MORNINGSTAR | SUSTAINALYTICS

Material Risk Engagement

2024 Q2 Report



Material Risk Engagement promotes and protects long-term value by engaging with high-risk companies on financially-material ESG issues.

Table of Contents

Table of Contents (cont.)

Engagement Approach

Morningstar Sustainalytics’ Material Risk/Strategy & Risk Engagement (MRE) engages with high-risk companies on the material ESG issues with the greatest levels of unmanaged risks. The purpose is to protect and develop long-term value in our clients’ portfolio companies. Material Risk/Strategy & Risk is an engagement overlay of Sustainalytics’ flagship product, ESG Risk Ratings.

The Stewardship team will engage with companies in Morningstar Sustainalytics’ Ratings universe, consisting of more than 4,500 investable issuers in developed and emerging markets, which have an ESG Risk Ratings score of 30 or more. The ESG Risk Ratings score reflects the unmanaged ESG risk, so the higher the score, the more risk the company is exposed to.

The engagement is driven by constructive dialogue. The research from the ESG Risk Ratings and the Controversies research are leveraged to encourage companies to cover gaps in Material ESG Issues risk management. Engagement Response, Progress, Positive Developments, and Milestones are consistently tracked to measure commitment and capability to change in addition to the engagement activities conducted. When a company improves by bringing the ESG Risk Ratings score to below 28, the Material Risk/Strategy & Risk Engagement case will be considered resolved.

Executive Summary

Palle Ellemann
Director/Product Manager, Stewardship
Engagement 360
Morningstar Sustainalytics

We are delighted to report on the activities and results of the Material Risk/Strategy & Risk Engagement (MRE) programme for Q2 2024. The quarterly report includes an article on ESG governance in the boardroom, two case studies of active engagements as well as case information on all resolved engagements.

Highlights for the Quarter

The companies we engage with continue to improve rapidly and we have been able to resolve 15 engagements in the second quarter, which occurs when the companies we engage with improve the ESG Risk Rating score below 28, indicating a move into the Medium ESG Risk Rating category, and lower unmanaged ESG risk. During Q2, the team has:

- Conducted 58 meetings.
- Exchanged 352 emails/phone calls.
- Achieved 78 Positive Developments and 42 Milestones. As expected, we are seeing a high number of Positive Developments and Milestones achieved, when we can document this progress via new company disclosure.

ESG in the Boardroom

We are sharing an article about the governance and oversight perspective of ESG from the boardroom. The emergence of ESG has challenged the boards to revisit the governance structure, but not all have been equally effective in doing so. Furthermore, ESG has questioned the traditional skillset of the board and whether or not the boards need to attract DEI (Diversity, Equity and Inclusion) and climate change experts, if these are material ESG issues for the companies.

Looking Ahead

In Q3, we anticipate our engagement activities will increase as there will be more companies releasing new annual ESG disclosure and it will be a good time to review company performance and update our suggested actions for the companies. This will also mean that we should be able to record a higher number of Positive Developments as it can be verified in the disclosure.

Engagement Overview

322
engagements as of 30 June 2024

10
new engagements

584
companies engaged since March 2020

SDG 13 Climate Action
linked to 61% active engagements

Asia Pacific
region with the largest number of engagements

Oil & Gas Producers and Utilities
industries with the most engagements

Disclosure
top material ESG topic in engagement dialogues

Engagement Status

When we open an engagement, the status is Engage. We will then pursue engagement until we change status to:

Resolved The company has achieved the engagement objective.

Archived Engagement is concluded, the engagement objective has not been achieved.

Disengage Engagement is deemed unlikely to succeed.

334 engagements as of 01 April 2024

10 new Engage

15 Resolved

5 Archived

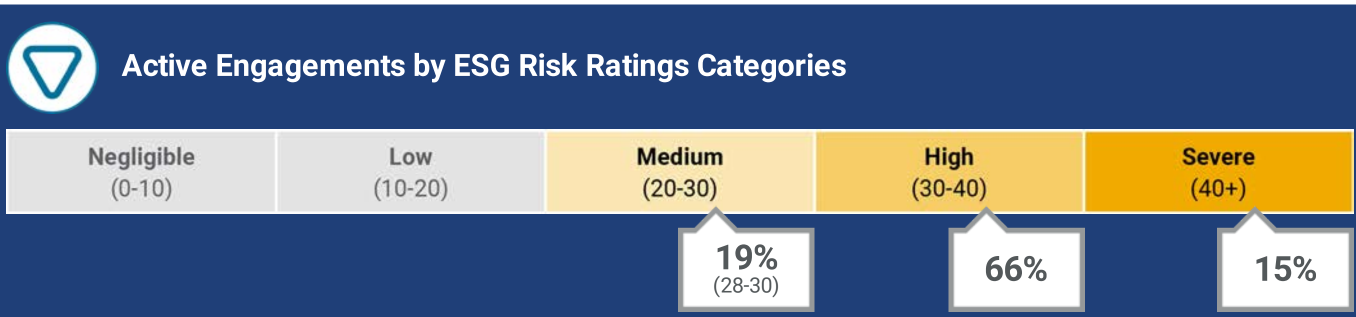
0 Disengaged

322 engagements as of 30 June 2024

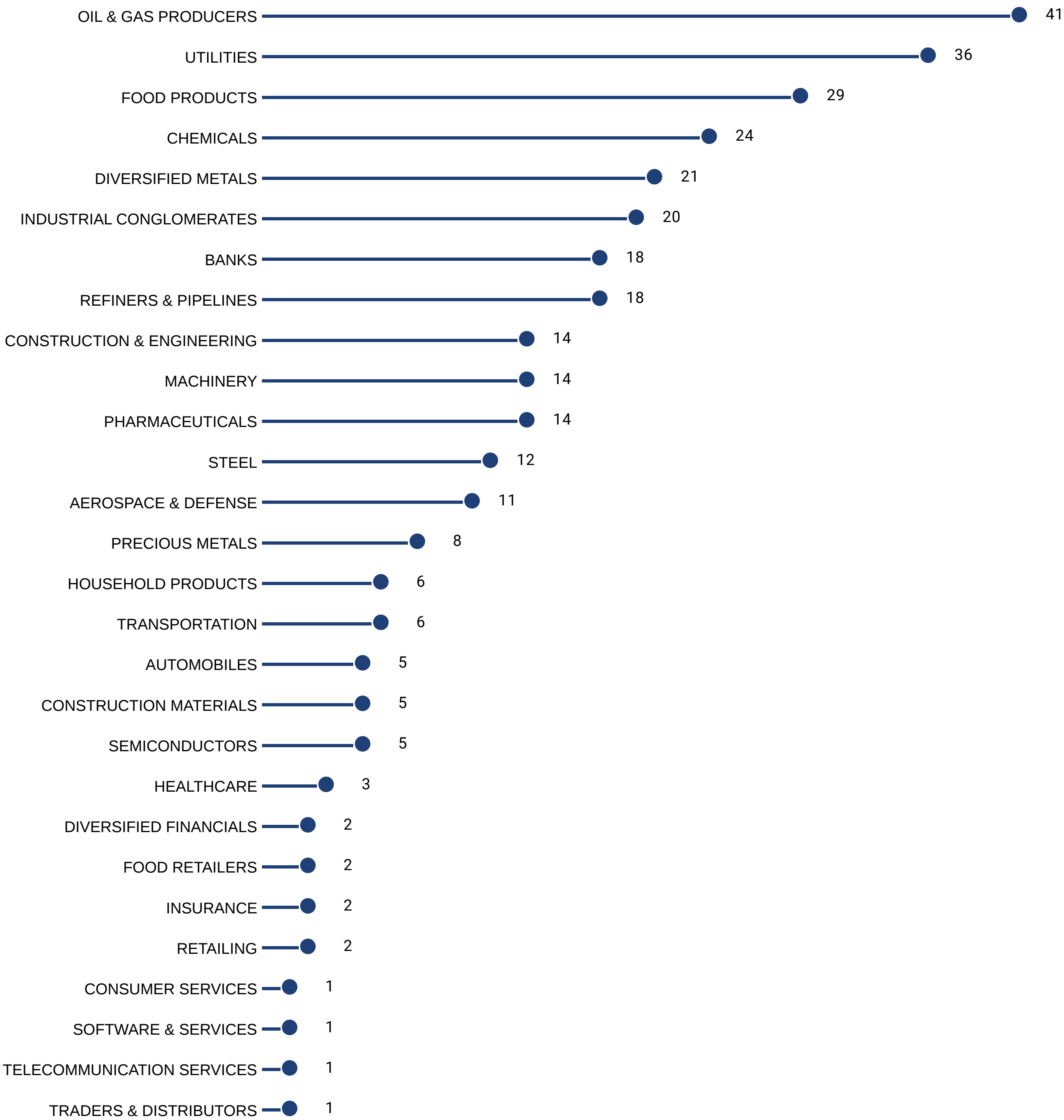
344 engagements during Q2 2024

On a regular basis, universes are rebalanced and issuers might therefore be delisted and removed from our data set. In such circumstances, opening and closing engagement counts will not match.

