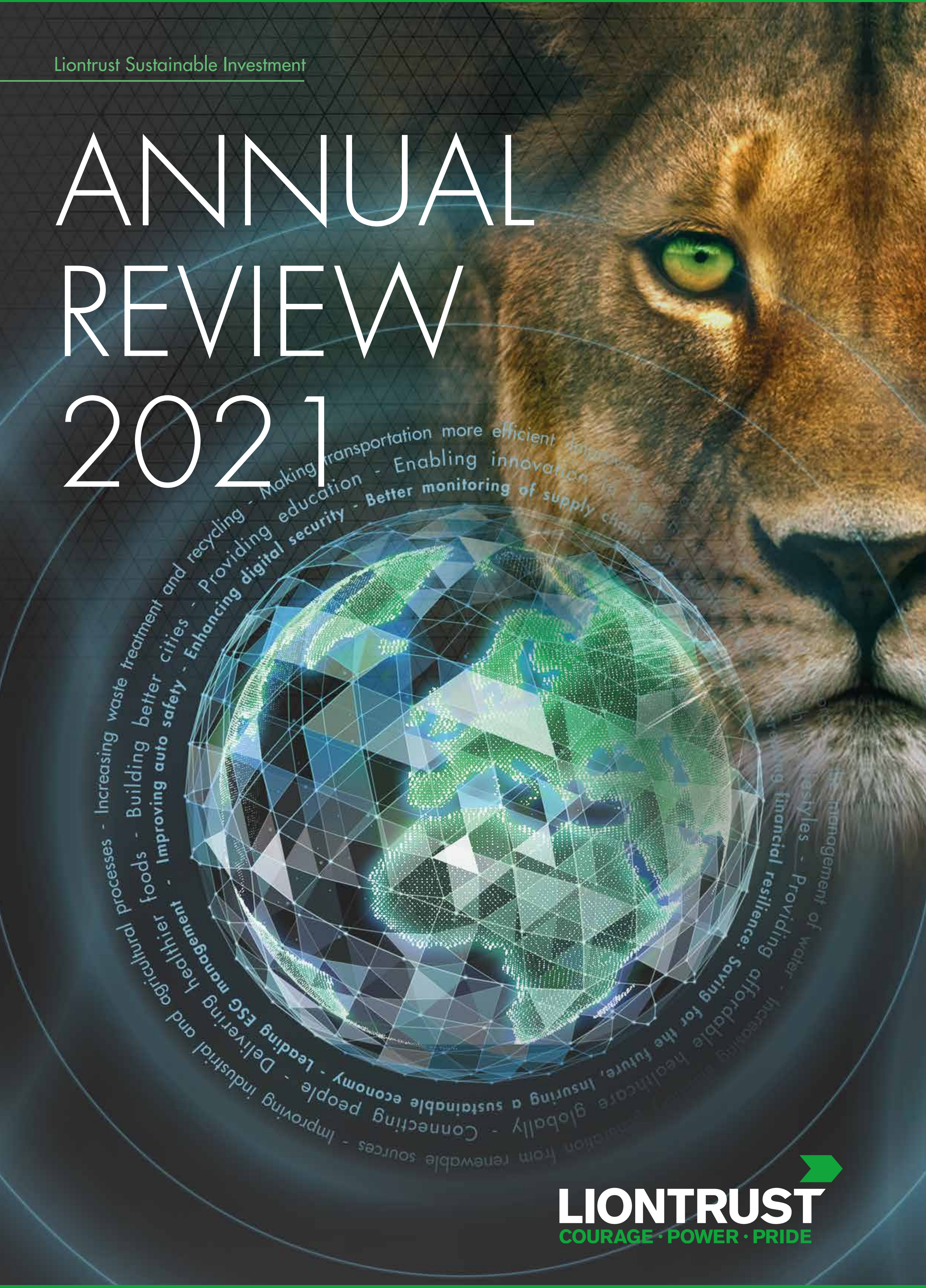
Liontrust Sustainable Investment

ANNUAL REVIEW 2021



LIONTRUST
COURAGE · POWER · PRIDE


Increasing waste treatment and recycling -
Building better cities - Providing
Improving auto safety - Enhancing digital

Contents

Introduction

Since we launched our Sustainable Future (SF) funds in 2001, our proposition to clients has been to seek to deliver superior returns by investing in sustainable companies that are making our world cleaner, healthier and safer. We believe these businesses have better growth and greater resilience than the market understands so we can aim to use this underappreciated advantage to deliver outperformance from our actively managed equity, fixed income and managed funds.

In addition, by allocating capital to these businesses and engaging with management, we can accelerate environmental and societal improvements.

With 2021 a more challenging backdrop for our SF investment process, it is worth reiterating exactly what we mean by a sustainable company and why we continue to believe there is alignment between doing good things and business success.

If you examine how change happens, there tend to be three actors at work. First, an understanding is developed of a particular issue and likely ways to resolve it are discovered (air pollution is harmful to health, for example), then society/government lay the groundwork for action – via new regulations, taxes and other incentives – and finally companies take advantage of the opportunity to develop, commercialise and distribute solutions. This moves the dial of the possible and accelerates the process. What is interesting from an investment point of view is that the businesses involved in this triangle tend to experience strong and persistent demand growth and face less competition due to the novelty of the product or service they are delivering.

We continue to believe human ingenuity, co-operation and desire to improve our lives leads to solutions, as well as that profit-making companies backed by capital from investment managers like Liontrust have a big part to play.

It is reasonable, though, to ask whether this model will work for such enormous challenges as tackling climate change, biodiversity collapse or increasing inequality. On climate change, for example, we have been aware of the issue for more than 30 years, and yet the latest IPCC (Intergovernmental Panel on Climate Change) report, issued in February 2022, shows greenhouse gases at record levels and that we are already experiencing some of the predicted extreme weather-related impacts.

With more than 80% of global energy still coming from fossil fuels according to figures from the International Energy Agency, is this not a challenge too far for the system outlined? We believe not. Change is rarely linear, and when a cheaper, better solution is developed, it can displace the old at an exponential rate. Yes, progress has been slow, but we are confident the rapid growth in renewables and adoption of electric vehicles is exactly one of these exponential transitions.

For years, renewables plodded along supported by regulation and subsidies, then there was a tipping point where, in region after region, it became the cheapest form of new energy generation. Since 2010, solar has fallen by 90% in price and onshore wind by 60% (as per International Renewable Energy Agency data) – and this cost deflation continues. The consequence of such growth is the picking off of fossil fuel generation, starting with coal. Since 2008, regardless of the US president in power, the country's Energy Information Administration reports that coal power has fallen by 61%.

We are often asked whether we invest in turnaround situations, such as oil companies pivoting to renewables, for example. This sounds like a potentially attractive strategy but we avoid it for two reasons. First, it is rare for companies to execute successfully such a pivot (think Kodak and the digital camera or Nokia and the smartphone) and, second, we like to stick to a strategy we know well and that has demonstrated long-term success.

Therefore, we continue with our thematic approach to select winners and avoid those losing due to inevitable change. Over the last two decades, we feel we have made good on that initial aim of delivering superior returns by investing in sustainable companies. Along the way, there have been periods of underperformance and 2021 has been one of these, but the longer-term picture supports our view that sustainable companies can deliver superior returns.

Looking to the future, we see no reason why the powerful trends in which we have invested should not persist, and so look forward to the next two decades with confidence.

Peter Michaelis, Head of Sustainable Investment at Liontrust

For more information on Sustainable Investment plus our funds and team, go to **www.liontrust.co.uk/sustainable**

HOW WE INVEST: OUR SUSTAINABLE VISION

Identifying superior stocks

01

Thematic analysis
– identifies companies with strong and dependable growth prospects due to alignment with our themes

02

Sustainability analysis
– focuses on those companies with excellent management and core products or services that contribute to society or the environment

03

Analysis of business fundamentals
– selects only those companies positioned to deliver high returns on equity

04

Valuation analysis
– determining that the shares of the company will be worth significantly more in the future

Our SF investment process is based on the core belief that sustainable companies have better growth and are more resilient than the market gives them credit for. We use this underappreciated advantage as we look to deliver outperformance across equity, bond and managed portfolios and, in supporting sustainable companies, accelerate environmental and societal improvements.

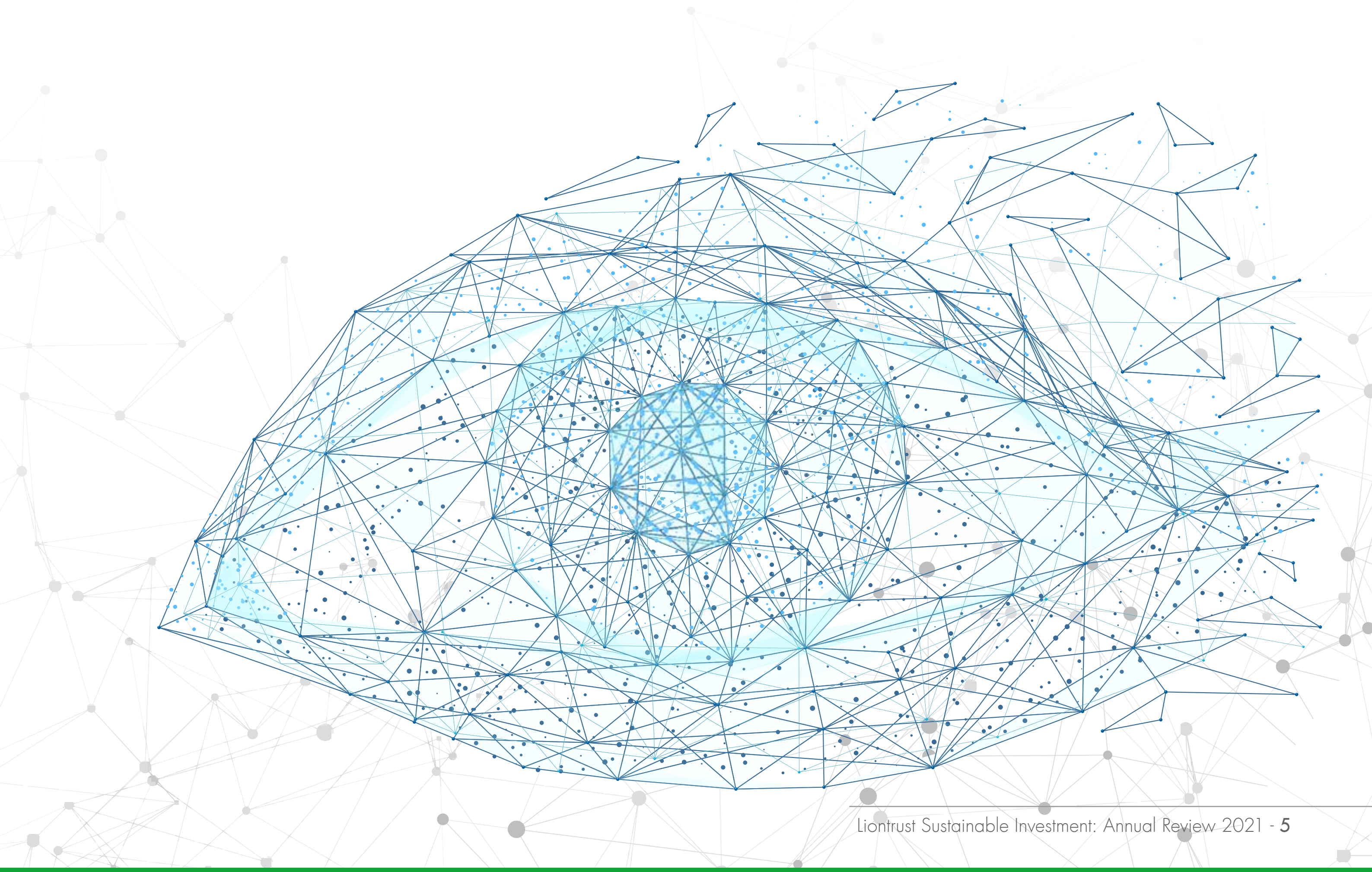
We are seeking to invest in the economy of the future and, to do this, the team looks at the world through the prism of three mega trends – Better resource efficiency, Improved health and Greater safety and resilience – and 20 themes within these, all contributing in different ways to creating a cleaner, healthier and safer planet:

Cleaner: Using our resources more efficiently (water, increasing recycling of waste, lower carbon energy sources and energy efficiency).

Healthier: Improving our quality of life through better education, healthier lifestyles and diet or better healthcare.

Safer: Making the systems we rely on safer or more resilient. This includes transport safety, keeping our online data safe with cyber-security and spreading risk through appropriate insurance mechanisms.

Understanding these trends helps to identify areas of long-term structural growth and we then look to invest in companies on the right side of these transitions, contributing towards a better world while making profits for our investors.



01 Thematic analysis – strong and dependable growth prospects

Better resource efficiency

- Improving the efficiency of energy use
- Improving the management of water
- Increasing electricity generation from renewable sources
- Improving the resource efficiency of industrial and agricultural processes
- Delivering a circular materials economy
- Making transportation more efficient or safer

Improved health

- Providing affordable healthcare
- Connecting people
- Delivering healthier foods
- Building better cities
- Providing education
- Enabling innovation in healthcare
- Enabling healthier lifestyles
- Encouraging sustainable leisure

Greater safety and resilience

- Increasing financial resilience
- Saving for the future
- Insuring a sustainable economy
- Leading ESG management
- Enhancing digital security
- Better monitoring of supply chains and quality control

While themes are at the heart of our idea generation, there are three further criteria all companies have to satisfy.

02 Sustainability analysis: A company might have significant exposure to a theme, but we also have to check how sustainable the rest of its activities are. For each business, we determine key ESG (environmental, social and governance) factors that are important indicators of future success and assess how well these are managed via our proprietary Sustainability Matrix (which can be seen on page 24). Every company held by the SF funds is given a Matrix rating, which analyses the following:

- Product sustainability (rated A to E): Assesses the extent to which a company's core business helps or harms society and/or the environment. An A rating indicates a company whose products or services contribute to sustainable development (via our investment themes); an E rating indicates a company whose core business is in a conflict with sustainable development (such as tobacco or polluting activities like coal-fired electricity generation).
- Management quality (rated 1 to 5): Assesses whether a company has the appropriate structures, policies and practices in place for managing its ESG risks and impacts. Management quality in relation to the risks and opportunities represented by potentially material ESG issues are graded from 1 (excellent) to 5 (very poor).

Companies must score C3 or higher to be considered for inclusion in our SF funds.

03 04 Analysis of business fundamentals and valuation analysis: Companies in which we invest have robust business fundamentals with a proven ability to deliver high returns on equity (RoE) through sustaining margins and asset turnover. Typically, these companies have a maintainable competitive advantage through scale, technology or its business model.

We then predict the likely sales, earnings and other financial returns we expect to see from these companies over the next three to five years, integrating our view of their quality into these. Applying the relevant valuation multiple allows us to derive a price target achievable in the next three years. When this shows significant upside (typically, we look for greater than 10% a year), the investment is recommended as a buy and available to be included in our funds

Growth
Theme driven

Growing addressable market
Share gainers
Structural tailwinds

Resilient returns
High quality companies

High barriers to entry
Aligned management team
Sustainable competitive advantages

Quality of earnings
Resilient, dependable

Recurring revenues
Cash flow conversion

- **Forecast financial outcomes over the next five years**
  Determining future revenues, margins and earnings
- **Identify the valuation metric relevant to the stock**
  Price/Earnings, EV/EBITDA, Price to Book
- **Determine the future level of the valuation multiple**
  Will the multiple fade, be sustained or expand?
- **Derive the valuation that the shares can reach over the coming years**
  We look for greater than 10% pa return

Meet the team

We have a 17-strong investment team that has been managing funds in this way for 21 years, with a mix of experience and youth. On the latter, four graduates joined our ranks in 2021. A key differentiator is the fact that all the sustainable elements are fully integrated within a single team. We do not have separate fund management and ESG divisions, for example; instead, every member is responsible for all aspects of financial and ESG analysis relating to an investment decision. Because of this approach, our team engages with companies across a broad range of issues relating to different stages in our investment process, including screening criteria, sustainable themes and company-specific ESG issues (details of which can be found throughout this Annual Review).

We also have a four-strong external Advisory Committee to provide another layer of expertise in key areas of social and environmental impact: Tony Greenham, Tim Jackson, Valborg Lie and Ivana Gazibara (who was the latest member to join in 2021).

