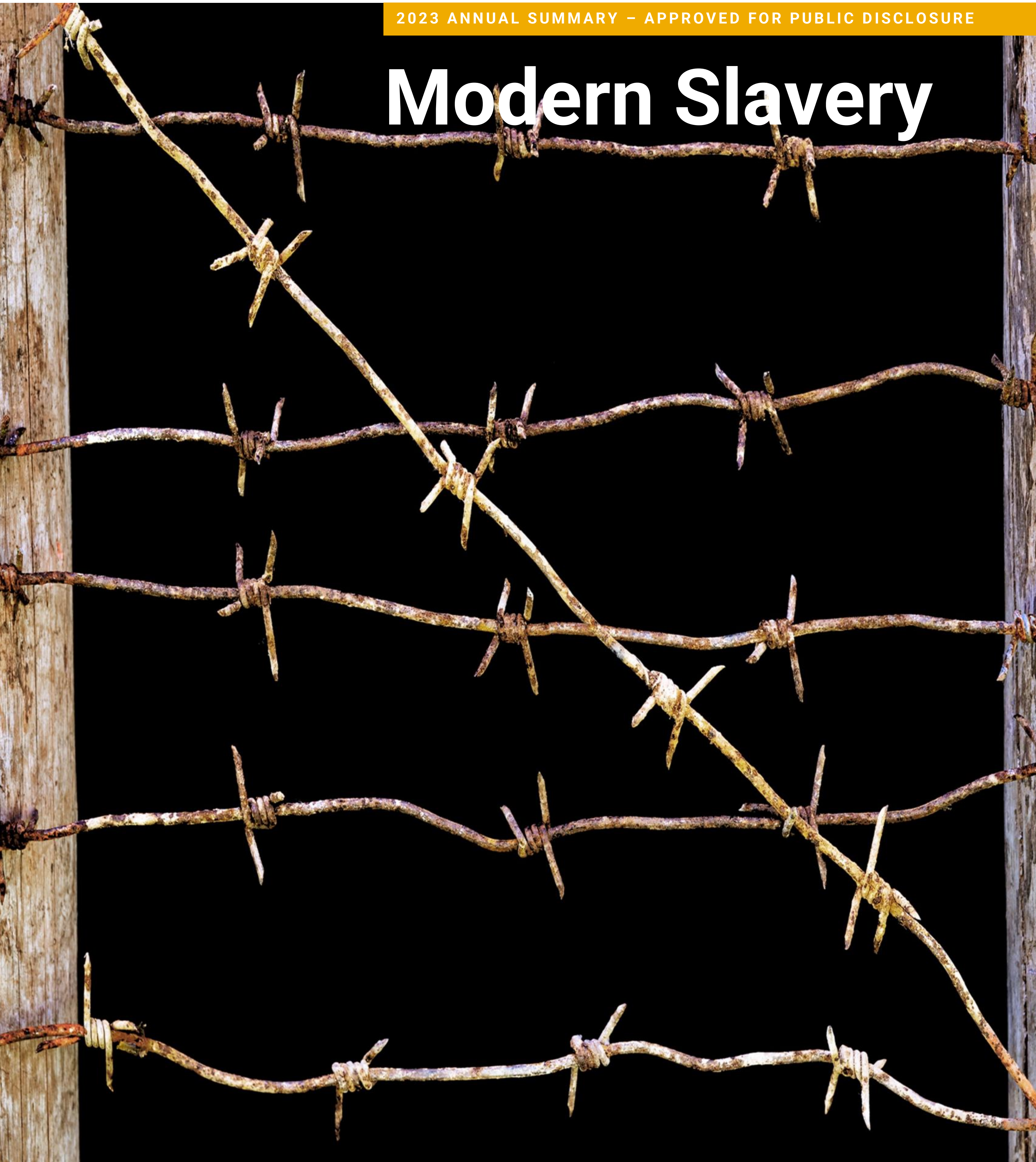
MORNINGSTAR | SUSTAINALYTICS

2023 ANNUAL SUMMARY – APPROVED FOR PUBLIC DISCLOSURE

Modern Slavery



Modern Slavery Thematic Engagement

There are around 50 million people in modern slavery and, of these, over half—some 27.6 million—are in forced labour. [1]These numbers represent an increase in the global estimates. It is likely many will be familiar with the figures since being reported in 2022. However, often repeated headline statistics can lose their impact. Consequently, it is important to remember that most forced labour—approximately 17.3 million—is located in the private economy.[2] This means major companies are potentially connected to this extreme form of exploitation through their value chains, especially where these are extensive and opaque. In the context of increasing regulation, the risks to businesses and investors are manifold.

