February 2021

THE MISSING
'G' IN SUSTAINABILITY

Alquity

LIFE CHANGING INVESTMENTS

1. INTRODUCTION

Sustainable funds have gained significant traction over the last few years, as investors are increasingly aware of the Environmental, Social and Governance impact of their investments. Morningstar reported that assets managed to ESG principles reached $1 trillion for the first time in August 2020. We expect that this trend will only accelerate.

The environmental aspect of sustainability receives significant attention in light of efforts to move to a carbon neutral world and to limit global warming to below 2 degrees following the 2015 Paris Agreement on Climate Change. Social issues, for example in terms of worker safety & protection, have gained greater visibility during the Covid pandemic.

However, we increasingly notice that governance issues are being ignored by fund managers. This is particularly an issue in Emerging Markets, where regulatory and governmental structures may still be developing, resulting in potentially fewer checks and balances on corporate behaviour.

> *Morningstar reported that assets managed to ESG principles reached $1 trillion for the first time in August 2020.*

2. ALQUITY PRINCIPLES OF GOVERNANCE & RED FLAGS

At Alquity, we believe strong governance is critical to long-term sustainability. As responsible investors, we need to have confidence that the future sustainability commitments made by companies will be delivered.

To make the standards we expect explicit, we have created the Alquity Principles of Governance which detail our expectations in terms of the independence, behaviour and composition of Boards, as well as policies on share option schemes and remuneration etc. We exercise our voting rights in line with these Principles.*

Furthermore, our process prohibits investment in companies that fail our red flags. These include companies in certain sectors that do not produce emission or water usage details, or that do not have a Health & Safety policy, as well as companies with ongoing and unresolved governance concerns. In 2020, we excluded approximately 30% of our Emerging Market universe of companies for failing our ESG red flags alone.

* These principles are available to download from our website. Please *click here*.

ESG RED FLAGS

ENVIRONMENTAL

- **No disclosure on water usage/conservation levels for significant users (e.g. beverages)**
- **>5% of revenues or profits attributed to coal and fossil fuels exploration and production**
- **High risk industry company not publicly providing emissions data or when requested**
- **Ongoing business controversies and unresolved scandals**

SOCIAL

- **High risk industry company without a Health & Safety policy**
- **>5% of revenues or profits attributed to tobacco, narcotics, armaments, adult entertainment, gambling or liquor**
- **Zero tolerance for "controversial weapons"**
- **Ongoing business controversies and unresolved scandals**

GOVERNANCE

- **No independently audited accounts**
- **Company doesn't meet investors or arrange regular open-access calls**
- **Company refusing to provide identity of majority shareholders**
- **Ongoing business controversies and unresolved scandals**

Samsung Electronics

We will use Samsung Electronics, which is one of the largest companies in Emerging Markets as an example of our methodology, and the tension between Environmental, Social and Governance factors.

Whilst this is a stock that is widely held in numerous "sustainability" themed funds, our ultimate conclusion is that the company fails our governance assessment and as such we are not investors in the business. Our analysis below is based on freely available and widely published reports and data.

Samsung's sustainability report is highly granular and, amongst many other topics, details the company's climate change strategy and measures to reduce greenhouse gas emissions (GHG), as well as measures to accelerate the transition to the circular economy (in line with United Nations Sustainable Development Goal 12) in terms of recycling and sustainably sourced packaging, privacy and cybersecurity policies etc. These are all excellent policies and aims.

Governance policies and standards are however only discussed in approximately 10 of the 120-page report. As experienced emerging markets investors this raises questions that requires a deeper dive before being able to form a view on the company's overall ESG quality. In addition, events relating to Jay Y Lee, grandson of the founder and de-facto leader of the company raise concerns.

