Morgan Stanley

INVESTMENT MANAGEMENT

2022 U.K. Stewardship Code Report

FEBRUARY 2023

Signatory of:

UK STEWARDSHIP CODE

From Our Leadership

MSIM has long supported the principles of the U.K. Stewardship Code and is committed to continuing to deliver long-term value and sustainable outcomes for a wide constellation of stakeholders.

We believe stewardship activities are integral to the role of active investors, who aim to proactively identify and respond to a wide range of topics that affect the long-term value of a business or asset, including strategy, capital allocation, capital structure, operational performance and delivery, risk management, pay, sustainability matters and corporate governance. We view effective management of stewardship and sustainability issues as a core component of our business strategy and continue to evolve our approach in line with the evolving regulatory and industry landscape, as we believe it is fundamental to the long-term success of our organisation and our ability to deliver value for our clients.

MSIM's approach to stewardship is driven by our investment teams, and differentiated across strategies and asset classes. In 2021/2022, we drove our strategic vision forward, making strides in our integration with Eaton Vance, as we continue to synchronise our businesses, products and sustainability and stewardship approach. To that end, we are in the process of implementing enhanced sustainability oversight and governance, risk management and controls to support our increasing stewardship activities across our business.

However, we recognise the need to continue evolving and enhancing our approach to stewardship in the face of significant challenges, such as the Ukraine-Russia conflict, global energy crises and climate change. Stewardship is therefore an ongoing journey, and we know there remains much work to be done. This report highlights our approach to, and progress on, that journey as we continue to integrate stewardship activities within our investment processes and workplace. It provides in-depth examples of how our investment teams aspire to act as good stewards of clients' capital. We are pleased to share our 2022 U.K. Stewardship Report and look forward to continuing to deliver this value to our clients in 2022 and beyond.

Ruairi O'Healai
EMEA COO at Morgan Stanley Investment Management and
CEO at Morgan Stanley Investment Management Ltd.

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Please note that this Stewardship Report relates to the reporting period from 1 July 2021-30 June 2022 only. MSIM's organisational structures, governance, policies and practices described in this report may evolve and change over time, as we continue to enhance our approach to stewardship and sustainability, as well as our control framework generally (having regard to considerations such as changing regulatory expectations, best practice, stewardship priorities and client feedback, among others).

DISCLAIMERS

Morgan Stanley is the parent company of Morgan Stanley Investment Management Inc. and its affiliates. References to "Morgan Stanley" in this document refer to the parent company, not to Morgan Stanley Investment Management Inc. In some instances, Morgan Stanley Investment Management Inc. may leverage or be a part of Morgan Stanley's processes and/or initiatives related to sustainable investing.

SECTION 1

Purpose and Governance

PRINCIPLE 1

Purpose, Strategy and Culture

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

Overview

Morgan Stanley Investment Management ("MSIM") is a global investment manager delivering innovative investment solutions across public and private markets worldwide. MSIM has been creating value for its clients for over 40 years and operates in more than 20 countries. MSIM has $1.4 trillion in assets under management ("AUM")[1] as of 30 June 2022. Our integration with Eaton Vance ("EV")[2] continues, bringing together two thriving organisations with distinctive and highly complementary strengths in investment management, distribution and client service.

MSIM has a decentralised approach towards investment management, consisting of independent public and private markets investment teams and asset class platforms. Each investment team has a unique talent pool of experienced professionals, and dedicated resources focused on a specific investment discipline, including corresponding sustainability, stewardship and engagement approaches. As set out below, our investment teams are organised by capability into the following four categories:[3] High-Conviction Equities, Active Fixed Income and Liquidity, Alternative Investments and Custom Solutions.

It is our unique business that differentiates MSIM from competitors, specifically in global reach, experience, and reputation for providing customised solutions to clients. By creating a culture that fosters investment diversity, innovation and independent thought, we seek to generate sustainable, superior returns for clients over the long term—demonstrated in our investment strategies that span the risk/return spectrum across geographies, investment styles and asset classes.

Stewardship efforts at MSIM are accordingly led by investment teams on a decentralised basis, and stewardship priorities and actions adopted may vary across investment teams depending on multiple factors, such as the objectives of the strategy, asset class and investment time horizon, as well as the research, portfolio construction, philosophy and process used by that team. The investment teams will, however, be guided by, and operate in accordance with, the broader stewardship, sustainability, risk management and operating framework that MSIM has established at an organisational level (in particular, MSIM's Engagement and Stewardship Principles and the Sustainable Investing Policy described below) that is coordinated by MSIM's Sustainability Council. Specific client requirements, where applicable, and the evolving regulatory and industry landscape are also taken into account in periodic reviews to further develop our stewardship efforts, aligning with our objectives as active managers and good stewards of our client capital.

We believe that this model delivers better outcomes for clients, investees and markets, as each investment team will be best placed to determine the stewardship and engagement efforts that will be effective in delivering increased and long-term value for its investment strategies and clients.

This report sets out how MSIM approaches and drives stewardship at both an organisational and investment team level.

[1] Assets under management includes all discretionary and non-discretionary assets of Morgan Stanley Investment Management and all advisory affiliates. MSIM Fund of Fund assets represent assets under management and assets under supervision. MSIM direct private investing assets represents the basis on which the firm earns management fees, not the market value of the assets owned. Alternatives Investments includes fee-earning assets under management, unfunded commitments and fund leverage, representing the total investible capital for the platform. Assets in the Sustainable Investing category are a subset of the other four categories.

[2] Morgan Stanley completed its acquisition of Eaton Vance on March 1, 2021.

[3] For the purposes of AUM consolidation, Eaton Vance AUM (including its four investment brands: EV Management, Calvert Research and Management, Parametric Portfolio Associates and Atlanta Capital) has been included within our asset class categories.

Our Purpose

CLIENT-CENTRIC

As a client-centric organisation, our purpose is to provide investment and risk management solutions to a wide range of investors and institutions, including corporations, pension plans, intermediaries, sovereign wealth funds, central banks, endowments and foundations, governments and consultant partners worldwide. Our purpose has remained unchanged, and the manner in which MSIM's purpose has guided our stewardship approach and efforts during this reporting period is more fully detailed under Principle 7 and Principle 9.

MSIM is the asset management division of Morgan Stanley, a global financial services provider, that partners with clients and stakeholders to mobilise capital at scale to tackle global sustainability challenges, including climate action and inequality. Morgan Stanley is deeply committed to delivering long-term value for clients and shareholders, and, in doing so, look for opportunities to deliver its services in a manner that benefits/mitigates harms to the environment and society. With the support of Morgan Stanley's global resources, MSIM offers clients personalised investment solutions, including the intelligence and creativity of some of the brightest professionals in the industry.

