ABERFORTH PARTNERS

Compliance with the UK Stewardship Code

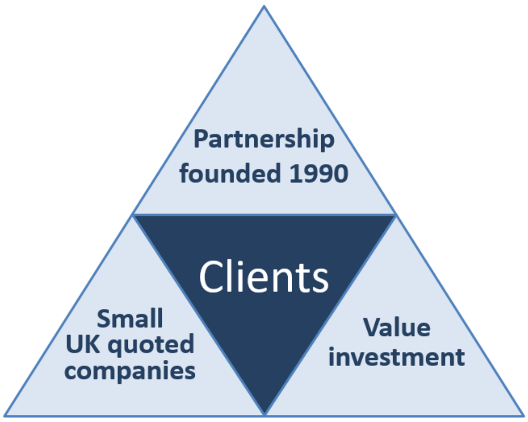
This document provides details of Aberforth's approach to stewardship and its compliance with the UK Stewardship Code in the reporting period to 31 December 2020. Those looking for more information can contact Sam Ford – the investment partner responsible for co-ordinating stewardship issues – by email on stewardship@aberforth.co.uk or by phone on 0131 220 0733.

Principle 1

Signatories' purpose, investment beliefs, strategy and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

Context

Aberforth was established in 1990 and remains wholly owned by partners working at the firm. Since then, its purpose is unchanged and is encapsulated by the accompanying diagram. Specifically, the purpose is to deliver superior long-term investment returns for its clients and, by extension, for the ultimate beneficiaries of its clients' portfolios.



The target client base, detailed in Principle 6, is institutional or wholesale investors that want to give their own clients exposure to small UK quoted companies.

Three central aspects of the firm – partnership, a focus on small UK quoted companies and a value investment philosophy – support the pursuit of this purpose. The features set out below are described in more detail in Aberforth's investment philosophy document, which can be found HERE.

- Aberforth was designed by its founders to be a simple business in the belief that this would improve the investment outcomes for its clients. The firm has remained focused on one asset class and, aided by a self-imposed cap on its assets under management, avoids the complexity and proliferation of strategies that are associated with the asset-gathering model pursued by much of the fund management industry. Aberforth believes that its chosen asset class – small UK quoted companies – is relatively inefficient and, through fundamental analysis, lends itself to the active management of a diversified portfolio of stocks. Aberforth's investment universe is the Numis Smaller Companies Index (excluding investment companies) [NSCI (XIC)], which is the bottom ten percent of the main UK equity market by market capitalisation.

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- All Aberforth's portfolios are managed in accordance with a value investment philosophy. Encouraged by historical evidence, Aberforth believes that this philosophy plays a central role in the achievement of superior long-term returns. Given this unwavering adherence to value investment, Aberforth's primary consideration in any investment decision is, unsurprisingly, valuation. The firm also believes that discreet engagement with the boards of investee companies – on matters such as governance, capital allocation, environmental impact and social policies – can improve investment returns, to the benefit of clients.

- Aberforth's success in remaining true to its value investment philosophy and in keeping its business simple has been facilitated by the firm's ownership structure: it is a limited liability partnership, wholly owned by partners who all work full-time in the firm. The interests of Aberforth and its clients are reinforced by the partners each investing a significant portion of personal savings in the collective funds managed by the firm. The partners' intention is to ensure the perpetuation of the partnership through transition to the next generations. The partners see themselves as guardians of a business at the centre of which are its clients: investment expertise, exceptional service and integrity combine to nurture strong client relationships and thus to extend the longevity of the business beyond the tenure of any individual.

Clients are at the heart of Aberforth's purpose and culture, but successful stewardship of clients' capital can also be of broader benefit. While small companies have a less significant impact than their larger peers on the economy, the environment and society, that is not a reason for such issues to be de-emphasised and Aberforth believes that all companies should consider these issues in their operational and strategic decision-making. Any matters that might affect the valuation of an investee company are relevant to Aberforth's investment process and can be the subject of engagement with the company's directors.

Relevant matters include environmental, social and governance (ESG) issues, particularly as their increased profile affects stockmarket valuations. Consideration of these issues is integrated into Aberforth's investment process, alongside a broad range of other factors. Aberforth believes that a company's system of governance is crucial to how its environmental and social policies are designed and implemented. It is therefore important that boards describe their approach to managing these issues. Except when requested by clients, Aberforth does not exclude investments from portfolios on the basis of ESG matters alone. There is evidence that investment returns can be enhanced by investment in and engagement with companies that face ESG challenges and are already seeking to address them or can be encouraged to do so.

Activity

Aberforth ensures that its investment beliefs, strategy and culture enable effective stewardship by the "vertical integration" of all roles in the investment process. Each investment manager is responsible for several stockmarket sectors. For each holding within the allocated sectors, the investment manager undertakes company analysis, dealing, engagement and voting. The advantage of this approach is a coherent stewardship message to the boards of investee companies that is consistent with the initial investment thesis. The controls on this approach are twofold. First, investment decisions are made collegiately by the group of investment managers based on a portfolio approach to capital allocation. Thus, an individual investment manager always receives scrutiny, challenge and assistance when necessary. Secondly, stewardship as implemented by the investment managers is subject to review by the partnership through its Stewardship Group (see Principle 2).

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Outcome

Influenced by the value investment philosophy and a belief that individual directors can have greater effect on the fortunes of a small company, stewardship permeates Aberforth's investment process and culture. This is demonstrated by data provided in the responses to Principles 9, 10, 11 and 12. Aberforth's emphasis on stewardship is reinforced by the fact that its clients, in aggregate, are significant investors within the universe of small UK quoted companies, often holding significant stakes in investee companies. Accordingly, governance considerations and engagement are one of the principal topics at Aberforth's investment meetings. Interactions with the directors of investee companies are discussed, as are significant voting issues arising from general meetings. The competence and performance of the chair are subject to particular scrutiny since that role is the most important within the UK's governance framework as described in the 2018 UK Corporate Governance Code. Voting is undertaken at all shareholder meetings and is reported to clients. The firm's voting policy can be found HERE. Strategies for engagement with companies in which Aberforth's clients own meaningful stakes are regularly reviewed, with escalation tactics developed and additional resource dedicated to more complex situations. The firm's engagement policy can be found HERE.

An assessment of Aberforth's effectiveness in serving its clients and beneficiaries may be conducted with reference to the firm's purpose of delivering superior long-term investment returns. The longest standing client – Aberforth Smaller Companies Trust plc – launched on 10 December 1990. From then until 31 December 2020, it had produced a compound annual NAV total return of 12.1%*. This exceeded the 10.3%* return from small UK quoted companies, as measured by the NSCI (XIC). Part of the superior return was attributable to the value investment philosophy, as value stocks outperformed the index as a whole. Over the same period, the total return of larger UK companies, as measured by the FTSE All-Share Index, was 8.0%*. This size premium therefore supports Aberforth's focus on small UK quoted companies.

* Sources: Aberforth Partners LLP; FTSE International Limited; Numis/Paul Marsh and Elroy Dimson – London Business School.