A multi-year pattern of criminality

Jay Y Lee was returned to prison on 18th January 2021 after being convicted in a retrial on charges of embezzlement and bribery in 2016 of Korea's then President Park. The aim was to win government support for a merger of two Samsung affiliates which was necessary to cement Jay Y Lee's succession within the Samsung Group (the retrial follows an initial guilty verdict in 2017). His lawyers described this act as 'part of normal business activity'. He had already spent 1 year in jail after the 2017 verdict, and was then released on appeal with the remaining jail term suspended. The Supreme Court reversed that ruling in 2019, leading to the retrial and the resultant 2.5-year sentence just announced.

Furthermore, this is not the only ongoing legal action involving Jay Y Lee. In September 2019, he was charged in a separate case of accounting fraud and stock manipulation relating to Samsung C&T and Samsung Biologics.

Jay Y Lee is not on the Samsung Electronics board of directors, but he effectively runs the entities within the conglomerate following the death of his father, Lee Kun-Hee in October, as Samsung is a traditional, hierarchical Korean company. He was described as 'chief decision maker' by Nikkei Asia in January 2021 who then further commented that; 'experts say that the company may suspend big decisions such as M&A and large investments until Lee is in a position to take up the reins'. The Wall Street Journal makes a similar point in their headline that the 'Tech giant is rudderless for the second time in 4 years'. This point is also made by former Samsung executives, for example ex-CEO Yoon stated when Jay Y Lee was first convicted 'No one would get on a ship without a captain because you know its dangerous'. That is the situation that has now re-occurred, and we believe that the leadership vacuum will result in a negative impact on Samsung's outlook in future years.

Jay Y Lee succeeded his father Lee Kun-Hee at the helm of the group, following the elder Lee's transformation of Samsung Electronics into a world-leader. During this time, Lee Kun-Hee was also convicted twice. Firstly. in 1996 for paying bribes to President Roh to help smooth the succession process within Samsung. Subsequently in 2008, police raided his house to investigate whether Samsung was operating a slush fund to bribe prosecutors, judges and politicians. As a result, he was convicted for tax evasion and given a 3-year suspended sentence. He was pardoned in 2009 by President Lee, whose own corruption trial sensationally revealed that this was in exchange for a further bribe.

In an attempt to draw a line under the family's troubled history with prosecutors, Jay Y Lee stepped down from the board in 2019 but remained Vice Chairman. In an effort to improve governance, the role of Chairman and CEO were separated with Lee Sang-Hoon (no relation) promoted from CFO to Chairman. This move, along with the appointment of 3 co-CEOs from long-term senior Samsung executives untarnished by scandal, unfortunately did not prove successful. The newly appointed Chairman (Lee Sang-Hoon) was subsequently convicted of union sabotage in 2020, dating back to when he was CFO in 2013. He was sentenced to 18 months in jail.

He resigned and was replaced by Jae-Wan Bahk as Chairman, who is a former Finance Minister. He has not been charged with any crime, although his office was raided by prosecutors in 2018 on suspicion that he took bribes from the state spy agency in 2008.

No catalyst for change

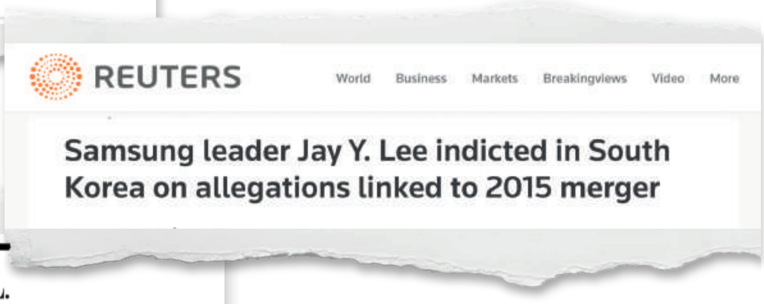
This repeated, multi-year pattern is a significant governance issue in our view and one that should not be ignored. Our concern is further accentuated by the hierarchical nature of Korean companies, and lack of effective oversight from the independent directors on the board. Although 6 of the 11 directors are independent (including the Chairman), and thus the company 'ticks a box' in terms of governance, we would question whether the directors actually have sufficient gravitas or relevant experience to act as an effective bulwark and protect the interests of minority shareholders. Their backgrounds include Korean banking, medicine, academia, law and politics. Compare this to the independent directors on the board of Taiwan Semiconductor, another dominant, mega Asian Technology Company, who include the ex-CEO of British Telecom, the founder of Acer, the CEOs of Applied Materials (US) and Xilink (Israel) and the Chairman of Delta Electronics.