With 1,248 investment professionals worldwide, and 54 offices in 24 countries as of 30 June 2022, MSIM is able to provide in-depth local knowledge and expertise while channeling the strength of our global presence and resources.

INNOVATIVE INVESTMENT SOLUTIONS

We have a proven ability to translate information into creative and original solutions for investors. At the centre of this process are our independent teams of portfolio managers, researchers, traders and specialists. These experienced individuals excel at looking beyond the status quo. They thrive on defining new frontiers in investment management, leading the initiative to add value through ground-breaking strategies. They are drawn to our corporate culture of empowerment and accountability, which requires that they do their best for our clients.

COMMITMENT TO SUSTAINABILITY

Our Sustainable Investing Policy ("SI policy") applies to and guides MSIM's public and private markets investment teams and regional entities, and, specifically, the provision of portfolio management/investment advisory and fund management services for MSIM-branded funds.

As noted previously, given that MSIM comprises independent investment teams and asset class platforms, the specific approach to sustainability that may be deployed by each portfolio management team will depend on multiple factors, including, but not limited to, the objectives of the product, asset class and investment time horizon, as well as the specific research and portfolio construction, philosophy and process used by that team. Investment teams deploy their skill and judgement in assessing the materiality of ESG-related risks and opportunities as appropriate for certain investment strategies.[4]

MSIM's investment teams act as responsible long-term investors and are responsive to ESG factors that can present both risks and opportunities to investment portfolios in a manner that is consistent with our fiduciary duties and the investment strategies of our clients. MSIM's commitment to sustainability is expressed in three key ways:

1. **STEWARDSHIP AND ENGAGEMENT:** investment teams deploy the shareholder rights and stakeholder influence that MSIM exercises on behalf of our clients to encourage, where relevant, strong ESG practices with issuers, borrowers and counterparties;
2. **ESG INTEGRATION ACROSS ASSET CLASSES:[4]** thoughtful consideration of material ESG factors may be integrated as appropriate for certain MSIM investment strategies, asset classes and client needs; and
3. **SUSTAINABLE INVESTING SOLUTIONS**: providing our clients with investment solutions that are aligned with their returns objectives alongside their sustainability preferences and needs.

Our Culture and Business Principles

At MSIM, we believe that long-term and enduring success lies in having a strong culture and talented employees who live our values. Our culture guides our employees, and our five core values inform everything we do:

1. Do the Right Thing;
2. Put Clients First;
3. Lead With Exceptional Ideas;
4. Commit to Diversity and Inclusion; and
5. Give Back.

[4] Some investment strategies do not integrate ESG where it is not currently feasible or appropriate to do so (e.g., certain passive investment strategies, certain asset allocation strategies, or where requested by clients).

Maintaining a strong employee culture is the focus of our Firm Culture, Values and Conduct Committee, which is made up of senior managers from across the firm with oversight from the Board of Directors.

The fair treatment of customers is central to our Firm culture. Our business principles demand that we put clients first—that we act in our clients' best, long-term interests and build their trust while we build our franchise. Our Code of Conduct is central to this programme—establishing standards of behaviour and ethical codes of conduct that all new hires, and every employee, annually, are required to certify that they understand and will follow. In most circumstances, our Firm strives to set higher standards of conduct than the minimum imposed by law or our regulators.

MSIM provides support and mentoring for development through various means, including classroom and online training sessions, learning lunches with prominent internal and external business leaders, guest speaker presentations, networking and diversity groups. We believe that a supportive and entrepreneurial environment, combined with the Firm's global resources, makes employment at MSIM an attractive long-term choice for all our employees—which, ultimately, makes MSIM an attractive, long-term choice for clients as well. Please see Principles 2, 5, 6, 7 and 9 in particular for details on how we have embedded these core values in the resourcing of our stewardship function, our engagement priorities and actions during the reporting period.

MSIM's Approach to Stewardship, Engagement and Sustainable Investing

We understand stewardship to involve the responsible allocation, management and oversight of managed assets, with a view to creating long-term value for clients and promoting sustainability within financial markets, societies and the world. We therefore consider stewardship to be relevant across the investment cycle, from pre-investment due diligence to post-investment monitoring, engagement and exercise of investment rights. In our view, stewardship and ESG/sustainable investing go hand in hand; by holding ourselves and our investees to account on a broad spectrum of environmental, social and governance factors, we are able to generate sustainable long-term growth for our clients, the markets and the regions in which we operate.

Although MSIM consists of independent investment teams that deploy team-specific stewardship, engagement and sustainability practices tailored to their corresponding investment strategies, our investment beliefs, strategy and culture are collectively guided by the seven key principles laid out in our Sustainable Investing Policy, which outlines our approach to stewardship and sustainable investing:

1. **GOVERNANCE:** We maintain internal governance structures and resources that work to advance Sustainable Investing across certain business activities;
2. **ESG INTEGRATION:**[3] We are committed to generally considering and incorporating material ESG issues (including both risks and opportunities) when evaluating investment opportunities across both public and private markets, as appropriate;
3. **SUSTAINABLE FUNDS:** Beyond ESG integration, we are committed to providing clients with investment solutions that provide intentional exposure to sustainability as an investment theme or themes, as appropriate;
4. **STEWARDSHIP, ENGAGEMENT AND VOTING:** We seek to encourage and partner with selected portfolio companies on material issues during the period of ownership of their securities to improve both financial and sustainability performance;
5. **ADVOCACY AND COLLABORATION:** Where relevant, we seek to collaborate with industry peers and standard-setting organisations and to participate in public policy engagements to advance Sustainable Investing practices;
6. **ONGOING TRAINING:** We recognise that the impact of sustainability factors on the economy and our investments and assets is rapidly evolving. As such, we are committed to a culture of ongoing learning and improvement through our training programmes; and
7. **REPORTING AND TRANSPARENCY:** We foster transparency by providing our stakeholders with the appropriate level of information on sustainability.

Over the past year, we have taken steps to ensure our seven key principles continue to deliver effective stewardship and sustainable investing in line with client interests and requirements, as well as developments in the global regulatory and industry landscape. As a result of our ongoing review of internal policies and procedures, product framework and stewardship activities, we are in the process of: (1) implementing enhanced sustainability oversight and governance; (2) refining both our internal sustainability product framework; (3) targeting engagement and collaborative initiatives; (4) launching baseline MSIM Sustainability training; and (5) continuing to build our ESG data and technology capabilities to support both client and regulatory reporting. Progress in these areas is detailed in each Principle of this report, particularly Principles 2, 4, 5, 7, 8, 9 and 10.