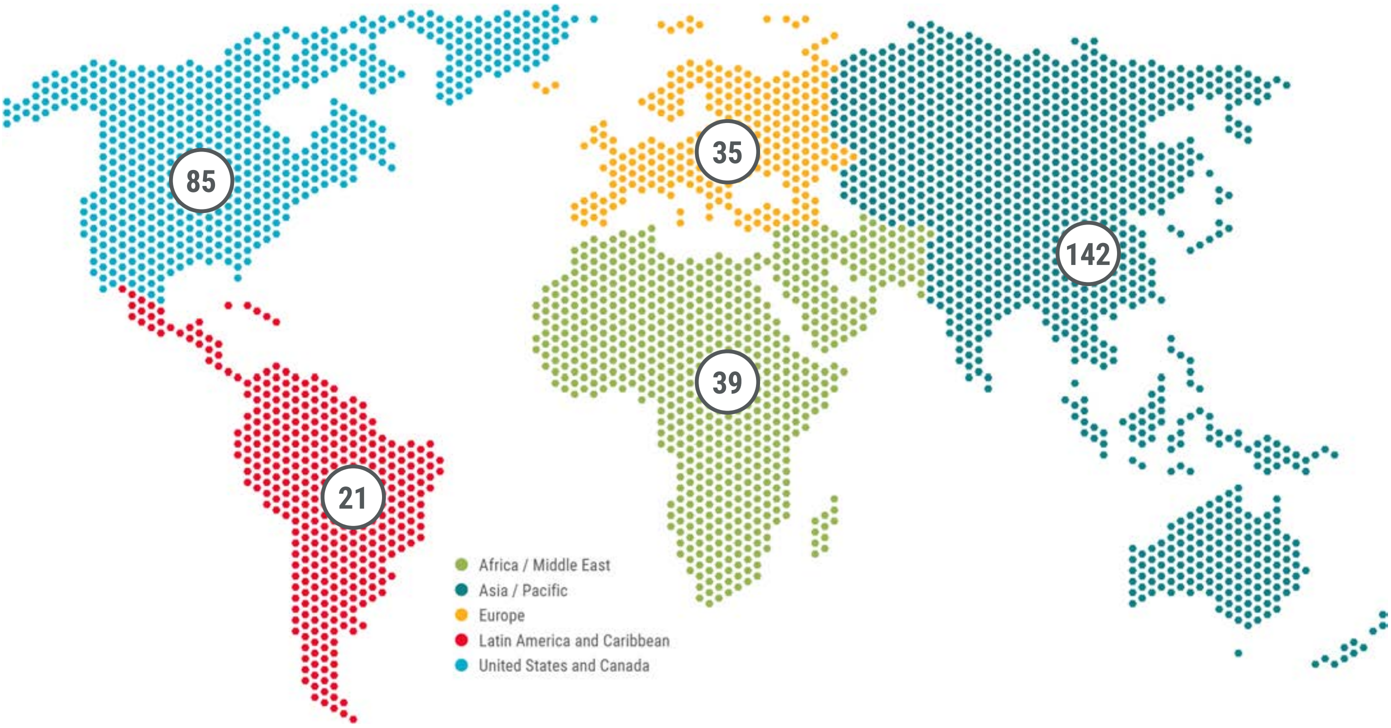
Active Engagements by ESG Risk Ratings Categories



Industry Distribution



Engagements by Headquarter Location

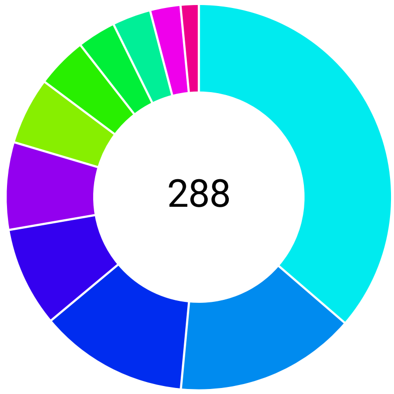


Engagement Topics

During the reporting period, our engagements addressed a number of topics across the environmental, social and governance pillars.

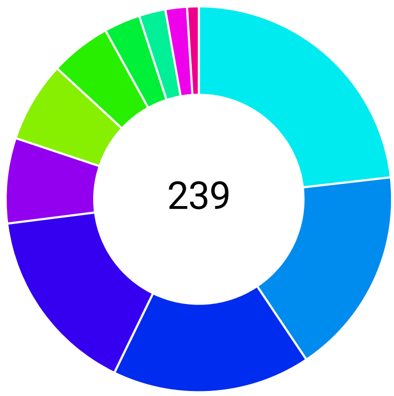
Environmental

- NET ZERO DECARBONIZATION (106)
- CLIMATE CHANGE (44)
- WATER SECURITY (36)
- WASTE MANAGEMENT (24)
- WATER QUALITY (21)
- BIODIVERSITY (16)
- LAND POLLUTION AND SPILLS (12)
- AIR POLLUTANT EMISSIONS (9)
- NATURAL RESOURCE USE (9)
- DEFORESTATION (7)
- CIRCULAR ECONOMY (4)



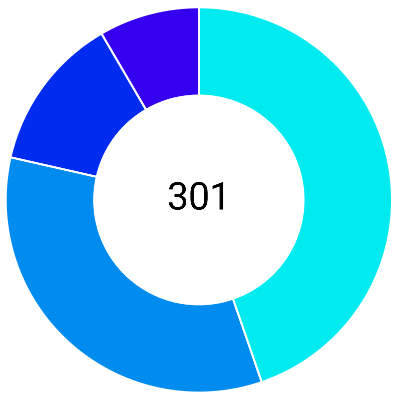
Social

- PRODUCT QUALITY AND SAFETY (56)
- HUMAN CAPITAL (42)
- COMMUNITY RELATIONS (40)
- OCCUPATIONAL HEALTH AND SAFETY (38)
- DIVERSITY, EQUITY AND INCLUSION (DEI) (17)
- HUMAN RIGHTS (16)
- DATA PRIVACY AND SECURITY (12)
- INDIGENOUS PEOPLE (7)
- MARKETING PRACTICES (5)
- LABOUR RIGHTS (4)
- HIGH-RISK TERRITORIES (2)



Governance

- DISCLOSURE (135)
- ESG GOVERNANCE (102)
- BUSINESS ETHICS, BRIBERY AND CORRUPTION (39)
- BOARD COMPOSITION (25)



Note : An engagement can cover one or more issues and objectives reflected in overlapping issue statistics.

Sustainable Development Goals - Mapping Engagements

All engagements are mapped to the 17 UN Sustainable Development Goals (SDGs). The mapping is done by Morningstar Sustainalytics and refers to the focus and objective(s) of the engagement.

1 No Poverty	1%	10 Reduced Inequality	2%
2 Zero Hunger	1%	11 Sustainable Cities and Communities	20%
3 Good Health and Well-Being	12%	12 Responsible Consumption and Production	45%
4 Quality Education	1%	13 Climate Action	61%
5 Gender Equality	3%	14 Life Below Water	2%
6 Clean Water and Sanitation	6%	15 Life on Land	5%
7 Affordable and Clean Energy	20%	16 Peace and Justice, Strong Institutions	57%
8 Decent Work and Economic Growth	22%	17 Partnerships to Achieve the Goal	2%
9 Industry, Innovation and Infrastructure	14%		

Case Study: Vistra Corp.

Material Risk/Strategy & Risk Engagement — Engagement Since: 25 February 2021

Industry: **Utilities**

Base Location: **United States**

ESG Risk Rating: **29.3**

Vistra is a leading US integrated retail energy provider and power generation company based in Texas, serving four million residential, commercial and industrial retail customers. Vistra is also the largest competitive power generator in the US.