Although there is a perception that the culture has changed at Samsung, we believe this is wishful thinking. Other companies, facing similar (but less severe and repeated issues) created robust compliance committees and have not suffered any subsequent controversies. If Samsung were serious about a wholesale root-and-branch culture change, we would argue that major changes to the board would be a good place to start.


YONHAP NEWS AGENCY

Prosecutors raid ex-finance minister's office over suspected bribery

Dated: Feb. 06, 2018


REUTERS

World Business Markets Breakingviews Video More

Samsung leader Jay Y. Lee indicted in South Korea on allegations linked to 2015 merger

Dated: Sept. 1, 2020

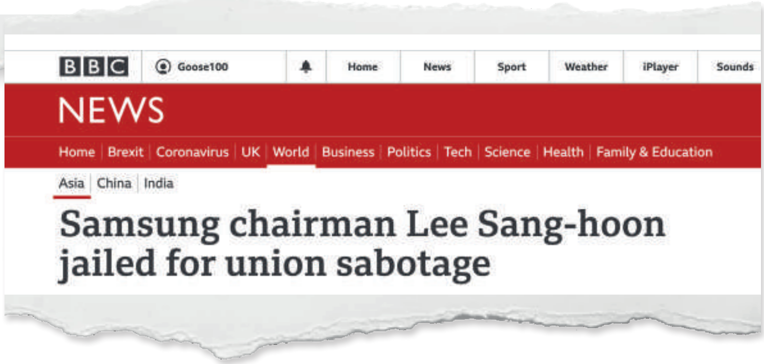

THE WALL STREET JOURNAL.

BUSINESS | ASIA

Samsung Is Without a Leader as Jay Y. Lee Returns to Prison

Tech giant is rudderless for the second time in four years

Dated: Jan. 18, 2021


BBC Goose100 Home News Sport Weather iPlayer Sounds

NEWS

Home | Brexit | Coronavirus | UK | World | Business | Politics | Tech | Science | Health | Family & Education

Asia | China | India

Samsung chairman Lee Sang-hoon jailed for union sabotage

Dated: Sept. 17, 2019

4. CONCLUSION

Every fund manager has their own investment style, and Alquity's process focuses on Environmental, Social and Governance issues to deliver a qualitative rating that is the antithesis of a "box ticking" approach. This process has led us to conclude that Samsung Electronics fails our ESG standards. We believe that the shortcomings in leadership and governance will potentially result in delayed decision making and negatively impact Samsung's competitive advantage and outlook in future years. Furthermore, and perhaps more pertinently, we would question whether responsible and mission-driven investors in sustainable funds would really be comfortable with owning a company whose senior management have repeatedly faced criminal convictions. In our opinion, this calls into question the entire ethos of the company and the sustainability of the firm in the long run.

Sources: Euronews, Forbes, Wikipedia, Yonhap, SCMP, The Verge, Telegraph, Reuters, Nikkei Asia, FT, Telecoms.com, BBC

> *Although there is a perception that the culture has changed at Samsung, we believe this is wishful thinking.*
>
> *Other companies, facing similar (but less severe and repeated issues) created robust compliance committees and have not suffered any subsequent controversies.*

5. CONTACT INFORMATION

EUROPE	ASIA	UNITED KINGDOM	LATIN AMERICA	NORTH AMERICA
Benoit Ribaud	**Suresh Mistry**	**Alex Boggis**	**Cyn Cano**	**Renee Arnold**
+44(0) 7702 257 865	+44 (0) 7973 309687	+44(0) 7702 257866	+44(0) 207 5577 871	+1 215 350 9063
benoit.ribaud@alquity.com	suresh.mistry@alquity.com	alex.boggis@alquity.com	cyn.cano@alquity.com	renee.arnold@alquity.com