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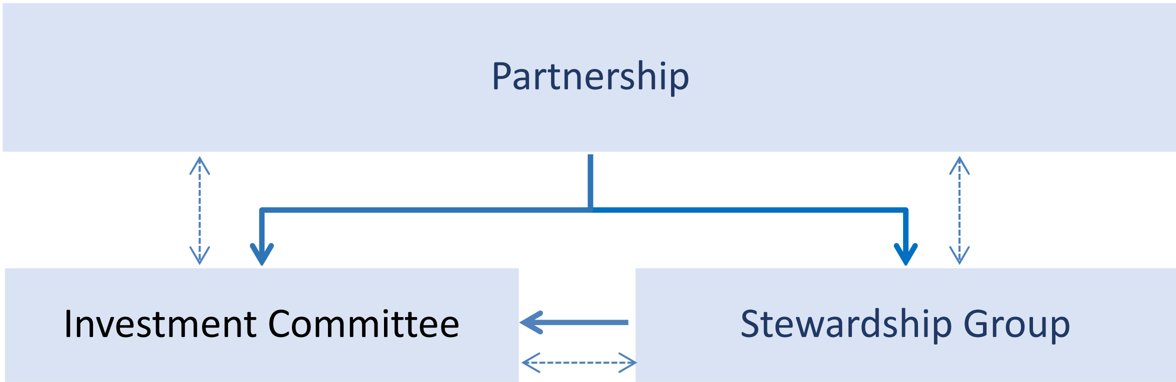
Principle 2

Signatories' governance, resource and incentives support stewardship.



Activity

The organisational structure and processes that support stewardship within Aberforth are inextricably linked. Stewardship starts with the partnership model itself, which places the client at the centre of Aberforth's business, as described in Principle 1. The commitment to stewardship is demonstrated in the leadership by a partner, Sam Ford, for all stewardship activities. He chairs the Stewardship Group, on which he is supported by three others including the partner responsible for operations. Having the operations partner as a group member provides an additional perspective, independent from the investment function. As described below, stewardship decisions are taken by the investment managers. These decisions are made within a framework set by the Stewardship Group, which reports to the partnership.

Among its peers of investment houses addressing small UK quoted companies, Aberforth has a relatively large team of experienced investment professionals. At 31 December 2020, the team comprised seven members, with average industry experience of 24 years. The investment managers have a deep understanding of the sectors and companies they cover. This means that the boards of investee companies, who have a single point of contact at Aberforth, can be more receptive to stewardship engagement. The firm therefore believes that its investment process lends itself well to an integrated approach of stewardship: stewardship decisions are taken by the investment manager responsible for individual investments with input from other members of the investment management team. Further detail on Aberforth's investment philosophy and process can be found HERE.

In implementing its stewardship policies, Aberforth's principal investment is in its investment management team, who conduct their own research, analysis and engagement. The firm recruits experienced individuals, whose diversity of knowledge and experience accumulated elsewhere can contribute to the refinement of its processes. Further relevant training is undertaken. To support its systems and the efforts of its people, Aberforth has invested in and developed a series of proprietary applications linked to a SQL database. These are tailored to the firm's approach and are integral to its investment process.

Aberforth makes limited use of data and analysis from third-party providers. The firm continues to be disappointed with the coverage and quality of data relevant to small UK quoted companies. There are current relationships with a proxy voting adviser and with a supplier of carbon data. The former is long standing and subject to annual effectiveness review. The relationship with the carbon data provider has been extended to allow for further evaluation.

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The structure and ethos of the partnership mean that separate reward structures to incentivise stewardship are not necessary. Aberforth's model is for all its investment managers, and therefore all those with responsibility for enacting stewardship policy, to become partners in the firm. Investment managers are rewarded on the basis of the firm's overall performance, rather than being tied to the investment results of individual sectors or funds.

Outcome

Aberforth has consistently applied its approach to stewardship since the foundation of the business in 1990. This task is made easier by the firm's relatively flat hierarchy and by the fact that its principals are directly responsible for implementing the stewardship policy. The voting policy (found HERE) and the engagement policy (found HERE) attest to the rigorous implementation of Aberforth's approach to stewardship.

The firm is comfortable with its existing governance structures, but there are ways in which its processes, particularly regarding environmental and social considerations, can be improved. Several improvements have recently been or are currently being implemented.

- Oversight of stewardship policy and practice has been broadened with the formation of the Stewardship Group, as described above.
- Minute-taking at the formal weekly investment meeting continues to be enhanced to improve the recording of ESG issues as they arise. Any items relating to ESG matters are specifically identified within the minute to improve tracking and reporting.
- The firm has renewed its relationship with a third-party supplier of carbon data.
- In 2020, the firm improved its system for capturing and recording all *ad hoc* phone and email engagement with investee companies. The effectiveness of this improvement should be apparent in 2021's engagement data.
- There is a system in place to capture and record instances where the firm has voted against the recommendations of its proxy voting adviser. Examples and explanations are included in voting disclosures.
- The firm continues to monitor the quality and usefulness of third-party systems and ESG data providers. To date, the depth and breadth of ESG coverage by third parties of small UK quoted companies remain inadequate, although such services are reviewed periodically. The addition of external carbon data last year has been extended through 2021.
- Given Aberforth's concern about the quality of third-party data provision, Aberforth uses an internal process for identifying, analysing and tracking important environmental, social and governance items. The aim is to improve objectivity and comparison, to help identify areas where engagement may be required and to monitor how companies' practices change over time. This project requires an enhancement to the SQL database, which is under way.
- Reporting of stewardship activities is being enhanced. Numerous examples are provided, though some remain anonymised to maintain commercial sensitivity and the effectiveness of discreet engagement. The tracking project noted above will also improve reporting, as will presentational changes to Aberforth's website.

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Principle 3

Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.

Context

As an independent limited liability partnership, whose sole specialisation is investment in small UK quoted companies, many of the traditional conflict of interest scenarios faced by larger, more diverse investment management entities do not apply or are less relevant to Aberforth.

The firm has a policy for the identification and management of conflicts of interest, with the objective of ensuring that clients are not adversely affected. Any conflict of interest that arises is duly considered by senior management, including the compliance team. The conflict is recorded and managed in a way that ensures that all clients are treated fairly. Where it is impractical to manage such a conflict it will be disclosed to the relevant clients. Aberforth's conflicts of interest policy is shared directly with clients and can also be found HERE.

The policy describes situations in which conflicts of interest may arise. From the stewardship perspective, the most relevant are conflicts that can arise (a) between Aberforth's interests and those of its clients, (b) among its clients or (c) between the interests of the firm's partners or employees and its clients.

Activity

The following points explain how Aberforth has identified and managed conflicts of interest relevant to stewardship.

- In buying and selling shares, the firm only ever deals as agent on behalf of its clients and never as principal on its own account.
- The firm's bespoke order management system is designed to deliver fair allocation of aggregated orders between multiple clients. This is subjected to regular compliance monitoring.
- The firm has controls in place to ensure that mandate restrictions directed by clients are known by investment managers and are reflected in systems.
- The firm's policy on gifts and hospitality prohibits the giving or accepting of gifts that may give rise to a conflict of duties owed to clients or the firm and may otherwise only be accepted where the gift or hospitality is modest and infrequent.
- Aberforth encourages long-term savings and investment by partners and employees. Personal dealings in investments are generally permitted, subject to compliance with the personal dealing policy. That policy requires all personal dealing to be approved by a partner and specifically prohibits investment in any company that is a constituent of the investment universe.
- Private wealth managers, on behalf of their clients, are significant investors in the collective funds managed by Aberforth. Some of these wealth managers are constituents of the investment universe and the firm can invest its clients' funds in them. On such occasions, the investment decisions are taken in a manner consistent with clients' mandates and Aberforth's purpose and investment philosophy, as described in Principle 1.

