International Alpha

Stewardship Report to 31 March 2022

BAILLIE GIFFORD

Actual Investors

Risk factors and important information

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Introduction

Welcome to the International Alpha Stewardship Report. At Baillie Gifford, we believe actual investing requires long-term shareholders to regard themselves as part-owners of a business on behalf of their clients, as opposed to being renters or speculators. It is only by taking the associated responsibilities of this role seriously, such as those related to governance and sustainability, that we can hope to maximise the opportunities available to you, our clients. We believe that responsible shareholders understand the motivations of management and other key stakeholders, consider the broader impact of a company's activities, call out poor conduct, and provide support or advice where required. Far from acting as a burden on profitability and operational performance, good stewardship helps enhance the long-term profits and sustainability of a business, which in turn could lead to superior investment returns for its part-owners.

In this, our third stewardship report, we hope to shed some light on our activities in this area – why and how we do what we do, what some of the successful engagements have been and also some areas that require further work. We look forward to your feedback on how we might continue to improve our stewardship reporting.

In this year's stewardship report we will discuss our approach to ESG integration in the research process, highlight recent engagements, dig into the specific example of our engagement with one of the building materials holdings CRH in Ireland, call out how we plan to prioritise engagement for next year, and go into detail on how our carbon footprint work has evolved since we last reported to you. We will also provide various portfolio metrics. As part of our ongoing efforts to improve stewardship and sustainability, we have continued to build out our dedicated internal resource of subject matter experts. As such, we begin this report with an interview with Catherine Flockhart (CF), Partner and Head of ESG, and Tom Walsh (TW), Partner and International Alpha Investment Manager, to discuss the journey both we as a firm and International Alpha as a strategy have been on in recent years.

An ESG journey – an interview with Catherine Flockhart and Tom Walsh

We speak to Catherine Flockhart, head of ESG at Baillie Gifford and Tom Walsh, investment manager, about the evolution of ESG at Baillie Gifford in recent years.

Catherine, there has been considerable focus in our industry on the integration of ESG (environmental, social and governance) within investments. Could you tell us about Baillie Gifford's progress and ambition regarding this?

CF: As long-term investors, we have always implicitly integrated ESG into our approach. Company culture and the sustainability of growth prospects have far more bearing on those of us who invest with a five-year-plus time horizon and fundamental conviction than they do on those speculating on short-term share price moves.

Over the past few years, we have improved the sophistication and depth of our ESG integration. Beyond looking at company culture and the sustainability of growth prospects (which in turn tacitly touched on environmental and social sustainability), we now do far more detailed work on companies' environmental and social credentials, both pre-buy and on an ongoing basis.

Our ambition in this area is perhaps a little different from others'. Just as we do not believe in an investment policy committee dictating investment views for our teams, we do not believe a 'house view' on a particular ESG topic will lead to meaningful, nuanced integration. We invest in companies, not issues, and remain true to our bottom-up approach.

Furthermore, we are firmly of the view that a company's ESG credentials cannot be boiled down to a single number. Nor can they be effectively outsourced to an ESG function that operates in isolation from those making investment decisions for clients.

Instead, we aim to ensure our investment teams have the autonomy to prioritise ESG topics that are of material importance to their clients and the investments they hold. We aim to support individual teams on several fronts. Firstly, with embedded ESG analysts, secondly with specialist teams such as our Climate Team, and finally with cross-department research groups considering key issues, including human rights and corporate governance.

This is all underpinned by a strong central voting and data function. We want to encourage a tailored approach, share best practices and encourage improvement across the firm.

Tom, as it specifically relates to International Alpha, how has the Portfolio Construction Group (PCG) developed its own tailored approach to integrating ESG factors within our processes?

TW: As Catherine says, we've always taken the view that it is impossible to invest for the long term without considering the sustainability of a company's products and practices. That said, in the past we would generally incorporate such aspects into our consideration of other elements of the investment case, such as growth, competitive advantage or quality of management.

Increasingly we've realised we can add more value by being more explicit in our consideration of sustainability and ESG factors. Our research framework now includes specific sections that address sustainability and governance, and every stock has been assessed against a high-level sustainability framework. All of this is designed to increase the degree to which the investors address the risks and opportunities that ESG factors present, allowing for pre-emptive engagement where appropriate and a more rounded understanding of the companies in which we invest client capital.

The involvement of ESG specialists in the process has also grown considerably. A decade ago, we used to draw upon a shared resource based in a central ESG team with interactions largely arising in reaction to company events or issues. We now have two dedicated ESG analysts fully integrated into the central desk team.

They are fully involved in stock discussions and portfolio reviews, so their views can be incorporated at the pre-buy stage and throughout our ownership. They are also helping to shape a proactive agenda of research and engagement that enables us to open conversations with holdings before potential issues become headline concerns. This all helps enhance our fundamental investment analysis and maximises the potential of the companies in which we invest.

Catherine, can you elaborate on the growth in the dedicated ESG function and its value to us as a firm?

CF: We have made a significant investment in our ESG resource. Since the end of 2020, our number of dedicated ESG professionals has risen from 24 to 40, however it is the change in structure of our ESG team that has added most value. It has gone from being a centralised group of generalist ESG analysts to being strategy-specific ESG analysts embedded with investors, supported by an expert Climate Team and a central Voting and Data Team.

Another clear example of our recent progress is how we address the environment. Our focus on strong growth companies means portfolios have been well-positioned with regard to climate change based on simple carbon footprint analysis. But our understanding of the challenges posed by climate change and the sorts of questions we need to be asking of the companies in which we invest has vastly improved in recent years.

Tom, changing tack a little, during your time as a member of the ESG Steering Group, what changes in the firm's approach have been key to enabling better integration of ESG factors?

TW: The two key changes the steering group facilitated were to the resource that Catherine has described, and equally important, to our overall mindset. We pushed to raise the profile of ESG internally and challenged all investment teams to grasp the opportunity to enhance client returns by being more thoughtful and explicit in our analysis of ESG factors. Integrating analysts into the investment teams has been a big part of this, as has the work of the ESG research groups. The Climate Team has been pivotal in highlighting the challenges and opportunities the climate transition will pose and raising the general level of understanding as to how this will start to impact the companies in which we invest.

Our core investment philosophy is a qualitative rather than quantitative one, and on ESG it is much the same. To enable this, as Catherine has pointed out, we've invested considerably in specialist analysts, systems development and identifying best-in-class data providers that can support investors and ESG specialists alike. We'd much rather understand the underlying issues and nuance than rely on overly simplistic third-party scoring systems or crude exclusion policies and this does require resource. The willingness of the firm to commit to such an investment has been crucial in helping to move us forward.

Looking to the future Catherine, how will integration continue to evolve?

CF: A key area of focus for the next 18 months will be to bed down our significantly expanded ESG function. Cultural integration within our investment teams is critical to success. As long-term shareholders, we have ambitions to do more meaningful engagement with the companies we hold.

We also want to continue to improve the efficiency of getting ESG data to our investment managers to help with the seamless integration of ESG and investment factors within their decision-making.

And we want to expand the sources of external insight we use on ESG, as we have done within our investment research. We will continue to develop our approach to climate, as best practice on how we interpret the science on this topic continues to move at pace.

Finally, we want to improve our reporting on all these topics to our clients. As ever, though, we will continue to take a long-term view regarding the companies in which we invest. And we will maintain focus on important issues that are likely to present a major long-term opportunity for our clients.