Engagement Update

Four conference calls with Vistra have been held since 2021. The latest meeting in May 2024 focused on material risk and net zero transition, and we discussed the Vistra's progress towards its low carbon transition strategy and its disclosures on non-GHG air emissions, effluents and wastes. While the company demonstrates consistent improvements in its disclosure practices and climate transition strategy development, challenges remain regarding disclosure of the company's capital allocation to finance the low carbon transition and specific details regarding how these investments will contribute to achieving the company's GHG emission reduction targets and long-term net zero goal.

Focus Area

Discussions focused on the Vistra's effluent and non-GHG emissions management, decarbonization targets, climate transition strategy and associated metrics, data, and incentivization programs. Dialogue around Vistra's biodiversity and nature related risks was underpinned by its decommission and conversion processes of its coal plants, where Vistra described its current evaluation of utilizing land distribution for new solar power generation and battery storage systems on its properties, including those with decommissioned coal plants.

Engagement Outcomes

Positive developments were observed with Vistra's enhanced reporting regarding scope 1 and 2 GHG emissions, stakeholder relations, emergency response and spill management. The company remains open to suggestions to improve its disclosure practices. Vistra's upcoming 2023 Sustainability Report will include disclosure of its recently performed materiality assessment.

Insights & Outlook

The engagement showcases Vistra's ambitious yet cautious approach to achieving its decarbonization goals and demonstrates the company's proactive viewpoint to reclaiming decommissioned coal plants while also underscoring areas requiring enhanced disclosure. Investor queries on biodiversity and nature related risks, supplier engagement for scope 3 emissions reductions, and adequacy of disclosures regarding public policy engagement indicated growing interest in these areas.

Case Study: NEL ASA

Material Risk/Strategy & Risk Engagement — Engagement Since: 22 April 2020

Industry: **Industrial Machinery**

Base Location: **Norway**

ESG Risk Rating: **28.4**

NEL ASA is a hydrogen technology company delivering optimal solutions to produce, store and distribute hydrogen from renewable energy to industries, energy, and gas companies.

Engagement Update

We have held a total of five meetings with NEL, with the latest meeting in May 2024. The company has always been responsive and willing to continuously engage with Morningstar Sustainalytics and learn from investor perspectives. Since the beginning of our engagement, NEL has shown a strong commitment to formalizing and structuring its ESG governance, risk, and performance management. Additionally, the company has acknowledged the need to expand and improve the quality of its ESG disclosure.

Focus Area

At the start of the engagement, Sustainalytics discussed topics such as ESG governance and materiality, risk management, and sustainability strategy. As the company's approach to ESG evolved, the focus has recently shifted to product stewardship, eco-design and circularity, and human capital management.

Engagement Outcomes

NEL's ESG journey has been systematic and consistent. Early in the engagement, NEL established a cross-functional ESG management team to coordinate and implement ESG-related initiatives, and also conducted a comprehensive materiality analysis by consulting its main internal and external stakeholder groups. Following the assessment, it published an ESG policy explicitly outlining commitments regarding the strategic direction and objectives of the company's ESG program. The next phase of NEL's ESG program involved implementing a robust approach to govern business ethics risks, launching a whistleblowing function, and reporting statistics in line with best practices. Since 2023, NEL significantly accelerated its ESG program in response to the upcoming EU Corporate Sustainability Reporting Directive (CSRD). Some recently notable Positive Developments include advancements in eco-design, end-of-life initiatives, the implementation of a robust stewardship governance approach, a high level of externally certified management systems, and a heavily invested human capital management program.

Insights & Outlook

The engagement has showcased NEL's shift from a reactive to a proactive approach to ESG, anticipating and preparing for regulatory changes and evolving stakeholder expectations. The well-established and open dialogue provides Morningstar Sustainalytics with timely opportunities to offer tangible suggestions, supporting the company in further scoping and focusing its ongoing ESG efforts in line with investor information needs.

Engagement Results

58
meetings

352
emails and phone calls exchanged

15
engagements Resolved

42
Milestones achieved

78
Positive Developments

55%
of engagements with Good or Excellent Response

46%
of engagements with Standard Progress

Engagement Progress

Progress reflects the pace and scope of changes towards the engagement objective that the company is making, assessed on a five-point scale.

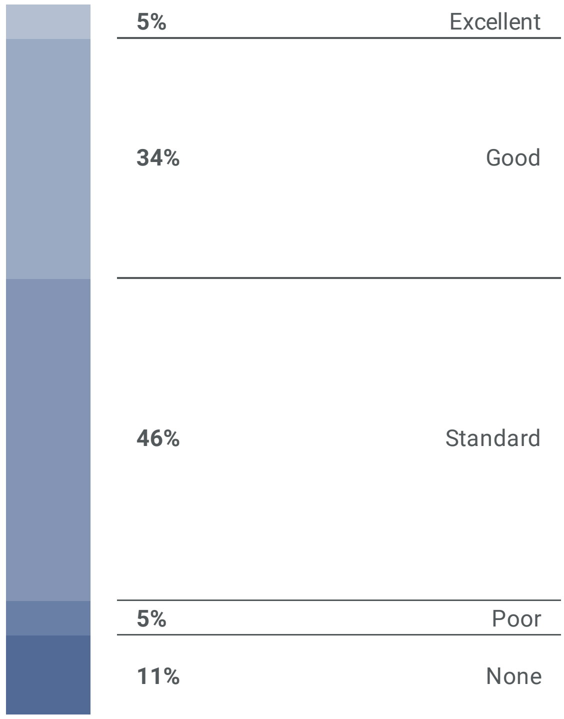
Excellent The company has adopted a proactive approach and addressed the issues related to the change objective.

Good The company has taken sufficient measures to address the issues related to the change objective.

Standard The company has undertaken a number of measures to address the issues related to the change objective.

Poor The company has indicated willingness to addressing the issues related to the change objective, but no measures have been taken yet.

None The company has not made any progress against the engagement objective.



Engagement Response

Response reflects the company's willingness to engagement diaolgue with investors, assessed on a five-point scale.

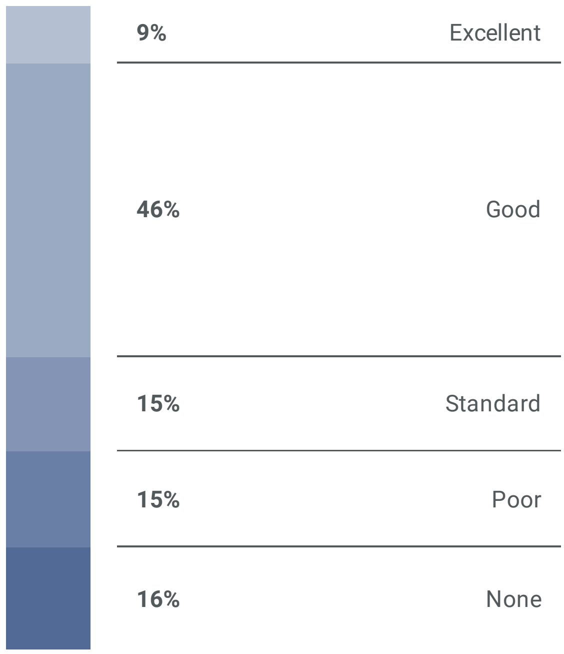
Excellent The company is proactive in communicating around the issues related to the change objective.

Good The company addresses all the issues related to the change objective.

Standard The company provides responses to some of the issues related to the change objective.

Poor The company has initially responded but not properly addressed the issues related to the change objective and is unwilling to engage further with us.

None The company has not responded to the inquiries.



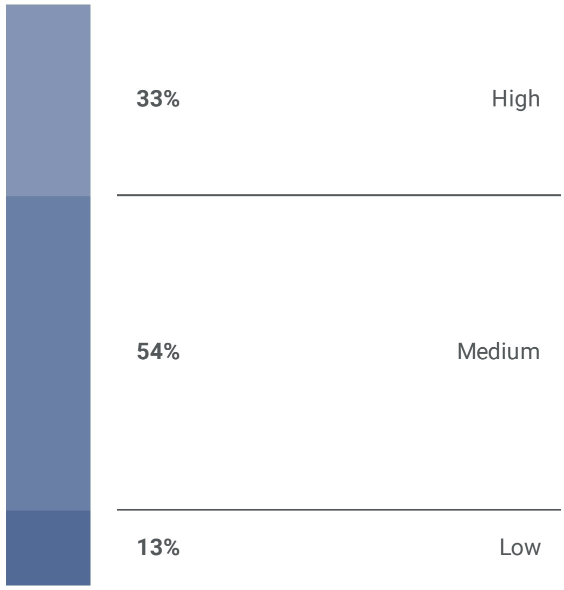
Engagement Performance

Performance describes the combined company Progress and Response.