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- Clients' interests are represented directly with the managers through the independent boards of the investment trusts, the independent non-executive directors of the unit trust management company (on behalf of the unit trust) and directly by client representatives on behalf of the segregated charity clients.
- Aberforth's partners are not permitted to take board positions on investee companies or to sit on the boards of two investment trusts that the firm manages.
- A conflict may arise should a director of an investment trust managed by Aberforth be invited to join the board of a company in which the firm's clients invest. How this situation is addressed is described in one of the examples in the Outcome section below.

Outcome

Examples of the management of conflicts in practice are noted below. In the last year, updates were conducted to the risk, compliance and control framework, from which no matters of concern arose.

Example: client board conflict

It is not unusual for directors of the boards of the two investment trusts managed by Aberforth to be sought as potential board members of other organisations, which may give risk to potential and/or actual conflicts with stewardship of clients' capital. Whenever this has occurred, it has been addressed through consultation and consideration by the director in question, the board's chair and Aberforth. After thorough assessment, it was concluded that there was no direct conflict of interest. Further, it was determined that any potential indirect conflicts arising could be managed and mitigated with transparency and safeguards. Such instances are considered on a case-by-case basis. In a previous case, it was considered that the conflicts could not be mitigated to an acceptable level and the board director in question withdrew from the process.

Example: client stewardship engagement

In building a relationship with any client, Aberforth takes time to ensure that its corporate philosophy HERE and investment approach HERE are understood. In turn, Aberforth takes time to discuss and understand clients' stewardship principles and requests. Consistent with this approach, the firm discussed with one client its specific investment and stewardship requirements, part of which was an exclusion list. With a good understanding of these requirements, Aberforth provided additional feedback on their suggested portfolio restrictions to support their stewardship objectives. Ultimately this was appreciated, adopted and confirmed by the client. The investment approach for the client was updated.

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Principle 4

Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.

Activity

Fundamental research is one of the main components of Aberforth's investment process. Market-wide and systemic risks are directly relevant to the valuation of investee companies and are identified by the investment managers in the course of their industry and company analysis. Additionally, within the bottom-up research process, there is a top-down check in place: two investment managers are charged with keeping abreast of developments in the macro-economy and in financial markets. Emerging systemic risks and their impact on companies or industries are discussed at investment meetings. Target valuations may be adjusted in light of these discussions, which might lead to changes to holdings in investee companies. If a market-wide issue has relevance to Aberforth itself, it is discussed by the partners and actions are taken as appropriate.

Aberforth's partners and employees participate in industry forums, both to help identify risks and, if relevant, to influence how the risks are addressed. Such action is undertaken with the aim of improving how financial markets, usually the market in small UK quoted companies, function. While Covid-19 has limited physical attendance and led to the cancellation of many events, forums in which Aberforth has participated over the last year include The Investment Association, CFA UK, the Financial Reporting Council (as part of the stewardship consultation), the Financial Conduct Authority and the Bank of England.

As set out in more detail under Principle 7, Aberforth sees climate change as a systemic risk to economies and financial markets. It takes this into account when assessing the prospects and valuation of individual companies. It engages with the boards of investee companies when their stances on climate change are affecting their valuation. Aberforth has not engaged in public advocacy. This reflects the complexity of the topic, with nearer term economic impacts a likely consequence of meaningful remedial action on climate change. The scope of the judgement required here is broad and prioritisation is a matter for broader society as mediated by government. This stance does not shift responsibility from Aberforth: it considers the impact of potential government action on climate change when assessing the prospects and valuation of investee companies.

Example

A common response to the liquidity issues created by Covid-19 was the widespread cancellation of dividends, including cases in which companies had already moved ex dividend. There was often little or no consultation with shareholders ahead of these decisions. Aberforth wrote to the chairs of all its investee companies to remind them of the role and importance of dividends and the impact of cancellations on the ultimate beneficiaries such as ordinary savers, pensioners and charities. A copy of this letter can be found on the website and is linked HERE. Aberforth does not advocate the payment of dividends were they to threaten companies' financial viability. However, dividends play a crucial role in attracting capital to companies and are therefore important to the resilience of the small cap sector and broader economy.

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Example

Covid-19 and the various measures deployed to control it represent a serious challenge to many UK companies and, by extension, to the economy. A large number of businesses in Aberforth's investment universe were unable to access the two initial support programmes from the Bank of England (BoE), the *Coronavirus Business Interruption Loan Scheme* and the *Covid Corporate Financing Facility*. Aberforth therefore engaged with the BoE to highlight the gap and to relay relevant information obtained from discussions with companies. Subsequent measures introduced by the BoE have helped to address the issue.

Example

The UK's exit from the EU (Brexit) was a market-wide risk for the UK economy and its financial markets. A large proportion of small UK quoted companies are reliant on the domestic economy. To complement analysis of political developments, Aberforth conducted a survey of its investee companies' views on the risks and opportunities of Brexit. This provided valuable insight into the issues relevant to various industries and to the state of preparedness of individual businesses. Through sharing the results of the survey with clients and investee companies, the exercise may have contributed to their preparation for Brexit.

Outcome

Aberforth's approach to investment, based on fundamental analysis, puts it in a good position to identify and assess systemic and market-wide risks. These risks have been considered through the investment process and have, in some cases, led to adjustments to target valuations of investee companies and changes to holdings. While acknowledging its small size in an industry of asset-gathering giants, Aberforth will continue to engage with other stakeholders on systemic and market-wide risks where such action seems likely to improve the investment outcomes of its clients or, consistent with Principle Five of the FCA's Principles for Businesses, the functioning of the financial system.

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Principle 5

Signatories review their policies, assure their processes and assess the effectiveness of their activities.

Activity

Aberforth's approach to the assurance of its stewardship policies is based on internal review. This approach has been adopted since the small size of the firm and its ownership structure mean that its principals are able to scrutinise and amend as appropriate stewardship policies and their implementation. Providers of external assurance are considered, but it is not yet clear that they would add the value provided by third parties in other areas of the firm's activities, such as the AAF 01/20 framework issued by the Institute of Chartered Accountants in England and Wales.

There are three layers to the internal assurance approach: two are formal – the Stewardship Group and the partnership as owners of Aberforth – and one informal. The informal layer is a benefit of the firm's size and simplicity. The investment managers, who put stewardship policies into practice, work together in the same room. Contentious issues may be discussed as they arise and with reference to policy, which increases the likelihood of consistent implementation. At the formal level, the Stewardship Group is charged with formulating the firm's policies and reporting on their implementation through the investment managers' stewardship activities. Important inputs to the group's work are benchmarking against peers and participation in relevant industry forums. The group reports to the partnership annually, which gives the ultimate approval to the stewardship policy and its implementation.

An additional level of assurance is provided by the boards of the collective funds managed by Aberforth. The firm presents its stewardship report, together with voting records, to these boards annually. Elected by the underlying shareholders of the funds, the boards review and challenge the reports, as well as providing an additional check on whether they are fair, balanced and understandable. Aberforth's other clients benefit indirectly from this scrutiny.