And finally, Tom, how do we continue to improve our efforts as a strategy and a firm?

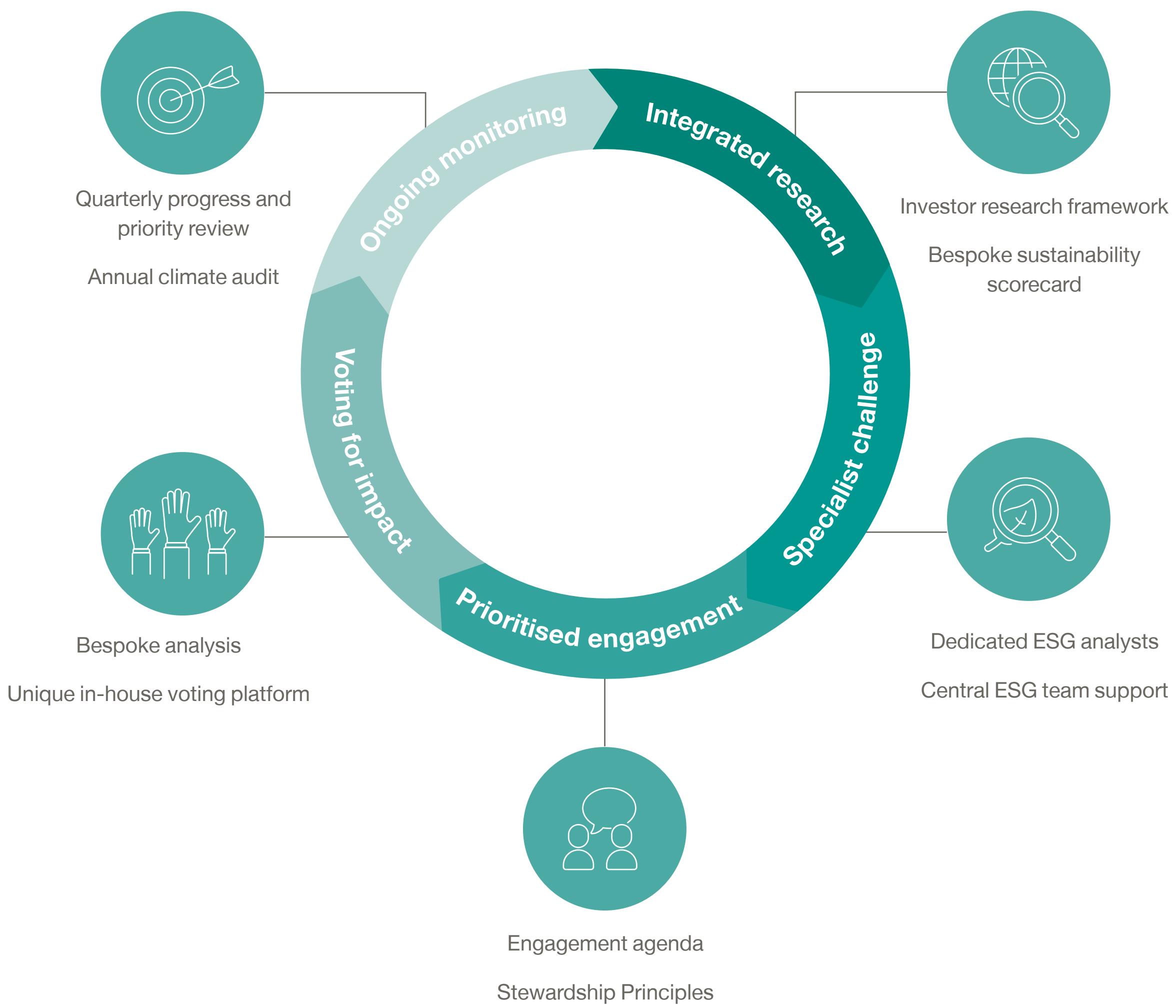
TW: As with all aspects of our investment approach, the most important thing is to keep challenging ourselves and not rest on our laurels. The more we focus explicitly on ESG and sustainability, the greater our understanding of the issues at play will become. That will result in higher quality conversations with company management and allow us to be more proactive in our engagement work. The ambition is not to become 'activists' but to play our part as supportive long-term shareholders in helping companies to maximise their potential.

We've already established world-leading capability in governance and have made huge progress in recent times on climate. But there is also still much more we can do to understand other aspects of environmental and social impact. In some cases, the immediate impact on investment returns is more obvious than in others, but recent history has shown that societal and regulatory expectations of the corporate sector are changing. Investors and companies need to be ahead of this.

We'll keep investing in IT systems and best-in-class third-party data providers that enhance our analysis. More importantly, we'll broaden and deepen our range of information inputs. We'll develop in-house expertise through our graduate training programme and dedicated ESG research groups, and we will expand our network of industry experts and academics. This will ensure that we have a well-rounded perspective that draws on the best and brightest minds in the world.

International Alpha's approach to ESG integration and stewardship

Our investment style and long-term time investment horizon of 5-10 years means we are driven to understand what environmental, social and governance issues may be material to the investment thesis on each stock we own on your behalf. The diagram below summarises how we go about integrating ESG and stewardship within our investment process.



While the pillars of this process have been consistent for many years, as with every aspect of our investment approach, we are continually looking to improve and build upon our strengths. In recent years, such enhancements have come against a backdrop of heightened focus on the integration of ESG factors within our industry. In many ways we welcome rapid developments among policy makers. However, as third-party data providers increasingly place the onus on companies and investment managers to monitor, assess and report on non-financial factors, the result has been a noticeable increase in the data and information that companies are producing, without much regard for the quality or usefulness of that data. For us, the data is only one element within a thoughtful and holistic process.

Integrated research

For ESG factors to be fully considered in the investment research process, responsibility for assessing non-financial factors must start and end with the investment manager. As such, the consideration of financial alongside non-financial factors sits at the heart of every research report that is written.

In our last report you will have seen reference to consideration of stewardship in the investment research framework. We now go one step further and separate out governance and sustainability. In the former we focus on how ownership, management and governance structures support or weaken the investment case. In the latter, we focus on how sustainability factors might impact the investment case, whether as a result of how a company operates or the impact of the products or services it provides. We believe exploring both aspects is vital to understanding whether a growth opportunity will endure and prove to be financially rewarding over the long term.

Our investment research framework

Growth	Competitive advantage	Governance
How much can this company grow over the next 5–10 years?	**What is the edge and will it endure?**	**Will management realise this opportunity?**
Scale of opportunity? Industry backdrop? Growth shade?	Core competence? Customer attraction? Difficulty to copy?	Incentives and alignment? Capital allocation? Checks and balances?

Sustainability	Financials	Valuation
How do sustainability factors impact the investment case?	**What is the cost of, and return on, realising the opportunity?**	**Is it attractively valued?**
Climate impact/strategy? Stakeholder treatment? Societal impact?	Attractive returns? Improving/sustainable? Capital requirements?	Why mispriced? Skew of outcomes? Upside potential?

Specialist challenge

Our investors have benefitted from a dedicated senior ESG analyst since 2017. However, December 2021 marked the integration of the analysts to sitting within the International Alpha investment team alongside the investors. The role of the ESG analysts in supporting the investors remains unchanged. They attend stock discussions, input views on stock research ahead of the discussion, support the investors on stewardship activities and liaise with investors and the central ESG function on material AGM votes.