High Good or Excellent Progress in combination with Good or Excellent Response.

Medium Standard Level of Progress and Response.

Poor Poor or None Progress in combination with Poor or None Response.



Engagement Milestones

Milestones are our five-stage tracking of progress in achieving the engagement objective.

42
Milestones achieved in
Q2 2024

Milestone Framework Structure

Milestone 5 Change objective is considered fulfilled.

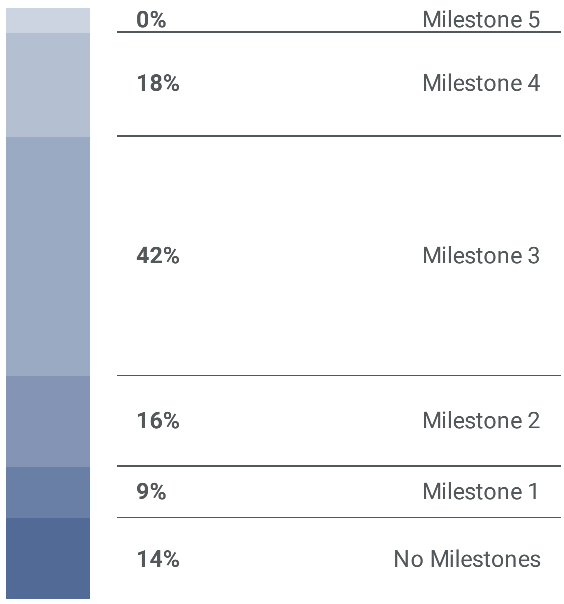
Milestone 4 Implementation of strategy has advanced meaningfully, and related issuer disclosure maturing.

Milestone 3 Strategy is well formed and has moved into early stages of implementation.

Milestone 2 ESG risk management and strategy established.

Milestone 1 Acknowledge of issue(s) and commitment to mitigation.

Engagements by Highest Milestone Achieved



Engagements Resolved

COMPANY	COUNTRY	INDUSTRY	ISSUE	QUARTER
CF Industries Holdings, Inc.	United States of America	Chemicals	Focus on Carbon and Emissions, Effluents and Waste	Q2
Chemical Works of Gedeon Richter Plc	Hungary	Pharmaceuticals	Focus on Access to Basic Services	Q2
Conagra Brands, Inc.	United States of America	Food Products	Focus on Product Governance	Q2
Envista Holdings Corp.	United States of America	Healthcare	Focus on Product Governance	Q2
Glanbia Plc	Ireland	Food Products	Focus on Product Governance	Q2
Graco, Inc.	United States of America	Machinery	Focus on Risk Assessment and ESG Disclosure	Q2
Grupo Bimbo SAB de CV	Mexico	Food Products	Focus on Corporate Governance	Q2
Hyundai Engineering & Construction Co., Ltd.	South Korea	Construction & Engineering	Focus on Risk Assessment and ESG Disclosure	Q2
Hyundai Motor Co., Ltd.	South Korea	Automobiles	Focus on Product Governance	Q2
Mitsubishi Heavy Industries, Ltd.	Japan	Machinery	Focus on Carbon Products and Services	Q2
OGE Energy Corp.	United States of America	Utilities	Focus on Risk Assessment and ESG Disclosure	Q2
Peab AB	Sweden	Construction & Engineering	Focus on Carbon and E&S Impact of Products and Services	Q2
PPL Corp.	United States of America	Utilities	Focus on Carbon and Emissions, Effluents and Waste	Q2
Shin-Etsu Chemical Co., Ltd.	Japan	Chemicals	Focus on Carbon Own Operations	Q2
Sumitomo Chemical Co., Ltd.	Japan	Chemicals	Focus on Carbon Own Operations	Q2

Resolved - CF Industries Holdings, Inc.

ESG Risk Ratings Score

Negligible	Low	Medium	High	Severe
(0-10)	(10-20)	(20-30)	(30-40)	(40+)

27.8

INDUSTRY:
Agricultural Chemicals

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
Carbon – Own Operations
Emissions, Effluents and Waste

RATIONALE FOR RESOLVED STATUS:
CF Industries. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- CF Industries has established and disclosed roadmaps to achieve its 2030 scope 1 C02e emissions intensity reduction goal and its scope 1 and scope 2 net-zero by 2050 goal. The company included details of its decarbonization projects for each area of its business aligned with impacted emission scopes along with broad indications of project timelines and progression levels. CF Industries' decarbonization roadmap demonstrates the main decarbonization levers the company expects to achieve its goals, including Process CCS, N20 Abatement, Reformer Flue Gas CCS, Residual Emissions, Virtual Power Purchase Agreements (VPPA) and Renewable Energy Credits (REC), as well as the absolute C02e reductions associated with each lever.
- As part of its goal to reduce Scope 3 emissions by 10% by 2030 (2020 baseline year), CF Industries purchased billion cubic feet (BCF) of natural gas certified to have 90% lower methane emissions intensity than the industry average. According to the company, this is the first known certified natural gas purchase for use in industrial manufacturing.
- In October 2022, CF Industries entered into the largest-of-its-kind commercial agreement with ExxonMobil to capture and permanently store up to 2 million tons of CO2 emissions annually from its Donaldsonville manufacturing complex in Louisiana.

In the latest ESG Risk Rating update, CF Industries' score improved by 1.6 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Chemical Works of Gedeon Richter Plc

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

27.3

INDUSTRY:
Pharmaceuticals

BASE LOCATION:
Hungary

ENGAGEMENT FOCUS:
Access to Basic Services
Product Governance
Business Ethics

RATIONALE FOR RESOLVED STATUS:
Chemical Works of Gedeon Richter Plc has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- In 2023 Gedeon Richter released a Position on the Conduct of Clinical Trials and Trial Data Transparency, which outlines its processes, control systems, and adherence to global standards.
- Gedeon Richter introduced comprehensive reporting on relevant product quality issues and indicators such as disclosure on number of product complaints and product recalls, number of drug safety reports per year, number of external and internal pharmacovigilance audits carried out.
- Gedeon Richter implemented a robust whistleblowing mechanism with relevant disclosure.

In the latest ESG Risk Rating update, Gedeon Richter's score improved by three points, bringing it into the medium risk category and below our 28-point threshold for engagement.

Resolved - Conagra Brands, Inc.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.9

INDUSTRY:
Packaged Foods

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
Product Governance
Resource Use
Corporate Governance

RATIONALE FOR RESOLVED STATUS:
Conagra Brands Inc. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Conagra's Board of Directors has a Nominating and Corporate Governance Committee overseeing climate-related issues, reviewing ESG goals, policies, and risks. This committee assesses stakeholder expectations and receives regular reports from management on ESG-related risks.
- All Conagra production facilities and over 95% of Tier 1 suppliers are GFSI-certified, ensuring high food safety standards. Regular training, incident investigations, corrective actions, and external audits are integral to their operations.
- Following a 2022 meeting with Sustainalytics, Conagra released its inaugural CDP Water Security Report in 2023, detailing their achievements and targets in waste and water reduction. It aims for 100% renewable, recyclable, or compostable plastic packaging by 2025 (currently at 93%) and has achieved a 2.7% reduction in water use intensity in FY 2022, saving 148.7 million gallons, toward a 20% reduction goal by 2030.

In the latest ESG Risk Rating update, Conagra's score improved by 8.4 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Envista Holdings Corp.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.9

INDUSTRY:
Medical Devices

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
Product Quality and Safety
Ethical Marketing
Human Capital

RATIONALE FOR RESOLVED STATUS:
Envista Holdings Corp. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Envista has introduced compliance programs that oversee anti-bribery, anti-corruption, and ethical marketing. Envista ensures product quality through ISO 13485 standards and internal audits and maintain ethical practices via global policies and regular employee training.
- Envista has implemented a comprehensive cybersecurity program which includes annual audits, risk assessments, and compliance reviews. Overseen by executive management and the Board, the program features an updated Information Security Policy and a Global Security Incident Response Plan.
- The company focuses on talent retention and diversity through development programs, performance evaluations, and career initiatives. In 2022, over 1,500 employees engaged in various voluntary trainings. With a 53% female and 50% ethnically diverse U.S. workforce and robust pay equity measures, Envista demonstrates its strong commitment to diversity.