As with other MSIM investment teams, Calvert teams have their own independent philosophies and strategies when it comes to stewardship and the management of client assets. However, Calvert currently also has its own overarching framework built on the foundation of the Calvert Principles for Responsible Investment (the "Calvert Principles"), which provide a framework for Calvert's evaluation of investments and guide Calvert's approach to stewardship and proxy voting on behalf of clients through active engagement with issuers. For further information, please see Principles 9 and 11 below. Calvert (as well as other Eaton Vance affiliates) continues to be integrated into MSIM with a view to optimising our approach to stewardship across the entire organisation.

Engagement as Active Investors and Owners

As active investors and owners, we believe that we have a duty to be good stewards of our clients' capital. We fulfill this duty by engaging with selected companies in which we invest and by effectively exercising our proxy voting and other rights as shareholders. These stewardship activities give us the opportunity to guide companies in which we invest toward better environmental, social and governance practices, which we believe contribute to attractive returns for our clients over the long term. Our approach to Stewardship and Sustainable Investing across asset classes and progress made over the past year is described in greater detail under Principle 7 and Principle 9.

Our Investment Beliefs

Our investment teams' beliefs are guided by our MSIM/Firm purpose and core values (as outlined above), as well as our clients' best interests and their stewardship needs (please see Principle 6). Accordingly, our investment teams generally share certain overarching investment beliefs, including the following:

- Risks are necessary to achieve return but must be appropriately managed, hedged or diversified;
- Investing responsibly and engaging as long-term owners reduce risks and may positively impact returns over time;
- Engagement is generally more effective in driving change and delivering better outcomes than divestment;
- Collaboration, where appropriate, with targeted objectives is more impactful in delivering meaningful outcomes; and
- Thoughtful consideration of material ESG factors and risks (as appropriate to specific MSIM investment strategies and asset classes) is an important aspect of active investment management.

We consider these overarching investment beliefs to be aligned with our core values, client-centric purpose, commitment to sustainability and duty as long-term active owners to be good stewards of the capital we manage.

That being said, due to the nature of our independent investment teams, MSIM does not have centralised investment beliefs across asset classes and strategies; rather, each of our investment teams has its own investment philosophies and strategies in managing client assets, which make up our diversified product platform. We believe in individuality and encourage diverse investment opinions, hence our stewardship strategies and implementation are not homogenous. As noted previously, we believe that this approach drives better outcomes for investors, as the investment teams directly responsible for managing their assets and strategies will be able to set, follow and deliver on investment beliefs that are appropriately tailored to corresponding client interests, strategies and the capital they manage.

In response to our clients' needs and best interests, we made the strategic decision, earlier this year, to expand our investment capabilities, capitalising on our existing investment strengths while furthering objectives in maintaining a relentless focus on generating alpha across public and private markets. As such, preparations have begun to expand our Private Credit platform in Europe, as well as operations to launch a multi-jurisdiction, multi-asset class and multi-brand exchange-traded fund ("ETF") platform that will further enable us to match our world-class investment capabilities with the diverse set of investment vehicles our clients increasingly demand.

Our decision to expand our platform is a result of rigorous analysis and our own fundamental beliefs on firm strategy and industry structure, combined with our guiding principles and an assessment of risk and reward aligned with client demand. Further details on our European Private Credit and ETF platform can be found below, and in Principles 6 and 7.

Examples of our investment teams' diverse beliefs and philosophies, which guide their corresponding desired investment outcomes, are set out below:

HIGH-CONVICTION EQUITIES

International Equity

For over 25 years, the International Equity team's investment philosophy for the global strategies it manages has been to own high-quality companies with the potential to successfully compound over the long term. These companies compound by steadily growing while sustaining their high returns on operating capital. As long-term owners, the team believes it has to care about and engage with long-term issues that may impact the companies it invests in. As such, the team views long-term, portfolio manager-led engagement as a critical factor underpinning the active investment process. A core belief is that engagement is a marathon and not a sprint. Accordingly, International Equity's engagement approach is aligned to this long-term investment approach, with the aim of delivering better outcomes for clients and the companies we invest in on behalf of our clients.

The International Equity team also believes that it is important to integrate ESG analysis into the investment process, and looks to focus explicitly on material ESG risks and opportunities, and their effect on the sustainability of future returns on operating capital. This is based on the team's conviction that companies with sustainably high, long-term returns on operating capital should outperform the market. In order to deliver for shareholders in the long term, a company's management must navigate the changing needs of their wider stakeholders, from customers and employees to regulators and the broader society. Companies are likely to struggle to deliver long-term returns if they don't address material long-term ESG risks. Equally, a company's ability to lead the way on social and environmental issues can be a positive force for corporate success, as it may help open new markets, drive consumer loyalty and improve employee retention and stakeholder engagement.

Both fundamental and ESG analyses are portfolio manager led; in other words, conducted by the portfolio managers and investment analysts in the team.

Counterpoint Global

At Counterpoint Global, a key investment belief continues to be that investing for the long term aligns with interests of long-term shareholders, which often means focusing on disruption and sustainability themes. Accordingly, the team takes a long-term, oriented approach to investing, which focuses on identifying differentiated insights on multi-year opportunities. Investments are made in unique companies whose market value can increase significantly for underlying fundamental reasons. As a result, the team's portfolios are typically concentrated and differentiated from their benchmarks.

Environmental awareness and social responsibility underpin this investment philosophy, and the team believes that innovative companies can use sustainability initiatives and programmes to differentiate their franchises in the marketplace. The team's Sustainability Researchers, together with Disruptive Change Researchers, Consilient Researchers and investors within Counterpoint Global that cover different companies, are responsible for sustainability research for respective investments. In this way, the team is able to leverage each member's expertise to identify opportunities and risks presented by environmental and social trends.

Global Opportunity

The Global Opportunity team believes that by applying a price discipline to investments in high-quality companies—e.g., companies the investment team considers demonstrate competitive advantages and long-term growth that create value—it can best capture opportunities and manage risk for clients.

The Global Opportunity team believes that strong stock selection is derived from long-term investments purchased at a large discount to intrinsic value. These long-term investments are best protected when they are sustainable with respect to disruption, financial strength and ESG externalities, and best enhanced when the underlying company has strong competitive advantages and growth that create value.

The investment team typically favours companies it believes have sustainable competitive advantages that can be monetised through growth. The investment process integrates analysis of sustainability with respect to disruptive change, financial strength, environmental and social externalities, and governance (also referred to as ESG).

Their stock selection focuses on finding high-quality companies, developing insights around competitive advantage and uniqueness that can make them successful over time, and having the perspective to hold them when there are short-term disruptions, as long as those disruptions do not affect the thesis, which it believes will deliver outperformance over the next three to five years. Furthermore, concentrating the portfolio in the best ideas, while maintaining reasonable diversification, is a way to maximise the reward while reducing the risk of unknown variables.