Prioritised engagement

We view stewardship through engagement as an important part of being able to go beyond merely renting shares to being active owners on your behalf. We see the opportunity in being able to add value on our clients' behalf by improving or avoiding poor business practices. We continue to prioritise proactive engagement, considering each company individually, the materiality of the issue at hand and potential for us to influence change where needed. The research and engagement agenda on page 13 lays out three issues we have identified for the coming year.

Voting for impact

No part of our decision-making or voting execution is outsourced. Every AGM for each holding is analysed by a member of our central ESG services team. That member liaises with the investment managers and dedicated ESG analysts on decisions where voting action is recommended. Every vote is processed via a bespoke in-house voting platform that integrates into our investment systems.

Ongoing monitoring

2021 saw the creation of an ESG data team within the Central ESG function to support the investment teams with data provision and analysis for the ongoing monitoring of ESG factors within portfolios. We use third-party data providers to support our efforts within International Alpha to monitor the portfolio for material business practice or governance issues, with the outcomes presented quarterly to the Portfolio Construction Group (PCG) alongside an update on our proactive ESG engagements and material voting outcomes. As we explain in more detail in this report, we have also enhanced our approach to monitoring the progress the companies in our portfolio are making on climate commitments and carbon reduction. This climate audit will be completed annually and reported to the PCG.

Research and engagement priorities

You will see the three priorities for the coming year highlighted in the graphic below. We thought it was also worth updating you on our priorities from our previous report, and what we learned. As a reminder, in our last stewardship report we highlighted the following priorities for engagement: approach to carbon reduction, sourcing and supply chain, and data security and governance.

On climate change, as outlined in some of our engagement examples in this report, we encouraged businesses to begin reporting climate data and reduction targets for the first time to shareholders, and we are pleased to say several companies have now begun doing this. Climate change will continue to be a focus for us with those companies for which we deem it material to the long-term investment thesis. One example of this would be the Irish building materials manufacturer, CRH, whose story is outlined later in this report.

Through engagement, we have developed a better understanding of best practice when approaching supply chain standards for traceability and labour. Sustainability concerns have influenced our decisions on a number of holdings, both with a view to selling out of existing holdings and avoiding taking new holdings where concerns were identified.

Ensuring companies and their boards instil a corporate culture that balances data security and privacy with commercial opportunity has been a key learning and focus of our engagement in the last year. This has taught us that appropriate technical skills to face this challenge, at board level, will be of paramount importance for all portfolio holdings.

Over the coming year we look forward to advancing our understanding of, and challenging company management on, the three areas below.

Climate ambition

We will prioritise engagement with companies according to their climate impact and ambition. We will look to assess their ability and willingness to adapt to the challenges of the climate transition and emphasise our belief that success in this regard will be increasingly important for commercial and financial success.

Board diversity

We will identify and engage with those boards who we feel could benefit from improved diversity. This diversity can take many different forms: gender, skill set, cognitive approach and industry expertise to name a few. We will also work to identify best practice with regards to diversity at board level, and what the tangible benefits of that diversity are.

Tax practices

Recent OECD-led efforts to coordinate taxation policies across the globe highlight the increasing regulatory focus on corporate tax practices. We will review taxation approaches across holdings within the portfolio to identify best practice, define what that looks like, and prioritise engagement with those whose practices puts them at risk of regulatory scrutiny or change, jeopardising the investment opportunity for our clients.

Our Stewardship Principles

Baillie Gifford's overarching ethos is that we are 'Actual' investors. We have a responsibility to behave as supportive and constructively engaged long-term investors. We invest in companies at different stages in their evolution, across vastly different industries and geographies and we celebrate their uniqueness. Consequently, we are wary of prescriptive policies and rules, believing that these often run counter to thoughtful and beneficial corporate stewardship. Our approach favours a small number of simple principles which help shape our interactions with companies.

Prioritisation of long-term value creation

We encourage our holdings to be ambitious and focus their investments on long-term value creation. We understand that it is easy to be influenced by short-sighted demands for profit maximisation but believe these often lead to sub-optimal long-term outcomes. We regard it as our responsibility to steer holdings away from destructive financial engineering towards activities that create genuine economic and stakeholder value over the long run. We are happy that our value will often be in supporting management when others don't.

A constructive and purposeful board

We believe that boards play a key role in supporting corporate success and representing the interests of all capital providers. There is no fixed formula, but it is our expectation that boards have the resources, information, cognitive and experiential diversity they need to fulfil these responsibilities. We believe that good governance works best when there are diverse skillsets and perspectives, paired with an inclusive culture and strong independent representation able to assist, advise and constructively challenge the thinking of management.

Long-term focused remuneration with stretching targets

We look for remuneration policies that are simple, transparent and reward superior strategic and operational endeavour. We believe incentive schemes can be important in driving behaviour, and we encourage policies which create genuine long-term alignment with external capital providers. We are accepting of significant payouts to executives if these are commensurate with outstanding long-run value creation, but plans should not reward mediocre outcomes. We think that performance hurdles should be skewed towards long-term results and that remuneration plans should be subject to shareholder approval.

Fair treatment of stakeholders

We believe it is in the long-term interests of all enterprises to maintain strong relationships with all stakeholders – employees, customers, suppliers, regulators and the communities they exist within. We do not believe in one-size-fits-all policies and recognise that operating policies, governance and ownership structures may need to vary according to circumstance. Nonetheless, we believe the principles of fairness, transparency and respect should be prioritised at all times.

Sustainable business practices

We believe an entity's long-term success is dependent on maintaining its social licence to operate and look for holdings to work within the spirit and not just the letter of the laws and regulations that govern them. We expect all holdings to consider how their actions impact society, both directly and indirectly, and encourage the development of thoughtful environmental practices and 'net-zero' aligned climate strategies as a matter of priority. Climate change, environmental impact, social inclusion, tax and fair treatment of employees should be addressed at board level, with appropriately stretching policies and targets focused on the relevant material dimensions. Boards and senior management should understand, regularly review and disclose information relevant to such targets publicly, alongside plans for ongoing improvement.

Engagement highlights

A selection of the company engagements that took place during 2021/2022 for holdings across the International Alpha strategy.[1]

Ryanair (Airline)

Encouraging Ryanair to be proactive towards environmental issues has been a long-standing engagement point with the board and management. We have seen real progress over the last 18 months as the company now:

– has a sustainability team of three people

– is submitting its carbon data to the Carbon Disclosure Project

– is being proactive towards the need to adopt Sustainable Aviation Fuel (SAF) with 2030 targets announced

– is funding a research programme on SAF with Trinity College Dublin

Copa (Airline)

In 2021 we encouraged the CEO and CFO to publicly disclose Copa's carbon emissions. Soon after our engagement, the company notified us that it was disclosing its emissions for the first time and was submitting them to the Carbon Disclosure Project for third-party verification. The company also set the aim of disclosing carbon reduction targets. The willingness to receive and respond to our lead on this important issue was evident and hopefully has wider benefit to other stakeholders.

Amadeus (Technology)

We opposed executive remuneration at the 2021 AGM and provided feedback to the board on how Amadeus could improve its reporting and approach to executive remuneration. We were joined in our opposition by 61 per cent of shareholders. We also suggested improvements around better disclosure to shareholders as we were uncomfortable with the adjustments made in response to the impact of Covid-19. The latest remuneration report (2022) has incorporated our feedback and provides shareholders with enhanced disclosures and guarantees around future use of discretion.