In 2021, to address investor concerns that modern slavery risks were being insufficiently managed by businesses, Sustainalytics commenced a three-year engagement with a focus on two high-risk industries: (1) construction and (2) apparel. The engagement has aimed to encourage companies to adopt fit-for-purpose strategies that include six key areas: governance and reporting; purchasing practices; living wages; stakeholder collaboration; worker empowerment; and robust auditing and grievance mechanisms.

The theme is now in its concluding stages, with final dialogues having taken place or mostly scheduled with the 16 participating companies. Throughout the Thematic Engagement, we have leveraged the expertise of stakeholders, raised awareness of risk, highlighted procedural gaps and weaknesses and shared good practices. Many companies have taken steps to strengthen their policies and processes. Yet most are still unable to locate violations within their spheres of influence, despite the rise in modern slavery. In addition, company actions often take time. The inability of businesses to find extreme forms of abuse may reinforce a perception that risks are either well-managed, negligible or non-urgent. This investor engagement has provided the space to constructively challenge these assumptions and encourage actions beyond commitments, policies and monitoring. Companies are listening, though concrete action often takes time.

Developments in 2023

In 2023, several legal global milestones were achieved. In December 2023, the Corporate Sustainability Due Diligence Directive (CSDDD) moved nearer to reaching its legislative endpoint, after a provisional agreement was reached between the EU Council and Parliament—the two co-legislators. As textiles and construction materials are deemed to be high risk sectors, many companies carrying out these activities will be captured by this much anticipated law.[3] The CSDDD has raised the stakes. One of the most important provisions of

[1] Global Estimates of Modern Slavery, September 2022, ILO, IOM and Walk Free Foundation.
[2] Ibid.
[3] Companies with over 250 employees and with a turnover of more than 40 million euro if at least 20 million are generated in one of the sectors (textiles, agriculture, food manufacturing, trade of mineral resources, construction).

the CSDDD is that victims will have up to five years to bring a claim where it can be shown that harm has arisen due to failures of human rights due diligence. Trade unions and civil society organizations will also be able to bring forward cases on victims' behalf. Further, national supervisory bodies will have the power to impose sanctions of up to 5% of global turnover if due diligence is not properly implemented. Consequently, it is all the more important that those at the apex of businesses, i.e., Boards and the C-Suite, seriously question why their compliance regimes are not identifying modern slavery risks and demand better due diligence. Evidence of forced labour may not be making its way into corporates' field of vision. In a recent investigation, reported in October 2023 that looked into working conditions, Amazon, McDonald's and the InterContinental Hotels Group were linked to allegations of forced labour in Saudi Arabia.[4] Human rights experts once again called out the problems of audits (e.g., potentially falsified information and concerns about both lack of auditor independence and transparency). The CSDDD will likely mean being wise after a serious human rights event will no longer cut it. Indeed, business models may also be impacted. This is because where businesses use suppliers that cause adverse impacts that are non-preventable or cannot cease, they may be required to terminate those relationships (as a measure of last resort). In December 2023, allegations once again surfaced of major apparel brands linked to Uyghur forced labour.[5] It will remain to be seen how the risks will be navigated and if this may result in restructuring parts of the supply chain.

In July 2023, the EU published the European Sustainable Reporting Standards (ESRS) 1 and 2 and the topical standards, which include own workforces and workers in the value chain. These form part of Annex 1 of the Corporate Responsibility Reporting Directive. ESRS 2 set out general disclosures which are mandatory to report against. The ESRS states the starting point of sustainability disclosure is for businesses to conduct a materiality assessment. This needs to be based on the principle of 'double materiality'. In other words, companies will likely need to consider both whether forced labour may harm their business financially *and* the impact on workers. It is expected that prudent companies in construction and manufacturing will improve their disclosure on working conditions as a result of the ESRS because forced labour is over-represented in both sectors when compared to the overall global workforce.[6]

In May 2023, Canada passed its Fighting Against Forced Labour and Child Labour in Supply Chains Act. From next year, companies that fall within scope will be required to publish reports annually on measures taken to prevent and reduce forced labour or child labour risks. This is

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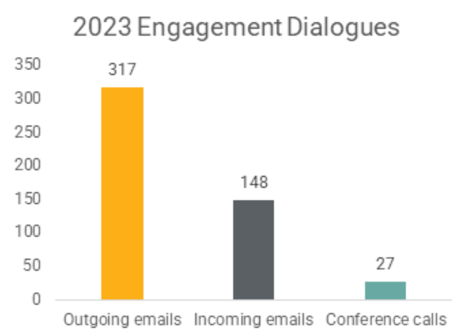
[4] McDonald's and Amazon's ties to alleged labor trafficking: five key takeaways, The Guardian, 10 October 2023