Equities

Theme and other responsibility | Academic background | Industry tenure / Team tenure

Peter Michaelis
Head of Sustainable Investment team

- *Better monitoring of supply chains and quality control*
- *Building better cities*
- *Enhancing digital security*
- *Improving the efficiency of energy use*

- MA in Physics from Oxford University
- MSc in Energy & Environmental Engineering from Sussex University
- PhD in Environmental Economics from the University of Surrey

- 22 years / 21 years

Simon Clements
Investment Manager

- *Improving the management of water*
- *Improving the resource efficiency of industrial and agricultural processes*
- *Making transportation more efficient or safer*

- BSc in Economics from the University of Newcastle, Australia
- Graduate Diploma in Applied Finance & Investment from Securities Institute of Australia
- CFA Charterholder

- 26 years / 13 years

Mike Appleby
Investment Manager

- *Delivering a circular materials economy*
- *Increasing electricity generation from renewable sources*
- Business development

- BSc (Hons) in Biological Sciences from the University of Edinburgh
- MSc in Environmental Management from Imperial College London

- 22 years / 18 years

Harriet Parker
Investment Manager

- *Connecting people*
- Leading engagement activities

- BSc in Economics & Management from the University of Bristol

- 18 years / 18 years

Laurie Don
Investment Manager

- *Enabling innovation in healthcare*
- *Providing affordable healthcare*

- BSc (Hons) in Computer Science from Durham University
- CFA Charterholder

- 14 years / 7 years

Martyn Jones
Investment Manager

- *Delivering healthier foods*
- *Enabling healthier lifestyles*
- *Encouraging sustainable leisure*
- *Providing education*

- MA in Management from The University of Glasgow
- CFA Charterholder
- MSt in Sustainability from the University of Cambridge

- 10 years / 8 years

Equities (continued)

Chris Foster
Investment Manager

- *Increasing financial resilience*
- *Insuring a sustainable economy*
- *Leading ESG management*
- *Saving for the future*

- MA in Economics and Mathematics from the University of Edinburgh
- CFA Charterholder

- 9 years / 7 years

Mingming Huang
Portfolio Manager Assistant

- Analytical support for thematic analysis and engagement

- BSc Mathematics with Business Management from Queen Mary University of London

- 3 years / 3 years

Sarah Nottle
Trainee Analyst

- Equities and Sustainable investment

- BCom in Finance and Commercial Law and BA in International Relations from University of Sydney
- IMC

- 4 years / < 1 year

Ed Phelps
Trainee Analyst

- Equities and Sustainable investment

- BSc (Hons) Economics from University of Nottingham
- Studying for the IMC

- < 1 year / < 1 year

Fixed Income

Stuart Steven
Head of Fixed Income

- Portfolio construction
- Banks

- BA in Accountancy from Stirling University
- MSc in Investment Analysis

- 28 years / 12 years

Kenny Watson
Investment Manager

- Credit positioning and high yield
- Utilities, retail, household goods, travel and leisure

- BA in Accounting and Economics from the University of Strathclyde
- Chartered Accountant

- 25 years / 8 years

Aitken Ross
Investment Manager

- Interest rates
- Insurance and financial services

- BSc in Accountancy and Finance from Dundee University
- MA in International Financial Analysis from Newcastle University
- CFA Charterholder

- 12 years / 10 years

Jack Willis
Investment Manager

- Credit positioning
- Telecoms, property, healthcare, industrials, chemicals

- BSc in Mathematics with Finance from the University of Leeds
- MSc in Finance and Investment from the University of Leeds
- CFA Charterholder

- 8 years / 6 years

Hannah Jones
Portfolio Manager Assistant

- Sustainability analysis and portfolio administration

- Studying for the IMC

- 7 years / 5 years

Nancy Kondelidou
Trainee Analyst

- Credit and Sustainable investment

- Bachelor of Laws (Hons) / MSc Law & Finance from Queen Mary University
- CFA Level 1

- < 1 year / < 1 year

Deepesh Marwaha
Trainee Analyst

- Credit and Sustainable investment

- BA (Hons) Economics & Human Resources from University of Strathclyde

- < 1 year / < 1 year

Governance & Stewardship team

The Governance & Stewardship team works closely with the Sustainable Investment team and supports other Liontrust investment teams on areas such as AGM voting and policy implementation, and PRI and FRC Stewardship Code reporting.

Sinead Lennon
Governance & Stewardship Manager

- Postgraduate certificate in International Business Ethics and Corporate Governance, Birkbeck University
- BA (Hons) in Business Studies, Dublin Business School
- IMC

- 9 years / 9 years

Natalie Bell
Stewardship Manager

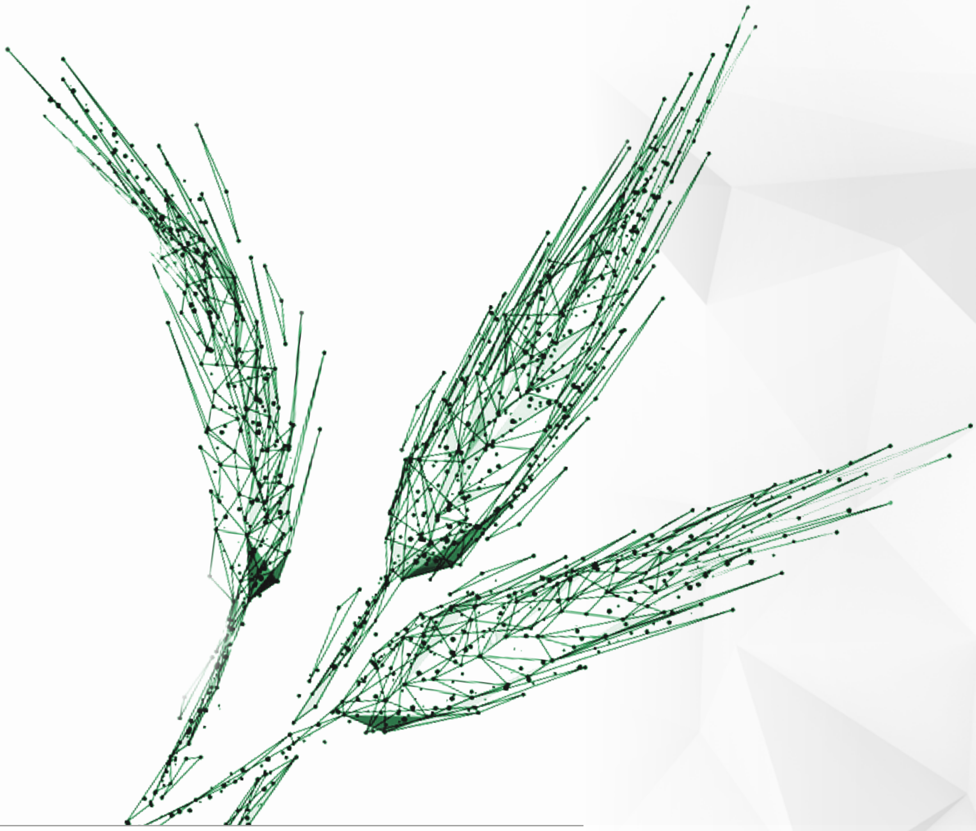
- BA (Hons) in Politics from the University of Nottingham

- 8 years / 1 year

Kitty Woodham
Governance Executive

- MSc in International Public Policy, University College London (UCL)
- BA (Hons) in French & Spanish, University of Bristol

- 1 year / 1 year



Advisory committee

Our sustainable investment team employs the services of an Advisory Committee which provides guidance and expertise in key areas of social and environmental impact.

Tony Greenham is Director of Economy, Enterprise and Manufacturing at the RSA (Royal Society of Arts, Manufactures and Commerce), where he leads a programme of policy research into the future of work, social impacts of technology, green industrial strategy and economic democracy. He is a former corporate stockbroker and has written extensively on financial sector reform including the undergraduate economics textbook *Where Does Money Come From?*

Valborg Lie is Stewardship Manager at LGPS Central, responsible for bespoke engagement and voting services to support investment objectives. Valborg has a wealth of experience, working on responsible investment (RI) issues over the last 15 years. From 2005 to 2013, she worked as Head of RI within the Norwegian Ministry of Finance overseeing the management of the Norwegian Government Pension Fund Global (GPFG), one of the biggest sovereign wealth funds globally. Valborg leverages an extensive network of institutional investors and SWFs globally to help promote and build RI best practices.

Tim Jackson is Professor of Sustainable Development at the University of Surrey and Director of the Centre for the Understanding of Sustainable Prosperity (CUSP). From 2004 to 2011, he was Economics Commissioner on the UK Sustainable Development Commission, where his work culminated in the publication of the controversial bestseller *Prosperity without Growth – economics for a finite planet*.

Ivana Gazibara is a futures and systems change expert with more than 15 years of experience in sustainability strategy and innovation. She is currently working with the TransCap Initiative to build the field of systemic impact investing. Ivana has previously led Forum for the Future's futures practice, overseeing thought leadership projects, strategic foresight work with partners, and internal and external horizon scanning networks. She has also incubated and led The Futures Centre, the only open, participatory futures platform focused on tracking and making sense of change with the purpose of advancing a sustainable future. Prior to that, Ivana was part of SustainAbility's emerging economies team, working to build the organisation's practice in India and Brazil. Ivana has an MSc in Development Management from the London School of Economics and a BA in Peace and Conflict Studies from the University of Toronto.

Performance of our funds - quartile rankings to 31.12.21

	Sector	1 year	3 years	5 years	10 years
Sustainable Future Managed	IA Mixed Investment 40-85% Shares	1	1	1	1
Sustainable Future Cautious Managed	IA Mixed Investment 40-85% Shares	3	1	1	N/A
Sustainable Future Defensive Managed	IA Mixed Investment 20-60% Shares	3	1	1	N/A
Sustainable Future Managed Growth	IA Flexible Investment	1	1	1	1
Sustainable Future Global Growth	IA Global	3	1	1	1
Sustainable Future European Growth	IA Europe Excluding UK	4	1	1	1
Sustainable Future UK Growth	IA UK All Companies	4	1	1	1
UK Ethical	IA UK All Companies	4	1	1	1
Sustainable Future Corporate Bond*	IA Sterling Corporate Bond	3	2	2	N/A
Monthly Income Bond Fund	IA Sterling Corporate Bond	1	3	2	1
GF SF Pan-European Growth Fund**	FE peer group	3	1	1	1
GF SF European Corporate Bond Fund**+	FE peer group	2	2	N/A	N/A
GF SF Global Growth Fund+^	FE peer group	3	N/A	N/A	N/A

Source: FE Analytics, primary share classes, total return (net of fees, income/interest reinvested). Funds versus comparator benchmark quartiles as at 31.12.21, generated 06.01.22 *Manager inception date 20.08.12. ** In Euros. +GF SF European Corporate Bond Fund launched 29.05.18 and GF SF Global Growth Fund launched 12.11.19 ^ In US dollars.

Past performance is not a guide to future performance. The value of an investment and the income generated from it can fall as well as rise and is not guaranteed. You may get back less than you originally invested. Please refer to the Key Risks page for more information

Discrete returns (%) - To previous quarter 12 months ending

	Dec-21	Dec-20	Dec-19	Dec-18	Dec-17
Liontrust Sustainable Future Managed 2 Inc	13.5	21.3	24.7	-0.5	16.1
IA Mixed Investment 40-85% Shares	10.9	5.3	15.8	-6.1	10
Liontrust Sustainable Future Cautious Managed 2 Inc	9.2	12.8	19.5	-2.2	13.4
IA Mixed Investment 40-85% Shares	10.9	5.3	15.8	-6.1	10
Liontrust Sustainable Future Defensive Managed 2 Inc	6.8	11.3	16.8	-2.2	11.9
IA Mixed Investment 20-60% Shares	7.2	3.5	11.8	-5.1	7.2
Liontrust Sustainable Future Managed Growth 2 Acc	16.5	33.2	26.4	1.1	18.1
IA Flexible Investment	11.3	6.7	15.7	-6.7	11.2
Liontrust Sustainable Future Global Growth 2 Acc	17.4	32.3	29.4	1.3	18.8
MSCI World	22.9	12.3	22.7	-3	11.8
IA Global	17.7	15.3	21.9	-5.7	14
Liontrust Sustainable Future European Growth 2 Acc	13.7	24.3	25.9	-14.8	19.8
MSCI Europe ex UK	16.7	7.5	20	-9.9	15.8
IA Europe Excluding UK	15.8	10.3	20.3	-12.2	17.3
Liontrust Sustainable Future UK Growth 2 Acc	12.5	5.3	30.2	-6.7	20.7
MSCI UK	19.6	-13.2	16.4	-8.8	11.7
IA UK All Companies	17.2	-6	22.2	-11.2	14
Liontrust UK Ethical 2 Acc	10.4	2.8	37.8	-7.3	22.5
MSCI UK	19.6	-13.2	16.4	-8.8	11.7
IA UK All Companies	17.2	-6	22.2	-11.2	14
Liontrust Sustainable Future Corporate Bond 2 Inc	-2	7	11.8	-3.6	7.2
iBoxx Sterling Corporate All Maturities	-3.2	8.6	11	-2.2	5
IA Sterling Corporate Bond	-1.9	7.8	9.5	-2.2	5.1
Liontrust Monthly Income Bond B Gr Inc	-0.2	5.5	9.4	-3	8.9
iBoxx Sterling Corporates 5-15 Years	-3.3	8.6	10.7	-1.7	5.7
IA Sterling Corporate Bond	-1.9	7.8	9.5	-2.2	5.1
GF Sustainable Future Pan-European Growth A1 Acc*	20.4	13.5	32.4	-17	13.6
MSCI Europe	25.1	-3.3	26	-10.6	10.2
GF Sustainable Future European Corporate Bond A5 Acc*	-0.3	1	7.3	N/A	N/A
iBoxx Euro Corporates All Maturities Index	-1.1	2.7	6.3	N/A	N/A
GF Sustainable Future Global Growth B5 Acc USD	15.4	38	N/A	N/A	N/A
MSCI World	21.8	15.9	N/A	N/A	N/A

Source: Data as at 31.12.21. FE Analytics, primary share class, total return (net of fees, interest/income reinvested). Funds versus comparator benchmarks. GF SF European Corporate Bond Fund launched 29.05.18 and GF SF Global Growth Fund launched 12.11.19 so discrete data is not available for five full 12 month periods. *In Euros

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More challenging year in 2021

Our equity and managed funds started 2021 behind their benchmarks as the stock market seemed to focus on 're-opening' plays. During the second and third quarters, this reversed somewhat and the funds made up most of the ground lost in the first quarter. In the final quarter of 2021, markets began to factor in higher inflation and therefore higher interest rates (and higher discount rates), and given our quality growth focus, the SF equity and managed funds have had a period of weaker relative performance since the end of September 2021.

The primary reason has been a marked change in market leadership, with value sectors recovering strongly, including oil, banks, and mining companies. Investor confidence in the near-term outlook for these sectors has been supported by increases in interest rates, commodity price rises and general inflation as economies emerge from pandemic-supressed economic conditions.

The other side of rising interest rates is a challenge to the valuation of growth companies – a higher rate picture leads, theoretically, to a higher discounting of future profits, so businesses with larger future profits should mechanically be valued at a lower level. For the SF funds, this raises two questions:

- Should we change our portfolios to invest in more value-like names?
- Is the growth outlook for businesses in which we invest weakened, and do they still offer potentially good long-term share price rewards?

The answer to the first is an emphatic no. We have used the same approach for more than 20 years and it has served our clients well. Yes, there have been periods of underperformance as a consequence of value rallies – notably in 2003, 2009 and 2016 – but by sticking to our investment process, we have more than compensated for these periods. By their nature, value stocks re-rate relatively rapidly, and then it is done. Our preference is for companies that can maintain long-term and high earnings growth.

The second question is one we concern ourselves with every day in the analysis of the companies in our funds. There have been stocks that have performed well through the pandemic, such as Oxford BioMedica, in manufacturing the Oxford-AZ vaccine, and Softcat, in providing the technology to enable small and medium-sized enterprises (SMEs) to work effectively through lockdowns. But our longer-term view of their growth is not predicated on pandemics and lockdowns continuing. Overall, we are still very comfortable that the businesses in which we invest will deliver strong growth, and that over the next five years and beyond we will see strong share price performance from them.

We believe our ability to focus on the long term is one of the few remaining competitive advantages in markets (referred to as time arbitrage). We also feel that during periods of stress, time horizons typically shorten. It is therefore crucial for us to retain this focus on the long term – we are acutely aware this would be an almost impossible task without our clients continuing to support us in doing so.

While 2021 was a challenging period for our funds, we would encourage investors to put this in the context of strong returns over three, five and 10 years, and longer where relevant. All our funds with a 10-year track record to the end of 2021 are in the first quartile of their respective IA sectors.

Short versus long-duration

Taking a step back, what are active investors trying to achieve? We are all, whether considered value or growth, trying to identify mispriced securities for which the current market price does not reflect intrinsic value. The only real difference between investors is their time horizon: some (including us on the Sustainable Investment team) focus on the long-term growth potential of cashflows whereas others prefer to concentrate on near-term cashflows. This is the critical point that has been moving markets so violently – what rate do we use to discount future cashflows?

For companies for which the market expects strong growth for years to come, a large proportion of valuation is attributed to future cashflows. Conversely, for companies with lower expectations, little value is ascribed to future growth and the bulk of the value is in near-term cashflows. Given the strong growth prospects of companies we invest in, our funds in general are longer duration relative to the market and have therefore been more negatively impacted by recent changes in discount rates.

Given this shift, there has been a rush into lower valuation, lower duration parts of the market; this includes cyclical, commodity and energy companies. But let's ask ourselves again – why have interest rates increased? To try to control runaway inflation.

Inflation increases input costs for companies, squeezing profit margins. Management teams have a few options to protect margins and deal with increasing costs: they either try to offset them with efficiencies or, more likely, pass cost increases on to customers with price hikes. But for this to work, you have to invest in companies with pricing power and again, given the scarcity of truly high-quality businesses, these tend to have higher valuations and thus higher duration.

Therefore, a counterintuitive situation has occurred where the prospect of higher inflation has negatively impacted exactly the sort of companies best placed to cope with it. In contrast, lower-quality companies without pricing power or strong profit margins, which are likely to suffer over the long term from higher inflation, have become popular in this rotation. It strikes us as an odd short-term move.

Equally, at times of indiscriminate sell-offs, the market presents us with fantastic opportunities to add to our highest-conviction companies at very attractive valuations, as well as starting positions in companies we have long admired but, prior to now, were fairly valued by the market. We have had the opportunity to do both recently.

War in Ukraine

While falling outside the confines of 2021, it would be remiss of us not to mention Russia's invasion of Ukraine, which continues to bring turbulence to markets. We share everyone's shock at these events and the main concern is the safety of innocent people.