[1]Note: not all companies are held in all client portfolios.

Atlas Copco (Industrial)

In 2021, we commissioned Mike Berners-Lee, a leading academic and consultant on climate change, to analyse Atlas from a climate perspective. The report described how Atlas Copco was early in raising climate issues in its reporting but had since lagged behind best practice in terms of concrete commitments to decarbonise. We arranged for Mike to join us in discussing his findings with Atlas and found the conversation constructive. Subsequently, the company released ambitious targets to reduce absolute emissions across its value chain aligned with a 1.5 degree future.

Prosus (Technology)

Sustainability is a strategic priority for Prosus and they asked us to engage with 300 employees directly. We shared guidance on how we view ESG issues and what the company should focus on. Prioritising long-term value creation, preserving what is unique about its culture and ignoring short-term pressures (including generic ESG standards) were key areas we promoted for a more sustainable business.

Denso (Autoparts)

Denso aims to deliver carbon-neutral manufacturing by 2035, which we commended, but they are yet to state clear targets for their downstream footprint (zero-emissions sales). We have made clear our desire for them to be more ambitious regarding climate aspirations and sought more detail regarding their use of carbon offsets.

Japan

Wizz Air (Airline)

Prior to taking a holding in Wizz Air, we had concerns regarding the company's approach to environmental and social issues. Following direct engagement with management, we felt reassured by their plans to be proactive towards carbon disclosure, to engage with external parties on longer-term solutions to reduce carbon tax, and to continually review their internal processes to look after employees. We decided to take a holding and engagement on these topics with management have continued.

China

Alibaba (Technology)

We have been encouraging Alibaba to improve its ESG reporting, and following our engagement, the company have committed to improving greatly in 2022. We commended the ambition in Alibaba's recently published carbon neutrality action plan, which seeks scope 1 and 2 emissions neutrality by 2030, and we agreed with the company that they could do more to improve ESG reporting beyond this one example related to climate. We have also shared examples of good sustainability reporting practices with the company against which we will access better reporting in the future.

Rio Tinto (Mining)

Following the destruction of Juukan Gorge in May 2020, we had an extensive engagement programme with the board of Rio Tinto. Engagement has focused on the company's response to the disaster, understanding its root cause and encouraging improvements to Rio's ESG practices. We recommended replacing the chair and implementing enhanced governance practices to improve communication from the mine site to the board room. We also emphasised our support for rebuilding relationships with the local community.

Australia

Case study: CRH

CRH is the largest building materials business in both North America and Europe and has leading regional positions in Asia. We have owned shares of CRH on behalf of clients since June 2009.

Cement production is a leading contributor to climate change. Scientists suggest it's responsible for as much as 8 per cent of human-created CO_2 emissions, more than aviation or shipping. The reality is that CRH earns most of its money elsewhere, with only 16 per cent of its sales coming from cement. Nonetheless, the material accounts for 82 per cent of the Irish firm's direct greenhouse gas emissions, what are known in the industry as scope 1 emissions, making CRH one of the most climate-impactful companies in the world.

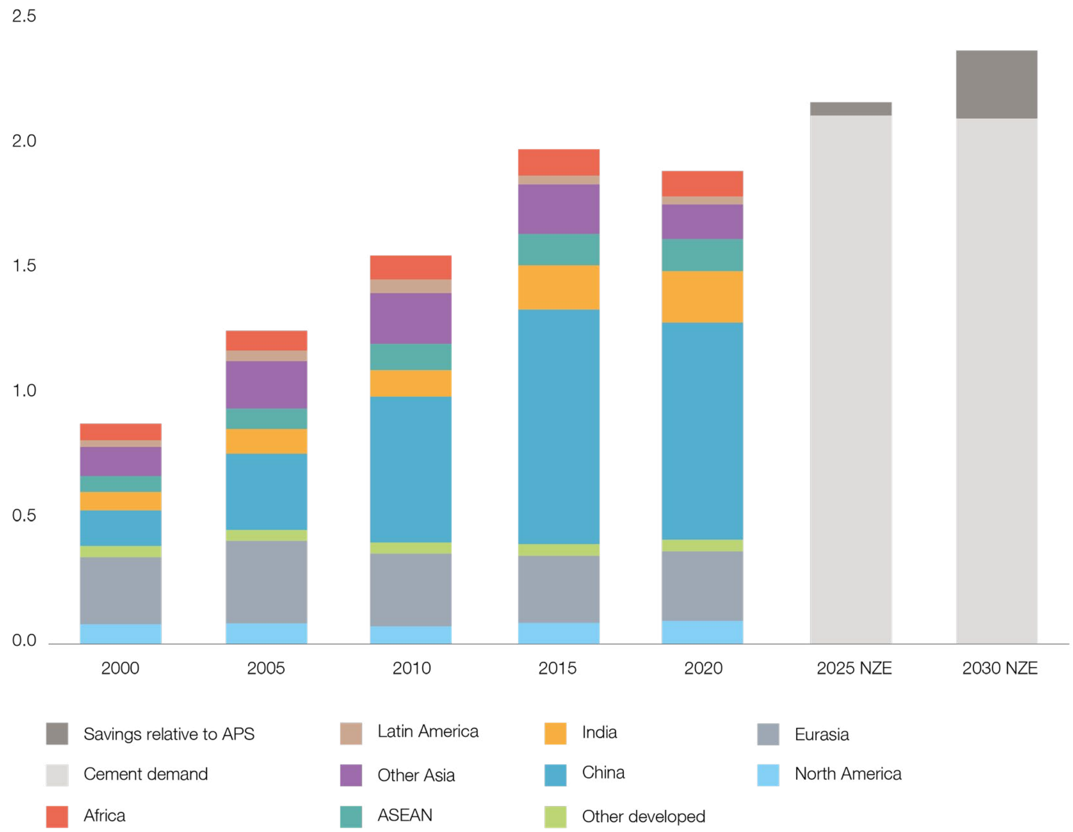
CRH, and the world, face rising carbon taxes. Putting aside the important environmental concerns, the firm could potentially end up making a loss on every bag of cement sold if it does not tackle this issue head-on.

It is easy to understand why the path of least resistance is for CRH to sell this business. We find ourselves in agreement with the company that whilst selling is the easy option, there is a better, more beneficial option to consider.

Cement's critical role

In conversations with CRH's leadership team it becomes clear why they think a sale would be a mistake. They are convinced cement will continue to be a systemically important material: it acts as a binding agent in concrete, the construction industry's building material of choice, and a product that is vital to building out infrastructure necessary for the continued economic development of many countries around the world. Global demand is expected to keep rising, presenting an opportunity for them to grow both organically and through acquisition.

Global cement demand for building construction, 2000–2020, and in the Net Zero Scenario (NZE), 2025–2030



Source: IEA, Global cement demand for building construction, 2000-2020, and in the Net Zero Scenario, 2025-2030, IEA, Paris[1]

With the world still in need of cement, the focus needs to be on how to decarbonise the manufacturing process rather than forcing a company willing to do so to sell out at a knock down price. Indeed, the company themselves have challenged investors to ask themselves what would happen to its cement business if it were to fall into the hands of a private buyer. The insinuation is that a short-term focused owner might slash investment, turn a blind eye to CO_2 and extract as much value as possible until regulations forced them to shut the business. It is hard to see how this would benefit anyone but the irresponsible owner.