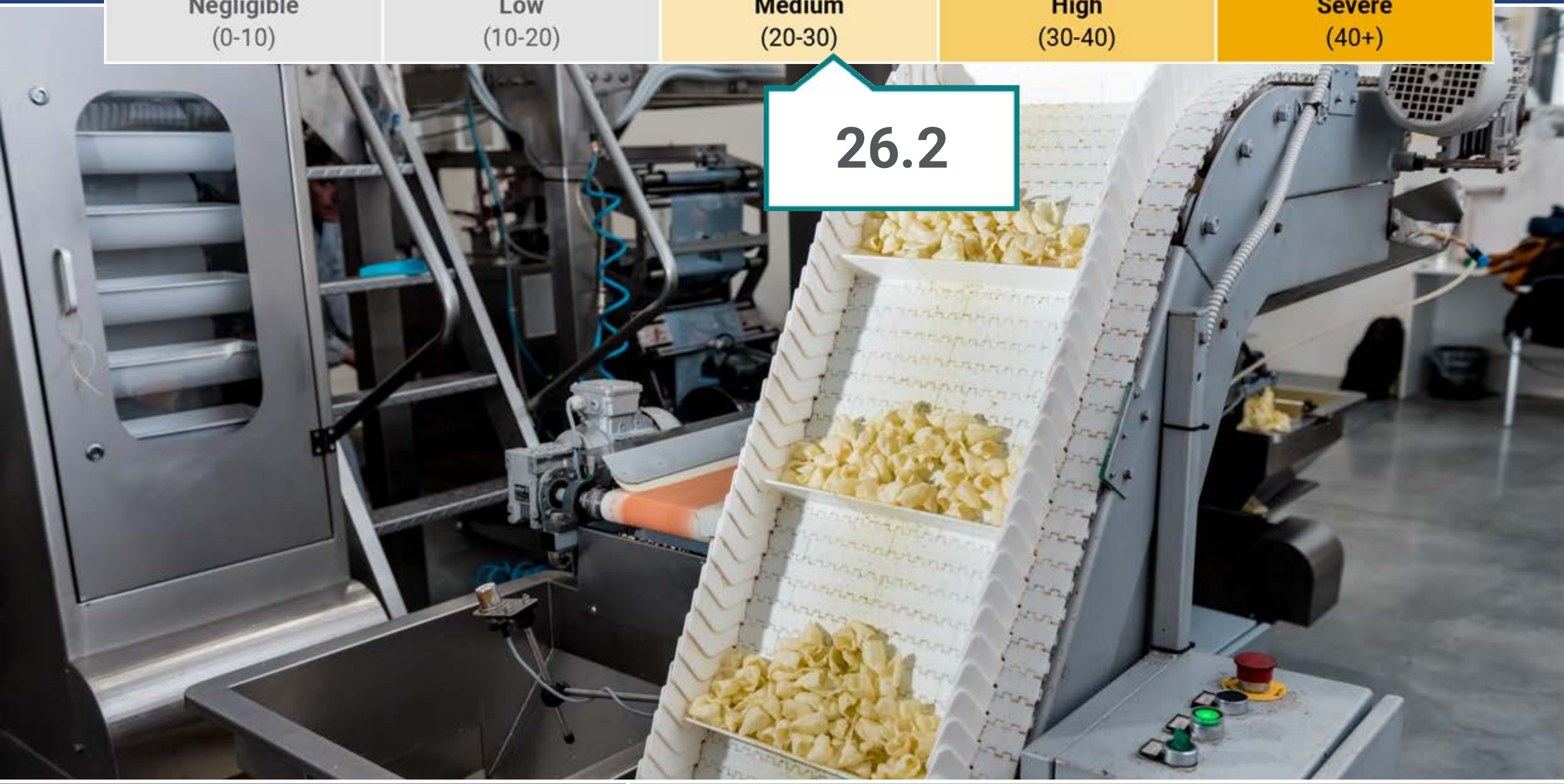
In the latest ESG Risk Rating update, Envista's score improved by 6.5 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Glanbia Plc.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.2



INDUSTRY:
Packaged Foods

BASE LOCATION:
Ireland

ENGAGEMENT FOCUS:
Product Governance
E&S Impact of Products and Services
Land Use and Biodiversity – Supply Chain

RATIONALE FOR RESOLVED STATUS:
Glanbia Plc has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Glanbia provided details on external certifications, clarifying that each of its sites is audited annually by internationally recognized third-party schemes such as the Global Food Safety Initiative and the National Sanitation Foundation.
- Glanbia disclosed its approach, governance, management, and responsible practices concerning responsible labeling and ethical marketing across both its B2B and consumer-facing segments.
- The company disclosed a robust ESG strategy that is firmly embedded in its core business. A comprehensive double materiality assessment identified and prioritized material topics, which are effectively managed and reported.

In the latest ESG Risk Rating update, Glanbia's score improved by 15 points, bringing it into the medium risk category and below our 28-point threshold for engagement.

Resolved - Graco Inc.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.9

INDUSTRY:
Industrial Machinery

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
ESG Disclosure
Risk Assessment

RATIONALE FOR RESOLVED STATUS:
Graco Inc. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Graco published its inaugural ESG report for fiscal 2021 at the end of 2022. The report content was guided by a materiality assessment done in consultation with stakeholders and by benchmarking reporting frameworks such as SASB, GRI and TCFD. The identified issues show good alignment with those identified by Morningstar Sustainalytics.
- Graco enhanced transparency on its ESG management structures in its 2021 ESG Report. The company has established a cross-functional ESG Steering Committee to coordinate a companywide approach to managing ESG issues and disclosures.
- In 2021, the company update the Corporate Governance Guidelines to reflect the Board's oversight of corporate strategies and initiatives relating to sustainability including ESG matters.
- Graco started reporting on work health and safety performances including the total recordable incident rate, days away restricted or transfer rate, fatality rate and hours of safety training initially in the 2021 ESG Report and subsequently in its 2022 ESG Report as well.

In the latest ESG Risk Rating update, Graco's score improved by 6.2 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Grupo Bimbo SAB de CV

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.7

INDUSTRY:
Food Products

BASE LOCATION:
Mexico

ENGAGEMENT FOCUS:
Product governance
E&S impact from products
Carbon – Own operations
Human capital

RATIONALE FOR RESOLVED STATUS:
Grupo Bimbo has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Grupo Bimbo has published its first set of Nutritional Guidelines to inform efforts on improving the nutritional value of products in the portfolio. It has developed various strategies to address the challenge with obesity in Mexico and elsewhere.
- Grupo Bimbo has signed the RE-100 pledge to source 100% electric energy from renewable sources by 2025. Grupo Bimbo has aggressively invested in renewable energy generation to cover their own needs. By 2020, the renewable energy capacity at Grupo Bimbo was equal to 80% of their energy consumption. By 2025, all Grupo Bimbo operations will be 100% covered with renewable energy.
- Grupo Bimbo has hired a new CEO and thereby separates the role of the CEO and the Chairman of the Board.