Each Global Opportunity team investor is responsible for integrating ESG by applying the Health, Environment, Liberty and Productivity ("HELP") and Agency, Culture and Trust ("ACT") framework within our quality assessment, proxy voting and engaging with portfolio companies. Our investors primarily source information from discussions with company management and public disclosures, supplemented by various research resources.

Emerging Markets Equity ("EME")

With more than three decades of investing in emerging markets with both top-down macro expertise and bottom-up stock analysis, the EME investment team has long recognised the importance of sustainable development and ESG challenges in its investment beliefs. The team's engagement and research process includes identifying sustainability opportunities or themes that it believes are most pressing to address for emerging markets.

EME seeks company management teams in quality businesses that understand long-term environmental, social and governmental trends, and integrate these considerations into their strategies. When the EME investment team evaluates companies, their investors place a great deal of emphasis on the quality of leadership and sustainable drivers of growth. Socialisation of ESG factors in emerging markets means an added set of disclosures, which are critical not just to a fuller understanding of ESG risks but offer an additional lens on the quality of the businesses.

EME evaluates sustainability and ESG risks through direct company engagement—with a focus on improving performance on material ESG factors. The team's long institutional history in Emerging Markets gives it the ability to put materiality into historical context and focus on what matters for a more sustainable transition—for example, on climate change, sustainable economic growth and affordability or circular economy. EME's engagement is portfolio manager led and focuses in on material key metrics that we follow with companies over long periods. Over the last year, EME has focused heavily on decarbonisation, metrics to define sustainable development and alignment, and building out its suite of sustainable strategies—which seek to invest in solutions and help companies become more sustainable, rather than avoid them altogether.

ACTIVE FIXED INCOME AND LIQUIDITY

The Active Fixed Income team's investment philosophy is to act as a fundamental value investor, by aiming to outperform the selected benchmark over a full market cycle of three to five years through active management positioning. The team's approach to investing is a medium-/long-term, value-driven strategy. The team is most likely to take significant active positions when fixed income markets imply extreme forecasts or are away from reasonable levels. Because their approach to investing is based on long-term value signals, underperformance may occur when there are fluctuations in bond prices resulting from sudden or short-term swings in market sentiment. The team's culture is founded on collegial debate, to ensure each investment decision is challenged and validated.

The same underlying philosophy and culture is applied to sustainability: the team believes ESG factors have the ability to impact the fundamental risk of a bond and, in turn, its price and liquidity. Accordingly, all Fixed Income research analysts across credit, rates, emerging markets and securitised teams are responsible for integrating ESG considerations into their analysis and, where relevant, discussing with Portfolio Managers how they may translate into risks or opportunities for an investment.

The Liquidity investment team takes a conservative investment approach, balancing the desire for capital preservation with attractive levels of income, allowing investors to realise an efficient cash investment portfolio. This involves active management of interest rate risk and opportunistic, but defensive, portfolio management strategy and structure. The team's liquidity solutions are underpinned by a rigorous and independent credit and risk process, focusing on high levels of weekly liquidity and structuring portfolios to minimise interest rate risk that could arise from future interest rate movements. As a result of this, the Liquidity team has a short-term investment horizon of around one year or less. The focus on capital preservation is implemented through a rigorous approach to managing and mitigating headline and tail risk, which includes sustainability-related risks, and which therefore may imply that the Liquidity team may not invest in certain sectors.

To support both the Active Fixed Income and Liquidity teams, a dedicated Sustainable Investing team sits within Fixed Income & Liquidity, led by the Head of Fixed Income Sustainable Investing, who has a dual role as the Global Head of Sustainability for Investment Management. The Fixed Income Sustainable Investing team works as an integral part of the investment team, maintaining a daily dialogue with Credit Analysts and Portfolio Managers to help assess the ESG characteristics of investments and to coordinate engagement efforts with bond issuers. The Fixed Income Sustainable Investing team also advises investment teams on how to best integrate sustainability objectives or specific ESG-related criteria into products, to meet client demands, and support the monitoring and reporting process of such criteria.

Integration With EV Fixed Income; Collaboration With Calvert Research
Following MSIM's acquisition of Eaton Vance, the Fixed Income investment platforms of both businesses have been integrated into one. As a result, the Fixed Income team now comprises portfolio managers, credit analysts and portfolio specialists from both the legacy MSIM business and Eaton Vance, working together across the platform's investment teams. The investment beliefs of the Fixed Income platform are largely unchanged—other than an even stronger focus on sustainability. Collaboration with Calvert Research and Management (EV affiliate) is also in progress, leveraging sustainability-related research capabilities.

ALTERNATIVE INVESTMENTS

Private Credit & Equity ("PC&E")

The PC&E business focuses on providing private capital predominantly to middle-market companies. Equity investments range from minority equity stakes in growth businesses to majority control of more mature companies. Debt investments include first-lien, second-lien, mezzanine, and uni-tranche loans to sponsor-backed and non-sponsor-backed companies. In general, PC&E's investment philosophy is to look to make investments in high-quality businesses that are leading players in their industries and have significant growth potential. The team believes in the value of working with founders and management teams that are looking to grow to the next level of size and sophistication.

A key investment belief of the PC&E business is that ESG risks and opportunities should be considered throughout the investment life cycle, starting from the investment due diligence phase, where investment teams seek to identify ESG risks and value drivers, and continuing through to the post-investment phase, where investment teams seek to partner with investees to maximise ESG opportunities and value drivers where possible. Given the range of private equity and credit products on the platform, the varying levels of control, and different industries and sectors of focus, teams take a tailored approach in considering ESG factors during the investment and ongoing monitoring process.

For example, within the PC&E business, the Private Markets Solutions team manages an over $1 billion Impact Investing platform, which was launched in 2014 in partnership with the Morgan Stanley Institute for Sustainable Investing. The globally diversified private markets platform seeks to drive positive social and environmental impact by providing access to a diversified portfolio of private equity investments and innovative client solutions within less-efficient areas of the private markets, which, because of size, complexity or time-sensitivity, may be overlooked or avoided by other market participants. The development of the Private Markets Solutions team's Impact strategy underscores the team's creativity in seeking to achieve tailored objectives across over $16 billion in client assets and, more specifically, through its robust customised platform.