We support CRH's ambitions to become a low-carbon leader. But our role as one of its largest investors goes beyond cheerleading its efforts. When engaging with the CEO, other executives and the board, we've pressed them on how well the company's emissions-cutting efforts truly compare to their competitors. And critically whether they are being ambitious enough.

[1]https://www.iea.org/data-and-statistics/charts/global-cement-demand-for-building-construction-2000-2020-and-in-the-net-zero-scenario-2025-2030

Engaging for improvement

Since the start of 2021, Baillie Gifford's investors and our Senior ESG Analyst, Tara-Jane Fraser have had more than half a dozen meetings with CRH beyond its scheduled investor events.

At these meetings we have:

1. Confirmed ambition to lead the transition to lower carbon cement

We felt the company were beginning to fall behind peers in their decarbonising ambition and we wanted to see this change, particularly around carbon reduction targets. Following our engagement, the management team incorporated our feedback with updated targets, pledging a group wide 25 per cent cut in CO_2 emissions between 2020 and 2030. This includes bringing forward a specific emissions-reducing target for its cement plants by five years to 2025.

Helpfully, decarbonising also has financial benefits. Consumers are potentially willing to pay a premium for a greener product resulting in higher margins. Should CRH achieve their goals they will still emit some carbon, but decarbonising will go a long way to offsetting this potential future cost. By way of demonstrating their ambitions in this regard, the company has recently tied 5 per cent of its executives' long-term incentive plan payments to delivering on its carbon goals.

2. Encouraged innovation

CRH's net zero roadmap outlines the different options the company has available to decarbonise:

- making more use of alternative materials to reduce the quantity and intensity of clinker, the limestone-based ingredient responsible for most of cement's emissions
- replacing fossil fuels with greener alternatives
- investing in renewable energy

While positive, these options are the same as other cement companies. HeidelbergCement announced another carbon capture venture last year and Holcim Group (previously LafargeHolcim) seems to be making progress on low-carbon cement.

Therefore we were encouraged to learn that CRH have announced a $250m innovation venture fund to support the development of new technologies and products. They explained that the fund's size was less important than the message it sends about their intentions.

Alternative solutions arising from this innovation fund include a carbon capture trial at a Canadian plant that uses cement kiln dust to trap CO_2. Another involves a trial to substitute a type of clay for clinker in the US. We will monitor these trials as they progress to ensure we retain conviction that CRH are staying ahead of their competition.

3. Requested further disclosure

We welcomed improved disclosure around lobbying in relation to climate change and are beginning to engage on further integrating the cost of climate change within their financial accounts.

Thus far, the firm has not broken down its emissions for all product lines or shared their specific targets. Understanding that different companies report carbon in different ways and over different timelines, management suggested investors should be wary of like-for-like comparisons. While true, we believe it is still helpful to hold CRH to account by referring to its peers' progress.

the scale of the market for low-carbon cement is likely to be huge

Challenge and support

CRH has the potential to become a decarbonisation leader in an industry that enables the construction of a better future. We view it as our role to support the company in its ambition, but we do not shy away from asking the challenging questions. This is the value of an investor with an aligned interest that goes beyond box-ticking.

Companies prosper when they disrupt an industry with a product for which there is pent-up demand. And the scale of the market for low-carbon cement is likely to be huge because it could play such a critical role in delivering a net zero world.

In closing, there are two further developments we would highlight to clients and on which we will update in future stewardship reports. The first is that Baillie Gifford has joined the collaborative engagement Climate Action 100 group on CRH. This group consists of a small number of existing shareholders working together to push for greater ambition on achieving carbon reduction targets and on better disclosure. We joined this group to support our independent engagement efforts with the company. Secondly, the problem of carbon emissions will be solved by companies not directly involved in 'dirty' industries, but who are able to apply technology to help CRH and its peers. One such company is Aker Carbon Capture, and on the following page you can see a brief illustration of the journey we have been on to become the largest external shareholder in this important industry leader.

Case study: Aker Carbon Capture

Carbon capture is a process for reducing carbon emissions. It involves the capture of carbon dioxide (CO_2) from industrial processes, such as steel and cement production, or from the burning of fossil fuels in power generation, before those emissions enter the atmosphere. Aker Carbon Capture (ACC) technology uses a mixture of water and organic amine solvents to absorb the CO_2. This technology can lower the emissions of industrial plants by >90 per cent. This is an exciting investment opportunity as the cost of carbon capture has fallen, the cost of emitting carbon is rising, and the pressure on corporates to have credible net zero strategies is increasing.

As the following diagram illustrates, while a recent investment for Baillie Gifford clients, ACC is a company we have been following for more than a decade. They currently have a 3–4 per cent market share in a $1bn market, but the market is forecast to grow to $25bn by 2030[5] and ACC hopes to gain a low double-digit share of that market growth.

2005

With roots stretching back to 1996, Aker Carbon Capture (ACC) began development of its Clean Catch technology in 2005.

2008

Angus Franklin (PCG member) researches Aker Solutions (parent company of ACC) and its development of a leading carbon capture technology 'Just Catch' (renamed from Clean Catch).

Toby Ross notes long-term investment potential in carbon capture projects. Monitoring Aker's carbon capture business identified as being able to better help us understand this.

2009

ACC technology first offered commercially.

2020

Aker Solutions spins off ACC, allowing direct access to carbon capture technology.

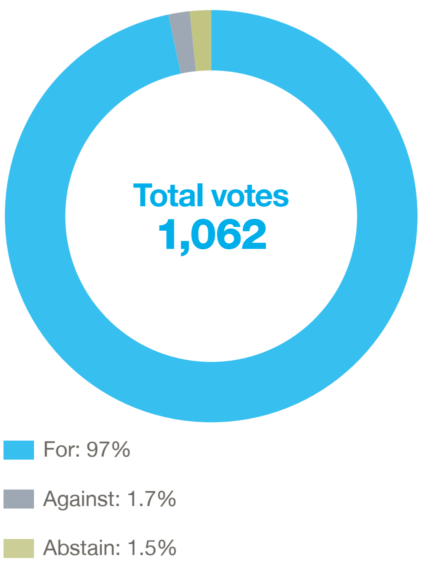
2021

Jenny Davis writes ACC buy note, highlighting carbon capture has been a long-awaited solution to a known problem, but without the business model to make it happen. Baillie Gifford takes initial position on behalf of clients. Baillie Gifford becomes largest external ACC shareholder.

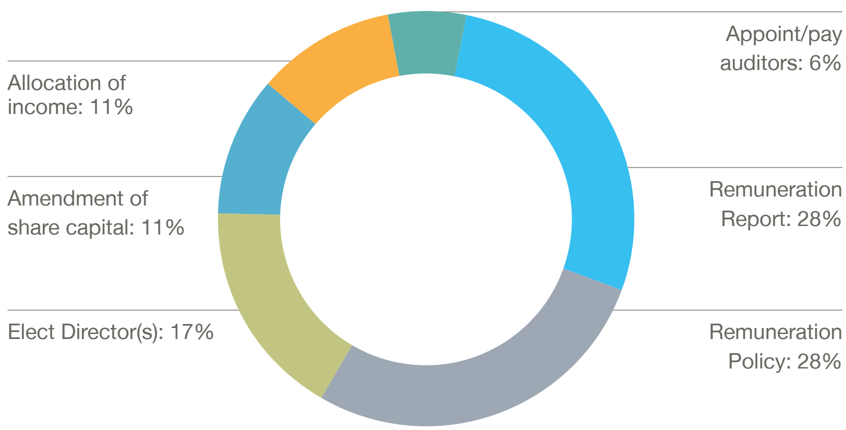
Proxy voting

Engaging with a company's board and management is a key component of our stewardship and engagement activities. Exercising the voting rights linked to our clients' holdings is a valuable way for us to communicate support, provide constructive feedback and act on our stewardship principles. We do not outsource any of our decision-making or processing, and conduct our proxy voting through our bespoke, in-house platform. We have a dedicated ESG Services Team who coordinate voting between our investment managers and embedded ESG analysts to ensure all decisions are investment-led and consider our long-term relationships with companies.

