

Airlie Funds Management stewardship strategy – climate related risks and opportunities

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OVERVIEW

Magellan Financial Group Limited (“**MFG**”) and Magellan Asset Management Limited (“**MAM**”) (together “**Magellan**”) are a signatory to the Net Zero Asset Manager (“**NZAMi**”)¹ initiative.

The purpose of this document is to clearly outline the stewardship (engagement and voting) framework for Magellan’s Australian equities business, Airlie Funds Management (“**Airlie**”, “**we**” or “**our**”), relating to climate risks and opportunities. This strategy has been developed by senior members of the Investment Team and approved by Magellan’s Risk and Compliance Committee (“**RCC**”) and the Head of Australian Equities.

As many countries have committed to transition their economies to net zero by 2050 and expectations from stakeholders, including investors, regulators and governments increase, Airlie wants to ensure that companies in our portfolio remain resilient and take advantage of opportunities. To do this, we are assessing alignment to net zero under the Net Zero Investment Framework (“**NZIF**”)² as part of our commitment to the NZAMi.

Asset managers that have signed the Net Zero Asset Managers commitment have committed to develop and implement “a stewardship and engagement strategy, with a clear escalation and voting policy, that is consistent with an ambition for all assets under management to achieve net zero emissions by 2050 or sooner.”

1. ENGAGEMENT AT AIRLIE

Airlie’s long-term investment horizon gives us the opportunity to engage with companies over an extended period on issues that are important to protecting and creating shareholder value. This includes the risks and opportunities that arise from climate transition risk and physical climate risk.

Engagement process

Airlie aims to engage with portfolio companies on a broad range of Environmental, Social and Governance (“**ESG**”) themes identified by the Investment Team as material to those companies. This includes climate transition and physical risks.

Engagement has two primary objectives, both of which are designed to have a positive impact on shareholder returns over time:

1. **Risk assessment, management, and opportunities:** to better understand the risks and opportunities over time. As long-term investors, we build up knowledge and insight, which we discuss and challenge during engagements. These learnings often deepen our understanding within and across industries. The output of this engagement contributes to the analyst’s assessment of the credibility of the company’s climate strategy and targets which feeds into the assessment of alignment with net zero.
2. **Influence:** encouraging and supporting change to a company’s approach or the setting of climate related targets. As long-term investors, we build constructive relationships which better enable us to drive positive change at a company. The urgency with which we seek to influence usually correlates to the time horizon over which we expect the risk or opportunity to arise. However, with regards to climate transition risk and physical risk, we recognise the importance to set and report against ambitious short-, medium- and long-term targets that are on a Paris aligned pathway to limit warming to 1.5 degrees Celsius.

This climate engagement strategy and voting policy applies to all Airlie strategies and has been developed with guidance from the Net Zero Stewardship Toolkit².

For all portfolio companies, there is a minimum requirement to assess the alignment to net zero using the NZIF. Companies are then prioritised for engagement based on materiality of the financed emissions and their classification of alignment to net zero. These companies are classified as ‘high priority’ and subject to enhanced engagement.

2. APPROACH TO ASSESSING ALIGNMENT TO NET ZERO

The assessment of climate risk within the Airlie investment portfolios is within our framework for assessing ESG risks.

¹ NZAMi is an international group of asset managers committed to supporting the goal of net-zero greenhouse gas emissions by 2050 or sooner, and to supporting investing aligned with net zero emissions by this date. [Signatories – The Net Zero Asset Managers initiative](#)

² <https://www.iigcc.org/resources/net-zero-stewardship-toolkit>

Airlie’s analysts first identify and assess a company’s ESG risks, including climate risks, as part of our initial and ongoing company research. This can involve direct engagement with management of the companies being analysed.

The Airlie Investment Team review climate related targets and commitments for companies we invest in, at least annually. This review includes:

1. **Ambition:** A commitment to net-zero by 2050;
2. **Targets:** Near- and medium-term emission reduction targets with a preference for external validation;
3. **Strategy:** Alignment to reporting in accordance with the Taskforce for Climate-related Financial Disclosures (“TCFD”) and a credible strategy to achieve targets.

We consider these commitments represent prudent risk management in a transitioning economy to net zero.

A key input is our analyst’s view on the credibility of a company’s initiatives and climate strategy to achieve their targets. We also consider disclosure of emissions (Scope 1, 2, 3) and the progress towards targets.

Utilising both Airlie proprietary analysis and other data (including company statements, press articles, external data providers, Science Based Targets initiative (“SBTi”) and expert networks), each company is assessed for their alignment to net zero.