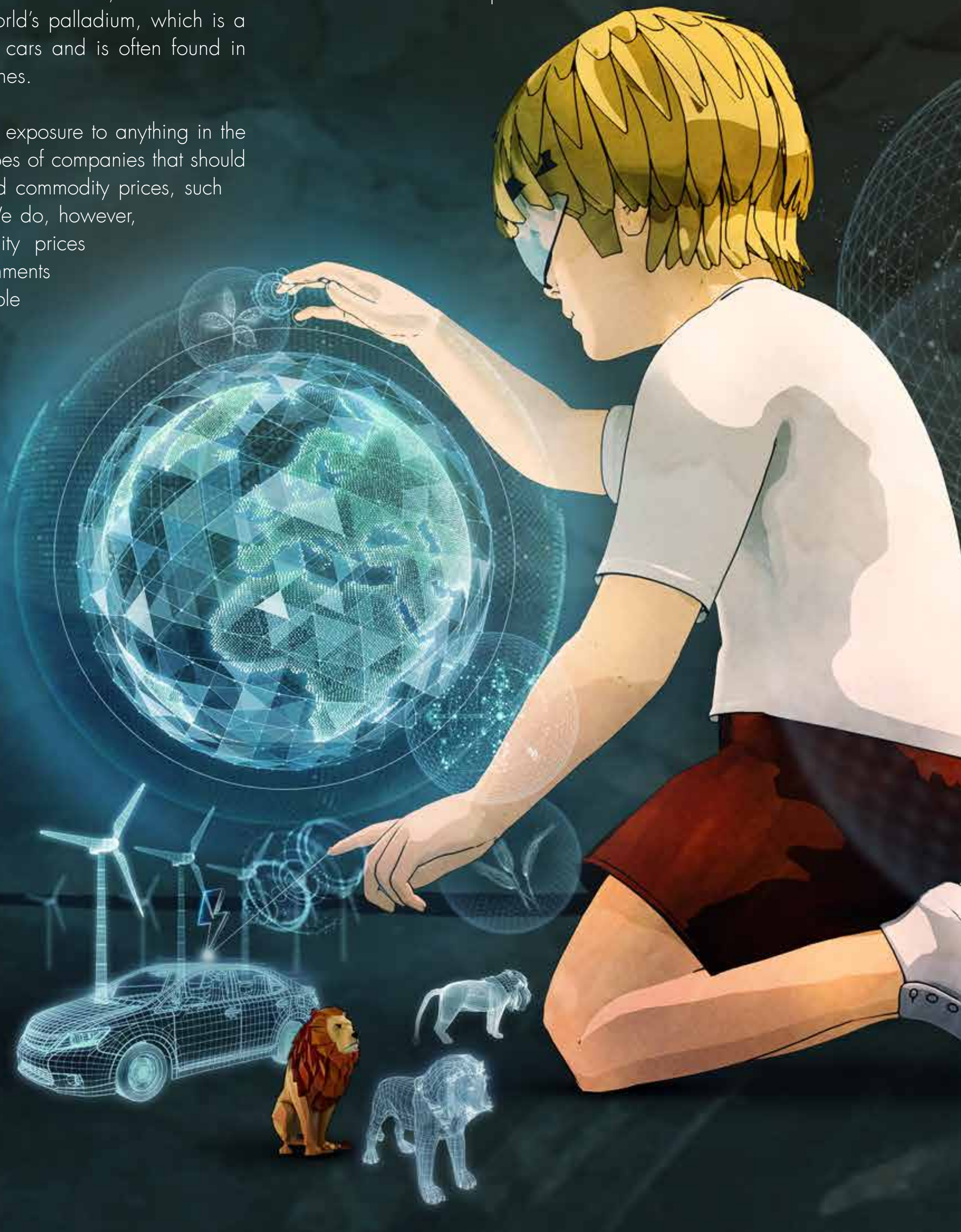
If we look at our funds, we have no direct exposure to Russia and Ukraine. We also have negligible indirect impact from either economy (this is not zero, however, as some companies will have very small revenue exposures to Russia).

Russia is a major producer of many commodities, however, so sanctions have the potential to impact the broader global economy in ways that are difficult to predict. The country also accounts for around 10% of the world's supply of oil according to International Energy Agency figures, as well as being an exporter of many precious metals. The US bank Stifel, for instance, estimates that Russia produces up to 40% of the world's palladium, which is a metal used in catalytic converters for cars and is often found in electronic devices such as mobile phones.

As would be expected, we have zero exposure to anything in the arms manufacturing space or to the types of companies that should benefit directly from higher energy and commodity prices, such as miners and fossil fuel extraction. We do, however, believe higher energy and commodity prices should increase the willingness of governments and businesses to invest in renewable energy and focus more on improving their efficiency of energy use.

The need to cut fossil fuel use is clear, and the situation in Europe reinforces the case for both the greater supply security that renewables can offer and reducing reliance on many of the major oil-producing countries. This would be a major benefit to the world, making it more likely that climate goals are achieved, and it also has potential implications for our portfolios. As it stands today, around a third of our SF funds are invested in companies whose products and services are designed to make the use of resources more efficient.

While we are clearly following events closely, we do not attempt to forecast macroeconomic factors and question the ability of anybody to do so with any consistency. We continue to focus on our core competence: identifying businesses exposed to strong sustainability trends that will endure and grow their value per share regardless of the economic backdrop.



The Bond angle

Three pillars of the process

Maximise Sustainability 1

Sustainability analysis
Positive screening
Negative screening
Best in class

Maximise Quality 2

Credit analysis
High-quality issuers
Macro analysis

Maximise Value 3

Finding value
Dynamic approach
Focused portfolio

Our bond funds had a solid 2021, driven by a combination of positive contributions from rates, sector allocations and security selection. We remain underweight interest rate risk through short duration positioning versus the benchmark indices, due to the team's belief that government bonds remain overvalued.

Given the strong rebound in the global economy and our view that inflationary pressures were more permanent than central bankers' 'transitory' claims, we felt there would be upward pressure on government bond yields. This proved to be the case, with policymakers turning more hawkish in December and the Bank of England raising base rates to 0.25% (and then again in February and March 2022) despite lingering uncertainty about Covid variants – and our short duration position helped performance as yields rose into 2022.

On the credit side, the funds benefited from sector allocations and security selection: our overweight positioning in banks and insurance had a positive impact on performance, which reflected our constructive view on the outlook for credit.

Looking to the rest of 2022 and beyond, our strategic view remains largely unchanged. We believe the rebound in the global economy will continue and markets will focus on inflationary pressures within economies and, most critically, central banks' response to these, with the risk of policy error as they attempt to control inflation without stifling recovery.

While some of these pressures are transitory, we continue to believe the broad-based nature of rising inflation will be 'stickier' than central banks believe and hold this view across the UK, US and Europe. This is supported by supply chain disruptions, tight labour markets and high energy prices, as well as the ongoing unwind of consumer savings.

Despite tapering and rate rises by central banks, we retain the view that government bond yields are too low and should rise further given the growth and inflation outlook, with the SF bond funds positioned to benefit from such moves. Corporate spreads remain resilient, supported by robust underlying fundamentals and technicals. Already strong fundamentals should continue to improve as recovery continues and more periods of weak earnings drop out of calculations, further supporting spreads.

As conditions improve, we expect companies' focus to remain on enhancing fundamentals, including creditor-friendly debt reduction and balance sheet repair, and technicals should also remain supportive as demand for corporate bonds persists as a source of yield. We remain committed to existing high-quality positions and believe they are well set to continue to perform as the market benefits from measures taken by central banks and national governments, and a generally improving economic outlook.

How banks can help the energy transition

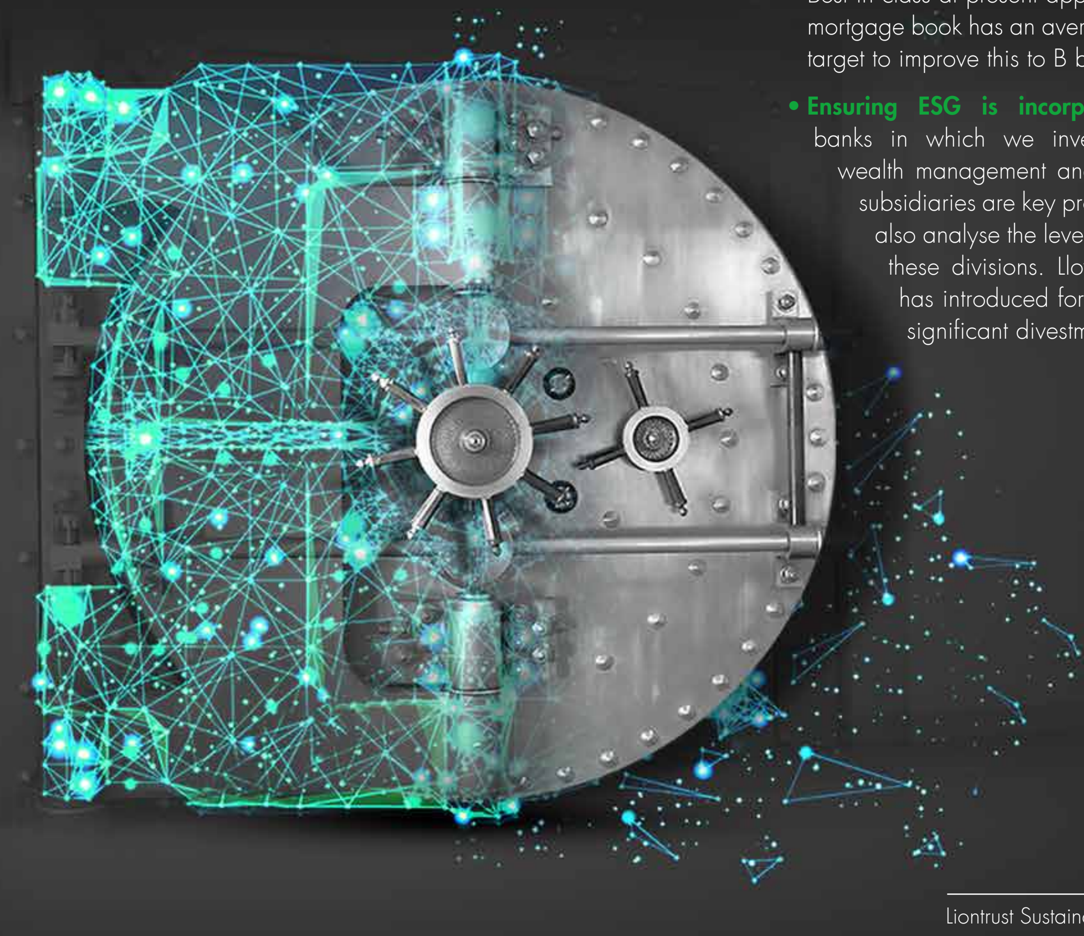
STUART STEVEN

Banks have a key role to play in the shift towards a low-carbon economy, with their lending policies, influence with corporates and scope to provide sustainable financing all vital to reducing greenhouse gas (GHG) emissions.

From our analysis, it is clear different regions and countries are moving at radically different rates, however. Specifically, the majority of EU and UK banks are embracing scientific-based approaches that are broadly consistent with the Paris Agreement, whereas countries such as the US and China are not there yet.

Across our SF bond portfolios, we aim to invest in banks that are targeting net-zero by 2050 or before (including indirect Scope 3 emissions), and most are looking to achieve this through a combination of the following factors:

- **Reducing lending to high-carbon sectors:** As part of our analysis of banks, we are looking to assess the standard of policies that control lending to controversial sectors; consistent with our screening criteria, we will not invest in those where lending to these areas exceeds 5% of the total. This can involve targets to exit financing to coal-fired power stations and thermal coal mining, for example, with dates typically dependent on where a business is based. For those in developed regions (EU/OECD), most banks are aiming to stop this lending by 2030, whereas the end point is more like 2040 (due to humanitarian concerns) in the developing world. Similarly, we also look for Paris alignment for lending to oil and gas companies.
- **Provision of green/sustainable finance:** On top of avoiding controversial sectors, many banks are also setting out detailed targets to provide lending to sustainable and green companies and projects. HSBC is a strong example here: having met its initial target of $100 billion between 2017-2020, it is now aiming to provide aggregated lending of between $750 billion and $1 trillion to support decarbonisation of corporate clients by 2030. This equates to between 25% and 30% of its total loan book.
- **Working with corporates to reduce their emissions:** As a further measure, banks including NatWest and Lloyds are seeking to cut emissions within their corporate loan book by at least 50% by 2030. This is interesting as it ensures the transition is taking place across a broad range of sectors, including SMEs and micro-cap companies.
- **Improving the energy efficiency of their mortgage book:** While still at an early stage in the UK and Europe, we are starting to see this become more of a focus, with several banks setting targets to improve the average energy rating of their mortgage book. Best in class at present appears to be Rabobank, whose current mortgage book has an average energy rating of C, with a stated target to improve this to B by 2024 and A by 2030.
- **Ensuring ESG is incorporated across divisions:** Several banks in which we invest also have asset management, wealth management and insurance operations; given these subsidiaries are key providers of capital to the economy, we also analyse the level to which ESG is incorporated within these divisions. Lloyds Scottish Widows, for example, has introduced formal exclusionary criteria, resulting in significant divestments by its investment portfolios.



KEY THEMES


on and access to clean water – Le
– Increasing financial resilience
Improving industrial processes – Increasing electi
Provi

Sustainable investment themes

Themes sit at the heart of the SF investment process, identifying areas of structural growth associated with improvements in resource efficiency, quality of life and the safety and resilience of society. We continue to review these to ensure they are current, consistent and clear, adding new areas if we believe they are warranted or reorganising and combining existing themes if this makes sense given changing circumstances.

As a result of the 2021 review, we incorporated *Improving transport safety* into *Making transport more efficient* to become *Making transportation more efficient or safer*, bringing the overall number down from 21 to 20.

The amended definition is as follows:

Urban transport systems are improved by reducing congestion as well as emissions (which make local air quality toxic), as the mode shifts from self-driven cars to trains, tubes and buses. We are also interested in active transport such as bicycles as a healthier way to travel short distances. We have identified companies whose products improve safety of travel and reduce accidents. Much of our early work focused on autos but we should not assume cars will remain dominant, particularly with safe, efficient mass transport key to reducing emissions. Whatever the mode of travel, we concentrate on the companies making the kit to improve safety, from active safety systems to more efficient braking.

Theme updates

Healthcare outlook post-Covid

LAURIE DON

Healthcare remains a huge focus as the world grapples with Covid-19 and its variants but from a longer-term perspective, our hope is that the pandemic has opened people's eyes to the importance of getting this area right. Lessons learnt during such a challenging period should encourage greater understanding of how best to manage health in the years ahead.

Our focus as sustainable investors is on a cleaner and safer world in future but people have to be healthy enough to enjoy this. In broad terms, the key is to take a more proactive stance in monitoring and preventing disease before it occurs. Although this may feel expensive, it is far cheaper and ultimately better in terms of patient outcomes than dealing with illness later.

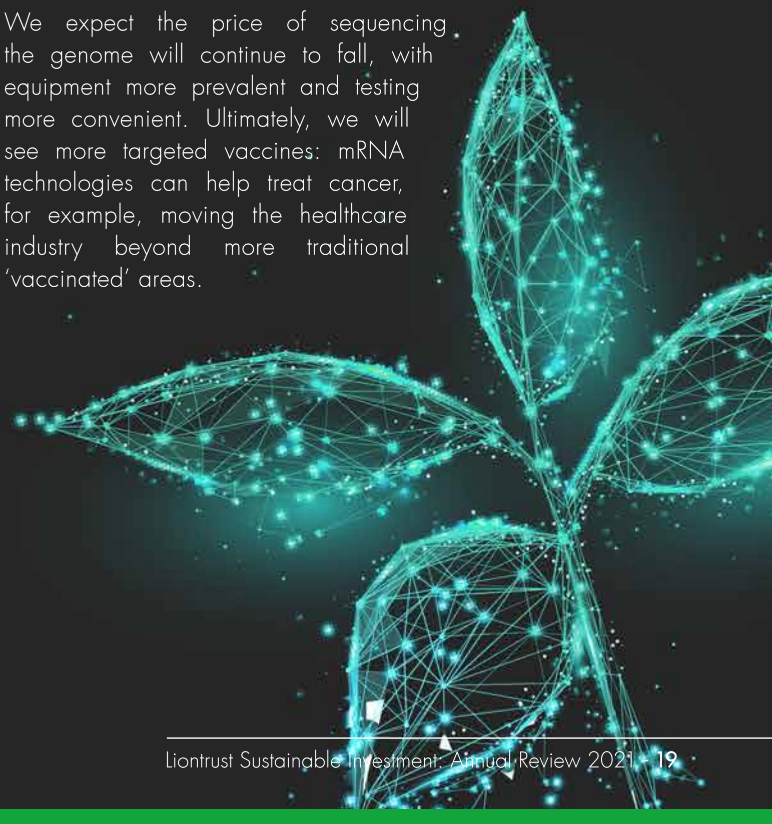
We are looking for innovative companies that can enable a step change in how particular areas of healthcare operate. The healthcare system will continue to cost more as the population ages and with the externalities of modern life (such as climate change and social media overuse). Because of this, we expect continuing pressure for the health system to do more with less (with fewer health workers relative to the population and reduced finances), and companies and products that fail to add value will be weeded out.

On the positive side, science continues to move forward and our understanding of genetics (in people and the wider natural world) has improved dramatically. We are seeing major advances in technology across areas such as gene editing and DNA sequencing and these are revolutionising how we think about treatment.

The traditional model has a large element of trial and error, with people seeking help when they feel ill and hoping whatever drug or procedure prescribed is effective – but this often proves too late. In contrast, we are moving towards a more personalised system where we can understand how someone's genetic make-up leaves them vulnerable to certain diseases, and this is opening up new ways to counter conditions such as cancer, dementia and Parkinson's.