Total resolutions voted



Where do we most often challenge?



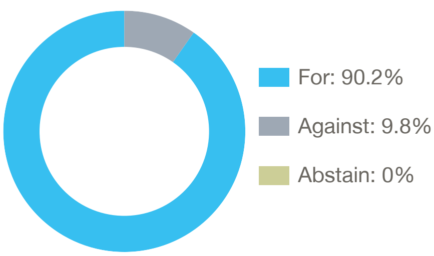
Numbers may not sum due to rounding.

*In total there were 1,092 proposals, however due to a practice called 'blocking', where some markets restrict the sale of shares in the period between votes being cast and the AGM, we did not vote 30 ballots in one company's AGM.

Our investment research process ensures we invest in companies with aligned management teams and robust governance structures. These structures translate into the results above, where we support a majority of the resolutions put forward by management. This voting action also reflects an active and ongoing dialogue where we have engaged on proposals prior to them being put to vote. For instance, in light of the Juukan Gorge disaster, we had several meetings with Rio Tinto as we felt there had been a failure in board oversight. We initially intended to oppose the re-election of Chair Simon Thompson at the 2021 AGM. However through direct engagement we learned more about the internal review process, that the Chair intended to step down at the 2022 AGM, and the timeline for seeking a suitable replacement. Given this commitment to succession and a clear timeline for progress, we decided a vote 'for' the Chair was the most pragmatic response, as it allowed for a managed transition and helped maintain constructive dialogue. Accordingly, we were pleased to see the appointment of a new Chair who we believe he has the skills and expertise to be a good steward for the business.

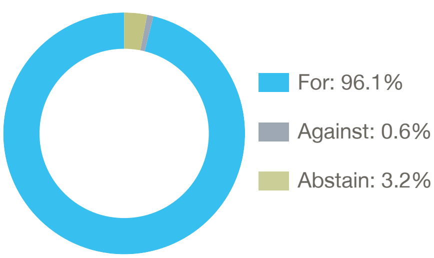
On the rare occasions where we feel the engagement process has not produced the desired result, or we are unhappy with decisions taken by management, we vote ‘against’ or ‘abstain’. Executive remuneration was where we challenged management most, making up 56 per cent of our voting opposition. The underlying issues included insufficiently stretching targets and overly generous pay packages. One of the biggest changes we have seen in remuneration over the past year is the inclusion of ESG metrics and goals into management’s pay. We view this as a positive evolution, increasing alignment with stakeholders. We will continue to evaluate how meaningful and stretching these metrics are on a case-by-case basis.

Management resolutions: Case studies of voting activity



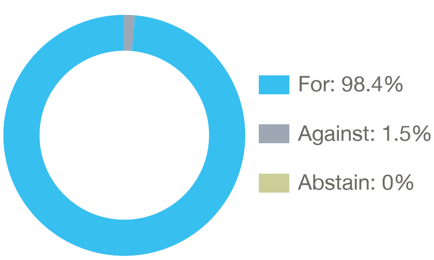
Case study – Edenred

We took voting action on proposals regarding remuneration as we had concerns about the disclosure of retrospective amendments made during 2020 and felt the shareholder consultation process should be improved. We wrote to CEO and Chairman, Mr Dumazy, after we submitted our ‘oppose’ vote to outline our rationale, which prompted him to request further engagement with us. We found the call useful as it provided us with the opportunity to suggest improvements to disclosure and the shareholder consultation process, which Mr Dumazy committed to follow up on.



Case study – Deutsche Börse

We opposed the election of the Chair of the risk committee. After being put forward for re-election, this board member had to stand down from a similar position at Credit Suisse due to ongoing investigations regarding their risk practices. While no evidence of wrongdoing had yet emerged, the ongoing investigations led to us feel his re-election to the same position at Deutsche Börse was inappropriate.



Case study – Shimano

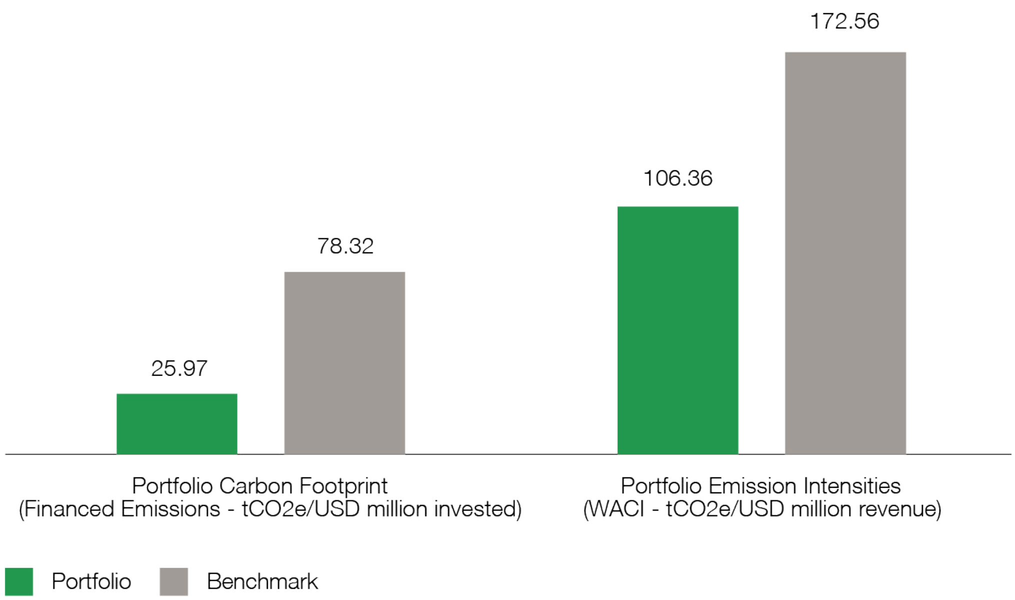
We opposed the low dividend payout as we believe the company’s capital allocation policy is not in the interests of shareholders. Having previously supported this policy, continued growth in the company’s cash pile led us to believe the company could manage their balance sheet more proactively and return more capital to shareholders.

Carbon footprint

We began publishing a carbon footprint analysis of the portfolio four years ago. Since then our understanding and ability to monitor overall emissions at a company level has continued to improve.

The graph below shows two metrics for measuring carbon intensity. The first metric measures carbon emissions relative to company enterprise value, and the second to company revenues (each is weighted according to the size of holding within the portfolio). The metric relative to enterprise value also represents the indicative amount of carbon emissions per annum for each $1m invested in the portfolio (commonly referred to as a 'portfolio carbon footprint' or financed emissions per unit of capital invested).