These are assessed against the Net Zero investment framework³ (NZIF) as to whether they are aligned to net zero, aligning, committed or not aligned to net zero.

Net Zero Asset Manager Initiative (NZAMi)

Measuring alignment using NZIF

	Net Zero Target	Interim target	Performance	Disclosure	Strategy	Capex alignment	Credibility
Achieving Net Zero	✓		✓	✓	✓		✓
Aligned: High impact	✓	✓	✓	✓	✓	✓	✓
Aligned: Low impact		✓	✓	✓			✓
Aligning		✓		✓	✓		✓
Committed	✓						✓
Not Aligned							✓
							Airlie view

Source: Developed for Airlie investment process utilising the Net Zero investment Framework

Engagement with portfolio companies is important to assess the credibility of their targets and understand any challenges in committing to these targets.

For companies that are not aligned to Net Zero, the Investment Team will engage and encourage target setting in line with this climate strategy. If there is no progress from companies in terms of setting Net Zero aligned targets or other criteria in assessing alignment to Net Zero, escalation will be considered including voting and potentially divestment. This is covered in the following sections.

3. ENGAGEMENT TARGETS AND OBJECTIVES

Companies will be prioritised for engagement based on Airlie’s assessment of climate related risk for that sector. All companies are assessed for alignment to Net Zero then prioritised for engagement based on whether they are in a high

³ [Net Zero Investment Framework Implementation Guide \(iigcc.org\)](https://www.iigcc.org/)

impact material sector⁴ and according to the size of Airlie's holding across different strategies. Companies may also be prioritised based on:

- progress to date – emission reduction and progress towards targets;
- real world impacts and available technology; and
- ability to influence.

Airlie has set the following engagement targets for companies in high impact material sectors.

- an engagement threshold which ensures that at least 80% of financed emissions in high impact material sectors are either assessed as Net Zero, aligned with a Net Zero pathway, or the subject of direct or collective engagement and stewardship actions.
- by 2030, at least 90% of financed emissions in material sectors are either assessed as net zero, aligned with a net zero pathway, or the subject of direct or collective engagement and stewardship actions.

If a company is assessed using the NZIF as:

- aligning
- committed to aligning or
- not aligned

an engagement plan is developed incorporating objectives to improve alignment with Net Zero based on NZIF. Time bound engagement objectives will be set considering the industry, geography, business model and alignment to Net Zero.

Engagement objectives are set which are communicated to the company including:

- a commitment to Net Zero emissions by the year 2050;
- a commitment to fully align financial disclosures with the recommendations of the TCFD; and
- external validation of emission reduction targets and the plans to achieve such targets. Airlie notes that the SBTi is its preferred standard for external validation of emission reduction targets.

Additional engagement objectives which may be included where it is deemed relevant by the analyst:

- improved disclosure of Scope 1, 2 and material Scope 3 emissions;
- enhanced disclosure and actions that supports a credible climate strategy to meet Net Zero aligned targets. This may include specific engagement objectives regarding scenario analysis, capital allocation alignment and transition plans;
- executive remuneration linked to climate related targets;
- board capabilities and oversight to manage climate change; and
- increased transparency regarding just transition which considers workers and the community for affected industries
- increased transparency on climate related lobbying.

These engagement objectives will be communicated to the priority companies by the Airlie investment team and reviewed at least annually.

4. ESCALATION

In cases where engagement has been ongoing without any progress on an issue considered to be a material climate related risk to future cashflows or valuation, the portfolio managers and analyst team will consider an escalation path that may include:

⁴ High Impact Material sectors are a subset of material sectors called "High Impact Sectors" defined by NZIF and GICS sub industry code – see appendix A.



Actions will be considered on a case by case basis and may include, voting against directors or management proposals, for example, 'Say on Climate' or voting for climate related shareholder proposals. This is discussed in Section 5 below.

Portfolio sizing (including divestment) will be considered by the portfolio manager where the risk is deemed material to cashflows and progress has not been achieved relative to the engagement objectives.

5. VOTING

Airlie intends to vote in a manner that is in the best interests of its clients and that is most likely to protect and promote the long-term economic value of the companies in which Airlie invests. Engagement with companies on climate risks and opportunities including the alignment of the company with Net Zero is the initial focus of the stewardship strategy. Voting as outlined below will be utilised as a tool after engagement with the company. The company will be notified where a vote is cast against the company recommendation.