Key areas to watch include gene therapies – a one and done cure for disease versus the traditional pharmaceutical model of taking a pill regularly for the rest of your life – and liquid biopsy, which enables early detection and monitoring of diseases through blood draws rather than solid tissue samples. This paves the way for early diagnostics and pre-emptive treatment: testing babies before birth and adults early and on an ongoing basis.

We expect the price of sequencing the genome will continue to fall, with equipment more prevalent and testing more convenient. Ultimately, we will see more targeted vaccines: mRNA technologies can help treat cancer, for example, moving the healthcare industry beyond more traditional 'vaccinated' areas.



Green hydrogen: fuel of the future?

MIKE APPLEBY

Amid ongoing debate about reducing emissions as part of the energy transition, there is growing excitement about hydrogen's potential as an ultra-low carbon fuel of the future.

We definitely see a role for hydrogen in aspects of transport, as well as in potentially decarbonising heat and as a storage medium for electricity. Our Sustainable Investment team has been looking at hydrogen for years and the recent resurgence in Hydrogen 2.0 appears to have a number of benefits over Hydrogen 1.0, which peaked with fuel cells before withdrawing to the sidelines a decade or more ago. How this will pan out, however, and the best ways to invest in this theme are still uncertain and we anticipate it will be some time before the economics are right for mass adoption.

The beauty of hydrogen is that when burned, the main by-product is water; the critical factor from an emissions standpoint, however, is how that hydrogen is produced. At present, virtually all hydrogen comes from using natural gas as a feedstock (grey hydrogen). Blue hydrogen is when this process captures and stores most of the resulting carbon emissions; green hydrogen, meanwhile, is made by electrolysing water (using electricity from ultra-low carbon sources such as wind and solar).

From an environmental and investment perspective, we are only interested in green hydrogen. Blue is a good idea but we have yet to see carbon capture and storage technology to make this economically viable. Using grey hydrogen as a future fuel also makes no sense as, by our calculations, the carbon emissions in producing it are worse than burning natural gas.

In terms of applications, hydrogen is used in transport, replacing batteries in warehouses for forklift trucks and similar machines. We see further potential for green hydrogen as fuel stock in logistics (trucks, trains and marine) but these newer applications are unlikely to be scalable before 2025 to 2030. Green hydrogen is also being used in pilot applications, particularly industrial processes such as chemicals and refining in Europe. This is proving an excellent learning ground and has the capacity to drive up the scale of this industry and bring down costs.

In heating homes, we think replacing natural gas with hydrogen will take time before grids are capable of carrying high proportions of the latter (many in Europe are being upgraded to plastic piping) and we are some way from green hydrogen being cheap enough to make that switch economically viable. There are trials under way to add hydrogen to the grid to around 30% levels (the remainder being natural gas), which has the potential to reduce emissions. Our view is that electrically-driven heat pumps will gain traction as we move towards 2035 before we see this green hydrogen gas network scaling up in the late 2030s or early 2040s.


Enabling SMEs to power more sustainable economic growth

CHRIS FOSTER AND SARAH NOTTLE

Ongoing innovation and a transition to a greener economy are integral to a more sustainable future, and a healthy pipeline of small and medium-sized enterprises (SMEs) remains an important driver of both.

We see enabling SMEs as both a vital structural growth trend and an anchor of a sustainable economy, with these companies making up 99% of all US businesses and accounting for 44% of the country's GDP and two-thirds of net job creation, according to US Small Business Administration.

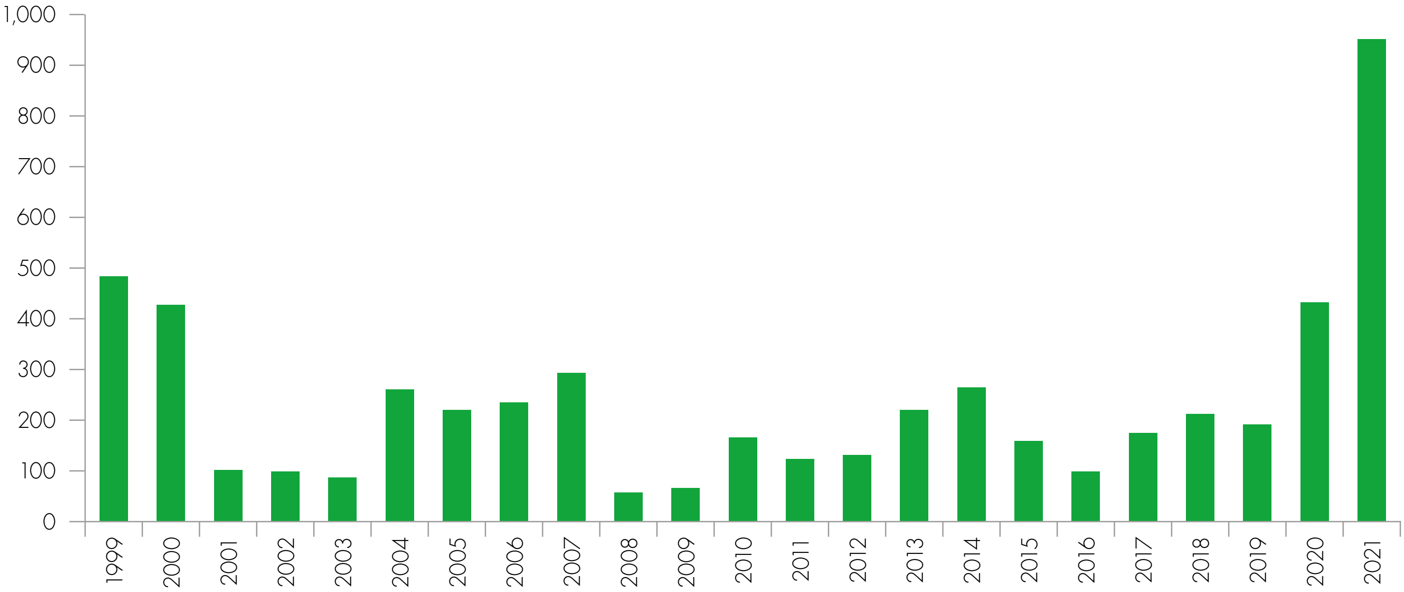
Defining an SME is jurisdiction dependent; they are considered to have a maximum of 500 employees in the US but fewer than 250 in the European Union. Whatever the definition, the basis of our investment theme lies in identifying companies offering products and services that give these businesses the best chance to succeed and grow. Even many high-growth companies start from sole proprietorship and, historically, there have been major barriers to developing a business idea, with SMEs needing capital, talent and knowledge to achieve scale against incumbents.

Their strength lies in greater agility to pivot quickly towards new technology or take advantage of gaps where larger businesses cannot. SMEs also encourage a more inclusive form of growth, reducing inequality across regions and demographics as well as providing opportunities for skill development. They are considered an important channel for inclusion and poverty reduction, as they contribute to achieving both economic growth and social objectives like improving the quality of jobs for low-skilled workers or marginalised groups.

Where are we finding these SME enablers across the market? While the environment for these businesses has improved, there remain issues in areas such as high costs of tax compliance, lack of access to credit finance and training opportunities, and barriers to digitalisation. On the latter, the divide between incumbents and SMEs tends to be narrow in web presence or connectivity, but substantially larger in more niche and potentially business-enhancing areas such as cloud computing, big data or enterprise resource planning software. Access to such technology can eliminate costs in maintaining expensive hardware or software and allow SMEs to take advantage of big data without significant investment in technology or personnel.

Looking to the future, enabling SMEs to overcome these hurdles should allow them to grow and provide innovative opportunities in the transition to greener goods and services, contributing to a more sustainable future. A 2013 study by the Carbon Trust, for example, shows that in the UK, SMEs already represented more than 90% of clean technology businesses.

Business growth: IPOs in the US from 1999 to 2021



Source: Statista/PwC


IMPACTS
transition to lower carbon fuels – Making transportation
the healthcare system – Delivering
of supply chains and quality control

Sustainability and impact

Measuring impact 1: How we think about sustainable companies and the positive impacts they make

We aim to outperform the market by investing in sustainable companies and use our influence as shareholders to drive positive change. To summarise our investment process (set out in detail on pages 5 and 6), we are looking to find sustainable companies characterised as being:

- On the right side of positive trends in our economy to make it cleaner, healthier and safer (and enjoying structural growth as a result)
- Proactively managed and whose overall business is aligned with positive trends
- Profitable and likely to continue to generate good investment returns
- Where we believe the market has underappreciated this profitable growth

This is what drives our investment decisions, and our investment process is designed to embed these aspects into our stock selection.

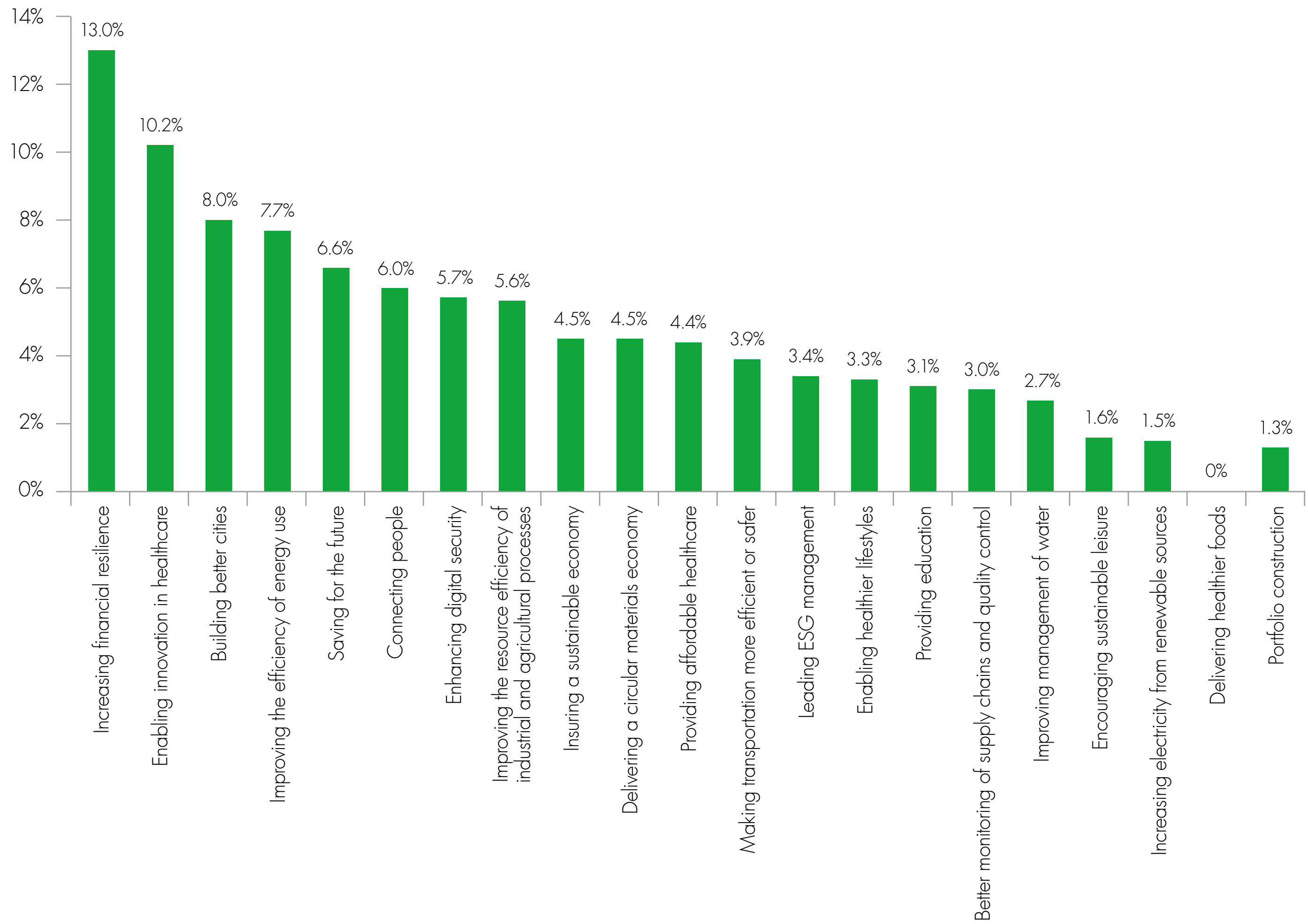
In terms of sustainability, the resulting portfolios are invested in companies that:

1) Are exposed to positive sustainable investment themes while avoiding structural decline
2) Have more sustainable products and services and are more proactively managed
3) Are subject to challenging engagement from us to improve how they are managed

Exposure of the SF funds to our Sustainable investment themes

As set out on page 6, we have identified 20 investment themes that help us to understand positive trends in the market and find companies exposed to structural (long-term) growth as well as avoiding those suffering structural decline. On average, our main SF strategies had the below broad weightings to these themes at the end of 2021; this demonstrates the diversified nature of our themes, giving the funds exposure to many different areas of our economy expected to experience secular growth.

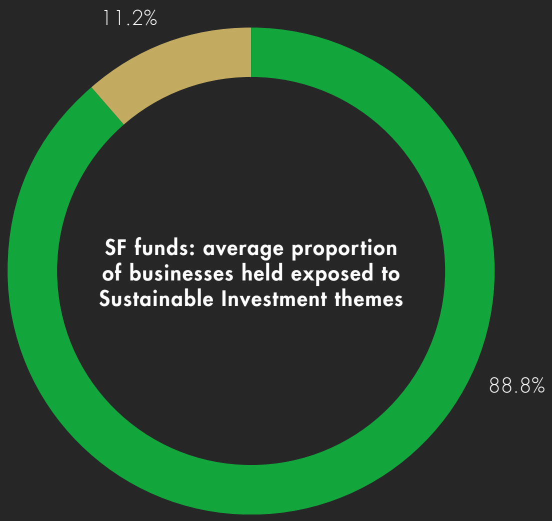
Exposure to Sustainable investment themes is disclosed for each fund individually and available from our website at liontrust.co.uk.



Source: Liontrust/Factset, 31.12.21: simple average exposure for SF UK Growth, SF European Growth, SF Global Growth and SF Corporate Bond funds.

For a company to be associated with one of our Sustainable themes, it needs to have at least 25% of the business' revenues exposed to the theme. On average, the main SF strategies have very meaningful exposure, with 88.8% of companies held greater than 50% and 11.2% greater than 25%.

This is disclosed for each individual fund and available from the Liontrust website.



Strongly exposed to theme (>50% of business)

Moderately exposed to theme (>25%, <50% of business)

Source: Liontrust/Factset, 31.12.21. Simple average exposure for SF UK Growth, SF European Growth, SF Global Growth and SF Corporate Bond funds.

Measuring impact 2: The overall sustainability of the businesses in which we invest

We measure a company's overall sustainability using our Matrix ratings. This captures the net contribution to sustainability from a company's products and services as well as how proactively the management team is handling its interactions with the environment and society to maximise positives while minimising negative externalities. For the main SF funds, the weighted average matrix rating is close to B2. This demonstrates how the funds are investing in companies whose products and services are better than the median, and this is also true for the quality of the management teams who are running their business more proactively – in terms of sustainability – than the market. We believe this is where the best opportunity set lies for investors, and we avoid areas of the market with less sustainable products and reactive management (the black area of the matrix below).

Source: Liontrust, 31.12.21

The weighted average Matrix rating is disclosed for each fund and is available from the Liontrust website.

We are often asked why we choose to have our own rating system rather than using one of the many options available from third-party ESG data providers. The reason we maintain our own system, and use our own discretion, is that we often disagree with ratings from third-party providers because we believe different aspects of a business are important when assessing sustainability. We do use third-party providers as we find their research interesting and their collated data useful, but this is a starting rather than the end point of our analysis.

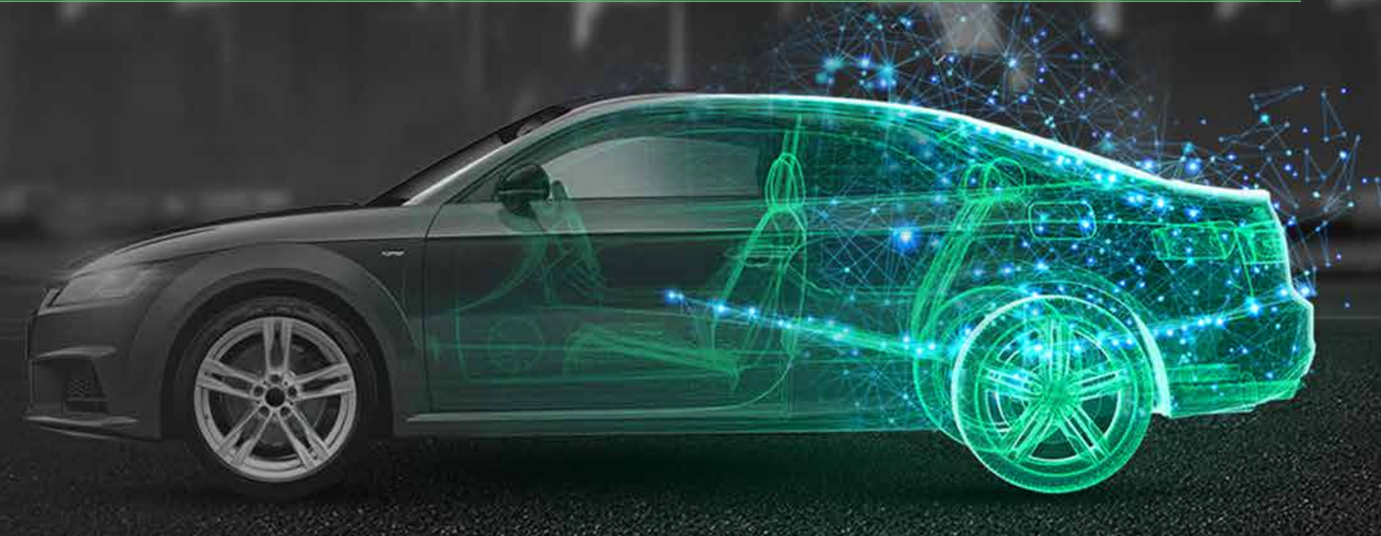
There is also no universally agreed linear measure of sustainability, and we believe drawing our own (often different) conclusions avoids taking third-party analysis at face value in what will inevitably become a commodity where the only barrier to use is what it costs.