FOR MORE INFORMATION ON ALQUITY, PLEASE CONTACT:

www.alquity.com **@Alquity** **Alquity Investment Management** **/Alquity**

6. DISCLAIMER

The information in this document (this "Document") is for discussion purposes only. This Document does not constitute an offer to sell, or a solicitation of an offer to acquire an investment (an "Interest") in any of the funds discussed herein. This Document is not intended to be, nor should it be construed or used as, investment, tax or legal advice. This Document does not constitute any recommendation or opinion regarding the appropriateness or suitability of an Interest for any prospective investor.

This material is for distribution to Professional Clients only, as defined under the Financial Conduct Authority's ("FCA") conduct of business rules, and should not be relied upon by any other persons. Issued by Alquity Investment Management Limited, which is authorised and regulated in the United Kingdom by the FCA and operates in the United States as an "exempt reporting adviser" in reliance on the exemption in Section 203(m) of the United States Investment Advisers Act of 1940.

The Alquity Africa Fund, the Alquity Asia Fund, the Alquity Future World Fund, the Alquity Indian Subcontinent Fund and the Alquity Latin American Fund are all sub-funds of the Alquity SICAV ("the Fund") which is a UCITS Fund and is a recognised collective investment scheme for the purposes of the Financial Services and Markets Act 2000 of the United Kingdom (the "FSMA"). This does not mean the product is suitable for all investors and as the Fund is invested in emerging market equities, investors may not get back the full amount invested.

This Document is qualified in its entirety by the information contained in the Fund's prospectus and other operative documents (collectively, the "Offering Documents"). Any offer or solicitation may be made only by the delivery of the Offering Documents. Before making an investment decision with respect to the Fund, prospective investors are advised to read the Offering Documents carefully, which contains important information, including a description of the Fund's risks, conflicts of interest, investment programme, fees, expenses, redemption/withdrawal limitations, standard of care and exculpation, etc. Prospective investors should also consult with their tax and financial advisors as well as legal counsel. This Document does not take into account the particular investment objectives, restrictions, or financial, legal or tax situation of any specific prospective investor, and an investment in the Fund may not be suitable for many prospective investors.

An investment in the Fund is speculative and involves a high degree of risk. Performance may vary substantially from year to year and even from month to month. Withdrawals/ redemptions and transfers of Interests are restricted. Investors must be prepared to lose their entire investment, and without any ability to redeem or withdraw so as to limit losses.

The Fund's investment approach is long-term, investors must expect to be committed to the Fund for an extended period of time (3-5 years) in order for it to have an optimal chance of achieving its investment objectives. This Document may not be reproduced in whole or in part and may not be delivered to any person (other than an authorised recipient's professional advisors under customary undertakings of confidentiality) without the prior written consent of the Investment Manager.

SWISS INVESTORS:

The prospectus, the Articles of Association, the Key Investor Information Document "KIIDs" as well as the annual and semi-annual report of the Fund is available only to Qualified Investors free of charge from the Representative. In respect of the units distributed in Switzerland to Qualified Investors, place of performance and jurisdiction is at the registered office of the Representative. Funds other than the Luxembourg domiciled Alquity SICAV mentioned in this document may not be admitted for distribution in Switzerland.

Swiss Representative: FIRST INDEPENDENT FUND SERVICES LTD., Klausstrasse 33, 8008 Zurich.

Swiss Paying Agent: Neue Helvetische Bank AG, Seefeldstrasse 215 CH-8008 Zurich

CANADIAN INVESTORS:

Alquity has engaged with Stikeman Elliott LLP as their legal representation and is relying on the International Dealer Exemption in the provinces of Quebec and Ontario. With respect to statutory rights of action along with connected and related issuer information please refer to our Canadian Wrapper and Prospectus. This material is for distribution to Professional Clients only and does not constitute any recommendation or opinion regarding the appropriateness or suitability of an investment for any prospective investor.