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Lessons from the 2020 Voting Season

CANDRIAM
A NEW YORK LIFE INVESTMENTS COMPANY

Table of contents

Introduction
COVID-19 and its impact on shareholder activity

Before COVID-19 had struck, there was no indication that the 2020 shareholder voting season would be anything out of the ordinary.

The pandemic gripped global markets right at the beginning of the season, leading to disruptive changes across corporate landscapes in the following months. Prior to this, it had been anticipated that the main focus for AGMs in Europe would be around the alignment of corporate practices with the recent Second EU Shareholder Rights Directive (SRD II), but the circumstances forced other issues to the surface as well.

All around the world, there have been significant delays and cancellations of annual general meetings (AGMs) during the early stages of the pandemic, leading to audit process failures in Asian markets and other challenges. However, this did not stop some of the emerging voting trends, such as climate-related resolutions, which featured prominently at a number of important meetings.

Virtual Meetings

The global COVID-19 pandemic has been closely monitored by market regulators and governments as it expanded across different regions and countries. Most governments took steps to help facilitate shareholder meetings, guaranteeing the approval of financial statements in due time while preventing the risk of infecting large groups of people at in-person events. Online electronic participation has been widely encouraged, with Virtual Shareholder Meetings (VSMs) reaching an all time high, and yet we saw a large number of cancelled meetings, postponements as well as concerns over shareholder participation. To press this point, a group of US investors wrote to the Securities and Exchange Commission (SEC) in July 2020 to push for the setting of standard protocols to facilitate active participation of shareholders voting by proxy at VSMs.

"Virtual Shareholder Meetings reached an all time high."

Impact on Proposals

From all the types of resolutions submitted to shareholder vote, dividend distributions and remuneration proposals have been the most affected. In Europe, many companies withdrew dividend and share buyback proposals to assist management in their requests for state aid and temporary furlough assistance. The European Central Bank, the European Banking Federation and the European Insurance and Occupational Pensions Authority requested supervised issuers to suspend dividends and other kinds of shareholder remuneration to preserve capital during this time of high uncertainty. The second most impacted type of resolution seen across Europe was say-on-pay as many companies announced fixed executive and board pay cuts or/and the annulment of annual bonuses. While such moves were generally welcomed, there was some concern about potential adjustments to long-term incentive schemes.

Audit Delays

Shareholders in Chinese and Japanese companies have seen serious delays in the audit processes of financial statements. It has been a record-breaking year in terms of non-standard audit opinions for Chinese issuers, including unqualified opinions with emphasis of matter, qualified, adverse and disclaimer opinions. The reason for this had been, presumably, that COVID-19 prevention measures limited the auditors' capability to obtain sufficient audit evidence, as they were unable to access the companies' premises or to perform the relevant field work. On the contrary, most of Japanese AGMs reporting audit process delays opted for meeting postponement or adjournment. In Japan companies are required to approve financial statements within the end of the third month (i.e. 31 March for over two thirds of Japanese issuers).

Major Trends in 2020

While the COVID-19 pandemic had been the overwhelming influence that shaped the voting season, it was not the only one. As in previous years, there have been clear trends, including those driven by Environmental, Social and Governance (ESG) factors that transcended companies' short-term concerns. Here we provide our overview of what we believe were the main topics related to environmental and social (E&S) shareholder proposals, as well as the final stage for the transposition of the EU Shareholder Rights Directive II.

Transposition of the second Shareholder Rights Directive

The Shareholder Rights Directive II (SRD II) was enacted in 2018 to encourage and strengthen shareholder engagement. It introduced some of the biggest changes to European corporate governance for many years, such as transparency in the identification of shareholders and their proxy advisors, transmission of information, increased disclosure of corporate reporting and improved shareholder participation at general meetings. 2020 was the final year for its adaptation into local law by member countries (transposition) and marked a milestone for say-on-pay in Europe, requiring all issuers incorporated in EU member states to submit to shareholder vote both remuneration policy (forward-looking approval) and report (backward-looking approval). In relation to stricter requirements on say-on-pay, we have observed an increase in the average free float voting dissent level at European AGMs[1]. Investors clearly continue to pay close attention to the level of management remuneration. At the same time, we also saw how, in the last few years, this has been driving moves by some European companies to enhance their remuneration policies to increasingly conform with shareholders' expectations.

"SRD II introduced some of the biggest changes to European corporate governance for many years."

