmental and business ethics-related controversies. We asked about Vinci's approach to engagement with affected stakeholders, and queried the extent the company could influence its clients to consider the above issues. We pressed home the fact that operators, even if not directly responsible, face high reputational risks if local communities are not consulted on high impact projects. We also questioned the company on the implementation and monitoring of its commitments regarding human rights and how this applies to contractors. We were reassured by the company's efforts in this regard in its home market of France. We also encouraged Vinci to increase efforts and improve reporting in other geographies, especially countries where human rights are at risk. We requested more information on a particular project in Qatar, for which Vinci has come under scrutiny from unions and non-government agencies. We discussed Vinci's approach to business ethics and how it was monitoring the issue across countries. We encouraged the company to provide greater disclosure on the organisation and functioning of compliance, how it monitors business partners (including agents) and its approach to facilitation payments. We will continue to monitor the various projects that we believe present environmental and social risks.
Vodafone	We contacted Vodafone, the UK-listed telecommunications company, to discuss its approach to human rights issues in the telecoms sector. The main focus of our discussion was freedom of expression and privacy rights. The company has been a founding member of the Telecom Industry Dialogue, a multi-stakeholder initiative aimed at collectively advancing freedom of expression and privacy issues. We believe Vodafone is leading the way on this issue. In particular, we welcomed the publication of Vodafone's first Law Enforcement Disclosure Report, which we see as best practice in the telecoms industry. We also discussed the recent development of mobile payment and other m-services in developing countries, which we see as a driver of growth for the sector. Again, we see Vodafone as leading the way on this segment. We encouraged the company to provide greater disclosure on the business model and economic equation of these services, in particular m-health and m-education, which the company sees as part of its core business.

Sustainability engagement summary

Company	Environmental	Health & safety	Employee issues	Human rights	Business ethics
Afren	•	•	•	•	•
Alliant Techsystems				•	•
Associated British Foods					
BNP Paribas	•		•		•
British American Tobacco	•	•			•
Britvic	•	•		•	
Cineworld		•	•		
General Dynamics				•	•
General Motors	•	•			
Glencore		•			•
Hammerson	•	•	•		
Hanwha Corporation				•	•
International Personal Finance					•
J Sainsbury			•		
John Lewis Partnerships	•	•	•	•	•
L-3 Communications				•	•
Lloyds	•		•		
Lockheed Martin		•	•	•	•
Marks & Spencer			•		
Northrop Gruman				•	•
Novartis	•		•	•	•
Orange		•	•	•	
Petrofac	•	•			•
Poonsang Corporation				•	•
Raytheon				•	•
Singapore Technologies				•	•
Soco	•		•	•	•
Telenor		•		•	•
Textron				•	•
UBS			•		•
Vinci		•	•	•	•
Vodafone			•	•	•
Total	11	13	15	19	24

Sustainability engagement summary

Engagement summary Q3 2014



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