Measuring impact 3: Alignment of the SF funds with the UN's SDGs

We understand that investors want additional information on impact and therefore also disclose how our Sustainable themes are aligned to the United Nations' Sustainable Development Goals (SDGs) at specific performance indicator level. Each of our themes is limited to one main SDG, although, in reality, there are overlaps and most companies are exposed to helping meet more than one goal.

Investment themes mapped to primary SDGs

Our Sustainable Investment theme	Sustainable Development Goal
Delivering healthier foods *Enabling healthier lifestyles* *Enabling innovation in healthcare* *Providing affordable healthcare* *Encouraging sustainable leisure*	3 Good health and well-being
Providing education	4 Quality education
Improving management of water	6 Clean water and sanitation
Improving the efficiency of energy use *Increasing electricity generation from renewable sources*	7 Affordable and clean energy
Increasing financial resilience *Insuring a sustainable economy* *Saving for the future*	8 Decent work and economic growth
Improving the resource efficiency of industrial and agricultural processes *Connecting people* *Enhancing digital security*	9 Industry, innovation and infrastructure
Building better cities *Making transportation more efficient or safer*	11 Sustainable cities and communities
Delivering a circular materials economy *Better monitoring of supply chains and quality control*	12 Responsible consumption and production
Leading ESG management	Multiple SDGs, depending on company operations



SF funds' exposure to primary SDGs

SDG: 3
Good health
and well-being

SDG: 4
Quality education

SDG: 7
Affordable and
clean energy

SDG: 8
Decent work and
economic growth

SDG: 9
Industry, innovation
and infrastructure

SDG: 11
Sustainable cities
and communities

SDG: 12
Responsible growth and
consumption

Source: Liontrust, average weight of SDGs as mapped to our themes for SF UK Growth, SF European Growth (ex UK), SF Global Growth and SF Corporate Bond funds as at 31.12.21 (unweighted simple average).

How our themes are aligned to the SDGs where we have most exposure

Decent work and economic growth (SDG #8)

We have three themes aligned to this SDG to promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all.

Increasing financial resilience: We believe a resilient financial services sector is necessary for economic well-being through utility-like provision of banking, lending and effective ways of saving for the future, as well as mitigating risks through insurance. This does not mean any company in the financial sector is automatically investable but we do see positive ways they contribute to society when appropriately and proactively managed. This is aligned with the SDG Key Performance Indicator 8.3 to encourage growth of business through access to financial services.

PayPal is a US-based company that makes transacting online easier and safer for consumers and businesses. Identity theft and fraudulent transactions are significantly lower on PayPal than its competitors, and the value we see from this business should come from a long runway of growth amplified by the excellent position the company has created for itself.

Insuring a sustainable economy: We believe insurance can spread the risk faced by an individual or corporation and makes a beneficial contribution to society.

Prudential is predominantly a life and health insurer, listed in the UK and focusing on growth in Asian markets. As such, it is bringing insurance to those who have not had access to it before and those unlikely to be supported by the state.

Saving for the future: We see a growing need for people to be able to get good advice and choose appropriate investments to ensure they have saved enough for retirement. Failing to invest for the future and relying on state-funded pension schemes will result in a significant drop in quality of life as government finances come under increasing pressure, exacerbated by demographic shifts towards a higher proportion of people past working age.

Avanza is a Swedish savings platform in an underpenetrated market, providing clear benefits to society by helping individuals manage their savings in a cost-effective manner. This company is proactive on sustainable investment products, having decided to go with an opt-out mechanism that means over 90% of the funds its clients use are Morningstar sustainability rated three globes or better.

Industry, innovation and infrastructure (SDG #9)

We have three themes aligned with this SDG to build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation.

Improving the resource efficiency of industrial and agricultural processes: We like companies that provide products or services that help to make industrial processes more resource efficient, as well as safer for workers and users. We see investment opportunities in software and systems that help implement life-cycle design (including the disposal of products) and manage supply chains, and in the automation of factory processes to remove repetitive or dangerous mechanical tasks.

AUTODESK.

Autodesk is a leading software business, listed in the US, which serves the global construction and manufacturing industries. It is bringing technology to areas of the global economy that have been nascent in terms of adoptions, such as manufacturing design and particularly for construction and building sites. The global construction industry is in the midst of an infection point, as traditional paper architectural designs are replaced by digital designs on devices.

Enhancing digital security: As more of our lives and critical services are carried out online, we need to protect the data from theft. Digital security helps to make this growing area of the economy secure.

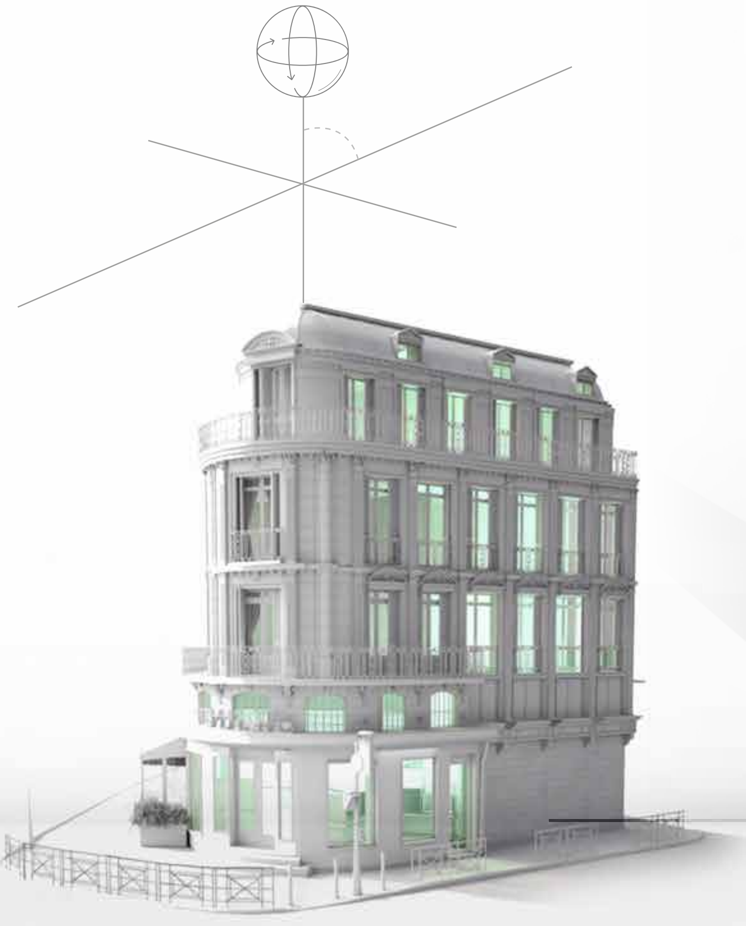
paloalto® NETWORKS

Palo Alto Networks provides technology to protect our digital way of life. Its firewall product is consistently rated the best by Gartner and the company achieves high customer satisfaction scores, giving us confidence it will succeed in making online information only available to those permitted to see it.

Connecting people: We believe access to easy communication tools and information, increasing amounts of which are online, is a requisite for a more sustainable economy.

helios towers

Helios Towers is the UK-listed owner and operator of telecom infrastructure assets. The company's assets are in high-growth African markets, and its strategy is to grow assets in underserved markets and contribute to providing reliable access to communications in these countries. This will enable telecom operators to make their networks denser to offer the greater capacity necessary to meet increased demand for mobile data services.



Good health and well-being (SDG #3)

We have five investment themes aligned with this SDG to ensure healthy lives and promote wellbeing for all at all ages. These include:

Enabling healthier lifestyles: Companies that promote healthier lifestyles, principally through increasing activity, taking exercise and sport, help meet the same Key Performance Indicator 3.4 of this SDG.

The Gym Group is the UK's second-largest and lowest-cost gym group and promotes physical activity through the provision of exercise classes, weights and cardio equipment at less than half of the price of traditional gyms. This makes membership more affordable for the broader population and helps to improve public health.

Providing affordable healthcare: Companies that help to deliver affordable, positive patient outcomes in managing disease also aid this goal.

IQVIA is a US company that uses data to design and run trials for new drugs before they get approved for general use. Designing these trials is complicated but IQVIA's innovation means drugs can be used quicker and cost less to test.

Enabling innovation in healthcare: Companies whose products or services promote innovation within healthcare are also helping towards this SDG by either coming up with new, more effective ways to treat diseases, providing essential equipment or services for biotechnology research, or through software to help make treatments more effective.

Evotec facilitates innovation in healthcare through its network of 350,000 scientists and shared platform. The company claims it can reduce costs and time to discover a new drug by up to 30% and 50% respectively. It also uses modelling that is 85% effective versus 50% effective animal testing, which paves the way for better, faster efficacy testing and a reduced need for the latter.

Sustainable cities and communities (SDG #11)

We have two themes aligned with achieving this SDG to make cities and human settlements resilient and sustainable.

Building better cities: Shelter is a basic human requirement and companies that build quality, affordable homes or key infrastructure needed in cities are helping to provide this.

Places for People is an issuer we hold in the Liontrust SF Corporate Bond Fund. This company funds the provision of social housing, which is a long-term positive for society.

Making transportation more efficient or safer: We like the modal shift in transport away from private car travel onto public transport, which reduces congestion, pollution and is safer.

National Express operates bus, coach and rail services and these mass transport solutions are far more efficient than individual cars, leading to lower emissions, less congestion and improved safety. Typically, a bus removes 30 cars from roads. The company is proactively managed and has exceptionally strong performance on safety, with a leading position in moving away from combustion engines in its fleet.

Affordable and clean energy (SDG #7)

We have two main themes aligned with achieving this SDG to ensure access to affordable, reliable, sustainable and modern energy for all.

Increasing electricity generation from renewable sources: Substituting coal-intensive fossil fuel electricity generation with renewable power sources reduces carbon emissions as well as providing a cost-effective means in some off-grid situations to connect people to cheaper, more reliable power sources.

Atrato Onsite Energy is a renewable energy infrastructure fund that invests in and instals solar modules on industrial-use roofs in the UK and then contracts the sale of electricity from this to the occupier. The result is more lower-carbon electricity generated and lower power costs for customers.

Improving the efficiency of energy use: We see many ways of making energy cheaper by reducing wasted energy while also cutting emissions through more efficient use. This goes across many areas of the economy and includes building insulation, efficient lighting, energy-efficient climate control, travel and industrial processes. Companies that provide services or equipment, particularly in upgrading the power grid network to be able to deal with changing production and consumption patterns of electricity, are an important part of achieving affordable clean energy.

SDCL Energy Efficiency Income Trust PLC is listed in the UK and invests in projects or assets that reduce the amount of energy wasted, thereby cutting energy bills for users and emissions. The projects owned cover a broad range of technologies globally, such as combined heat and power providing efficient heat and backup power to a London Hospital, cogeneration of heat and power in olive processing using olive wastes, and recycling waste gas technologies used in steel smelting in the US to make it more energy efficient.

Clean water and sanitation (SDG #6)

We have one theme aligned to this SDG, which pledges to ensure availability and sustainable management of water and sanitation for all.

Improving the management of water: Companies that can manage waste water treatment, or produce products or services that improve the efficiency of water distribution, are vital and in demand. Sanitation is a first line of defence against disease, much of which comes from contaminated water. We like companies that improve sanitation and give affordable access to clean water.

Ecolab, which is listed in the US, is the global leader in providing customers with technology that allows them to save key resources, particularly water and energy, in the industrial and hospitality sectors. From restaurants to steel mills, Ecolab's products and technologies significantly reduce water usage and save customers money, driving cost savings and efficiencies.

Quality education (SDG 4)

We have one theme aligned to this SDG, which pledges to ensure inclusive and equitable quality education and promotes lifelong learning opportunities for all.

Providing education: Education brings important benefits, including longer life expectancy, increased job opportunities and helping to stimulate economic growth, as well as leading to overall higher satisfaction in life. Companies providing education services offer vital knowledge and skills, which help to improve people's lives.

Unite is the UK's largest owner, manager and developer of affordable, safe and secure student accommodation, providing beds for more than 76,000 students with a pipeline to 2023 to add an additional 4,000 beds to its portfolio. Through offering affordable accommodation, it is enabling the provision of higher education, which drives greater levels of socioeconomic mobility as well as fostering research & development and innovation. Furthermore, the company also supports numerous initiatives to enable underprivileged students to attain higher education via free accommodation scholarships.

Measuring impact 4: The climate change crisis

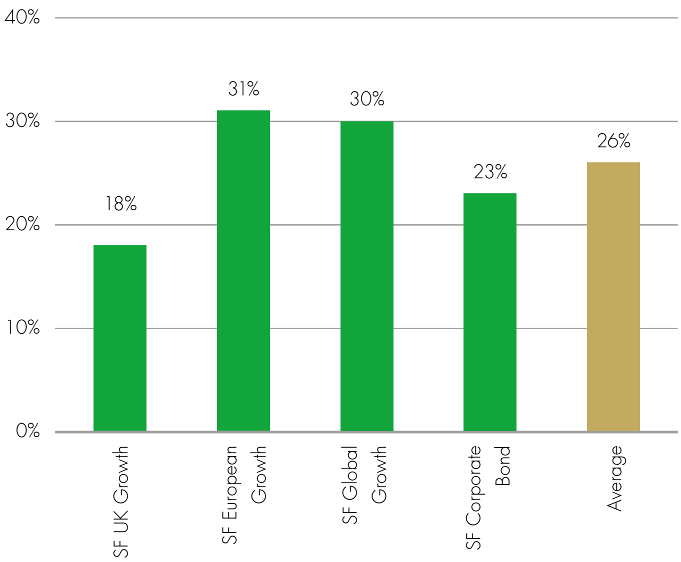
The world continues to grapple with the climate change crisis, and now is the time to accelerate the shift to an ultra-low carbon economy. The science is telling us we need to accelerate the pace of decarbonisation, as current progress and ambition both fall considerably short of meeting internationally agreed goals to limit average global temperature rises to less than two degrees centigrade, and ideally less than 1.5, in line with the Paris Accord.

We have been thinking about how climate change will affect our economy and how we can best position our investments for this since our SF funds launched 21 years ago. We believe the market continues to underestimate both the rate of change needed to decarbonise and the magnitude of the positive impact on companies helping this transition, as well as the structural decline in businesses continuing with carbon-intensive products and services where there are lower-carbon alternatives.

How does this affect our investment decisions?

First, we want to invest in companies helping to reduce emissions as they will experience significant growth. Of our 20 sustainable themes, all those associated with increasing resource efficiency will benefit from, and contribute to, the shift towards an ultra-low carbon economy. As well as using more renewables to generate electricity, equally important is reducing the amount of energy we waste, increasing recycling, improving how we manage water, making industrial processes more efficient, ongoing transport shifts, and the way we heat and cool buildings. On average, the SF funds have 26% invested in companies exposed to these better resource efficiency themes.

SF funds' exposure to better resource efficiency themes



Source: Liontrust/Factset, as at 31.12.21.

Second, we want to ensure the companies we own understand the magnitude of the energy transition and are managing their businesses in a proactive way that protects them from inevitably tightening regulations. We launched our 1.5 Degree Transition Challenge in early 2020 to engage with companies in our SF funds, encouraging them to increase their ambition to decarbonise and capture the benefits of doing so in an increasingly carbon constrained world.

Finally, there are some industries, no matter how proactively managed, on the wrong side of this transition and these will experience secular decline in demand for their carbon-intensive products or services. We choose to avoid areas such as fossil fuel extraction and production, internal combustion engine car manufacturers, airlines and energy-intensive businesses that are not positioning themselves for a lower carbon world.

Initial findings from our 1.5 Degree Transition Challenge

What, specifically, are we asking companies to do?

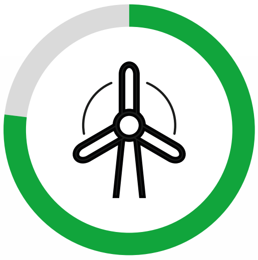
- To be more ambitious in emissions reduction targets to make their pace of decarbonisation consistent with what the science is telling us: requiring a 50% reduction in absolute emissions this decade.
- To show front-loaded timely targets for this: for example, a 50% reduction in direct emissions by 2030 based on a suitable baseline and a 25% decrease by 2025.
- To concentrate on reducing absolute emissions before considering offsetting at any large scale. We believe offsetting can be a distraction, and there are not enough legitimate carbon offsets of the scale required.
- To understand the largest sources of indirect (scope 3) emissions for their business and identify opportunities to reduce these aggressively.
- Something we are not asking is for companies to divest automatically from the more carbon-intensive parts of their business, especially if this is enabling customers to reduce emissions by using their products. Instead, we want businesses to innovate and come up with creative ways to operate in step with an ultra-low carbon economy.

Based on our work so far, around a quarter of companies with which we have engaged have absolute decarbonisation targets consistent with 1.5 degrees and a further 9% have committed to 2 degrees, which means a third overall are aligned with the Paris Accord. This obviously means two-thirds do not, at present, have targets in line with the science but this is moving quickly, with many demonstrating positive momentum (for more details, see page 38).