Outcome

The assurance approach described above has resulted in the following recent developments in Aberforth's stewardship policies and processes.

- The stewardship policy was amended to reflect the UK Stewardship Code 2020. This has subsequently been updated.
- The principal change to the stewardship process was in the creation of the Stewardship Group, which is tasked with the oversight of policies and their implementation by the investment managers. Responsibility was previously held by one partner.
- The voting policy was amended to reflect the Corporate Governance Code 2018.
- A project is well advanced to improve recording and measurement of stewardship activities, which will ultimately lead to deeper and more extensive external reporting. It should be noted that Aberforth's emphasis on discretion during its engagement means that some reporting will continue to be anonymised.

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Principle 6

Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.

Context

As explained in Principle 1, Aberforth's portfolios are managed in accordance with a value investment philosophy. Historical evidence suggests that this philosophy plays an important role in the achievement of superior long-term returns for clients. The firm believes that effective engagement with the boards of investee companies – on matters such as governance, capital allocation, environmental impact and social policies – can improve investment returns, to the benefit of clients. Where ESG matters impinge upon the investment case, the Managers engage with investee companies to understand how these issues may be addressed. The Managers are well placed to undertake this activity, since engagement has always been fundamental to their investment process.

Aberforth's intended clients are institutional or wholesale entities that seek to give their own clients exposure to small UK quoted companies. Aberforth's assets under management are invested entirely in small UK quoted companies. These are companies with a market capitalisation, at the time of purchase, equal to or lower than that of the largest company in the bottom 10% of the main UK equity market or companies in the Numis Smaller Companies Index (excluding investment companies). At 31 December 2020, the firm managed five funds: three collectives and two segregated funds for charities. All five funds are managed in a similar way in keeping with the value investment philosophy, though client specific variations allow classification into sub-strategies: Standard Value, Value and Income and Standard Value with Client Restrictions.

- Standard Value: Aberforth Smaller Companies Trust plc (ASCoT) has been a client since its inception in 1990. It is an investment trust listed on the London Stock Exchange, with assets of £1,157m* at 31 December 2020. Its underlying investors are overwhelmingly institutional, primarily private wealth managers. Direct retail investors, excluding current and former partners of Aberforth, represent circa 1%* of the fund. Non-UK investors represent circa 3%* of the fund.

- Standard Value: Aberforth UK Small Companies Fund (AFund) has been a client since its inception in 1991. It is an authorised unit trust scheme, with assets of £124m* at 31 December 2020. Its underlying investors are overwhelmingly institutional, primarily private wealth managers. Direct retail investors, excluding current and former partners of Aberforth, represent circa 2%* of the fund. Non-UK investors represent circa 1%* of the fund.

- Value and Income: Aberforth Split Level Income Trust plc (ASLIT) has been a client since its inception in 2017. It is a split capital investment trust listed on the London Stock Exchange, with assets of £189m* at 31 December 2020. Its underlying investors are overwhelmingly institutional. Direct retail investors, excluding current and former partners of Aberforth, represent circa 2%* of the Ordinary shares. Non-UK investors represent circa 0%* of the Ordinary Shares. This fund has a limited life, with a planned winding-up date of 30 June 2024.

- Standard Value with Client Restrictions: Charity A is a segregated fund managed by Aberforth for one of the UK's largest charities. A client since 2002, assets at 31 December 2020 were £200m*.

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- Standard Value with Client Restrictions: Charity B is a segregated fund managed by Aberforth for another of the UK's largest charities. A client since 2016, assets at 31 December 2020 were £67m*.

* Sources: Aberforth Partners LLP; Richard Davies Investor Relations.

Aberforth considers that a long-time horizon, of at least five years, is appropriate to meet the needs of its clients and their underlying beneficiaries. Over a shorter period, there would be a greater risk of volatility from economic and stockmarket cycles. In particular, the value investment philosophy followed by the firm can have prolonged periods out of favour. A longer time horizon also accords with how Aberforth assesses the prospects of the companies in which its funds invest. Several companies have been held by the funds for over a decade, though the average holding period is shorter. This reflects opportunities presented by the stockmarket to realise profits and recycle the proceeds into more attractively valued companies, a process Aberforth terms the "value roll".

Activity

The three collective funds – ASCoT, ASLIT and AFund – are overseen by boards of directors, who receive detailed quarterly reports and attend board meetings with representatives of Aberforth present. These meetings give the directors the opportunity to scrutinise the firm's chosen approach, its stewardship activities (including a record of significant votes), its stewardship code and investment horizons. Additionally, Aberforth's investment managers meet the funds' largest investors twice a year to explain performance against investment objectives and to set out factors relevant to the investment strategy. Engagement activity with investee companies is addressed, as long as it does not breach confidentiality. During the most recent round of visits in November 2020, the firm conducted 129 investor meetings, covering a majority of the holder registers of ASCoT, ASLIT and AFund. While the impact of Covid-19 meant that this number was lower than the previous November, the use of video conferencing often saw multiple offices joining the same meeting. Consequently, it is unlikely that there was a real reduction in the number of clients met. This biannual exercise gives the opportunity for investors to give feedback and for the investment managers to understand investors' requirements. Appetite for Aberforth's investment offering is formally tested every three years when ASCoT's Annual General Meeting contains an ordinary resolution to wind the company up, with the last occurrence being the March 2020 meeting. Individual shareholders are kept informed through annual and interim reports, monthly fact sheets and research produced by Kepler Partners.

The two charity funds receive quarterly reports and meet representatives of Aberforth on various occasions through the year. These relationships, including investment policy, are covered by investment management agreements. Both charity clients are concerned about exposure to fossil fuels. One supplies a strict exclusion list that it regularly updates. Aberforth also reviews the list to ensure that it accurately reflects the constituents of the investment universe. The other charity client does not operate an exclusion list, but Aberforth consults the client before proceeding with a potentially sensitive investment. In both cases, the important dynamic is dialogue between the firm and its clients.

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Outcome

Aberforth's approach to taking account of the needs of clients and beneficiaries is founded upon regular reporting, contact and dialogue with the clients and underlying investors in the collective funds. Given the diverse underlying ownership of the collective vehicles, there is inevitably a range of views on investment strategy and stewardship. It is not therefore possible at all times to accommodate the preferences of all beneficiaries. However, the boards of the collective vehicles scrutinise Aberforth's stewardship policy and monitor compliance with it. In the case of the segregated charity funds, consultation with their investment committees has led to potential investments not being made and to a refinement of exclusion lists. Over the past year Aberforth has followed its stewardship and investment policies for all its investments and for all its clients.

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Principle 7

Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.

Context

Aberforth's investment process takes into account all issues that its investment managers judge to be relevant to a company's valuation. An investee company's journey through the process – from pre-purchase analysis to final exit – is determined by the interplay between Aberforth's valuation of the company and the price attributed to it by the stockmarket. Any environmental, social or governance issue could, therefore, be of importance particularly as the increased profile of ESG affects stockmarket valuations. Consideration of these issues is integrated into Aberforth's investment process, alongside a broad range of other factors. Aberforth believes that a company's system of governance is crucial to how its environmental and social policies are designed and implemented. It is therefore important that boards describe their approach to managing these issues. Except when requested by clients, Aberforth does not exclude investments from portfolios on the basis of ESG matters alone. There is evidence that investment returns can be enhanced by investment in, and engagement with, companies that face ESG challenges and are already seeking to address them or can be encouraged to do so.