Another example is the newly formed European Private Credit team (which forms part of the broader Private Credit platform) whose investment philosophy is underwritten by a strong conviction that the ESG characteristics of a potential investment are essential to the credit process. On the one hand, a company's ESG performance is likely to bear considerably on its creditworthiness: environmentally friendly practices, good human capital and supply chain management, and governance frameworks signal strong management and adaptability. On the other hand, properly assessing a company's ESG credentials is vital to fulfilling the Fund's responsibilities as a socially and environmentally conscious product. Having said that, the team is conscious that ESG is a rapidly evolving field, and best practices in the private credit market are likely to shift over time. Consequently, the European Private Credit team will engage regularly with various firm-level and MSIM Sustainability teams, whose insight and guidance will be critical to maintaining an innovative and rigorous approach to ESG. In addition, the team will continue to collaborate with MSIM's private credit platform on designing ESG training programs for investment team members and refining its ESG due diligence process.

Private Global Real Assets

Our Global Real Assets platform comprises five investment teams focused on real estate and infrastructure equity and credit strategies, both private and listed (please see below for the two investment teams that comprise Global Listed Real Assets). With 21 offices in 15 countries throughout the U.S., Europe and Asia, regional teams of dedicated real assets professionals combine a unique global perspective with local presence and significant transaction execution expertise.

The Private Global Real Assets Group delivers comprehensive Private Real Estate, Infrastructure and Real Estate Credit solutions to our partners and clients via the following three investment teams:

Private Real Estate: Morgan Stanley Real Estate Investing ("MSREI") has been one of the most active property investors in the world for three decades, employing a patient and disciplined approach through global value-add/opportunistic and regional core real estate investment strategies.

MSREI recognises the importance of delivering financial value to our investors, and believes that appropriately evaluating and integrating ESG factors in the investment process may contribute to better risk mitigation and long-term investment returns. MSREI manages assets within its funds with the goal of enhancing value and reducing environmental impact. Therefore, the team endeavours to optimise the value of its funds while making decisions and investments that can have positive impacts for communities, businesses, governments and the environment.

MSREI promotes, encourages and develops solutions that contribute to sustainable development and building operations; seeks to pursue strategies to mitigate the effects of climate change; and improves the financial performance of its owned buildings, as documented by green building certifications and energy ratings. Select MSREI funds have set 2050 net-zero aspirations and interim Scopes 1 and 2 carbon reduction targets.

Private Infrastructure: Morgan Stanley Infrastructure Partners ("MSIP") is a global leader in private infrastructure equity investing, targeting assets that provide essential public goods and services primarily located in OECD countries, with the potential for value creation through active management.

MSIP believes that an efficient and well-functioning infrastructure is greatly beneficial for society, and that ESG integration throughout MSIP's investment life cycle reduces long-term investment risk and increases the attractiveness of its portfolio companies. A comprehensive ESG approach helps drive long-term value and is supported by MSIP leadership and focus from investment team members. The investment teams are committed to sustainability through an ESG approach, which calls for active management of ESG issues throughout the investment life cycle for each asset, including ESG integration in due diligence, acquisition and 100-day plans—post-close strategy and implementation, monitoring and improvement, and preparation for exit.

Private Real Estate Credit: With teams in both the U.S. and Europe, the Private Real Estate Credit teams are leading real estate debt fund managers and portfolio lenders. The teams realise the critical importance of a healthy environment to our global society, economy, business and people, and the importance of ESG considerations. To this end, investments teams strive to identify ESG risks and opportunities throughout the investment life cycle of each loan, where feasible. This is essential to reduce financial, regulatory and reputational risk. ESG factors may be considered at each stage of the investment process, including due diligence, investment decision and asset management, where possible. As a private real estate credit lender, teams are limited in ability to apply ESG practices across all investments (in contrast to that of the borrower/owner of the underlying real estate).

Global Listed Real Assets

Our Global Listed Real Assets business comprises Global Listed Real Estate and Global Listed Infrastructure teams and, as noted above, forms part of our Global Real Assets platform.

Global Listed Real Estate: The team's investment process utilises internal proprietary research to invest in public real estate companies the team believes offer the best relative value relative to the companies' underlying assets and earnings. Strategies combine a bottom-up approach, assessing the intrinsic value, equity multiples and growth prospects of each security, with top-down considerations that seek exposure across regions, countries and/or sectors, and integrate forecasted fundamental inflections, macroeconomic considerations, geopolitical and country risk assessments, among other factors. Analysts assess real estate-specific factors, broader equity factors, as well as ESG factors in their fundamental bottom-up analysis. These factors are synthesised into valuation models to arrive at an NAV, and equity multiple and forward growth rate for each issuer.

Global Listed Infrastructure: The team implements a value-oriented, bottom-up-driven investment process focused on obtaining infrastructure exposure at the most attractive relative valuations and also has regard for ESG issues. The team's fundamental analysis includes review of public filings, with consideration of financial strength and prospects, strategy, market potential, risks and liabilities, management quality, corporate governance and ESG-specific considerations.

As value-oriented, bottom-up-driven investors, the team's investment perspective is that over the medium and long term, the key factor in determining the performance of infrastructure securities will be underlying infrastructure values. In aiming to achieve core infrastructure exposure in a cost-effective manner, the team invests in equity securities of publicly listed infrastructure companies it believes offer the best value relative to underlying infrastructure value. Key considerations in constructing and managing the portfolio include valuation of the underlying portfolio holdings, diversification and liquidity.

Both the Global Listed Real Estate and Global Listed Infrastructure teams actively integrate sustainability into the investment process by assessing key ESG risks and opportunities in the bottom-up stock selection process primarily by leveraging third-party ESG providers; supplementing third-party research with proprietary research conducted by the team for assessing and quantifying risks and opportunities related to ESG; and through engagements with company management to discuss ESG-related strengths, weaknesses and opportunities. The teams may approach company management with competitive insights, financially sound business cases and practical solutions to potentially improve their real estate/infrastructure operations.

While ESG considerations are an integrated and fundamental part of the investment process, they are one of several key determinants used by the investment team to determine if an investment will be made or its size in the overall portfolio.

Custom Solutions

Our Custom Solutions Group comprises teams such as Global Balanced Risk Control, Outsourced CIO, Absolute Return, Long-Oriented and Risk-Targeted strategies, all of which are mainly multi-asset or bespoke, customised investment solutions.

Global Balanced Risk Control ("GBaR")

As one of the bespoke investment solutions teams, the GBaR team's strategy follows a top-down, global asset allocation approach, managed within a clearly defined, risk-controlled framework. The strategy aims to maximise returns over time, while actively managing total portfolio risk, as the team seeks not only to participate in rising markets, but also aims to mitigate the downside in more volatile markets. GBaR defines total portfolio risk in terms of volatility or value-at-risk (VaR). The team believes a well-diversified global portfolio, investing across equities, fixed income and cash, and focused on systematic risks that we expect to be rewarded, is the best way to achieve the optimal return for risk taken.