The biggest challenge is in achieving absolute reductions (cutting total direct emissions coming out of a business), as opposed to reducing the carbon intensity (the amount of carbon equivalent emitted per unit of sales or other measure such as cashflow or profit). This is especially challenging in fast-growing companies for which carbon intensity targets have to be significantly higher than how much the business is growing for there to be any reduction in absolute emissions.

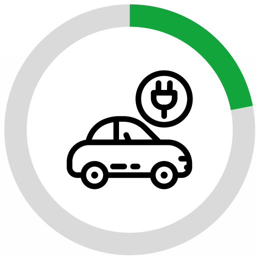
Responding in a timely manner to the climate crisis is important but we have to bear in mind climate change also has a social dimension. Many people work in industries facing formidable change and they must be able to afford to live a fulfilled life in an ultra-low carbon economy. We must remember to solve not only for the best climate change outcome but also ensure we use this as an opportunity to reduce inequality and help alleviate fuel poverty. If people do not willingly move with the energy transition, it will fail.

Active mitigation of carbon exposure – SF funds' average



77%

less carbon emitted than comparator indices



22%

of the portfolios invested in companies offering cleantech solutions

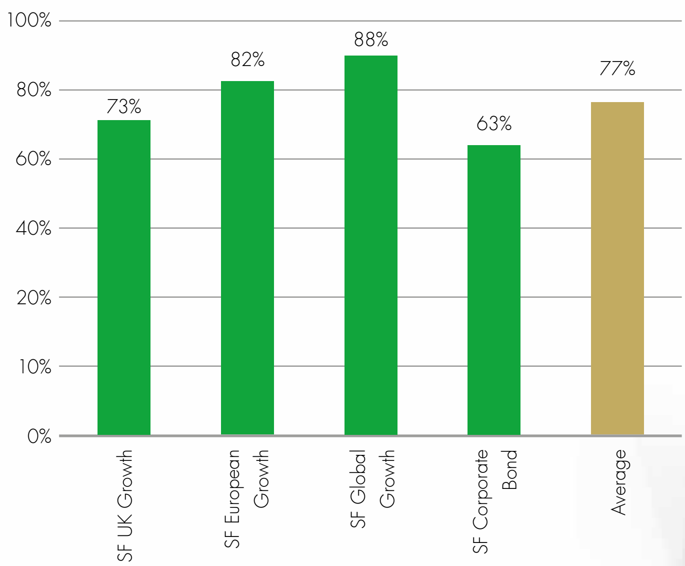
0%

invested in fossil fuel extraction

Source: MSCI Carbon Analytics Report, December 2021; average across SF UK Growth, SF European Growth, SF Global Growth and SF Corporate Bond Funds. For carbon emissions coverage data, see the chart below.

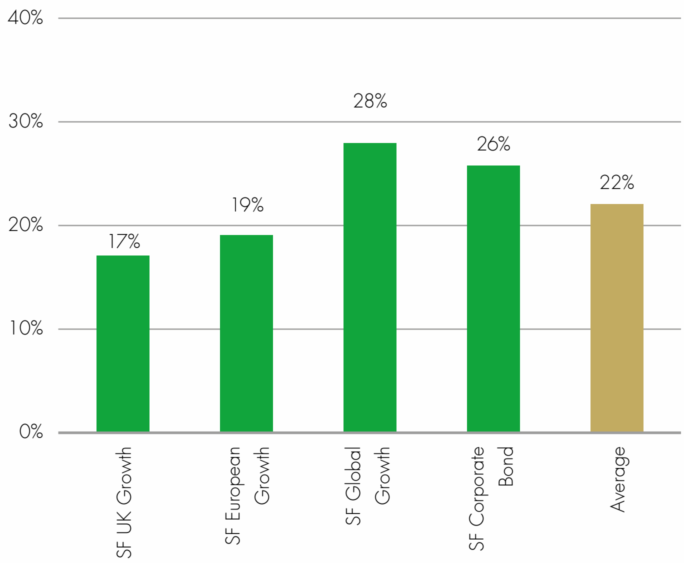
We have been disclosing the portfolio carbon emissions for our single strategy funds since 2012, which is carried out independently using MSCI Carbon Analytics. On average, the SF funds emit 77% less carbon dioxide than the markets in which they invest, have 22% exposure to companies whose products help to reduce emissions, and hold 0% in companies exposed to the extraction and production of fossil fuels (such as coal miners and oil and natural gas exploration and production).

Average carbon emissions **reduction** in SF funds compared to mainstream benchmarks



Source: MSCI Carbon Analytics/Liontrust, 31.12.21. tCO2e/$m invested (uses direct emissions, scope 1+2) from investee companies, cash and government bonds are excluded. For SF UK Growth, carbon emissions data available for 76.2% of the fund and 100% of the MSCI UK Index benchmark. For SF European Growth, carbon emissions data available for 88.3% of the fund and 99.8% of the MSSCI Europe ex-UK Index benchmark. For SF Global Growth, carbon emissions data available for 94.5% of the fund and 99.8% of the MSCI World Index benchmark. For SF Corporate Bond, carbon emissions data available for 86.4% of the fund and 95.8% of the iBoxx Sterling Corporates Index benchmark. All figures as at 31.12.21.

Average exposure of SF funds to companies offering cleantech solutions



Source: MSCI Carbon Analytics/Liontrust, 31.12.21.

In addition to funds emitting less carbon, there are important positive attributes of low-carbon portfolios. Current climate change policies, even if enacted, do not go far enough to limit the global average temperature rise agreed in the Paris Accord. We believe there will be an inevitable global tightening of regulations to limit the amount of greenhouse gas being emitted, and in the event of a tax on carbon, companies that can pass this on to customers will not face a negative impact on margins (and profitability). In contrast, companies unable to pass these costs on to clients will have to bear it themselves. The very low carbon emissions coming from businesses in the SF funds mean these portfolios will have more resilient margins as carbon-related regulations tighten.

Fund-specific data on emissions are included in our SF funds' sustainability and impact reports, which are updated every six months and available at liontrust.co.uk.

COP26 feedback and the road to 27

A key event last year was COP26 in Glasgow, and our report card of it reads some good, some bad and some moderate – with the latter covering the event's central goal of keeping the 1.5 degrees alive.

To give a quick history lesson, 2009's COP15 in Copenhagen was widely deemed a washout apart from introducing the broad target of keeping maximum temperature rises to below 2 degrees compared to pre-industrial levels. At that point, when widespread acceptance of the science behind climate change was still some distance away, average global temperatures had increased around 0.8°C from the 1880 baseline and were on the way towards a 3.5°C rise by the end of the century. If anyone is thinking these are small numbers, a degree here and there can mean the difference between another ice age or not.

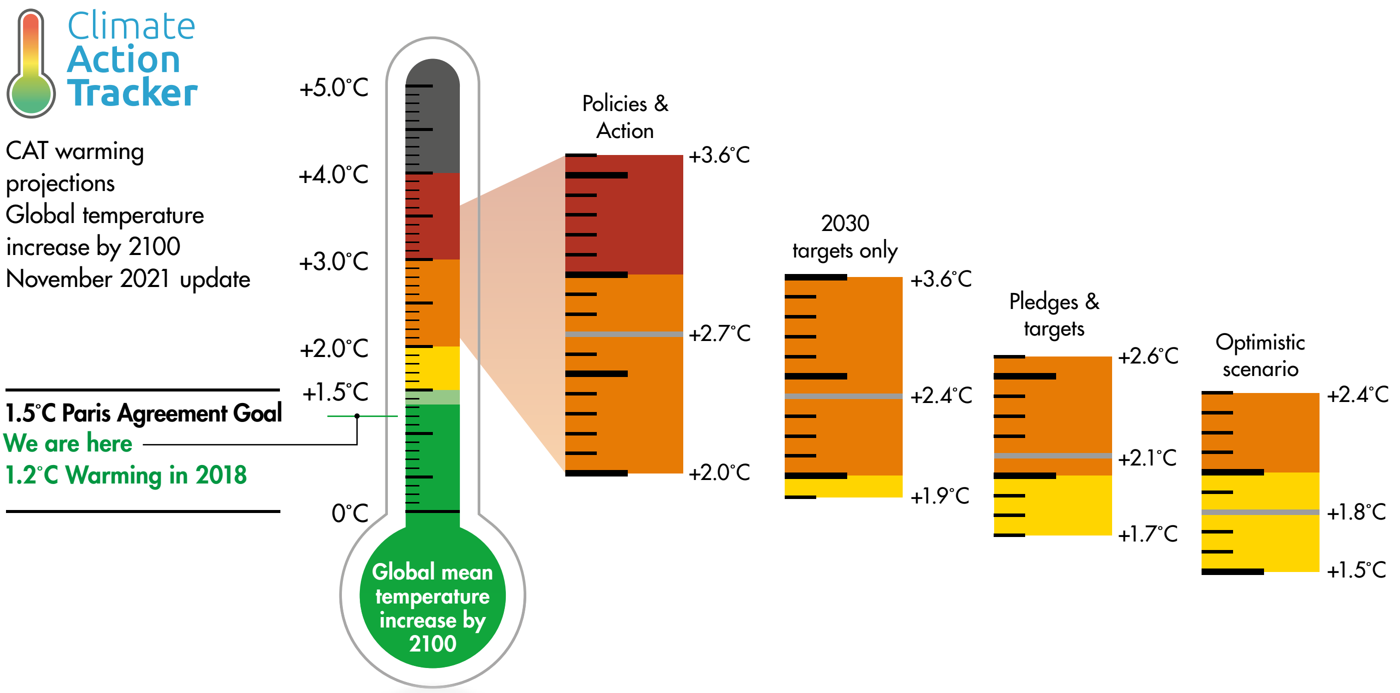
If we fast forward to 2015, COP21 in Paris is seen as the most successful so far, in that we finally saw a formally agreed goal to limit average rises to under 2 degrees, and ideally less than 1.5, by 2100. Countries were also asked to submit commitments on emissions reductions by 2030, called Nationally Determined Contributions (NDCs), that were to be reviewed five years later at COP26, which was delayed a year by Covid.

The world has now moved up to 1.2°C warming and if we consider the most optimistic scenario, which assumes full implementation of all announced targets including net zero, long-term strategies (LTS) and NDCs, we would be under the Paris target of 2 degrees, at 1.8°C, by 2100. Taking a more pragmatic view, real-world action based on current policies would see us well above the Paris Accord by that point at 2.7°C, which suggests growing urgency is required at the remaining Climate Change COPs running up to 2030 – starting at this year's 27 in Sharm El-Sheikh – and for those tightening regulations to reduce emissions globally over the next few decades.

As with many of the figures underlying our sustainable investment themes, data on climate change – particularly the current 1.2°C increase in average global temperatures – are alarming and the trajectory of GHG emissions does not look to be turning. Under the surface, however, there is evidence of an ongoing energy transition, and we always stress that change is both non-linear and tends to happen quickly.

Innovation and scale have driven down the cost of renewable technology, from solar through wind to lithium-ion batteries, translating into exceptional demand growth. From being prohibitively expensive a decade ago, solar energy is now the lowest-cost option available in the US, cheaper even than fracked natural gas. Alongside this demand growth for renewables has come demand destruction for high CO2-emitting areas: coal-fired electricity generation in the US has fallen 61% since 2008, for example, and dropped below nuclear in 2020 in terms of energy share.

Many of our sustainable themes are therefore linked to the shift away from fossil fuels, including energy and industrial efficiency, renewable energy and more circular economies, but also how we build our cities, how we feed ourselves and how we finance the investment needed to enable a rapid energy transition.



Source: Climate Action Tracker, November 2021, www.climateactiontracker.org. All use of company logos, images or trademarks in this presentation are for reference purposes only

Measuring impact 5: **Third-party models**

In our previous Annual Reviews, we have discussed client demand for impact measures and the challenges of proving 'additionality', along with the recognition that all businesses have both positive and negative impacts. We want to be confident in the information we provide to estimate these measures and there remains no standardised approach in this rapidly evolving discipline. Impact reporting is interesting, needed, constantly changing and can be confusing.

Despite this confusion, we continue to work on better ways to measure and disclose the environmental and social performance of our investments. Ultimately, we believe the terminology used to describe environmental and social performance is not that important; call it impact or not as it continues to change. What is important is how we communicate it and, critically, how it guides our investment process and influences the decisions we make.

We are committed to developing ways of measuring impact and meeting demand from clients who want to know what influence their investments are having on the real world. We will continue to review the growing number of approaches and are encouraged to see these becoming more detailed; some are much closer to identifying the specifics of companies and having measures based on revenues from individual businesses rather than at industry level. The latter misses out on the vital differentiation between companies in the same industry and how they can be very differently positioned to contribute to, or detract, from our common goals.

Where we find a third-party impact assessment that is broadly consistent with our approach and helps clarify what the impact is, we will make this information available. However, we want to be confident in what we claim about our funds and ensure we do not overstate or make what we regard as tenuous assumptions in the goal of finding real world impact indicators.

We are also responding to increasing regulation on disclosure requirements from the European Sustainable Finance Disclosure Regulation (SFDR). The SF funds sold into Europe are classified as Article 9 as sustainable investment is a major part of the objective. We anticipate increasing disclosure for all the SF funds, and UK equivalent regulations on sustainable investment disclosure are being finalised.

We continue to publish fund-specific sustainability and impact reports, updated every six months, and expect to include more sustainability-related data in these.

ENGAGEMENT

Our approach to engagement and voting

Engagement is integral to how our Sustainable Investment team ensures it invests in high-quality companies. Engaging gives us greater insight and helps to identify such leading companies but is also used as a lever to encourage better practices, challenging and encouraging them to proactively manage their business for the benefit of long-term shareholder value.

We meet companies face to face but also correspond through emails, calls and letters. Depending on the specific issue, our interaction with a company might include senior management, sustainability teams or experts within the organisation. We also engage collaboratively with other investors on initiatives that are aligned with the Liontrust Sustainable Investment team's engagement priorities and where we believe we are more likely to succeed collectively. In some instances, we lend our support to collaborative initiatives that can include targeting companies not held in our funds.

The team also conducts considered annual voting for companies held in the SF funds and we are very active owners. Our voting policy is publicly available and our voting decisions and rationale are also disclosed.

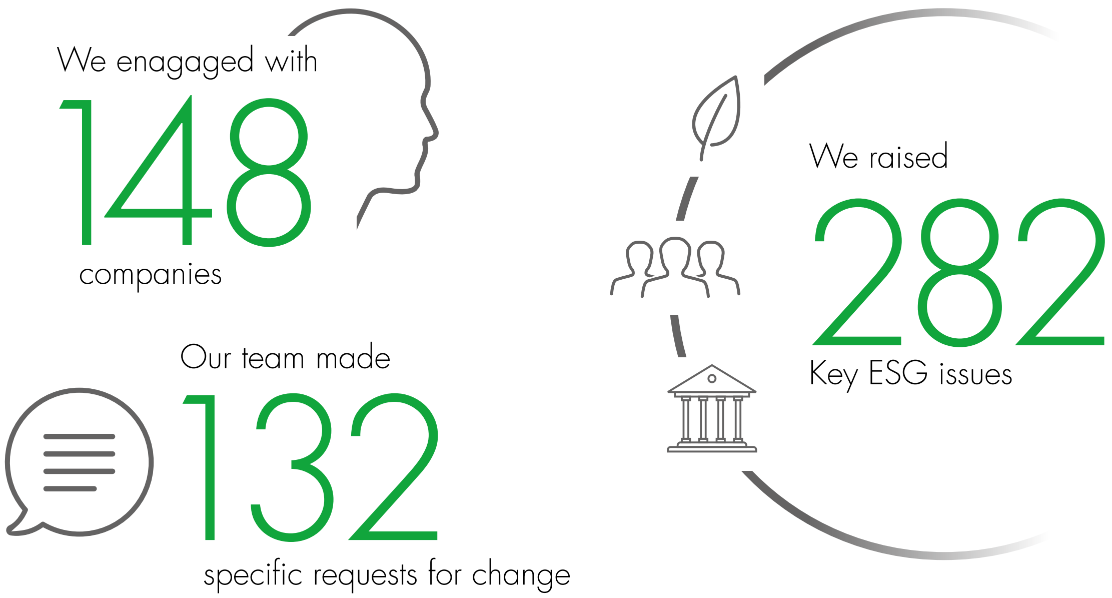
We record our engagement with companies, monitor our success and report on our activities to clients. In 2021, we engaged with 148 companies and raised 282 ESG issues; about two-thirds were related to proactive initiatives and the remaining third to reactive issues.

Our team made 132 specific requests for change, and we have so far identified that 43 (33%) of these have been either actioned or committed to by companies. We will be following up on requests that have not yet been actioned over the course of 2022.

2021 Annual Engagement Summary Table

Total number of ESG issues raised (E, S, G)		**282**
Environmental	Climate crisis, Water management	55
Social	Supply chains, Employee issues	119
Governance issues	ESG and impact disclosure, Corporate tax	81
Corporate Governance	Remuneration, Auditors, Diversity	27

Total number of ESG issues raised (Priority vs. Reactive)	**Examples include**	**282**
ESG issues raised – Priority initiatives	Climate crisis, Circular economy, Biodiversity, Corporate diversity, Workforce well-being, Transition to Sustainable Investment	190 (67%)
ESG issues raised – Reactive engagement	Controversies, ESG impacts, Supply chains	92 (33%)



2021 progress and next steps

We prioritised six proactive engagement initiatives in collaboration with our Advisory Committee at the beginning of 2021. The following details some of the highlights across these areas. In our experience, continued engagement over a longer time period is more likely to achieve better engagement outcomes than over a yearly reporting cycle, so these build on work we started in 2020.