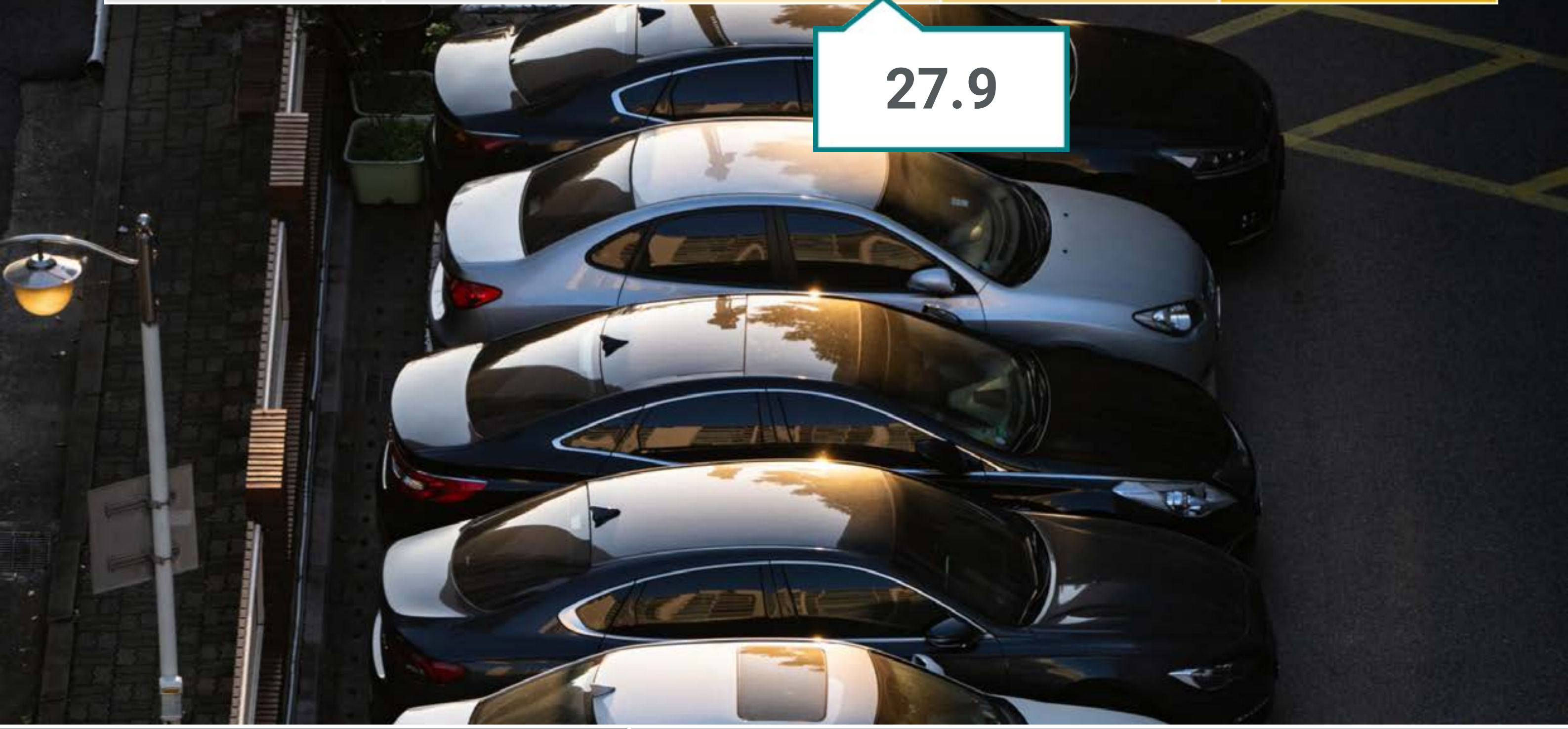
In the latest ESG Risk Rating update, Grupo Bimbo's score improved by 1.8 point, bringing it below the 28-point threshold for engagement.

Resolved - Hyundai Motor Co., Ltd.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

27.9



INDUSTRY:
Automobiles

BASE LOCATION:
South Korea

ENGAGEMENT FOCUS:
Product governance
Carbon – Products and Services
Human capital

RATIONALE FOR RESOLVED STATUS:
Hyundai Motor Co., Ltd. (HMC) has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- HMC has over the years significantly expanded disclosure on product quality and safety performance and now discloses statistics on product recalls and costs associated with these.
- HMC has improved the ESG governance with a clear reporting structure to the board level, where the redefined Sustainable Development Committee receives regular performance updates on the seven priority tasks. Additionally, it implemented a third party review of the board efficiency—driven by Korean university experts on corporate governance.
- Investor insight to human capital development has improved with disclosure on employee turnover and strike activities.

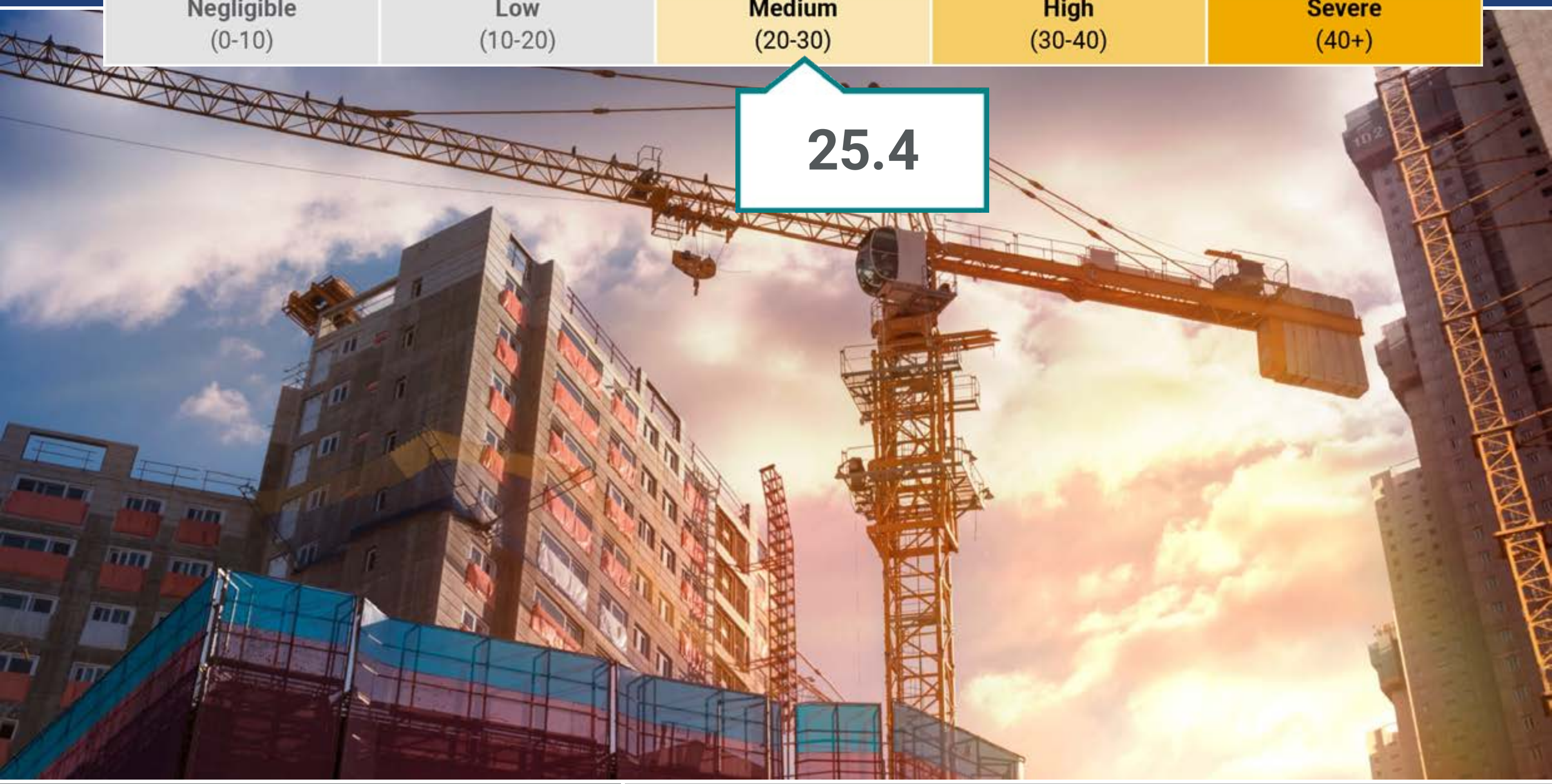
In the latest ESG Risk Rating update, Hyundai Motor's score improved by more than 8 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Hyundai Engineering & Construction Co., Ltd.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

25.4



INDUSTRY:
Non-Residential Construction

BASE LOCATION:
South Korea

ENGAGEMENT FOCUS:
Risk Assessment and ESG Disclosure

RATIONALE FOR RESOLVED STATUS:
Hyundai Engineering & Construction Co., Ltd. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Hyundai Engineering & Construction Co., Ltd. incorporates ESG KPIs such as environment, health and safety, and fair-trade practices into the Board's remuneration.
- Hyundai Engineering & Construction Co., Ltd. disclosed its management structure to ensure product quality.

In the latest ESG Risk Rating update, Hyundai Engineering & Construction Co., Ltd.'s score improved by 6.5 points, bringing it into the medium risk category and below our 28-point threshold for engagement.

Resolved - Mitsubishi Heavy Industries, Ltd.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.7

INDUSTRY:
Industrial Machinery

BASE LOCATION:
Japan

ENGAGEMENT FOCUS:
Carbon Products and Services
Corporate Governance

RATIONALE FOR RESOLVED STATUS:
Mitsubishi Heavy Industries, Ltd. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Mitsubishi Heavy Industries, Ltd. has confirmed a system to collect and monitor social data on a consolidated basis.
- Mitsubishi Heavy Industries, Ltd. has disclosed the detailed targets for some initiatives in the carbon transition roadmap.
- Mitsubishi Heavy Industries, Ltd. has defined ESG metrics to be incorporated into the Board's remuneration and will implement it from FY2023.
- Mitsubishi Heavy Industries, Ltd. has set targets for women in the executives and employees in manager positions.