The GBaR process is both scalable and flexible. For example, portfolios are managed to a variety of risk targets. This reflects the various requirements and levels of risk appetite of clients. The strategy is also highly flexible in its asset allocation, enabling the portfolio managers to adjust positioning dynamically, to maintain a stable risk profile, in line with agreed targets. A final level of flexibility comes in the team's implementation of asset class exposures, which can be achieved through a variety of instruments, again reflecting different client requirements and guidelines. For example, the team may invest through portfolios of direct securities holdings, ETFs or actively managed mutual funds. Alongside these instruments, there is also use of derivatives, in a non-leveraged way, for efficient portfolio management and hedging purposes. These are mainly equity index futures, FX forwards and CDS, with some use of options in portfolios where this is allowed for hedging, or where the client has a specific income objective.

Given this theme of flexibility, the GBaR team manages portfolios that meet a variety of client needs, including:

- Risk-targeting GBaR multi-asset portfolios, run to client-specific risk criteria, including volatility and VaR metrics;
- Income overlays on risk-controlled multi-asset portfolios;
- ESG-tilted, multi-asset portfolios, run to different risk targets. In addition, we have developed an enhanced sustainable investment offering, including restriction screening, integration, impact and engagement; and
- For European insurers, the team manages capital-efficient, multi-asset portfolios.

Given the increasing importance of ESG-related risks factors, such as climate change, the team has a dedicated sub-ESG group (comprising four of the 15 research analysts and portfolio managers who sit within the team), which is led by the team's Head of ESG Research.

Whatever the objective of a particular mandate, GBaR consistently follows the same asset allocation process that the team has successfully applied to client portfolios since 2009, but tailored to client-specific requirements.

Eaton Vance

Eaton Vance's investment philosophy is grounded in the belief that the team needs to anticipate investors' needs rather than merely following industry trends. The Eaton Vance business consists of four investment brands through which Eaton Vance offers active, passive, rules-based and responsible investing strategies that go beyond traditional, mainstream strategies:

i) **EATON VANCE MANAGEMENT**—offering fundamental active equity, income, alternative and multi-asset strategies;

ii) **CALVERT RESEARCH AND MANAGEMENT (CALVERT)**—a global leader in responsible active equity, income, alternative and multi-asset strategies;

iii) **PARAMETRIC PORTFOLIO ASSOCIATES ("PARAMETRIC")**—systematic investment strategies and custom portfolio solutions built on a foundation of investment science; and

iv) **ATLANTA CAPITAL**—actively managed, high-quality U.S. stock and bond portfolio constructed using bottom-up fundamental analysis.

Eaton Vance believes in taking a flexible and evolving approach to responsible investing. The teams work in close collaboration with Calvert, a global ESG leader whose philosophy is taken from the viewpoint of a global responsible investor, and the aim is to provide competitive returns for investors and drive positive change through their investments and active engagement efforts. Calvert believes that most corporations deliver a net benefit to society, through their products and services, creation of jobs and the sum of their behaviours, and utilises a principles-based approach to identifying issuers that provide positive leadership in the areas of their business operations and overall activities that are material to improving long-term shareholder value and societal outcomes.

Integration With MSIM

As outlined earlier in this Principle, EV entities continue to be integrated into MSIM, not only from a business, distribution and operations perspective, but also in terms of knowledge sharing, best practices and resources, including, but not limited to, ESG research capabilities, and product and engagement collaboration with select MSIM investment teams, where appropriate (please see Principles 7 and 10 for more details).

ETF Platform

The launch of MSIM's ETF platform will target multi-asset, active and systematic strategies that complement our leadership in separately managed accounts (driven by Parametric's premier position in customisation), the distinguished mutual fund history at MSIM and EV, and MSIM's private fund platform that now has over $200 billion in Alternatives capital for clients. Underpinning the ETF strategy is EV's leadership in U.S. wealth management and MSIM's strength in non-U.S. wealth platforms. This initiative will also enable us to match our investment capabilities, including ESG strategies, with a broader set of investment vehicles our clients increasingly demand, and can therefore have access to.

Fulfilling Our Purpose and Furthering Our Investment Beliefs Over the Next Three to Five Years

As a client-centric organisation, our purpose is to provide investment and risk management solutions to a wide range of investors, incorporating investment innovation supported by our commitment to sustainability. Our plans over the next three to five years focus on growth across all investment capabilities and all distribution channels.

We continue to focus on our purpose and furthering our investment beliefs to serve our clients' best interests, supported by our commitment to advance our sustainable investment and stewardship practices, as well as our client offerings, reporting and disclosures, to meet client needs and demands.

At the centre of this is our integration with Eaton Vance, where we continue to bring together two thriving organisations with distinctive and highly complementary strengths in investment management, distribution and client service. The combination further strengthens the innovative and highly relevant solutions we deliver to clients, consultants and business partners across the globe. These range from ESG research/capabilities to product collaboration and the launch of an ETF platform (as noted above), expanding our existing distribution channels, offering clients access to multi-asset/products through an expanded range of investment vehicles and solutions. We are targeting our first set of ETF products to include ESG-related products, which again is our response to client demand, further demonstrating our commitment to our client-centric approach.

ESG is a focal part in our stewardship efforts and, over the past year, we have further tightened this focus, demonstrated by our active engagement, voting and escalation activities (please see updates in Principles 9, 11 and 12). We have also been more selective in collaboration (Principle 10), targeting new initiatives where we can directly influence or contribute to influencing material causes, focusing on obtaining real outcomes.

To support the above and our stewardship efforts more broadly during the reporting period, we have reviewed and are in the process of implementing enhanced governance procedures, including an enhanced guiding framework, oversight and monitoring/controls on products and external commitments. Internal assurance is also in progress to assess areas on which we can further advance on, vis-à-vis our clients' requirements and interests. Further details can be found in Principles 2, 3, 4 and 5.

Our competitive positioning is largely dependent on meeting client needs and demand, and we are seeing an increasing demand for ESG-centric investment solutions across key asset classes from our clients. We continuously evaluate opportunities to round out our capabilities that can successfully work within our culture. However, our growth plans are never without consideration of managing capacity and resources across investment strategies, to ensure that we are continually able to meet client expectations and deliver high-quality services.

We believe that our global presence, thought leadership, and breadth of products and services enable us to partner with our clients to design solutions that are both flexible and tailored to meet the ever-evolving challenges of today's financial markets.

Our Effectiveness in Addressing Our Clients' Needs

In assessing the effectiveness of how we have served the best interests of our clients during the reporting period, we have taken into account inputs such as direct client feedback on our approach, the alignment of our stewardship and ESG priorities with client/investor priorities (again, based on client feedback), and relevant regulatory reporting and disclosure requirements that we or our clients are subject to, as well as the scale and growth of our diverse investment platforms.