Until all companies in our investment universe report suitably, we must acknowledge a data gap. For now, based on those companies that do report, both relative measures highlight that your portfolio has a materially lower carbon impact when compared with the MSCI ACWI ex US index, as has been the case each time we have published such measurements.



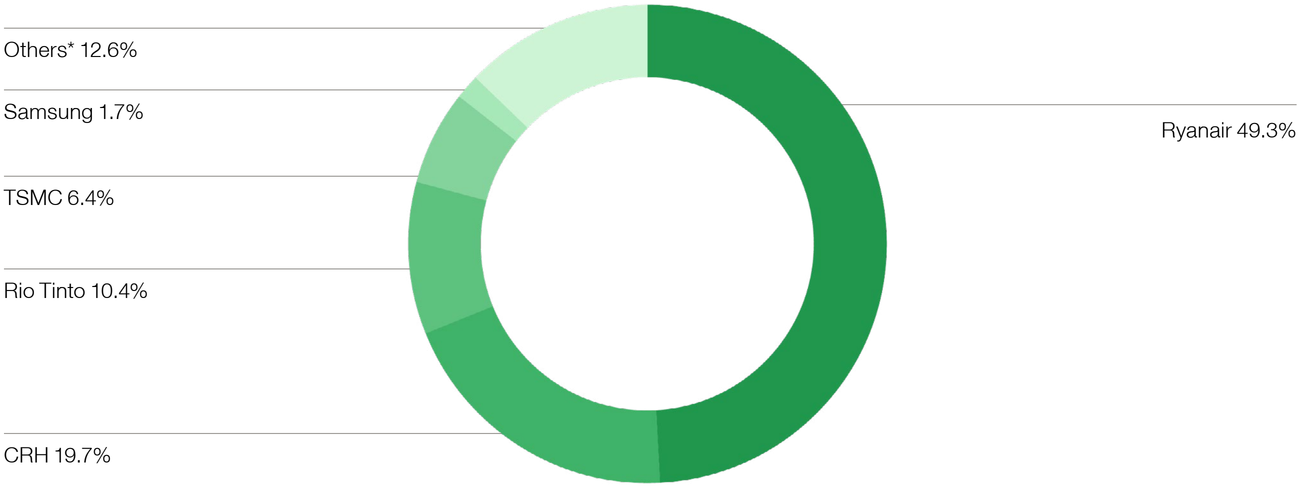
Source: Baillie Gifford & Co and underlying index provider. Based on a representative portfolio[2] as at 31 March 2022.

All metrics refer to scope 1 and 2 emissions only. Scope 1 emissions are those deriving directly from company activities (i.e. stack emissions and fuel use); scope 2 emissions arise indirectly as a result of electricity use. Emissions within these scopes are reasonably under the control of the company and can be expected to be calculated by all companies. We are continuing to engage with companies and research providers on the availability, comparability, and robustness of scope 3 emissions – those that result from activities of assets not owned or controlled by the reporting organisation, but that the organisation indirectly impacts in its value chain. We must acknowledge that for now, portfolio data remains incomplete. To reference how important better data is, it is estimated scope 3 emissions could be 5.5 times greater than total scope 1 and 2 emissions.

[2]Please note that the following stocks are not covered in the supplier's database so do not form part of the carbon analysis: BioNTech SE Sponsored ADR, Copa Holdings, S.A. Class A, Epiroc AB Class A, Hangzhou Tigermed Consulting Co., Ltd. Class A, Oxford Nanopore Technologies PLC, Ping An Insurance (Group) Company of China, Ltd. Class A, Spotify Technology SA, Topicus.com, Inc., Wizz Air Holdings Plc, Zai Lab Ltd.

The pie chart below shows the largest contributors to portfolio emissions. We have used this data to help prioritise engagements outlined in this report.

Top percentage contributors to the portfolio's weighted average carbon intensity



*Approximate data of 54 portfolio holdings.
Percentages may not sum due to rounding.

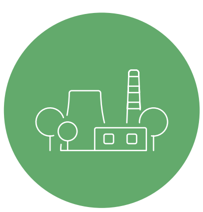
Source: Baillie Gifford & Co. As at 31 March 2022. Based on a representative portfolio.[3]

While analysing the carbon footprint of the portfolio has supported our understanding of both company and portfolio emissions, as we have highlighted previously, measuring the footprint is far from an exact science with at least two key shortcomings.

First, the carbon footprint is backward looking and takes no account of the nature of a company's activities and their necessity. Therefore, the output does not give a sense of how a company plans to approach climate change in the future and whether that presents a risk or an opportunity for the company and thus the portfolio.

Second, the scope is limited to emissions, and even then only a subset of total emissions as scope 3 are excluded. The methodology for calculating emissions is still evolving and being standardised across sectors. Therefore, in some instances, increasing emissions represents a positive change due to improved methodologies, improved reporting or indeed first-time reporting by some companies. This has the potential to lead to erroneous data signals which will require oversight on our part and shows the danger of relying on just one metric to measure and monitor company risk and opportunity.

These shortcomings led us to develop a more thoughtful framework of climate analysis which we have called the climate audit.



Scope 1

Direct emissions from operations

Scope 2

Indirect emissions from purchased energy

Scope 3

All other emissions associated with a company's activities

[3]Please note that the following stocks are not covered in the supplier's database so do not form part of the carbon analysis: BioNTech SE Sponsored ADR, Copa Holdings, S.A. Class A, Epiroc AB Class A, Hangzhou Tigermed Consulting Co., Ltd. Class A, Oxford Nanopore Technologies PLC, Ping An Insurance (Group) Company of China, Ltd. Class A, Spotify Technology SA, Topicus.com, Inc., Wizz Air Holdings Plc, Zai Lab Ltd.

Climate audit

We believe the climate audit has supported our aim for meaningful research and stewardship by:

1. providing a more granular understanding of the portfolio's carbon emissions

2. structuring an assessment of how ambitious holdings are being regarding future emissions reduction targets

3. developing a method to prioritise our engagement with companies

We completed our first climate audit in 2021 and used a range of qualitative and quantitative measures to look both backwards and forwards. This included:

- total emissions (actual or estimated)
- whether all scope 1, 2 and 3 emissions are disclosed
- whether the company reports to the Carbon Disclosure Project (CDP)[4] and their score
- whether any current and future carbon targets have been set
- the temperature alignment of the carbon targets (e.g. 1.5°C)
- whether targets have been approved by the Science Based Targets initiative[5]
- whether any net zero commitments have been made by the company

This holistic analysis enabled us to look beyond the easily available data and consider more broadly the role that each holding is playing in the climate crisis and the ambition with which it is taking on the challenges and opportunities that the climate transition will present. With this in mind, we developed the following framework to help summarise the climate ambition of holdings in the portfolio.

Emerald	Green	Amber	Red	Black
Pre-2050 aligned for scope 1 and 2 and material scope 3	Pre-2050 aligned for scope 1 and 2 and at least 2050 for material scope 3	2050 aligned on scope 1, 2 and material scope 3	Intimation to set targets or have set targets that are insufficiently stretching i.e., not 1.5 degree aligned	No carbon data reporting

[4]CDP is a not-for-profit charity that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts.