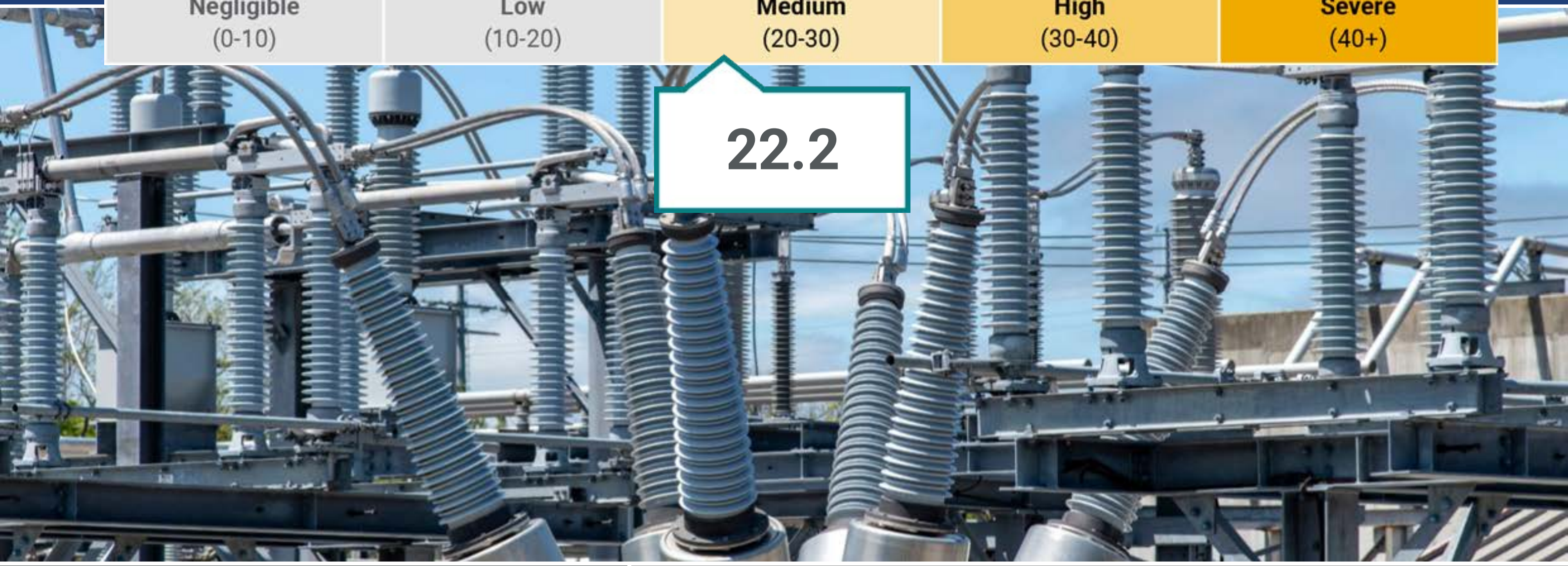
In the latest ESG Risk Rating update, Mitsubishi Heavy Industries, Ltd.'s score improved by 3.8 points, bringing it into the medium risk category and below our 28-point threshold for engagement.

Resolved - OGE Energy Corp.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

22.2



INDUSTRY:
Electric Utilities

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
Risk Assessment and ESG Disclosure
Carbon – Own Operations
Emissions, Effluents and Waste

RATIONALE FOR RESOLVED STATUS:
OGE Energy Corp. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- OGE Energy has published three years of emissions metrics (2019-2021) as well as three years of employee safety metrics in its 2022 Edison Electric Institute (EEI) ESG/Sustainability Template and year over year total recordable incident rate (TRIR) since 2007 in its 2021-2022 Stewardship Report.
- OGE disclosed management and reporting on its initiatives to reduce, recycle and reuse wastein its 2021-2022 Stewardship Report, including 2022 data for the amount of waste recycled relative to repurposed wood, paper and mixed office waste, lead acid batteries, lamps, scrap metal, computers and used oil.
- OGE published a Safety Management Information Sheet which includes an overview of the company's health and safety management programme and systems, managerial responsibility, hazard identification, emergency preparedness procedures, employee training, internal and external audit information and contractor safety requirements including pre-screening. The company discloses that it is continuously working to achieve an incident- and injury-free workplace and includes reference to the metrics it uses to track performance against this goal.
- OGE has developed a webpage and additional report disclosure focused on its biodiversity commitment to preservation as well as the biodiversity focused programmes and partnerships it is involved with. Details of its activities include pollinator initiatives, habitat protection of endangered species, avian protection, vegetation management and approaches to invasive species.

In the latest ESG Risk Rating update, OGE's score improved by 14.9 points, bringing the company into the medium risk category and below the 28-point threshold for engagement.

Resolved - Peab AB

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

28.2

INDUSTRY:
Non-Residential Construction

BASE LOCATION:
Sweden

ENGAGEMENT FOCUS:
Product Governance
Community Relation
E&S Impact of Products and Services

RATIONALE FOR RESOLVED STATUS:
Peab AB has improved its ESG Risk Rating score to 28.

Positive Development Highlights:

- Peab disclosed information about its strategy, ongoing activities, and several performance metrics in the areas of circular materials, waste recycling, and biodiversity protection to support its progress toward achieving 100% resource efficiency by 2040.
- Peab has established a robust governance approach to business ethics risks, including the implementation of a whistleblowing system available to all stakeholders, and reporting statistics in line with best practices.

In the latest ESG Risk Rating update, Peab's score improved by 12.9 points, bringing it into the medium risk category and at the 28-point threshold for engagement.

Resolved - PPL Corp.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

INDUSTRY:
Electric Utilities

BASE LOCATION:
United States of America

ENGAGEMENT FOCUS:
Emissions, Effluents and Waste
Carbon – Own Operations

RATIONALE FOR RESOLVED STATUS:
PPL Corp. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- PPL undertook a multi-year asset modernization and replacement program for natural gas infrastructure update projects in Kentucky, including replacing steel customer service lines, completing the removal of steel curbed services, completing the replacement of transmissions pipeline, and upgrading city gate stations and gas regulation facilities with new valves, piping and modern regulation and measurement equipment. In addition, in March 2023 the Rhode Island Public Utilities Commission approved $290 million to improve Rhode Island's electric and gas networks in connection with the latest Infrastructure, Safety, and Reliability plans proposed by Rhode Island Energy.
- PPL has disclosed proactive preventative actions to avoid spills, including a Spill Prevention Control and Countermeasure Plan as well as secondary containment and monthly tank inspections. The top causes of PPL Corp.'s significant spills—weather events and equipment failures—was disclosed in the company's 2023 Sustainability Report.
- The company's Environmental Policy Statement was enhanced and disclosed in August of 2022. The updated policy now includes commitments to use natural resources or energy more efficiently, report regularly on environmental issues, and monitor the company's environmental performance.
- PPL updated its Human Rights Statement to include a statement on Indigenous Rights and has published this updated statement on its website (Sustainability / Reports & Disclosures).

In the latest ESG Risk Rating update, PPL Corp.'s score improved by 6.6 points, bringing it into the medium risk category and below the 28-point threshold for engagement.

Resolved - Shin-Etsu Chemical Co., Ltd.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

26.3

INDUSTRY:
Specialty Chemicals

BASE LOCATION:
Japan

ENGAGEMENT FOCUS:
Carbon – Own Operations
Corporate Governance

RATIONALE FOR RESOLVED STATUS:
Shin-Etsu Chemical Co., Ltd. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Shin-Etsu Chemical Co., Ltd. provides investors with better insight to the robustness of their grievance mechanisms and discloses the number of reports received through the hotline system.
- Shin-Etsu Co., Ltd. has committed to achieve carbon neutrality goals by 2050.
- Shin-Etsu Co., Ltd. has set quantitative KPIs and targets for the material issues, (except one material issue: 'Contribution to industry and social initiatives'). This creates a more consistent performance management of the material issues.
- Shin-Etsu Chemical Co., Ltd. has established a reporting flow to the Board three times a year, which builds accountability on the board level.