1 Source: ISS Analytics, ***2020 European Voting Results Report***

“AGMs in the US featured prominently mandatory arbitration policies on discrimination and sexual harassment, reduction of the gender pay gap, and gender/ethnic representation on the board and in executive officer positions.”

E&S Proposals Political Spending in the US

The share of E&S proposals is still relatively low at European meetings compared to those in North America, where they have been steadily increasing over the years, particularly in the US. This trend has continued during the year, with lobbying expenditure remaining among the most frequently approved shareholder resolutions, including those of trade associations and other political advocacy organisations that companies can financially support. This is not surprising given the 2020 US presidential election and the role of US corporates supporting political parties, particularly as the last election was twice as expensive as the previous one. The newly elected President Biden was the first candidate ever to raise over USD1 billion during the election which cost USD13bn.

Surge of Social Issues in the US

Workforce and board diversity and human capital management were at the forefront of the American season, covering important matters such as mandatory arbitration policies on discrimination and sexual harassment, reduction of the gender pay gap, and gender/ethnic representation on the board and in executive officer positions. We saw an increase in investor community’s attention to these matters. For example, the AGMs of Facebook and eBay saw requests to provide additional information on how the companies intend to close gender/racial pay gap. In other cases, shareholders highlighted human rights-related risks, as was the case with the Tesla AGM, which faced requests to explain risks associated with forced and child labor in manufacturing, such as the manufacturing of cobalt-based batteries for electric vehicles.

More Environmental and Climate Awareness

Featured prominently among the key trends of the 2020 season were the risks posed by the changing climate, which increasingly attracts investor scrutiny. In fact, its importance has been reiterated this year through a significant number of environmental proposals often co-filed by investor communities lobbying for change. The priority remains the alignment of corporate transparency practices with the Task Force on Climate-Related Financial Disclosure (TCFD) recommendations, including Scope 3[2] mid- and long-term targets, and the setting of meaningful goals in compliance with Paris Climate Agreement strategy. The most targeted sector continues to be energy (for instance, Exxon Mobil, Chevron and Enphase Energy in the US, Equinor in Norway, and Fortum in Finland) but notably, fossil fuel lending by banks has recently become a key focus area globally (such as Barclays in the UK, Danske Bank in Denmark, JPMorgan Chase in the US and others in Canada, Australia and Japan). Some countries saw their first climate-related shareholder resolutions ever, such as in the case of France (Total SE) and Japan (Mizuho Financial Group).

"The boards continue to focus on aligning corporate transparency practices with the Task Force on Climate-Related Financial Disclosure (TCFD)."

2 Greenhouse Gas (GHG) emissions scope levels:
- **Scope 1: all direct GHG emissions.**
- **Scope 2: indirect GHG emissions from consumption of purchased electricity, heat, or steam.**
- **Scope 3: other indirect emissions that occur in the value chain of the reporting company (e.g. the extraction and production of purchased materials and fuels, transport-related activities in vehicles not owned or controlled by the reporting entity, electricity-related activities outsourced activities, and waste disposal.**

Source: *Final Report*, Recommendations of the TCFD

Our Voting Activity

At Candriam, we believe that voting is part of our responsibility as an asset manager and it is integrated within our investment processes. Our objective is to offer a better risk-adjusted return over the long-term, and to achieve it we take into account environmental, social and corporate governance (ESG) factors alongside financial criteria. By engaging and subsequently voting, we encourage investee companies to work in a sustainable and responsible manner. This is because, as an active investor, we take our social responsibility seriously.

Despite this extraordinarily difficult year, we were not discouraged from voting and engaging on a multitude of companies, as well as participating in collective investment initiatives, ultimately exercising the active ownership we advocate.

In 2020, we have pressed companies even harder than before, through our voting, on climate change issues, which clearly have been of growing concern to shareholders in 2020. As oil and gas prices plunged due to the pandemic, NextEra Energy, the world's largest supplier of wind power, reached an historical milestone as in October 2020 it temporarily overtook oil and gas giants Exxon Mobil and Chevron as the world's most valuable energy company. The shift reflects a global energy transition to clean energy from fossil fuels. Interestingly, Exxon Mobil shareholder meeting was targeted by several ESG shareholder proposals back in May, including requests for a costs and benefits analysis of voluntary climate activities and an assessment of public health risks of expanding petrochemical operations and investments in areas increasingly prone to climate change-induced storms, flooding, and sea level rise. The company pushed back hard, which ultimately resulted in rejections of the proposals. Nevertheless, it is clear that the tide of time is against business strategies purely based on oil and gas. That is the case of the French Total and the British Royal Dutch Shell, equally being asked to set and publish targets aligned to the Paris climate agreement. In both cases, the decision was driven by the belief that the extent of these companies' commitment to reduce greenhouse emissions is not good enough.