The following ESG topics are of particular relevance and interest at the current time.

- Aberforth's environmental framework is built on the view that climate change is a systemic risk to economies and financial markets. The analysis of companies includes an assessment of how strategy and operations affect climate change, and *vice versa*, and evaluates plans to mitigate these effects. Companies that can invest proactively to diminish climate change could see improved recognition by the stockmarket. True to the value investment philosophy, it is also possible that other investors might overreact to perceived risks and reduce company valuations such that attractive investment opportunities become apparent.

- From the social perspective, the durability of a business is dependent on it treating its customers, employees and suppliers with care and respect. Aberforth looks for evidence of how companies treat stakeholders and believes that can inform on the culture, which ultimately affects valuation.

- Aberforth considers diversity and inclusiveness when assessing governance structures. Those companies able to create and sustain cultures of inclusion are likely to attract and retain the best talent. Diversity is likely to improve decision making and so improve investment outcomes. Pragmatism, particularly for smaller companies, and fairness are also important considerations.

How Aberforth engages and votes on these issues is described in Principles 9 to 12. Further information can be found in the engagement and voting policies, linked HERE and HERE respectively.

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Activity

Integration of stewardship and investment is straightforward, facilitated by Aberforth's ownership, client engagement and portfolio management structures. As described under Principle 2, all investment managers are normally also partners of the firm. This ensures that the importance placed by the firm on issues such as ESG flows directly into company analysis, engagement and the management of clients' portfolios. Moreover, engagement with clients is also undertaken by the investment managers and so there is no barrier to the implementation of clients' objectives, time horizons and instructions into the investment process. This degree of integration is possible because of Aberforth's small size, the experience of its investment managers and its relatively flat hierarchy.

In practice, the firm divides the stockmarket by sector between its investment managers. Therefore, for the purposes of company analysis and the implementation of stewardship, one manager has lead responsibility for each company. In challenging and time-consuming situations, or when the clients' combined stake in a company exceeds 10%, a second investment manager is appointed to support the lead. A similar approach is taken to client engagement, with each client relationship led by two investment managers. Decision-making, whether at the portfolio management or client engagement level, is undertaken collegiately by the investment management team or, if relevant, by the partners including the operations partner.

Aberforth has controls to monitor the integration of stewardship into the investment process as described above. Stewardship activities are overseen by the Stewardship Group, whose role is set out more fully under Principle 2. Monitoring is facilitated by IT systems developed in-house. A review of these systems during 2020 led to further developments, which should enhance reporting from 2021 onwards. On-going review is likely to give rise to further refinements.

Outcome

Aberforth has a long record of frequent and in-depth engagement with investee company boards, which, together with its voting commitment, demonstrates the importance of stewardship to the investment process. Given the frequency of engagement, stewardship considerations affect the overwhelming majority of investment decisions, from new purchases to exit decisions. These investment decisions are always taken in the interests of long-term value for clients and investors, though, as described above, benefits to the economy, environment and society are also considered. The three examples below, which focus on ESG issues, are taken from different stages of the ownership life cycle.

Example: Spire Healthcare Group [Social – decision to purchase plus ongoing monitoring]

Spire Healthcare operates one of the UK's largest private hospital estates. Patients, staff, and customers have had their confidence in care standards tested after a rogue surgeon was found to be performing unnecessary and damaging operations. This ultimately led to criminal prosecution, severely damaging the company's reputation and brand in the process.

Beyond the immediate harm done to patients, Aberforth was concerned at the lasting effects of this episode on value. Discussion of the investment case led to further research, monitoring and engagement. Meetings with management and the chair ultimately reassured on the "quality of care" agenda: since 2016, a cumulative £24m – roughly half of operating profit in 2019 – had been invested into clinical oversight despite no clear view on the time frame for payback. Further diligence involved engagement with suppliers and medical practitioners to understand how other stakeholders would respond to the changes being made. The research concluded that Spire was making the investments required to achieve better standards of clinical care and, in turn, allowing the business to recover to market growth rates over time.

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Aberforth's funds took an initial position in Spire in 2019 and further purchases followed through 2020. Whilst the payback from the company's investments was uncertain, they have already proved beneficial to equity holders with the onset of the pandemic. The suspension of UK elective care procedures coincident with lockdown had the potential to cause financial distress for the company. Spire made the entirety of its estate available exclusively for the National Health Service and without profit. This facilitated crucial covenant waivers from creditors and is expected to serve all stakeholders well as the focus shifts to clearing a backlog of care to patients who have been forced to delay consultations and procedures.

Example: Eurocell [Environment – monitoring]

Aberforth's clients have had a longstanding investment in this extruder of UPVC components for windows and doors. The decision to invest was influenced by its sustainability credentials. Unlike its competitors, Eurocell is able to use recycled UPVC, which is collected from customers and processed in-house. This material competitive advantage provides a significant environmental benefit, as well as hedging against virgin polymer prices and creating superior profitability in a crowded market. While Eurocell's main customers are window fabricators, there is an opportunity to gain market share though educating the ultimate end customers (house builders and house holders) about the benefits of UPVC in durability, maintenance and thermal efficiency. This can help the company take market share and generate incremental economic profit whilst lowering the carbon emissions of its customers. Eurocell also has a finance facility in place that links the rate of interest charged to the proportion of recycled polymer used.

Example: TI Fluid Systems [Environment – monitoring]

TI Fluid Systems manufactures automotive fuel tanks and tubes for fuel, brake fluid and glycol. Parts of its business are therefore exposed to the internal combustion engine, which contributes to climate change. It seemed likely that the stockmarket's very low rating of the shares was in part due to this threat. Engagement with the directors therefore addressed how the company would cope with the rise of Electric Vehicles (EV) and Hybrid Electric Vehicles (HEV). Management articulated a coherent strategy that could ultimately see revenues benefit from EVs, as the company's average value per vehicle rises through sales of additional components and tubing for battery heat transfer. Last year saw important corroborations of this approach, with the announcement of various programme wins, including for VW's ID.3 and ID.4 EVs. Nevertheless, the transition to a fully EV world will be bumpy and engagement on the topic will continue.

Example: Kenmare Resources [Environment & Social]

Kenmare Resources operates a titanium minerals sand mine in Mozambique, which contains deposits of heavy minerals including ilmenite, rutile and zircon. The mining of natural resources tends to have a significant impact on the local environment and population, but stringent licensing requirements demand operational and behavioural excellence. Failure to adhere to these requirements could result in a loss of mine licence, substantial fine, or both.

One of the attractions of investing in Kenmare Resources is the lower impact of its operations on the environment compared to a more conventional mining operation. Kenmare's mine is surface based, does not involve explosions or chemicals, and is powered by hydro-generated electricity. Additionally, once mining is finished in a particular area, the topsoil is returned, with rehabilitation completed by the seeding or planting of native and/or other species of vegetation and food crops. The area of land is then returned to the local communities.