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Climate Crisis: 1.5° Transition Challenge	To encourage companies to adopt strategies to reduce absolute carbon emissions at a rate consistent with limiting global warming to 1.5 degrees. We want to ensure companies can change in a timely, just and profitable way and have robust strategies and targets in place to achieve this.	• Speak to all investee companies about their decarbonisation strategy and targets. • Understand the SF funds' alignment with the Paris Accord. • Publish our findings ahead of the United Nations Climate Change Conference of Parties (COP 26).	• We met with 36 companies for detailed discussions on their decarbonisation strategies. • 24% of companies are aligned with the 1.5 degree target and a further 9% with 2 degrees (as at November 2021). • We published our report on 1.5 Degree Transition Challenge in November 2021.	• Continue to speak to investee companies about decarbonisation strategies. • Monitor performance on near-term absolute emissions reduction targets. • Increase the number of investee companies that are aligned with the Paris Accord. • Challenge banks on financing the transition.

For details on our work on the 1.5° Transition Challenge, see page 32. The headline numbers are summarised below.

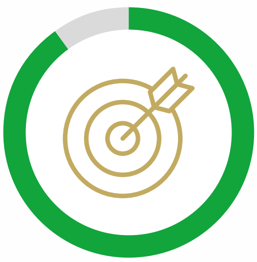
Contacted **71** companies overall

Met with **57** of these for detailed discussions about decarbonisation targets

This is **40%** of companies in which the SF funds invest

Of these

33 companies are responsible for **90%** of emissions



1/3 committed to 1.5 or 2 degrees by 2030

2/3 are involved in the Science Based Target Initiative (SBTi)

Source: Liontrust, September 2021

Case Study: Helios Towers

Held under our *Connecting people* theme, Helios owns and operates telecommunications towers and related passive infrastructure. The company provides tower site space to large MNOs and other fixed wireless operators, who in turn supply wireless voice and data services to end-user subscribers.

We met Helios several times in 2021 to discuss our 1.5 Degree Transition Challenge initiative. We covered the company's thinking ahead of it setting climate reduction targets, and it was clear from our initial meeting that Helios has ambitions to take a leadership position and is devoting significant resources to this. Helios has recently submitted a response to the Carbon Disclosure Project; we met the company to understand the timeline for setting emissions reduction targets, and were informed of plans to publish targets in November 2021. We were asked to input into the company's high-level stage of identifying and assessing climate risks.

We subsequently attended Helios's carbon reduction roadmap event and had a further meeting with those responsible for executing the strategy to gain additional clarity. Helios's roadmap for intensity targets is clear and we understand the assumptions and technologies the company is relying on to achieve these.

Positive meetings over the year affirm our confidence in the management of complex issues, and it is reassuring to see the company meet this challenge in a clear and practical way. Moreover, its lower carbon investments will see Helios shift from diesel to more hybrid technology, which could mean scope for margin improvement over time. Alongside other conversations with Helios over the year, we upgraded the management quality rating.

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Reversing the collapse in biodiversity	We will engage with companies in our funds exposed to key biodiversity impacts either in their direct operations or through their supply chains. We will encourage these companies to do more to protect and promote biodiversity, and to invest in nature-based solutions and technologies. We aim to collate examples of best practice and to see improvements in policies and practice that show how business can thrive alongside enhanced biodiversity.	• Increase the scope of this initiative to speed up the transition to a circular economy more widely, rather than just focusing on plastics. • Explore approaches beyond company engagement to reduce the burden of plastic pollution.	• We did not make good enough progress on this initiative but towards the end of the year set a strategy to address this in 2022.	• Create a new focus on Preserving and restoring nature. • Encourage investee companies to report on natural capital impacts from their activities, products and services, and gauge the level of preparedness for increased reporting, such as the Taskforce for Nature-related Financial Disclosures (TNFD). • Encourage investee companies to adopt policies and programmes that preserve and restore nature and promote biodiversity. • Explore new tools to better understand companies' dependencies on natural capital and how this might impact financial returns. • Explore collaborative engagement, such as the Biodiversity Pledge.

Case study: Downing Renewables and Infrastructure Trust PLC

Held under our Increasing electricity from renewable sources theme, Downing Renewable and Infrastructure Trust is a fund that owns renewable electricity generation assets such as wind, solar and micro-hydro power, and plans to invest in Geothermal power. These types of funds play a crucial role in owning renewable assets, which are displacing higher carbon alternatives off the electricity grid and therefore helping us move towards an ultra-low carbon economy.

We clarified the company's small hydro assets in Scandinavia and how they are managed. These are small, 'run of the river' assets, which are well established (some having been in existence for 100 years) with ecological systems around them. Downing is participating in the Swedish Nation Plan to maintain these assets, reducing the negative impacts through the addition of fish ladders and other best practice solutions. This meeting gave us confidence that these assets are suitable for the SF funds and we took a position.

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Encouraging a faster transition to a circular economy	We want to ensure companies are looking for ways to reduce their impact through circular practices. We will engage with companies to reduce the amount of single-use plastics and ask more about inputs, waste policies and the potential for more circular practices within their business models.	• This was a new initiative for 2021.	• We began exploring ways that we can encourage circular practices in supply chains. Our theme identified companies for the funds. • We did not manage to engage proactively on the issue of plastic waste with investee companies.	• This initiative will be rolled into the new initiative on Preserving and restoring nature, so our aims for 2022 are the same as for Reversing the collapse in biodiversity.

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Increasing corporate diversity	We believe companies that are more diverse are better able to prosper over the long term so we are engaging to encourage greater diversity. We are looking at gender and ethnic balance at a board level, senior positions and within the workforce, as well as at efforts to increase transparency and reduce pay gaps.	• Step up our voting pressure to increase corporate diversity in three ways: 1. Raising our threshold for voting from 30% to 33% female boards 2. Increased stringency when it comes to voting against rather than abstaining 3. Targeting companies with a lack of ethnic diversity	• We increased the Board gender threshold to 33%. • We voted against the Chair of the Nomination Committee due to a lack of gender diversity on the Board for 10 companies. • We withheld our support on the re-election of the Chair of the Nomination Committee of six investee companies. • We voted against five companies due to a lack of sufficient ethnic board diversity and abstained on one.	• Step up pressure by voting against a wider set of companies where there is a lack of ethnic diversity. • Look at gender and ethnic pay gap data for investee companies and engage on action plans to address imbalances. • Find and encourage best practice examples of wider D&I policies and practices, such as LGBQT+ and Neurodiversity.

In 2021, we increased our voting threshold from 30% to 33% for female boards and continued to see good progress on increased representation. We voted against the Chair of the Nomination Committee due to a lack of gender diversity on the Board of 10 companies and withheld support on re-election for a further six. This means we voted against or withheld support on 11% of a total of 147 votable meetings due to a lack of gender diversity. We voted against the same resolution due to a lack of ethnic diversity on the board of five companies over the year.

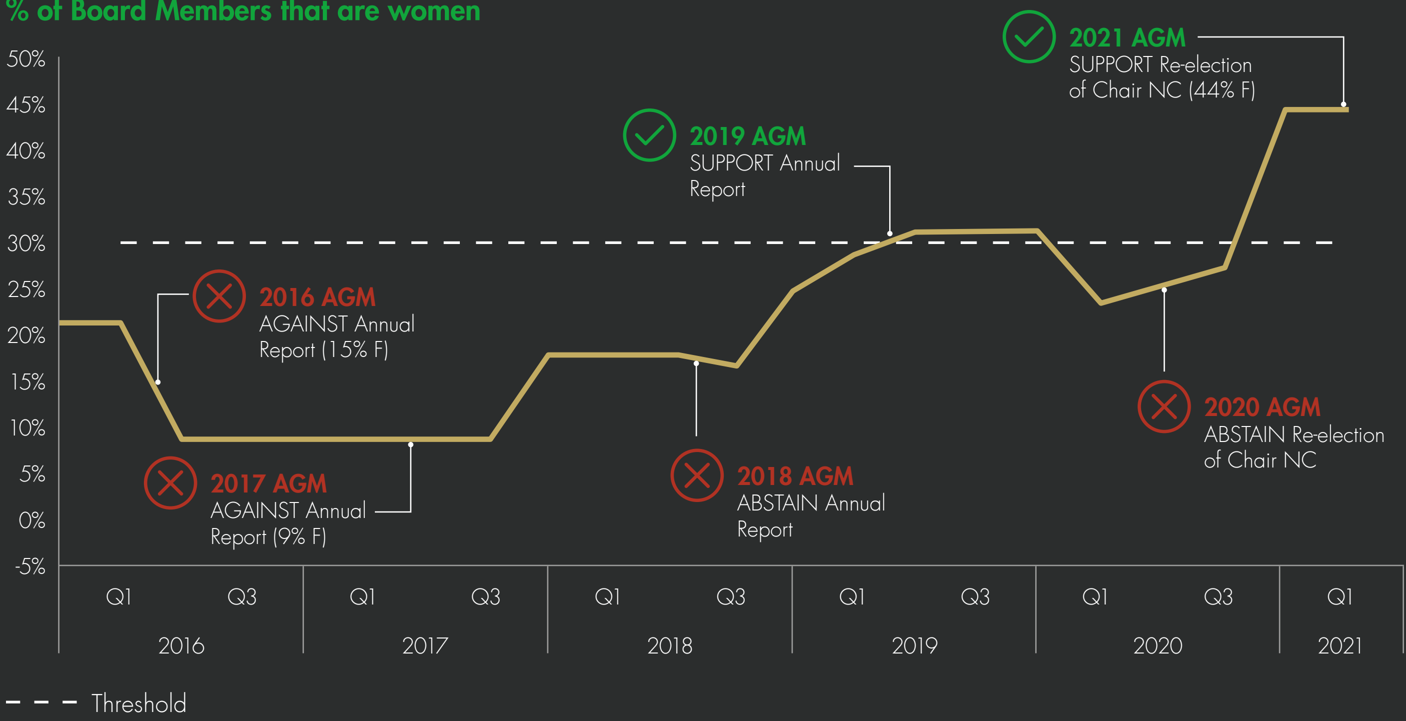
Overall, we have now targeted 40 companies when Board gender diversity was lacking from 2016 to 2021. Of these:

Board gender diversity	**Number of companies**	**Average % of women on Board (before we introduced our voting policy)**	**Average % of women on Board (after 2021 AGM)**
Improved and now have over 33% female representation	23 (58%)	21%	39%
Improved but still under 33% female representation on Board	12 (30%)	18%	28%
Did not improve	4 (10%)	22%	22%
Deterioration	1 (3%)	27%	25%

We were also finally able to support the re-election of the Chair of the Nomination Committee at the AGMs of several companies in 2021, having previously withheld support due to a lack of Board gender diversity. Adobe, Intuit, JLEN Environmental Assets Group and London Stock Exchange Group were all able to meet our higher threshold of 33%.

Case study: London Stock Exchange

% of Board Members that are women



Where NC = Nomination Committee and F = % Board Members Female
Source: Bloomberg data, Liontrust Voting, 2016 to Q1 2021. AGM: Annual General Meeting

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Ensuring worker well-being	How companies manage and look after their workforce through direct operations and workers further down their supply chains can directly affect corporate reputation and overall business performance. We will engage to encourage companies to offer decent work and pay living wages and to ensure they mitigate risks, protect workers' rights and maximise the opportunities to support employees. We will also encourage companies to use their influence to drive forward best practice further down their supply chains. Engagement will cover companies' response to and management of the pandemic, including workforce adaptation, Covid-19 safety, redundancies and supply chain impacts.	• Encourage investee companies to respond to the 2021 Workforce Disclosure Initiative (WDI) Survey. • Pay particular attention to how companies deal with worker health and safety as we move through the Covid-19 pandemic.	• We wrote to 78 companies to encourage them to participate in the WDI. • We thanked 11 companies that had already stated they would be participating. • Several of our holdings won WDI Transparency awards, including Puma, Standard Chartered and St. James's Place. • We engaged with six companies on Covid-19, focusing on those that were most severely impacted or exposed.	• Request investee companies complete the WDI 2022 Survey. Increase the proportion of investee companies participating in the 2022 survey (in 2021, it was 20%). • For companies that responded in 2021, encourage further disclosure in areas where it was lacking. • Use 2021 WDI data to engage with investee companies where there are specific opportunities, such as where are there gaps in reporting relative to peers, performance weaknesses or areas of concern.

Workforce Disclosure Initiative (WDI) Survey

The Workforce Disclosure Initiative was set up by ShareAction, funded by the UK's Department for International Development. Over 100 investors and $12 trillion in AUM are asking companies to provide more information on labour practices to identify badly managed workforces that are vulnerable to shocks.

As part of Liontrust's commitment as a signatory to the WDI, the Sustainable Investment team contacted 78 holdings in the funds to request they respond to the WDI's 2021 survey. Of these, 32 have now completed the 2021 Survey. Earlier in the year, we thanked 11 companies that had already confirmed they would participate in the 2021 Survey. Overall, 43 investee companies participated in the 2021 survey, equating to 20% (out of 217 entities held as at the end of December 2021), and 33 of these received a special mention for their transparent disclosure in 2021.

We believe that how companies manage human capital in their direct operations, as well as workers further down their supply chains, can affect long-term success. Our team will engage to encourage companies to offer decent work and and ensure they protect workers' rights and maximise opportunities to support employees. We will also encourage companies to use their influence to drive forward best practice further down their supply chains.

2021 Initiative	Description	We said we would:	In 2021:	In 2022, we will:
Encouraging the transition to sustainable investment	To date, savings and investments have typically been geared towards traditional investments that don't necessarily incorporate ESG. However, as demand for sustainable and ESG-integrated investments grows, and regulations to better classify what constitutes 'sustainable' investment follow suit, companies should play their part to promote it to further accelerate the transition needed for a more sustainable economy. We will focus on determining which companies are leading the way and which need to do more.	• Continue to engage with our financial holdings to encourage greater integration of sustainability issues, including responsible investment policies, lending practices and increased adoption of sustainable investing.	• We met with six investee companies on this issue.	• Encourage wider adoption of ESG/ Sustainable funds on financial platforms. • Continue to push for comprehensive responsible investment policies for insurance holdings.

Case study: Legal & General

Held under our *Saving for the future* theme, Legal and General manages capital and associated risks in order to provide customers with pension income and long-term savings. It benefits from the rise in defined contribution pensions and the de-risking of workplace institutional pensions.

We engaged to understand how actively the company is investing in the oil & gas, tobacco and weapons sectors with its internal assets and how ESG is integrated into investments. L&G said it has not excluded these sectors overall but there are issuers within them that it would not invest in (and has also actively divested) due to ESG and/or for credit reasons. Overall, its exposure to these sectors remains small: tobacco is less than 1% of the portfolio and oil & gas is around 2.5%, predominantly in integrated oil companies with transition plans. At present, there are around 50 oil & gas companies excluded because of the coal contribution to revenues or high emissions, and around 45 companies are excluded because of controversial weapons exposure.

L&G's philosophy is that engagement is always its first choice over exclusion, believing it can make a bigger impact on market standards by remaining invested and ultimately deliver better outcomes for clients. There are exceptions to this, such as the controversial weapons and thermal coal policies, which the company expects to evolve later this year. The company considers all active funds are ESG integrated and engagement is undertaken by the Stewardship team.

Controversies

Over the two decades we have been managing the SF funds, a key lesson we have learned is that 'sustainable' should not be taken to mean perfect. Investing involves making predictions about the future, which is extremely difficult. Therefore, we have to expect occasions – albeit rare – when the future does not turn out as predicted and our companies become embroiled in a controversy that challenges our initial assessment of their sustainability.

Over 2021, MSCI highlighted 196 'controversies', with 15 of these considered 'severe', including Kingspan. There were three that led to the team reviewing our sustainability rating, and for the others flagged, we were either aware of the issue or, after examination, deemed it immaterial to our assessment.

As soon as we are aware of any controversy, the next stage is to analyse the situation in detail, investigating to ascertain the involvement of the company in question, the seriousness of allegations made and how the business is responding. This gives us the context with which we can engage and we will then look to speak to senior management or non-executive directors as well as other interested parties such as nongovernmental organisations (NGOs) or industry experts. With this information, we are in a position to establish the impact of the controversy on our investment thesis (remembering that this includes the sustainability rating).

The three possibilities are:

i. The business no longer satisfies our criteria for a sustainable investment, so we exit the position.
ii. The risk and quality of the investment is affected so we feel a smaller portfolio position is appropriate and therefore reduce our exposure. This would be reflected in a downgrading of our sustainability matrix rating.
iii. The issue is being addressed by management sufficiently so that we can continue to hold our portfolio weighting while engaging with the company to ensure the situation is resolved.

Case study: Compass Group

A subsidiary of Compass Group was highlighted on social media for providing inadequate school meals after the government decided children should not return to schools due to the second wave of Covid-19, so we engaged on product safety and quality. After finding out more about what happened and the company's response, we concluded it was a one-off issue that is unlikely to be repeated given the significant steps that were taken.

Case study: Kingspan

We have invested in Kingspan for more than 15 years and have held the company in high regard for the benefits its products bring, playing a key role in energy efficiency in buildings and therefore carbon dioxide emission reduction. Revelations from the Grenfell Tower Inquiry, however, have raised concerns about the culture and controls within the insulation business.

We initially decided to downgrade Kingspan's sustainability rating (in our proprietary Matrix) from A1 to A4 in December 2020, a significant reduction in terms of management quality. This means we view a company as higher risk and Kingspan's weighting in our funds fell substantially as a result. Our view at that stage was to reserve final judgement until after the Grenfell Inquiry concluded and we could discuss the findings and recommendations with the company's management and other parties. As part of our continuing engagement, we requested a meeting with the new Chairman to understand his view of how the culture has changed, and needs to change further, towards safety. This was not forthcoming, however, which is disappointing given our large holding and long-term support of the business. This lack of engagement has prevented us from improving our rating from A4.