[5] Tailoring Responsibility: Tracing Apparel Supply Chains from the Uyghur Region to Europe, Sheffield Hallam University, December 2023, Yalkun Uluyol and a team of anonymous researchers

[6] 'People in forced labour are more likely to be in manufacturing, and much more likely to be in construction, than workers in the overall labour force.' Global Estimates of Modern Slavery, ILO, IOM, Walkfree Foundation, September 2022, p.34

far less reaching than the CSDDD and CSRD but fines of up to CAD 250,000 and convictions may be imposed on companies for failure to comply with the Act.

Engagement Update



The engagement continued with the 16 participating companies in 2023. In total, 27 engagements were held in 2023. This included eight final calls, with the remainder to take place in Q1 2024. In April, Sustainalytics was invited by one of the construction companies to join its stakeholder forum in Lille, France. In December, we also provided input into the company's materiality assessment on ESG. Participation in these exercises afforded more opportunities to raise the importance of modern slavery risks.

In 2023, penultimate and final engagements focused on several key performance areas, including purchasing practices, audit limitations and freedom of association. For example, we discussed the need to take more action on responsible purchasing practices by sharing with apparel companies the Common Framework on Responsible Purchasing Practices,[7] a best practice guidance. We also highlighted the importance of adopting further measures to identify the hidden practice of recruitment fees beyond policies and supplier questionnaires.

Whilst there has been measurable progress in 2023 across most companies, Sustainalytics recognizes that in the remaining months, the full engagement goal is not realistically within reach. Therefore, the final engagements have centred on providing recommendations to companies in key areas and giving constructive feedback. The aim has been to strengthen risk management, especially in light of regulatory changes. That said, the engagement has been meaningfully influencing companies, as highlighted below.

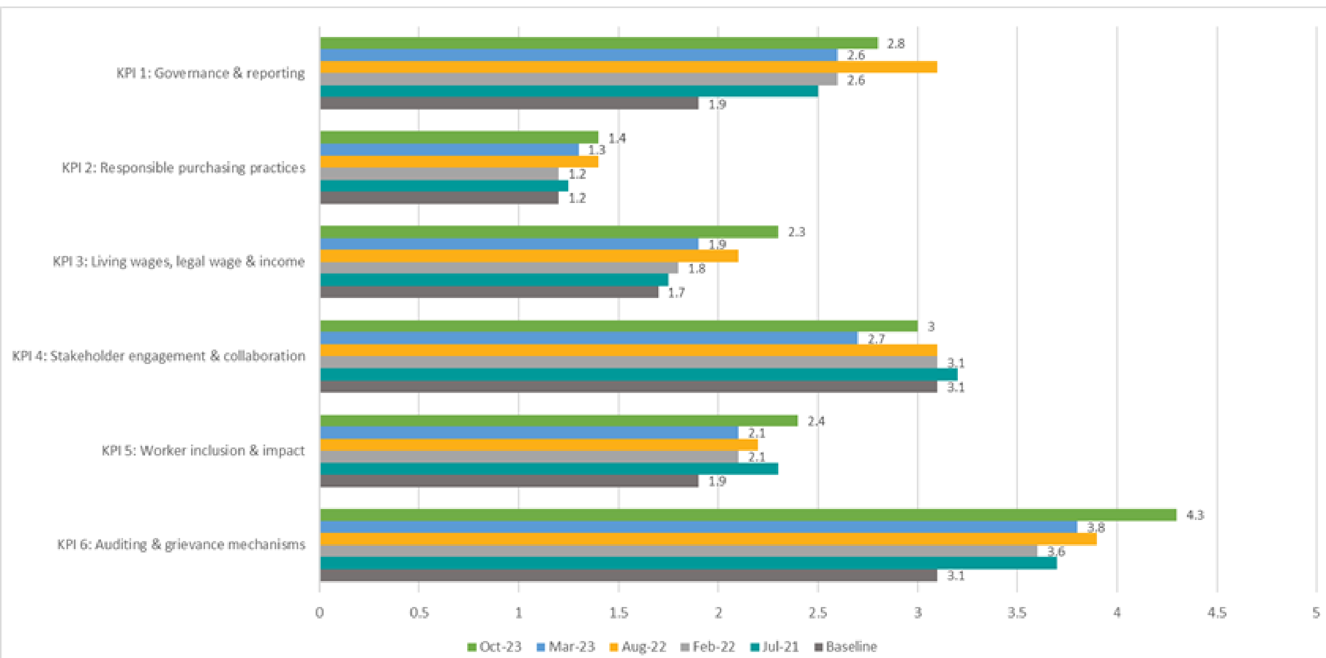
[7] Common Framework on Responsible Purchasing Practices, Building Resilience in the Textile Supply Chain, Version 1 – June 2022,