Our voting activity continues to focus on corporate governance policies, structures and practices as they can impact both short- and long-term performance as well as pose reputational risk. A well-functioning board of directors can also better carry out its agency role in the interests of all stakeholders. 2020 was characterised by several contentious shareholder meetings, with shareholders in some cases hoping to achieve board representation so that to better voice their concerns at a board level. One example has been the meeting of Lagardère SCA, where Amber Capital, its largest shareholder, took a strong stance against company's capital allocation and governance. It questioned Lagardère's holding structure, its legal form and the effectiveness of the supervisory board, and filed a proposal to replace eight directors with its dissident nominees. Despite non-approval, Amber resolutions gained substantial support of 40 percent of votes cast, on average. Way less support to a slate of dissident nominees was registered at Mediobanca's AGM. Activist Bluebell Capital Partners failed in its attempt to achieve board representation at the Italian investment bank, since the list of candidates presented jointly with another investor received the support of less than 3 percent. The dissident unsuccessfully sought to voice its concerns over company's governance and strategy by appointing up to four directors.

All in all, 2020 has been an exceptionally formative and insightful year for our voting team, who definitely did not rest on its laurels, but rather grasped all the interesting cues offered by such an unprecedented scenario, aiming to face 2021 with renewed tools and empowered scope. We believe that our careful voting activity is the ultimate way to move towards a more sustainable financial system, where companies and their shareholders engage and work together for the mutual benefit.

"In 2020 we have pressed companies even harder than before, through our voting, on climate change issues."

Looking ahead

With a new voting season ahead of us, we first look back at what is left of 2020. The social consequences have been tough. The number of layoffs and the sharp increase in the level of unemployment (the US had the worst year for job losses since 1939) has been certainly alarming, adding up to social tensions because of restrictions, isolation and protests (not to mention the killing of George Floyd and the resulting demonstrations against racism around the globe). Given the extraordinary impact of COVID-19 on economic activity and businesses, all market players have since then acted proactively, with authorities, companies, investors, and many other stakeholders urged to take concrete steps in response to the pandemic. We assisted in the move to instigate significant cuts to company dividends, something that we believe we will see more of in 2021. And if companies ask shareholders to cut their own remuneration, why should that not happen to managers' remuneration too? Many variable compensation plans have been affected by the consequences of the pandemic and we expect this to continue in 2021. This would mean that companies will face a challenge of retaining and supporting distinguished managers without falling into inappropriate excessiveness in the difficult market environment we are all facing.

"Companies will face the challenge to find the right balance in management remuneration, between retention and excessiveness"

“Nasdaq has identified ESG to be one of the hottest trends of 2021.”

We can also say with confidence that the investment community continues to take ESG-related issues more seriously. Throughout 2020, we have witnessed changing views and an increasing emphasis on materiality, employment practices, and companies’ responses to climate change. In 2021, it is likely that these concerns will result in more shareholder activism through engagement and proposals, while we are likely to see more merger and acquisitions activity in order to adapt to the drastic changes in business and industries. Therefore, there will be paying a much closer attention to ESG themes. Nasdaq has identified ESG to be one of the hottest trends of 2021. We expect that the focus on environmental aspects (such as climate change) and diversity issues (not only gender-based) will be more evenly spread across different global markets. The evidence has shown us that investors are not refraining from expressing ESG views at general meetings, and such a commitment remains a priority for Candriam too.

As we have put 2020 into the rearview and glanced at the new year, we would also like to dedicate few lines at our new voting policy for 2021. We have taken big steps in renewing it, driven by the aim to strengthen our stewardship commitment to promote those governance practices that we believe will best serve the interest of both our clients and our investee companies. The main changes concern how we define and implement our voting policy in full compliance with SRD II, as well as transparency and disclosure practices. Other important additions and clarifications have been implemented on governance issues (such as on diversity, audit, and independence) and social issues, particularly with regards to human rights. The Candriam 2021 Voting Policy is effective for meetings that occur on or after 1 January 2021. We invite you to examine the full text of these updates, which is contained in the **new version available on our website**.

€128 B
AUM as of
30 June 2020

550+
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