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Example: Vivo Energy [Governance / Environment / Social]

Vivo's business is the supply, storage and sale of Shell and Engen branded fuels and lubricants in Africa. The company is working on various initiatives to address the environmental effects of its business, such as optimising product deliveries to reduce distance travelled, more energy efficient service stations through solar power investments and the development of cleaner energy products. Vivo's environmental impact has to be weighed against its social impact – its network of 2,200 service stations, with their fuel and retail services, is a crucial socioeconomic resource in the 23 countries in which it operates. Engagement has made it clear that the company understands the importance of being a respected member of the communities, of doing business in the right way and of investing in local road safety education. On governance, the board includes four independent NEDs and two NEDs appointed by the major shareholders, Vitol and Helios. Despite the two non-independent NEDs, the composition of the board and its main committees is in line with the recommendations of the UK corporate governance code.

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Principle 8

Signatories monitor and hold to account managers and/or service providers.

Context

Aberforth has few third-party service providers in the area of stewardship, choosing instead to conduct most of these activities internally and directly. The firm currently has a long-standing relationship with a proxy voting adviser and more recently contracted with a provider of carbon data.

All other third-party services such as custodians, audit, IT and cyber risk management are covered by wider company policies and risk management documentation.

Activity

Aberforth currently employs the services of a proxy voting adviser. This relationship is subject to formal annual review but in practice is assessed continually throughout the year based on the timeliness and quality of their individual reports. To date the service provided has been satisfactory. Further information on Aberforth's voting policy can be found HERE.

During 2020 the firm contracted with a provider of carbon data. This was the first time the firm has purchased such data. The contract has been renewed for 2021 in order to provide more time to assess the service.

Other third-party providers of ESG information and data are kept under periodic review. At the time of the last review, Aberforth found the quality of information available within the universe of small UK quoted companies to be insufficiently comprehensive or of a high enough quality to merit its use. This will be assessed again during 2021.

Outcome

While Aberforth employs the services of a proxy voting adviser, investment managers are under no obligation to follow its recommendations and on many occasions take a different view. It is also the case that interaction with companies on issues raised by the proxy adviser can lead to a change in the investment manager's original voting decision. Internal reporting systems are currently being modified to ensure the capture and recording of instances in which the firm has voted against the proxy advice recommendation.

While it has been possible to capture raw carbon data internally, the third-party provider has added value through its portfolio analysis and scenario modelling. The contract with this party has been renewed for 2021 in order to investigate whether and how to integrate this into the investment process.

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Principles 9, 10 and 11

Signatories engage with issuers to maintain or enhance the value of assets.

Signatories, where necessary, participate in collaborative engagement.

Signatories, where necessary, escalate stewardship activities to influence issuers.

Context

Aberforth's policy on engagement can be found HERE. Responses to Principles 9, 10 and 11 have been combined to avoid repetition and to reflect the related nature of the three components.

Regular, open and constructive engagement with the executives and boards of investee companies has always been an essential element of Aberforth's investment philosophy and process. Aberforth engages directly and believes that its clients and investee companies benefit from a policy of discretion on live engagements. The firm's experience is that ill-timed disclosure and public confrontation hinders the chances of successfully effecting change.

A flexible approach to engagement is important. This reflects the diversity of business models and differing specific circumstances facing individual businesses, particularly within the universe of small UK quoted companies. Moreover, Aberforth is conscious that the broader economy benefits from a thriving smaller companies sector and that this may be stifled by a one-size-fits-all engagement policy.

While determined to encourage high standards of stewardship and corporate behaviour, Aberforth does not wish to burden small company boards unnecessarily with engagement guidelines that can appear to have been designed for larger companies. This, for example, might mean taking a pragmatic view on compensation in acknowledgment of the considerable competition for executive talent.

Activity

Aberforth's clients in aggregate often hold significant stakes in investee companies. The investment managers tend, therefore, to have good access to executive and non-executive directors. The preference is for face-to-face meetings, particularly when addressing sensitive topics. Meetings at the firm's Edinburgh office makes it easier for several members of the investment management team to participate. In practice, much of Aberforth's engagement is conducted through phone calls and e-mail.

The prioritisation of engagements is undertaken by the investment committee at its formal weekly meeting and *ad hoc* as required. Engagement is conducted by the investment managers. Their number and experience allow multiple engagements to occur at any given time. The investment manager with responsibility for the company presents the investment case to the investment committee and, if necessary, proposes an engagement strategy. The ensuing discussion, which takes into account the holding size and the ability to influence, results in the agreement of an engagement strategy and objectives. In common with the context and activity outlined in Principles 1 and 6, the objective of this engagement will be to either preserve or enhance value for clients. This way of operating is consistent across all Aberforth's client mandates.

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As part of on-going due diligence and appraisal of the investment universe, Aberforth typically meets executive directors of each investee company at least twice a year. These meetings address operational and financial performance, competitive positioning in the context of broader industry developments, outlook, strategy and capital allocation, all of which might involve environmental, social and governance issues. The outputs from these engagements are used to inform a view on a company's underlying value, which allows it to be considered in the broader capital allocation process.

Interaction with executives helps to understand a company and the issues affecting it, but the chair's role is pre-eminent within the UK's governance regime. The chair has oversight of the executives and is responsible for strategy and capital allocation. Accordingly, Aberforth's engagement approach emphasises contact with the chair. The frequency and depth of engagement with the chair increases proactively as the stake held by the firm's clients rises and reactively should the investment case deviate from its expected path. Aberforth also values engagement with the senior independent non-executive director (SID) and other non-executives. This becomes particularly relevant when the chair's performance is in question. In addition to the topics raised in executive meetings, engagement with non-executives can address upcoming votes, remuneration, executive performance, board succession, corporate strategy and capital allocation.

As part of its engagement approach, Aberforth operates a formal "significant stakes" process, which commences when clients' collective interests exceed 10% of the voting rights in an investee company. This triggers a review of the investment case pertaining to the company and engagement requirements, though becoming a "significant stake" is not in itself a reason to escalate engagement. An additional investment manager is assigned to the company. That manager may participate in meetings with directors and provides additional rigour and challenge to the existing investment case. "Significant stakes" are reviewed collectively and formally at least once per year. The upper limit for a "significant stake" is 25% of the voting rights of an investee company. Such a stake brings great influence, though Aberforth does not seek board positions. Rather, its *modus operandi* is to work with and through the company's executives and independent non-executives.

Since Aberforth's clients are often large holders of investee companies, the investment managers are usually able to engage directly and effectively with board members. There are, however, instances when a collective approach to engagement may be appropriate. These collective engagements can occur when Aberforth considers the cumulative holdings of the firm's clients insufficient to effect change. The firm's interaction with other investors is influenced by the terms of the Takeover Code. Beyond specific engagements, Aberforth sees value in the sharing of views with other industry practitioners and in participation in industry forums.

Escalation of engagement normally occurs when an investment thesis starts to stray from the expected path. The escalation process exists to protect the interests of Aberforth's clients. The weekly investment meeting is the forum for formal consideration of the status and effectiveness of live engagements. The investment manager responsible for the company in question leads the discussion, which involves analysis of the situation and the progress made to date. In discussion with the rest of the investment management team, an escalation plan is formed. The plan seeks to address the concerns of Aberforth and propose how, and in what time frame, they might be remedied. The first move in an escalation is usually to engage with the chair, but, if the chair is considered part of the problem, the focus turns to the senior independent director. Aberforth may also contact the company's advisers and other investors to inform them of concerns. Other options include a formal letter expressing concerns and expectations to the board, as well as the requisition of an Extraordinary General Meeting. In practice, the "significant stakes" process described above often overlaps with, and forms part of, an escalation plan.