Company Performance

Notable progress in 2023 included:

- Chinese sportswear retailer advised it plans to start disclosing its supplier list in Q1 2024, in response to the need to provide greater disclosure to investors on cotton.
- US retailer will start mapping its key suppliers. We were told our questions on audit limits were 'well heard' and that the engagement provided key learnings and better understanding of investor expectations.
- European sportswear brand is currently developing its long-term ESG targets and in December invited us to give suggestions on human rights targets, which we put forward.
- European construction company has rolled out human rights training, with a focus on forced labour and recruitment fees. It said the dialogue has been key to many changes.
- North American brand responded positively to our suggestions to complement its main tool to identify recruitment fees. It said it was looking at ways to improve.
- European construction company has been engaging with its peers and is looking to join a collaborative initiative on human rights. It welcomed good practices we shared.

Average company KPI score (maximum points are 9)



Case Study

All companies need to make strides to achieve the engagement goal. In recognition of this, we put forward recommendations to participants in the final dialogues, which aim to advance progress. This case study illustrates both the challenges of the theme and why it is that investor engagements are an essential lever to drive change.

When we commenced the project, it quickly became apparent that the governance of human rights (i.e., oversight by boards and senior executives) was not advanced. For example, several construction companies told us that modern slavery is not considered a material risk. The responses from companies across both sectors to questions about oversight mostly described output measures (e.g., policy sign-off and upward reporting to boards). We assumed this KPI (one of six on which the engagement focused) would mature over time as senior leaders increasingly became familiar with what good governance of human rights required of them, especially given the rapidly changing regulatory context. Three years on it is still difficult to discern how this area has developed across many of the engaged companies. In the final engagements that have taken place to date, we have recommendated companies report more to investors on how *active* oversight by the highest level takes place.

Companies' reactions to this recommendation have been similar. Many have responded that demonstrating active governance is mostly a matter of reporting more on what boards do (although a few have advised plans for human rights training for senior leaders). We recognize that companies may well be insufficiently communicating active diligence of those at the top but we would like to hear how senior leaders question due diligence processes (for example, why no cases of forced labour have been identified given risks are often systemic) or how it is that boards ensure management teams are sufficiently integrating human rights commitments into the overall business strategy.

Over the last few years, it is becoming increasingly clear that regulation, world events and societal dynamics are redefining the human rights risk landscape, yet it can seem as if governance is limited to policy sign-offs and a review of key results. Boards and senior teams need to ensure that human rights are not just seen through the prism of reputational considerations but the broader lens of double materiality (key to the EU's Corporate Sustainability Reporting Directive). Investors need to know that senior leaders are asking the right questions of their executives, joining up the dots between different areas of strategy (which may pull in opposite directions), and recognizing the opportunities too. When investors engage on the topic of governance of human rights it allows for companies to be constructively challenged, can lead to the development of new ways of thinking and encourage an exchange of ideas. Investors are in a position, unlike many stakeholders, to hold boards to account. Through dialogue, they can shine a spotlight on those at the top and set out their expections. In doing so, this can help to protect long-term value.The world is rapidly changing and old ways of addressing risk are increasingly looking out of date.[8] Boards need to be equipped for these new realities and investors can play a critical role in ensuring boards get there.

[8] The Global Risks Report 2023, 18th Edition, Insight Report, World Economic Forum

About Morningstar Sustainalytics

Sustainalytics, a Morningstar Company, is a leading ESG research, ratings, and data firm that supports investors around the world with the development and implementation of responsible investment strategies. For 30 years, the firm has been at the forefront of developing high-quality, innovative solutions to meet the evolving needs of global investors. Today, Sustainalytics works with hundreds of the world's leading asset managers and pension funds who incorporate ESG and corporate governance information and assessments into their investment processes. Sustainalytics also works with hundreds of companies and their financial intermediaries to help them consider sustainability in policies, practices, and capital projects. With 17 offices globally, Sustainalytics has more than 1,800 staff members, including more than 800 analysts with varied multidisciplinary expertise across more than 40 industry groups. For more information, visit www.sustainalytics.com.

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