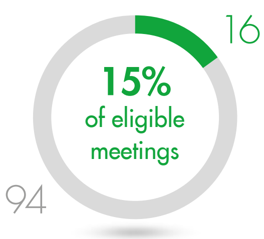
On balance, factoring in concerns on valuation, culture and management rating, we exited the company in the fourth quarter of 2021.

Voting summary 2021

In 2021, we voted at 95% (140 out of 147) of eligible meetings and against management or abstained on proposals on least one vote in 52% (76 out of 147).

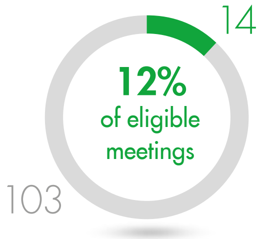
The following graphic shows (in green) the number and percentage of eligible meetings where we voted against or abstained on these particular issues.

Re-election of chair
(110 total votes)



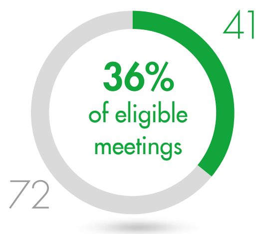
The re-election of the Chair of the Nomination Committee

Remuneration
(117 total votes)



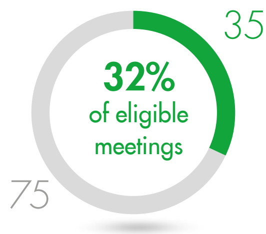
The approval of the company's remuneration report/compensation

Re-election of directors
(113 total votes)



The re-election of one or more company directors*

Ratification of auditors
(110 total votes)



The ratification of auditors/ authorisation for the Board to fix remuneration of external auditors

Source: Liontrust, December 2021. *Due to lengthy terms of office, bundled director elections or lack of independence.

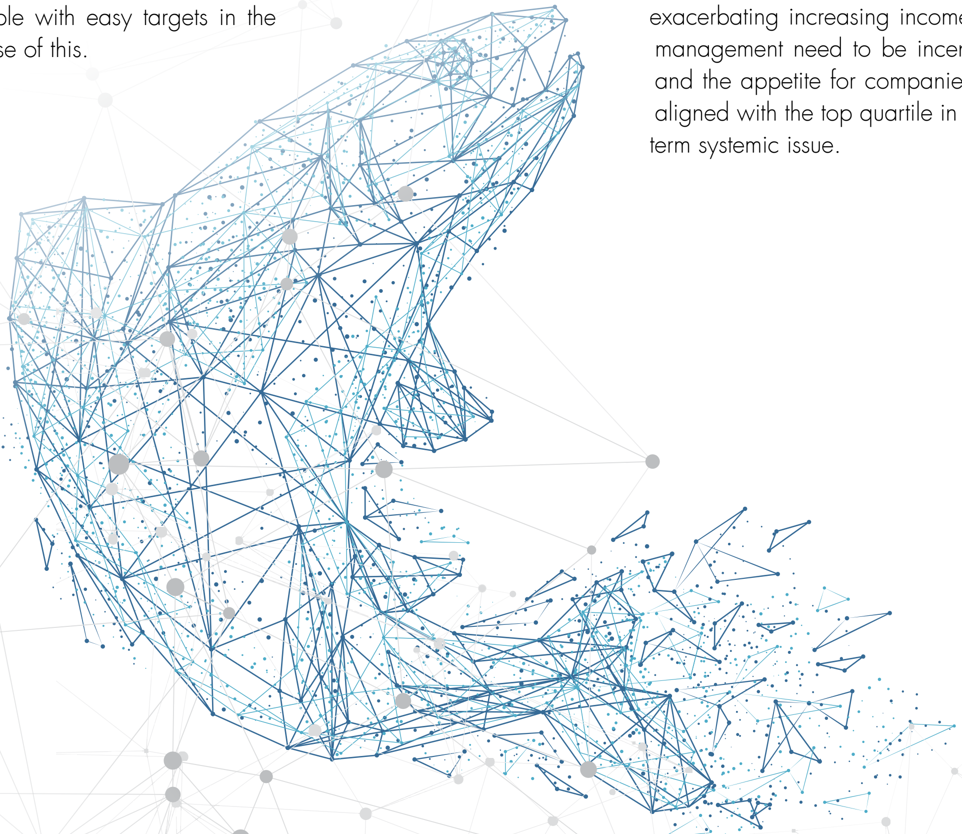
Case study: Abcam – remuneration

Held under our *Enabling innovation in healthcare* theme, Abcam provides high-quality research tools to enable the progression of life science research.

As a top 20 shareholder, we were consulted about a proposed new long-term incentive plan for the CEO and Senior Management and expressed our view that the plan was too generous. The company appears to be trying to compensate for perceived failings around what the CEO received historically but, in principle, we believe this is the wrong way to think about things. The past is the past and companies should not attempt to reward people with easy targets in the future because of this.

Although we understand there is global competition for talent, and thus the US is the correct comparison, in general we thought the level was too high. The peer group used was not disclosed in the proposal document, nor clearly explained, containing an eclectic mix of new founder-led businesses and significantly larger organisations. We believe CEOs and individuals should be incentivised and well rewarded for good performance but the articulation of this plan was not reassuring in our view. We downgraded our management quality rating for the company and reduced our position size.

For 2022, our team has committed to looking more closely into the topic of remuneration but, more specifically, the link to exacerbating increasing income inequality. While we believe management need to be incentivised correctly, pay quantum and the appetite for companies to keep reviewing pay to be aligned with the top quartile in their sector represents a longer-term systemic issue.



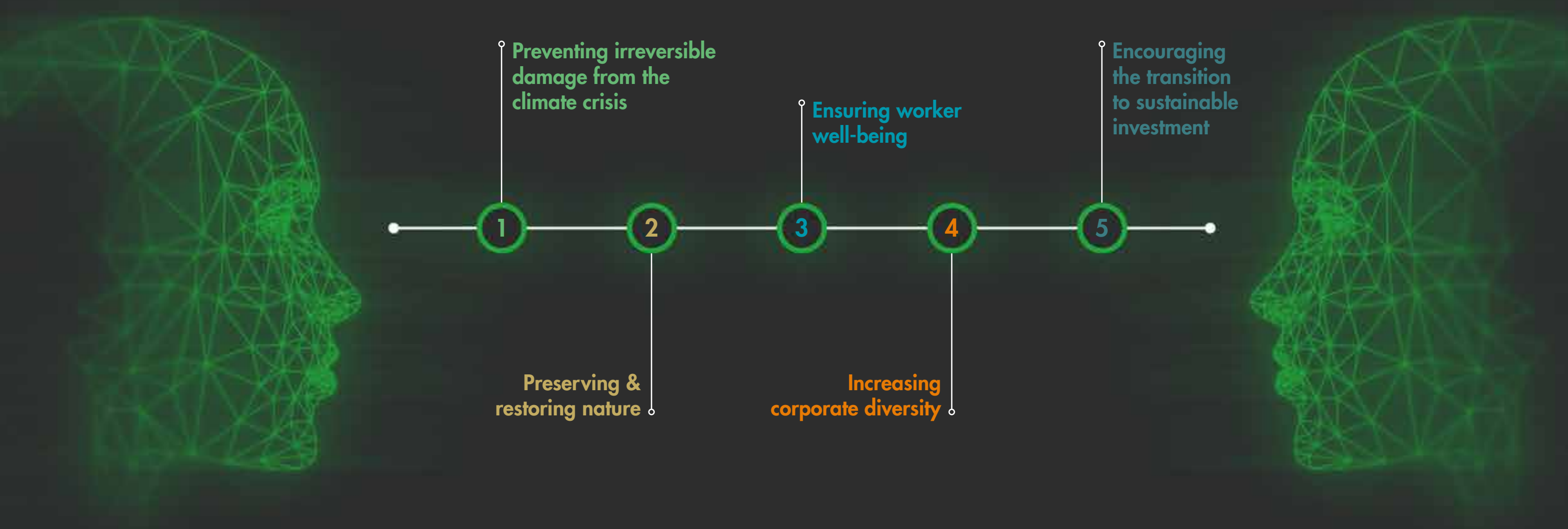
2022 proactive engagement intiatives

We prioritise proactive engagement initiatives, in collaboration with our Advisory Committee, at the beginning of each year. We assess how our holdings are positioned on these issues and, where appropriate, define target companies with whom we will engage. For 2022, there are two changes:

- Reversing the collapse in biodiversity and Encouraging a faster transition to a circular economy are combined into Preserving and restoring nature
- Engaging with banks on financing the transition will be included in our Climate Crisis initiative

In our experience, continued engagement over a longer time period is more likely to achieve better engagement outcomes than over a yearly reporting cycle, so we will continue with our other priority initiatives in 2022.

As well as continuing our efforts to increase corporate disclosure of ESG impacts, impact metrics, mitigation efforts and performance, our team will now focus on delivering improvements through the following five priority initiatives:



Preventing irreversible damage from the climate crisis

We recognise the urgent need to reduce carbon emissions across the economy to limit the negative impacts stemming from the climate change emergency. In addition, the climate crisis is set to have significant physical and economic impacts on human activity. The IPCC, IMF and Bank of England all recognise climate to be a systemic issue that will affect all types of sectors, and will affect companies' returns.

Objective: To encourage companies to adopt strategies to reduce absolute carbon emissions at a rate consistent with limiting global warming to 1.5 degrees. We want to ensure companies can change in a timely, just and profitable way and have robust strategies and targets in place to achieve this.

Preserving and restoring nature

TNFD: 'More than half of the world's economic output - $44 trillion of economic value generation – is moderately or highly dependent on nature. Nature loss therefore represents significant risk to corporate and financial stability.'

Objective: We will engage with investee companies to encourage better information and reporting of natural capital impacts from their activities, products and services, as well as policies and programmes that preserve and restore nature and promote biodiversity. We will also engage to understand better companies' dependencies on natural capital and how this might impact financial returns.

Ensuring worker well-being

How companies manage and look after their workforce through direct operations, and workers further down their supply chains, can directly affect corporate reputation and overall business performance.

Objective: We will engage to encourage companies to offer decent work and pay living wages and to ensure they mitigate risks, protect workers' rights and maximise the opportunities to support employees. We will also encourage companies to use their influence to drive forward best practice further down their supply chains.

Increasing corporate diversity

We believe companies that are more diverse are better able to prosper over the long term.

Objective: We will engage to encourage greater diversity, looking at gender and ethnic balance at a board level, senior positions and within the workforce, as well as looking at efforts to increase transparency and reduce pay gaps.

Encouraging the transition to sustainable investment

To date, savings and investments have typically been geared towards traditional investments that do not necessarily incorporate ESG. However, as demand for sustainable and ESG-integrated investments grows, and regulations to better classify what constitutes 'sustainable' investment follow suit, companies should play their part to promote it to further accelerate the transition needed for a more sustainable economy.

Objective: We will focus on determining which companies are leading the way and which need to do more.

Final Thought: Ivana Gazibara on The role of venture building in transformative change

Ivana is a futures and systems change expert with more than 15 years of experience in sustainability strategy and innovation. She is currently working with the TransCap Initiative to build the field of systemic impact investing and joined our Advisory Committee in 2021. The SF funds invest in well-established businesses with bright prospects but all our companies started from smaller beginnings, often with backing from venture capital. To ensure a long-term supply of sustainable businesses, we need a healthy venture capital system supporting those innovative companies that will be the SF investments of tomorrow. Ivana explains her interest in this pipeline in the following piece.

Over the past decade or so, as challenges like climate change, social injustice and biodiversity loss (to name a few) have come into clearer focus and become more urgent, there has been an explosion in sustainable entrepreneurship aimed at addressing these. Just anecdotally, I am a member of an angel investor club where most of the ventures coming our way contain some component of sustainability baked into their business models, despite the network not being exclusively focused on this area. Although there are still plenty of dog walking and food delivery apps being created, it is now trendy to start a 'sustainable business': by 2015, a third of all new ventures around the world had a social or environmental purpose as opposed to primarily a profit-maximising aim [1].

However, whether looking at traditional VCs, accelerators, incubators, or the more emergent space of venture builders/studios, there is still a tendency in sustainable entrepreneurship to focus on better ways of doing the same old stuff. Witness the creation of many sustainable fashion platforms, which might use better materials and more ethical means of production but are still fundamentally encouraging us to consume more. Or products trying to make a virtue of recycled plastics, which then cycle right back into the environment on the next round. Very few ventures are created to address the root causes of the systemic challenges we face.

If we think about what system change is, in its simplest terms, we are talking about a fundamental shift in how societies operate. We saw it historically with the agricultural revolution and the industrial revolution, the transition from horse and carriage to automobiles. Even today, we are arguably in the midst of it, with the tectonic shifts resulting from the digital transformation of our economies.

System change is not just something that happens to us, however; it can also be a deliberate act. The next transformation we need to work towards is a low-carbon, climate resilient and more just future. Achieving this will require enterprise to play a radically different role, and this is where venturing comes in; we will need future-fit ventures of tomorrow and the time to start creating them is now.

Within the venturing world, venture studios are a particularly interesting model because they often act as a funder and a builder of enterprise. This means that, when they identify gaps in particular areas, they can create enterprises that address these. This is not a new game, needless to say, but has traditionally focused on creating enterprises to capitalise on market gaps to maximise profits. What we need to do now is turn the process of venture building on its head so it centres on mission-led impact and aims for system transformation.

This, of course, is hard to achieve. In the words of one climate venture studio founder, it is tough enough getting a good pipeline of viable enterprises in which to invest, let alone thinking about how to coordinate strategically your investments to achieve system change. But this should be our holy grail, because creating future-fit ventures for tomorrow's world will require more than just profitable enterprises in isolation.

Here is what we need to be thinking about to bring systems thinking into the venturing process:

- **Defining your mission is ground zero.** As Ann Mei Chang says in Lean Impact [2]: 'Fall in love with the problem, not the solutions.' Lots of investors in this space are still simply collecting their impact investments on an asset-by-asset basis and ending up with what I call the mishmash of sustainability in their portfolios. Some have established themes around which to invest but it remains rare to find those thinking systemically about the impact they can create in real world systems, and how their portfolio can support this through the 'combinatorial effects' [3] of the enterprises they hold.
- **Map your system of interest.** Once you have identified your mission, system mapping will help you understand the actors and institutions coalescing around the challenge (hint: these are not always those you expect). This process also identifies the most impactful leverage points for change in the challenge area, and these should translate directly into your investment strategy.
- **Design an investment strategy that supports your mission and is informed by the wider system dynamics.** This ties back to the leverage points. A traditional venture-by-venture approach will not get us very far in this regard. We need ecosystems of ventures, which act as a set (or indeed, a portfolio) to systemically crack some of the problems of today. The Transformation Capital Initiative is an open innovation initiative pioneering this type of approach, with the idea of creating strategic portfolios where investments are deliberately composed around a broader system intervention approach.
- **Seek to create network effects.** No one venture, or even a portfolio of ventures, is going to create transformational change on its own. The critical thing to understand is that you, as a venture investor or builder, are a node within the wider system, so your impact can be transformational only if you are able to work with that system. For example, your mapping might uncover that the greatest impact opportunity in your area of focus is not commercially 'investable' yet, and might mean you need to partner with a grant-making body to build that market. A systemic approach will likely push the boundaries of your business model and will almost certainly mean working collaboratively with other actors in the system.
- **Help the ventures you build create impact goals.** Support the impact entrepreneurs you work with to centre their commitment to a mission, rather than being too attached to the solution. Metabolic Ventures, for example, structures its ventures in a way that ensures alignment with the impact mission and creates the right incentives by creating dual entities: a foundation and a commercial enterprise with limited liability. The foundation holds the overarching mission and mandate and has a minimum 51% stake in the commercial entity. The commercial entity replicates or scales a particular business model to fill a market gap, but is guided by the foundation [4].
- **Build the ecosystem.** Most venture spaces today run counter to this philosophy: they tend to operate in silos and are characterised by transactional behaviour where the financial successes of a few ventures cover the costs of the many failures [5]. What is left at the end of the venturing 'funnel' is a few isolated success stories operating without much of a supportive ecosystem. Yet creating a sustainable economy absolutely requires such an ecosystem to help build the right skills and capabilities, help create the networking effects that will enable tipping points in different sectors to occur, and generally create a supportive environment for sustainable business models to thrive [6]. We need not just one or two big bets to succeed, but a whole range of sustainable business models to emerge and find a supportive network that will shift the conditions of the system.

System change is complex, slow and messy, and for dominant practices to become replaced, we need actors across the system to play an active part in that transformation. Entrepreneurs have shown time and time again that they are able and willing to rethink old models; now it is time for investors and venture developers to rethink the enterprise-building ecosystem to catalyse the transformative change we need.

Notes

1 Global Entrepreneurship Monitor, 2015: https://www.gemconsortium.org/report

2 Mei Chang, A. Lean Impact: How to Innovate for Radically Greater Social Good. Hoboken, NJ: Wiley

3 Hofstetter, D. Transformation Capital: Systemic Investing for Sustainability, Climate-KIC, 2020: https://transformation.capital/assets/uploads/Transformation-Capital-Systemic-Investing-for-Sustainability-1-1_2021-06-25-114435.pdf

4 Monaghan, C. Systemic Venture Building, Metabolic, 2020: https://www.metabolic.nl/publications/systemic-venture-building/

5 The Impact Entrepreneur: Building a New Platform for Economic Security in Work, Rowan Conway, Charles Leadbeater & Jennie Winhall, RSA, 2019.

6 The Impact Entrepreneur.

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