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Outcome

Meetings with board members of investee companies are an important element of Aberforth's investment process. Each year, there are multiple meetings with each holding. During 2020 Aberforth conducted 396 executive level meetings and 125 non-executive meetings with companies held in its portfolios. These numbers compare with 338 and 92 respectively during 2019.

Enhancements to the systems used for monitoring and recording engagements were implemented during 2020. As this was completed part way through the year, not all engagement activity was fully captured in 2020. Therefore, the numbers reported above potentially under-state the degree of engagement conducted. It is intended that these new recording methods will see more comprehensive measuring and reporting of engagement in future reporting periods.

Given the impact of Covid-19, company engagement took on even greater importance during 2020. Aberforth sought to understand how companies were dealing with the operational restrictions of lockdown and its financial implications. This was especially important in light of the relaxation of pre-emption guidance, which allowed companies to issue up to 20% new equity without pre-emption rights. As discussed in Principle 4, these discussions also formed the basis of engagement with representatives of the Bank of England, who received feedback, through Aberforth, about companies' ability to access official support programmes. Engagement enabled better understanding of restructuring or capital allocation changes resulting from Covid-19 and of how investee companies were likely to emerge as restrictions were lifted.

The engagement examples below demonstrate the range of issues addressed in meetings with investee companies during the period.

Example: The Restaurant Group

Aberforth continued its engagement after voting against the acquisition of Wagamama in 2018, and the re-election of the chair and SID in the subsequent AGM. As a leisure business with physical venues, Restaurant Group has been adversely affected by Covid-19, but executive management have performed well to reposition the business as demand recovers. However, lockdown has challenged the balance sheet and refinancing is probable. Aberforth's confidence in the chair's oversight of capital allocation was shaken by the heavily dilutive Wagamama acquisition, which continues to affect the company's stockmarket valuation. Accordingly, Aberforth believes that it is in the interests of all shareholders for a new chair to be appointed and again voted against the re-election of the chair.

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Example: SIG

SIG's chairman acted decisively to address poor historical performance, articulating a cogent and refreshed strategy. However, the impact of the pandemic made additional capital funding inevitable. A depressed stockmarket valuation, together with confidence in SIG's market leading position and the ability to generate higher returns over time, gave confidence in significant upside and encouraged us to support strengthening the capital structure for the long term. Engaging proactively with the chair, Aberforth provided indicative support ahead of a £165m equity capital raise, which completed on 9 July. The structure of the equity raise was a firm placing and placing and open offer, which afforded greater flexibility in allocating new shares but came with the risk of dilution to existing shareholders. Usually, Aberforth's proactive engagement and support mean that clients' stakes can rise through the firm placing. However, in the case of SIG, this did not apply. Amid its refinancing discussions, the board was approached by Clayton Dubilier & Rice (CDR). The outcome of negotiations was that CDR would invest £82.5m through the equity issue to take a 26.7% stake and two board seats. Aberforth was consulted and judged that, in view of the circumstances and despite ownership dilution, it represented the best outcome for clients' capital. "PIPE" deals such as this are relatively uncommon in the UK, though better established in the US.

Example: Company A

Aberforth's clients are one of the largest shareholders in company A. In the years before the pandemic, the company had rebuilt its reputation and strengthened its balance sheet following previous over-expansion. The onset of Covid-19 threatened to undo this rehabilitation and the board proposed raising additional equity, as well as cutting the dividend, to protect the business.

To ascertain the need for additional equity, Aberforth had numerous meetings with the executive team and chair to understand the assumptions behind their downside scenario analysis. Having assessed this, and taking into account industry dynamics, Aberforth argued that there was not a need for equity at that time. The company did not raise new capital. This was a difficult decision given the significant prevailing uncertainty, but it proved correct given the subsequent return to profitability, resumption of dividends and avoidance of dilution.

Example: Gulf Marine Services

Following proactive involvement with the board in the appointment of the chair, Aberforth worked closely with the chair in respect of a restructuring proposal, which would have involved an equity raise and the deleveraging of the operating business. During this process the company was subject to a bid by a competitor, Seafox International, at a level that failed to reflect the long-term value of the business. The bid was unsuccessful, but, through a series of Extraordinary General Meetings, Seafox was subsequently able to remove existing directors and appoint its nominated individuals as directors. Aberforth voted against all such proposals and separately contacted the Takeover Panel to express concern about the process and ability for Seafox to gain effective control of the business despite their previous failed bid attempt.

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Example: Lookers

A potential fraud and weaknesses in accounting process caused a delay to the publication of its financial statements and the temporary suspension of the shares from 1 July 2020. Against this background, Aberforth increased engagement with the company, focusing on (a) the reasons for the publication delay, (b) the necessary steps required to strengthen governance, (c) the composition of the board and (d) remuneration, specifically, malus and clawback provisions. The chair and senior independent director reassured that the board was alert to these concerns and would take the necessary steps to enhance governance, systems, and controls. Subsequently, the search for a new chair commenced and, in this regard, engagement continues.

Example: Non-Standard Finance

Investment in this branch based non-prime lender was made for the prospect of organic growth through increasing the number of branches, with the expansion risk mitigated by robust underwriting from the face-to-face pre-lending process. Aberforth cautioned against the launch of a bid for Provident Financial questioning the timing and suitability of such an approach. This advice went unheeded, which led to extensive engagement with the chair and other non-executive directors to determine the level of scrutiny over the executives. Failing to reach a satisfactory conclusion, Aberforth lost confidence in the chair, informed him and voted against his re-election at the AGM. As these concerns continued to be overlooked, it was decided to sell clients' holdings in the company.

Example: Kenmare Resources

During 2020, Kenmare Resources successfully completed the movement of a dredge and 7,100 tonne wet concentrator plant 23km to a new, higher grade, mining area. The project should transform Kenmare's production and profit growth prospects for the medium term, and should result in significant cash generation once fully operational. Aberforth conducted several engagements with the executive team and chair about capital allocation, expressing the view that, in light of limited future capex requirements, a significant proportion of the cash generated from the expansion should be returned to shareholders through cash dividends.

Health and safety is a crucial focus for mining companies, including Kenmare, with potentially significant negative repercussions for poor operating standards. The company has a good record, so it was sad and surprising when a casualty was reported at the Moma mine in 2020. Aberforth engaged with Kenmare to understand the circumstances behind the fatality. It was explained that the death was not related to mining activity and that there had been no lapse in operating standards.

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Example: Air Partner

Clients of Aberforth had been longstanding investors in this aviation services business and one of the largest shareholders. Initially, Air Partner was a beneficiary of Covid-19 as the company was at the forefront of repatriating citizens and moving PPE across the globe. Naturally, this extra demand filtered into a stronger profit outlook, improved balance sheet position and a much higher share price. Despite this, the board approached major shareholders with a view to issuing equity to strengthen the balance sheet further.