It is the responsibility of the boards of each portfolio company to manage climate risks and consider climate opportunities. Alignment with the Paris Agreement and setting climate targets are a key commitment to assess a company's preparedness for the transition to a lower carbon economy. It is important for the board of a portfolio company to not delay the transition to a lower carbon economy and take action where possible in the near term. Reporting against TCFD, external target validation with for example SBTi and links between remuneration and climate targets are highly regarded. These initiatives improve transparency and credibility of risk management.

Airlie will consider supporting shareholder proposals which encourage companies to acknowledge, consider, and report on climate risks and opportunities where current ambition, targets, strategy and disclosure are not sufficient. This may include proposals which urge companies to evolve their current approach where enhancements are warranted to improve alignment with net zero.

The following table outlines Airlie's climate related voting framework. Each proposal will be considered on a case-by-case basis.

Vote	Net zero policy and actions	Criteria
Director	Consider voting against Chair or director where no progress is made towards Net Zero alignment and related engagement objective.	<ul style="list-style-type: none"> • Net Zero target. • Interim targets & external accreditation. • Progress against targets. • TCFD alignment. • Actions including capital allocation alignment.

Vote	Net zero policy and actions	Criteria
Remuneration	Consider voting against remuneration report where climate change is a material risk for the company and an engagement objective to link remuneration to climate targets has not been met in the specified timeframe.	<ul style="list-style-type: none"> • Analyst assessment of climate risk on future strategy. • Incorporation of climate targets in remuneration. • Credibility of climate strategy. • Actions including capital allocation alignment.
Mergers and Acquisitions	Consider voting against merger and acquisition related resolutions if it is detracting from alignment to Net Zero.	<ul style="list-style-type: none"> • Analyst assessment of new asset and alignment to Net Zero or ability to transition.
Say on Climate	Consider voting against management proposal where engagement objectives have not been met.	<ul style="list-style-type: none"> • Alignment to Net Zero criteria using NZIF. • Progress on climate related engagement objectives.
Shareholder proposals	Consider supporting proposals that improve alignment with Net Zero where the current ambition, targets, strategy and disclosure are not sufficient	<ul style="list-style-type: none"> • Alignment to Net Zero criteria using NZIF. • Progress on climate related engagement objectives.

6. REPORTING

As part of the commitment to Net Zero asset manager initiative we will provide asset owner clients with information and analytics on our climate related stewardship activities. Progress towards NZAMi commitments and targets will be reported through CDP, PRI and in our TCFD aligned report commencing a year after setting the targets.

APPENDIX A: HIGH IMPACT MATERIAL SECTORS

High Impact material sectors are a subset of the NZIF Material sectors and included in Appendix B of the NZIF Framework.

TPI Sector	GICS Sector Name	GICS Sub Industry / Code
Electricity utilities	Energy	Integrated Oil & Gas Electric Utilities
	Utilities	Independent Power Producers & Energy Traders Multi-Utilities
Oil & gas	Energy	Integrated Oil & Gas Oil & Gas Refining & Marketing Oil & Gas Exploration & Production Oil & Gas Storage & Transportation
	Materials	Diversified Chemicals
Oil & gas distribution	Energy	Oil & Gas Storage & Transportation Oil & Gas Exploration & Production
	Materials	Diversified Chemicals
Coal mining	Energy	Coal & Consumable Fuels Oil & Gas Refining & Marketing
	Consumer discretionary	Automobile Manufacturers
	Industrials	Industrial Conglomerates Trading Companies & Distributors
	Materials	Diversified Metals & Mining Steel
Autos	Consumer discretionary	Automobile Manufacturers
Airlines	Industrials	Airlines
Shipping	Energy	Oil & Gas Storage & Transportation
	Industrials	Marine
Aluminium	Materials	Aluminum Diversified Metals & Mining
	Industrials	Trading Companies & Distributors
Cement	Materials	Construction Materials
Pulp & paper	Materials	Paper Packaging Paper Products
	Materials	Steel
Chemicals	Materials	Commodity Chemicals Diversified Chemicals Fertilizers & Agricultural Chemicals Industrial Gases Specialty Chemicals
Diversified mining	Materials	Diversified Metals & Mining Copper Steel
	Information technology	Electronic Equipment & Instruments Technology Hardware, Storage & Peripherals
Other industrials	Industrials	Aerospace & Defense Construction Machinery & Heavy Trucks Heavy Electrical Equipment Electrical Components & Equipment
	Consumer discretionary	Consumer Electronics
	Materials	Construction Materials
	Materials	Construction Materials