[5]Targets are considered 'science-based' if they are in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement – limiting global warming to well-below 2°C above pre-industrial levels and pursuing efforts to limit warming to 1.5°C

The key takeaways of our initial climate audit were:

Emissions disclosure

63%	42%	15 companies	15 holdings	50%
63 per cent of the portfolio report their scope 1 and scope 2 emissions	only 42 per cent report their scope 3 emissions	15 companies are not disclosing any carbon data	15 holdings represent 90 per cent of total emissions	50 per cent of the holdings are already reporting to the CDP

The key benefit of this enhanced climate analysis is that it enables us to take a more thoughtful approach to our stewardship engagements on climate. With a broader picture of a company's footprint, disclosure and ambition, we can identify and engage with companies where lack of disclosure or climate ambition is deemed material (e.g. given the size of their emissions). As we continue to refine our approach and engage with companies to improve their disclosures and raise their climate ambitions, we look forward to sharing our progress with you.

How will we continue to evolve?

We plan to enhance our reporting of the specific risks and opportunities that climate change presents to the portfolio in the coming years. We feel that the Taskforce on Climate-related Financial Disclosures (TCFD) framework is helpful for this, allowing us to bring together our existing stock-level analysis and carbon footprint metrics with additional portfolio-level insights. As part of this, we will look to analyse the portfolio over different future climate scenarios and timescales to provide a view of the likely implications for the portfolio under these different versions of the future. Baillie Gifford is working with a number of external specialists to explore in detail the physical and transitional modelling that sits behind such analysis as we begin to incorporate it into our reporting. We look forward to sharing the outputs of our work with you as it evolves.

Portfolio metrics

We do not believe that a crude numerical approach to governance is the best way to assess the companies we invest in on our clients' behalf. Nonetheless, we recognise that certain metrics can provide a helpful overview when trying to assess overall progress across the portfolio on matters such as diversity and board independence. The following statistics provide a crude snapshot of the portfolio at 31 March 2021 and 31 March 2022:

	2020	2021	2022
Proportion of independent directors on company boards (%)	67	67	71
Female representation on company boards (%)	23	24	26
Board tenure (years)	9	9	9
CEO tenure (years)	n/a*	8	10
Holdings with female CEOs (%)	4	5	7

Source: Baillie Gifford & Co, MSCI. Based on a representative portfolio. Average across holdings.

*CEO tenure data only measured from 2021.

Appendices – voting rationale

Votes cast against

Company	Voting rationale
Amadeus IT Group SA	We opposed the election of the chairman of the remuneration and governance committee due to concerns with the changes made in relation to the executive's remuneration targets in 2020. We also had concerns with the composition of the committee due to the long tenures, and potential lack of independence, of three of its members.
	We opposed the backward-looking Remuneration Report due to concerns with the increases made to the CEO's pay package by the Remuneration and Governance Committee during the year under review.
Danone	We opposed a resolution to allocate our votes among all members of the slate, including any additional unknown candidates. By opposing, we are ensuring that our votes are only counted towards the candidates named ahead of the meeting.
	We opposed two resolutions relating to remuneration because we do not believe the performance conditions are ambitious enough.
	We opposed two resolutions which sought authority to issue equity because the potential dilution levels are not in the interests of shareholders.
	We opposed two resolutions relating to remuneration because we do not believe the performance conditions are ambitious enough.
Deutsche Börse	We opposed the election of the chair of the risk committee. After Mr Gottschling was put forward for re-election, he had to stand down from a similar position at another company due to ongoing investigations regarding their risk practices. While no evidence of wrongdoing has been found against Mr Gottschling specifically, the ongoing investigations at another company has led to us feeling unable to support his re-election to the same position at Deutsche Börse at this time.
Discovery Ltd	We opposed the forward-looking Remuneration Policy due to concerns with the backward-looking performance period. We prefer executive pay plans to be forward-looking and long-term.
Edenred	We opposed two resolutions to approve remuneration due to concerns regarding alignment between pay and performance.
	We opposed the scrip dividend (a dividend paid out in stock rather than cash) due to concerns regarding the discount to market price which we do not believe to be in shareholders' best interests.
	We opposed the election of the remuneration committee chair due to concerns regarding the forward-looking remuneration policy.
	We opposed the proposed forward looking remuneration policy as we did not feel the performance period or targets were ambitious enough.
	We opposed the remuneration report as were not supportive of the decision to change the previous year's pay targets without shareholder consultation.
Kingspan Group	We opposed the resolution to approve the Remuneration Report due to concerns about how generously Kingspan paid an executive given the circumstances of their departure.
Magnit PJSC	We opposed the auditor due to concerns with the level of non-audit fees.
Norilsk Nickel	We opposed the remuneration of directors due to concerns surrounding potential termination payments.
Rio Tinto	We opposed the low dividend payment as we believed the company's capital strategy was not in the interests of shareholders.
	We opposed the remuneration report as we did not agree with the decisions taken by the Remuneration Committee in the last year regarding executive severance payments and the authorisation of long-term incentive awards.
Shimano	We opposed the low dividend payment due to the strength of the company's balance sheet. We believed the company's capital strategy was not in the interests of shareholders at this dividend amount.

Votes withheld/abstained

Company	Voting rationale
Magnit PJSC	We abstained on the election of four directors. In this market directors are elected via cumulative voting, where voting shares can all be cast for one candidate or divided among two or more. We concentrated our votes on the CEO and independent directors.
Norilsk Nickel	We withheld support from seven non-independent directors and voted in favour of the election of six independent non-executive directors. Since the election of the directors was held by cumulative voting, we were able to concentrate our votes on the independent non-executive directors, increasing the likelihood that they would be elected to the board.
Toyota Tsusho Corp	We abstained on the low dividend payment due to the strength of the company's balance sheet. We believed the company's capital strategy was not in the interests of shareholders at this dividend amount.

Votes cast in favour of shareholder proposals

We did not vote on any shareholder proposals over this period.

Shareholder meetings where we voted in favour of routine proposals

Company
AIA Group, ASML, Adyen Nv, Alibaba Group Holding, Amadeus IT Group SA, Ambu, Atlas Copco A, Burberry, CRH, CSL, Chr Hansen Holding A/S, Cochlear, Constellation Software, DSV, Danone, Dassault Systèmes, Denso, Deutsche Börse, Discovery Ltd, Edenred, Epiroc A, Experian, FANUC, FinecoBank Banca Fineco S.p.A. Grifols SA, HDFC Corp, Hangzhou Tigermed Consulting, Hargreaves Lansdown, Heineken, Hong Kong Exchanges & Clearing, ICICI Lombard, IMCD Group NV, Inditex, Itau Unibanco SA-ADR, Japan Exchange Group, Just Eat Takeaway.com, Kingspan Group, Kone, Kuaishou Technology, Kuehne & Nagel, Magnit PJSC Spon GDR, Meituan, MercadoLibre, NAVER Corp, Nestle, Nidec, Nintendo, Norilsk Nickel ADR, Novozymes, Ping An Healthcare & Tech, Prosus N.V. , Prudential, Rational, Richemont, Rio Tinto, Ritchie Bros. Auctioneers, SAP, SEA Ltd ADR, SMC, Samsung Electronics, Scout24, Shimano, Shiseido, Sony, Spotify Technology SA, TSMC, Temenos, Tencent, Toyota Tsusho Corp, Umicore, Wizz Air Holdings Plc, WuXi Biologics Cayman Inc, Zai Lab HK Line

Full details of Baillie Gifford's voting is available at bailliegifford.com.

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