Aberforth conducted several meetings with the executive team and chair to understand the assumptions behind their analysis. Having assessed this, Aberforth decided there was not a need for equity at that time and relayed this message to the chair. Unfortunately, this engagement proved ineffectual and the company proceeded with the equity raise. This led to the sale of clients' holdings in the company.

Collective engagement

Working with other shareholders can be an important option in Aberforth's approach to stewardship with its investee companies. In 2020, there were six examples of collective engagement involving dialogue with other institutional investors. Several of these engagements continue into 2021. While all of these instances remain sensitive in nature and disclosure at this time would be counterproductive to the engagement objectives, it is the intention to disclose in due course when matters are concluded.

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Principle 12

Signatories actively exercise their rights and responsibilities.

Context

There are three main methods by which Aberforth exercises its rights and responsibilities.

- The investment managers engage with the boards of investee companies in order to understand the companies' strategies and governance and, if necessary, to effect change. The ability to engage is improved by Aberforth's willingness to take meaningful stakes in investee companies. On a majority of occasions, issues of board structure, dividend policy, remuneration and share issuance permissions will have been discussed before these issues are put to shareholders for approval at a General Meeting.

- Voting is a fundamental right for shareholders and is an important means by which Aberforth exercises stewardship on behalf of its clients. The firm's policy is to vote on every resolution put to shareholders at a General Meeting. Aberforth voted on all items at all general meetings over the past year, in line with its policy. Because of the depth and frequency of engagement with the boards of investee companies, Aberforth will have had the opportunity to influence important issues before they are put to shareholders at a General Meeting. This results in fewer votes against the board or abstentions than might otherwise be expected.

- The third method is to sell a holding – a basic concept but one that sets listed equities apart from some other asset classes. When an investee company encounters operational difficulties, Aberforth will typically engage to understand if a change of strategy or of personnel on the board might plausibly contribute towards an improvement in the company's prospects. If that does not appear forthcoming, Aberforth will typically exercise its right to sell the holding.

Aberforth manages five client funds, as described under Principle 6. Four of the funds follow the firm's voting policy, with the firm exercising the voting rights. One of the segregated charity accounts retains its own voting rights and may therefore override Aberforth's policy. Research from a proxy adviser is used, but the firm does not always follow its default recommendations. Aberforth's three collective funds do not engage in stock lending. The two segregated charity funds may do so.

Aberforth's voting policy can be found HERE.

Activity

Aberforth's voting record over the past year is available HERE. Votes were cast on all resolutions in respect of all shares held under Aberforth's voting control. No voting decisions were taken by another entity on behalf of these shares. Shareholdings and voting rights are monitored through in-house fund accounting systems and a third-party voting service provider, which are reconciled with custodians' records. Explanations for a selection of noteworthy voting decisions are provided in the Outcome section below.

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Outcome – voting examples

Non-Standard Finance

Vote AGAINST re-election of the chairman

Following the extensive engagement described earlier in this report, Aberforth lost confidence in the chair and voted against his re-election at the AGM.

The Restaurant Group – consolidated into single example below

Vote AGAINST re-election of the chairman

TI Fluid Systems

Vote AGAINST remuneration

As was the case in previous years, the potential rewards from the variable element of the proposed remuneration package were excessive – these could see the executives earn seven times their salary.

Amigo Holdings

Voted AGAINST board changes – several occasions

Two general meetings were requisitioned by the majority shareholder, Richmond Group. On both occasions, Aberforth voted against the proposals to remove the board of directors in favour of Richmond Group representatives. This would not have conformed to governance standards and potentially left the company at risk of not complying with certain FCA regulatory requirements.

Gulf Marine Services

Voted AGAINST shareholder proposal to change the board

As discussed in the Engagement examples, Seafox were unsuccessful with a bid for the company, but, through a series of Extraordinary General Meetings, was ultimately successful in appointing its nominated directors to the board, effectively achieving control of the company. Aberforth voted against all such proposals and contacted the Takeover Panel to express concern about the process and ability for Seafox to gain effective control of the business despite their previous failed bid attempt.

SDL

Voted AGAINST scheme of arrangement – proxy advisor was FOR

Voted AGAINST merger agreement – proxy advisor was FOR

Aberforh voted against the Scheme of Arrangement for the takeover of SDL by RWS. This was motivated by the all-paper terms of the deal, which exposed the clients to a richly valued company that, by virtue of its AIM listing and large size, could not be a long-term holding.

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Whilst voting FOR a resolution does not usually merit explanation, there are circumstances in which such votes are significant. The example below covers one occasion and demonstrates the importance of combining voting decisions with engagement.

Lookers

Voted FOR re-election of chair and non-execs

Following the company's potential fraud and delay to the publication of financial statements, Aberforth initially intended either to abstain or vote against a suite of non-executive directors, including the chair. In line with usual practice when considering such votes, Aberforth engaged with the company to explain the rationale. As part of that engagement process, the board offered reassurance that it was aware of the issues and that governance was not at odds with shareholders' interests. The discussion centred on the importance of not destabilising the board while it finalised the publication of the delayed financial statements. Pragmatically, therefore, the initial intention was reversed and votes in favour of the re-election of the chair and non-executives were lodged.

Votes different from proxy advisor recommendation

During 2020 there were 65 instances, in which Aberforth did not follow the voting recommendations of its proxy adviser. Some examples are set out below.

The Restaurant Group

Voted FOR remuneration policy – Proxy advisor was AGAINST

Voted FOR restricted share scheme – Proxy advisor was AGAINST

Voted AGAINST chair – Proxy advisor was FOR

Aberforth has engaged extensively with The Restaurant Group since investing in 2016 and continued to do so in 2020. The expensive and dilutive acquisition of Wagamama in 2018 raised concerns about the company's governance, which culminated in a vote against the transaction. During this process, engagement with the chair, and SID at the time, was unsatisfactory, which led to votes against at subsequent AGMs.

The pandemic exposed the misallocation of capital, with the business carrying too much debt and facing a significant loss of earnings. Aberforth supported a necessary equity issue: concerns about the chair were outweighed by confidence in the new CEO, who used the crisis to aggressively re-position the business away from underperforming legacy sites through a CVA. This significantly reduced the lease exposure of the company and improved future profit potential.

Despite these efforts, the executives did not have suitable incentives in place, with cash bonuses cancelled to conserve cash and LTIPs significantly under water. Further engagement with the board gave comfort about a proposed restricted shares scheme with profit underpin. Accordingly, Aberforth voted in favour of remuneration changes, which was against the recommendation of the proxy adviser.

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Redde Northgate

Voted FOR remuneration policy – Proxy advisor was AGAINST

The proxy adviser judged that a vote against the remuneration policy was warranted since concerns persisted about the Value Creation Plan. Aberforth engaged with the chair before the vote to understand the nature of the arrangements. The company confirmed that it would consult with shareholders, review the on-going appropriateness of the scheme and that no awards would be made under the plan in 2020. In light of this, a vote in favour was justified. As regards the remuneration report, the proxy adviser also recommended a vote against. In order to ensure alignment with shareholders, Aberforth agreed with the chair that there should be an incentive award, which recognised the aims of the newly enlarged group and the skills and experience of the executive directors. A vote in favour of the remuneration report was therefore warranted.

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