In the latest ESG Risk Rating update, Shin-Etsu Chemical Co., Ltd.'s score improved by 4.9 points, bringing it into the medium risk category and below our 28-point threshold for engagement.

Resolved - Sumitomo Chemical Co., Ltd.

ESG Risk Ratings Score

Negligible (0-10)	Low (10-20)	Medium (20-30)	High (30-40)	Severe (40+)

27.8

INDUSTRY:
Diversified Chemicals

BASE LOCATION:
Japan

ENGAGEMENT FOCUS:
Carbon – Own Operations
Bribery and Corruption

RATIONALE FOR RESOLVED STATUS:
Sumitomo Chemical Co., Ltd. has improved its ESG Risk Rating score to below 28.

Positive Development Highlights:

- Sumitomo Chemical Co., Ltd. provides investors with insight to its risk assessment for anti-corruption. This shows a robust risk awareness and management of the issue.
- Sumitomo chemical Co., Ltd. has committed to achieving the net zero goal by 2050.
- Sumitomo Chemical Co., Ltd. has set KPIs/targets for material ESG issues, which builds a robust structure for performance management of the ESG issues. The target setting also clarifies the direction and expectations for investors.

In the latest ESG Risk Rating update, Sumitomo Chemical Co., Ltd.'s score improved by 7.4 points, bringing it into the medium risk category and below our 28-point threshold for engagement.

ESG in the Boardroom

Palle Ellemann
Director/Product Manager,
Stewardship
Engagement 360
Morningstar Sustainalytics

Boardrooms are still struggling to get ESG right. Morningstar Sustainalytics Stewardship Services often experience this through our engagements with companies around the world. Some of the main challenges discussed during these engagements are related to the role of ESG in strategy and performance management, and how integrated ESG should be in the company's governance structure. The emergence of ESG has also questioned the expectations for the combined skillset of the board and, for example, to what extent the board needs expertise on biodiversity, DEI (diversity, equity and inclusion) and climate change. In this article, I will argue that ESG should be integrated into company risk management, operations, performance management, reporting, and governance. Furthermore, the board should have enough ESG knowledge to hire the right CEO and ensure integration of the right material ESG issues into the company's performance management systems and processes.

ESG has Reached the Board

During more than 12 years of engaging with companies across geographies, I have seen ESG rise on the agenda of most executive teams and board rooms. ESG is driven by different factors, not least regulation, and investors have played an important role with the integration of ESG into investment considerations. The fact that investors pay close attention means that company management and boards must also; because essentially, the board exists to serve shareholder interests.

Having realized that ESG is something they must now consider, boards have reacted in different ways. Some boards have tasked management to deal with ESG and have adopted a compliance perspective, where the board focuses entirely on making sure that the company is complying with regulatory requirements. This type of board would typically be addressing ESG once per year when they are signing off on ESG-disclosure. In these companies, ESG strategy development is often slow or absent and relies on the CEO to drive—which is not happening because ESG is not a board (and therefore business) priority.

Other boards have adopted a radically different approach and decided ESG merits a new board committee, often named the "Sustainability Committee." The advantage of this approach is that ESG and sustainability is visibly a highly prioritized issue on the board agenda and there is a clear board-level governance structure for ESG supervision. However, the fact that there is a sustainability committee doesn't mean that there is effective board-level ESG oversight. Some of the companies we engage with—in particularly in Asia—create a new board-level sustainability committee which also meets only once per year to sign off on the ESG disclosure. The sustainability committee is, in this case, a tick-box exercise and doesn't provide any meaningful governance oversight.

ESG Integration Builds Accountability from the Bottom to the Top

A more thoughtful and effective approach is to determine what ESG means to the company by way of an ESG materiality assessment. Through this exercise, the company identifies which ESG issues are material—preferably using a double materiality approach to include stakeholder perspectives and consider the impacts the company makes on society. The materiality assessment will typically highlight several ESG issues that are already addressed at the board level through existing board committees, such as business ethics and compliance supervised by a Risk Management and Audit Committee, occupational health and safety overseen by a Health, Safety and Environment Committee, and responsibility for human capital development with a Social and Ethics Committee. The board may also learn about new and emerging material ESG issues that it doesn't currently have a governance structure to oversee. At this point, it is up to the board (in collaboration with management) to define a threshold for what ESG issues are material enough to be supervised by the board, and which are not. The benefit of performing a meaningful ESG materiality assessment is the opportunity to make qualified decisions on what ESG issues to focus on, and what to give secondary priority.

Even if some material ESG issues are covered by existing board committees, it may be tempting for a board to establish a new Sustainability Committee to showcase how important sustainability is to the company. However, downsides of having a separate sustainability committee include unclear governance oversight (by way of interactions with various sub-committees) and unintentionally identifying sustainability and ESG as a separate function in the company.

What Gets Measured, Gets Done

There is typically a sustainability or ESG angle to any function in a company. Therefore, if companies can integrate sustainability into the organizational fabric, then they can secure a deep ownership to the issues in the organization. For ESG, like many other issues, the thumb rule is; what gets measured, gets done. True ESG integration means that ESG is integrated into the company's performance management systems with performance metrics, goals, and remuneration. The most effective companies build ESG metrics into their existing scorecards (or other performance management systems) and ensure consistent performance reporting vertically in the organization, which will align all employees around the same goals and focal points. ESG integration will additionally build accountability at the top of the organization—management and the board—as they receive ongoing updates on performance. This is why engagement managers in Material Risk/Strategy & Risk Engagement focus so much on performance reporting, the integration of ESG metrics, and how often this information reaches management and the board.

Who Knows Something About Biodiversity?

The emergence of ESG at the board level has questioned what skills a board should possess. If biodiversity or DEI turn out to be a material ESG issue for a company, does the board need to have a biodiversity or DEI expert? Some boards have tried to attract senior climate change and biodiversity experts, but this is quite challenging as these experts are rare and often don't have a business mindset. The question is also if it makes sense to have such deep ESG subject matter expertise on the board in the first place, as this could create an imbalanced relationship among board members on these issues. The expert could quickly bring any board-level discussion on the topics to a high level of detail, hindering other board members' contributions. In this case, the board could also overstep its oversight function and become too detail-oriented. The board's most important task is to hire the right CEO to manage the business, including ESG. Secondly, the board needs to know enough about the material ESG issues to ask management the right questions and collaboratively agree on the appropriate metrics to include in ongoing performance reporting to the board.

A company like **Bayer AG** uses ESG expertise constructively as Bayer has set up an independent external Sustainability Council to advise the Board of Management and other functions within the company on all sustainability matters. In this forum, the experts are among peers (with a similar level of expertise), and they can develop more detailed discussions to the benefit of themselves and the company.

ESG is Not New

Many of the issues that we deal with under the notion of ESG are not new, but the ESG framework has elevated boardroom discussion of these issues. Furthermore, materiality and impact analysis has broadened the scope of ESG issues that companies consider. ESG is not a new function or area, it is sound business risk management that is within the mandate and obligation of the board to address. The integrated approach is the most efficient and effective way of managing ESG issues—and a board can create oversight systems that mean they do not have to be ESG subject matter experts to provide effective oversight.

About Morningstar Sustainalytics and Contacts

Morningstar Sustainalytics is a leading ESG data, research, and ratings firm that supports investors around the world with the development and implementation of responsible investment strategies. For more than 30 years, the firm has been at the forefront of developing high-quality, innovative solutions to meet the evolving needs of global investors. Today, Morningstar Sustainalytics works with hundreds of the world's leading asset managers and pension funds who incorporate ESG information and assessments into their investment processes. The firm also works with hundreds of companies and their financial intermediaries to help them consider material sustainability factors in policies, practices, and capital projects. Morningstar Sustainalytics has analysts around the world with varied multidisciplinary expertise across more than 40 industry groups. For more information, visit www.sustainalytics.com.

Do you have any questions regarding our Stewardship Services?
Contact us today to connect with our team of experts.

Learn more at www.sustainalytics.com. or email at engagement.support@sustainalytics.com

Europe:
Amsterdam (+31) 20 205 00 00
Copenhagen (+45) 32 72 52 81
London (+44) 20 3514 3123
Frankfurt (+49) 69 3329 6555
Paris (+33) 1 184880642
Stockholm (+46) 8 505 323 33

Americas:
Boston (+1) 617 603 3321
New York (+1) 212 500 6468
Toronto (+1) 416 861 0403

Asia Pacific:
Sydney (+61) 2 8320 9436
Tokyo (+81) 3 4510 7979