2022 HIGHLIGHTS

A key indicator of our effectiveness has been the continued development and growth of bespoke investment solutions, custom portfolios, multi-asset-class strategies and outcome-oriented accounts for clients. As of 30 June 2022, our customisable solution strategies reflect more than $703 billion in AUM comprising half of our overall $1.4 trillion AUM. Our ability to provide these types of investment solutions rests on the talent of our employees, who bring the benefit of diverse backgrounds, experiences and perspectives. Our Parametric business adds to the customisation, efficient implementation, transparency and risk control for our investors. Parametric's custom or "direct" indexing, rule-based fixed income, transparent options strategies, flexible derivative overlays and responsible investing capabilities are now important additions to our MSIM family, known for high-conviction active strategies and compelling alternative offerings. We deliver the best of our Firm—and the best results for clients—by promoting a culture of inclusion and belonging where dedicated professionals collaborate and produce breakthrough thinking. As noted previously, we are also targeting our first set of ESG ETF products in response to client demand and interest.

Secondly, our effectiveness is also evident from the long-standing relationships we have with many of our key clients who have been invested in our strategies for decades, across different investment teams, either within a client capacity or as co-investors, alongside our investment teams. Our top 10 oldest legacy MSIM mandates[5] date back to the 1980s, spanning our Fixed Income, Equity and Money Market strategies. This is testament to our client relationships and fiduciary commitments, as well as our sustainability/stewardship alignment with client needs. Please see Principle 6 for further details of our long-standing client relationships.

We believe that another measure of our effectiveness in serving our clients' best interests is our focus on Diversity, Equity and Inclusion ("DEI"), which is a key focus area for many of our clients and investors. Driven by our commitment to seek strategies and investments that align with clients' interests and investment objectives, MSIM joined the U.K. Chapter of the 30% Club earlier this year, collaborating with more than 40 investors targeting Chairs and CEOs of listed companies to achieve beyond 30% female representation and at least one person of colour on the FTSE 350 Board and ExCo level by the end of 2023. This is one of many examples demonstrating actions we take to align our stewardship activities with clients' needs (Principles 6, 7, 9 and 10), going above and beyond to provide holistic asset management within and outside portfolio management.

Our Firm has also made progress in DEI as we continue to focus on increasing diversity representation across our workforce. More immediately, we have set goals to increase the number of women officers globally by 25%, and Black and Hispanic officers in the U.S. by 50%, and, in 2021, we made meaningful progress towards those goals. Our 2022 Managing Director class reached historic highs for diverse groups, with women representing one-third of promotions globally.

[5] Legacy MSIM refers to Morgan Stanley Investment Management, excluding businesses that were wholly owned by Eaton Vance Corp. prior to the acquisition of Eaton Vance Corp. by Morgan Stanley on 1 March 2021.

As signatories to the U.K. Women in Finance Charter and U.K. Race to Work Charter, we remain committed to demonstrating our continued investment in employees and firm culture. In line with U.K. legislative requirements, in 2017, we issued our first Morgan Stanley U.K. Group Gender Pay Gap report. Since the publication of that report, we have made progress in reducing the gender pay gap. In 2017, we reported our first Morgan Stanley U.K. Group Gender Pay Gap median as 35.2%. At the five-year mark, we have seen continued year-over-year progress in narrowing the pay gap, with a 2021 median figure of 29.8%, a reduction from our 2020 median pay figure of 30.4% and a 5.4 percentage point decrease from our first report. While we achieved our initial goal of 30% in senior roles in 2020, earlier than targeted, we aim to continue to exceed this goal and remain committed to growing female representation at all levels and addressing the Gender Pay Gap. For more details, please see our Morgan Stanley Diversity and Inclusion Annual Report, and our Morgan Stanley U.K. Gender Pay Gap Report.

Our Firm's diversity efforts are led by our Chairman and CEO, James P. Gorman, and supported across the organisation by a dedicated team led by Morgan Stanley's Global Head of Diversity and Inclusion, Susan Reid, whose centralised group ensures consistent best practices across our initiatives. In addition, each division across the Firm has a dedicated Diversity Council (including MSIM), as well as a dedicated Diversity and Inclusion advisor, who partners with members of senior management to help drive our representation and inclusivity efforts. Creating a sense of inclusion and belonging is key not only to improving diverse representation across our company, but also helping to ensure stronger work and results from all employees for the benefit of our clients.

PRINCIPLE 2

Governance, Resources and Incentives

Signatories' governance, resources and incentives support stewardship

Governance Structures and Processes

Our overall governance structures and processes have not changed significantly during this reporting period; however, as set out below, we have made (or are in the process of implementing) certain key enhancements in our resourcing of stewardship activities oversight and assurance framework to further strengthen our governance in this area.

BOARD REVIEW

In line with the U.K. Financial Reporting Council ("FRC")'s expectations for appropriate review, approval and sign-off of U.K. Stewardship Code Report submissions by an applicant's governing body, beginning in 2022, our current report has been reviewed and approved by the board of directors (the "Board") of Morgan Stanley Investment Management Limited ("MSIM Ltd") Board, and signed by Ruairi O'Healai, Chief Executive Officer of MSIM Ltd and EMEA Chief Operating Officer of MSIM.

MSIM Ltd is a private limited company established in England and Wales, authorised by the FCA to provide investment management and investment advisory services to clients. It is an indirect, wholly owned subsidiary of Morgan Stanley, a corporation incorporated in Delaware, USA, and listed on the New York Stock Exchange. The Board is responsible for creating and delivering shareholder value and for the governance of MSIM Ltd. A formal schedule of matters reserved for the Board has been approved by the Board. These matters include: (i) approval of MSIM Ltd's strategy; (ii) approval of any material change in MSIM Ltd's strategy (including, for example, strategic extension into materially new business or geographic areas, or a decision to cease operating all or any material part of the MSIM Ltd business); (iii) approval of final financial statements and letters of representation; (iv) approval of the MSIM Ltd risk appetite and risk tolerance statements and limits; and (v) approval of material regulatory filings or regulatory public disclosures relating to MSIM Ltd.

The Board is composed of six members. The Chair of the Board is an Independent Non-Executive Director; there are four Executive Directors (including the CEO) and one Non-Executive Director.

The Board receives updates periodically at its board meetings from the central MSIM Sustainability team[6] and other functional stakeholders on ESG-/sustainability-related regulatory, business, product and strategic initiatives, including developments in the U.K. FRC's stewardship and reporting requirements, internal progress on the U.K. Stewardship Code report, and ongoing stewardship activities.

MSIM'S SUSTAINABILITY GOVERNANCE STRUCTURE

We continue to view effective management of stewardship and sustainability issues as a core component of our business strategy, and continue to evolve our philosophy, as we believe it is fundamental to the long-term success of our organisation and our ability to deliver value for our clients. We believe that a successful stewardship framework requires committed leadership, a clear strategy, and appropriate checks and balances to ensure overall accountability and transparency.

[6] Please see below for further details on the role of the central MSIM Sustainability team.

To that end, we have established the appropriate governance systems, risk management and controls to support our stewardship and sustainability agenda, outlined in our Sustainability Organisational Chart *(Figure 2.1)* below. As noted previously, our governance structure has remained largely unchanged during the reporting period, because we consider it to have been operating effectively, but we have made certain enhancements, as outlined below, including from a resourcing perspective.

MSIM SUSTAINABILITY COUNCIL

At the top of our stewardship governance structure, our MSIM Sustainability Council is co-chaired by the Global Head of Sustainability for Investment Management and Chief Responsible Investment Officer of Calvert Research and Management. Recognising our independent investment teams' structure, the Council consists of a group of investment team leaders and senior, cross-functional business leaders, including: (1) senior sponsors for MSIM's Sustainable Investing efforts—MSIM's Vice Chairman and Head of Strategic Partnerships and the CIO and Co-Head of Multi-Asset Solutions; as well as (2) senior management who are members of the MSIM Operating Committee chaired and led by the Global Head of Investment Management and Co-Head of Firm Strategy and Execution.

The Sustainability Council advises on and guides MSIM's support for the sustainable investment strategies of each investment business, including: promoting definitions and frameworks for Sustainable Investing and stewardship; supporting the continued innovation of ESG products and solutions; championing Sustainable Investing across MSIM's staff and culture; and ensuring business readiness for evolving client/regulator demands. The Council is responsible for the Sustainable Investing Policy and MSIM's Engagement and Stewardship Principles, which it reviews to ensure that

FIGURE 2.1

MSIM Sustainability Organisational Chart

MORGAN STANLEY'S INSTITUTE FOR SUSTAINABLE INVESTING

Strategic partner that shares industry best practices and engages with MSIM to develop leading sustainable investing strategies.

MSIM Sustainability Council

Reports to the Sustainability Council to facilitate oversight

MSIM SUSTAINABILITY TEAM

- Executes MSIM's sustainable investing business strategy in partnership with investment teams. Includes the Global Stewardship team.
- Has oversight of the groups below.

GLOBAL STEWARDSHIP TEAM

- Has oversight of the Proxy Review Committee

ESG TECH WORKING GROUP

- Defines and develops technology projects to support overall MSIM Sustainable Investing strategy
- Co-reports to OpCo

SUSTAINABILITY PRODUCT AND REGULATORY WORKING GROUP

- Co-reports to MSIM Regulatory Oversight Committee

SUSTAINABILITY TEAM LEADS

- The Sustainability team organises forum with this group to ensure coordination and consultation on substantive ESG matters prior to implementation

PROXY REVIEW COMMITTEE

- Oversees MSIM's proxy voting policy (updated annually), vote execution and voting operations, record retention and conflicts of interest in voting

SUSTAINABILITY DATA AND TECHNOLOGY COUNCIL

- Provides oversight and agreement on high-level ESG data and tech operational priorities

ESG Risk and Portfolio Controls

GLOBAL RISK AND ANALYSIS TEAM

- Global Risk and Analysis ("GRA") team leads sustainability risk monitoring and analysis.

PORTFOLIO SURVEILLANCE GROUP

- Responsible for implementing ESG guidelines in portfolio controls in collaboration with the Risk team.

they accurately reflect the philosophy and processes that govern MSIM's sustainability and stewardship strategy.

MSIM GLOBAL HEAD OF SUSTAINABILITY

The Global Head of Sustainability for Investment Management leads MSIM's sustainability strategy and governance and the centralised Sustainability team (please see *Figure 2.2* below, under MSIM Sustainability Expertise) that supports all of MSIM's global investment teams. The MSIM Global Head of Sustainability has 18 years of industry experience and was previously the Head of Green & Sustainability Bond Origination for Morgan Stanley's Global Capital Markets Group.

The Global Head of Sustainability for Investment Management co-reports to the MSIM Vice Chairman and Head of Strategic Partnerships and to the CIO and

FIGURE 2.2

MSIM Sustainability Expertise[7]

RUI DE FIGUEIREDO

Co-Head and CIO of Solutions & Multi-Asset Group (NY) | 25 years industry experience

TED ELIOPOULOS

Vice Chairman and Head of Strategic Partnerships (NY) | 25 years industry experience

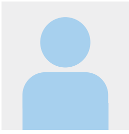
MSIM Sustainability Team

NAVINDU KATUGAMPOLA

Global Head of Sustainability for Investment Management, and Head of Sustainable Investing Fixed Income (London) | 18 years industry experience

ZENABU LABRI

Executive Director, Head of Sustainability Regulation and Policy (London) | 12 years industry experience



Incoming Executive Director, Head of Proxy Voting and Stewardship (London) | 20 years industry experience

SOFIA NALA KNIGHTLEY

Vice-President, Head of Sustainable Strategy and Solutions (London) | 13 years industry experience

VARUN MEHTA

Executive Director, Head of Sustainability Data & Technology (NY) | 13 years industry experience

FRANCES KELLY

Analyst, Sustainable Investing (London) | 2 years industry experience

ABBY LENDVAI

Analyst, Sustainable Content (London) | 1 year industry experience

GABY CORNEJO

Quantitative Analyst (NY) | 1 year industry experience

Global Stewardship Team

GAUTAM KAPOOR

Executive Director, Global Stewardship (Mumbai) | 16 years industry experience

ANSON CHAN

Vice-President, Global Stewardship (NY) | 20 years industry experience

MAMTA JOSHI

Senior Associate, Global Stewardship (Mumbai) | 9 years industry experience

RAJAT BHARGAVA

Associate, Global Stewardship (Bengaluru) | 4 years industry experience

NAVEEN SINGH

Associate, Global Stewardship (Bengaluru) | 6 years industry experience

[7] MSIM Sustainability Team Chart, as of 30 June, 2022, including incoming Head of Proxy Voting and Stewardship.

Co-Head of Multi-Asset Solutions, the senior sponsors for MSIM's Sustainable Investing efforts on the MSIM Operating Committee.

CHIEF RESPONSIBLE INVESTMENT OFFICER OF CALVERT RESEARCH AND MANAGEMENT

The Chief Responsible Investment Officer of Calvert Research and Management is responsible for the continued development of Calvert's research, engagement and stewardship functions. The Chief Responsible Investment Officer of Calvert was previously the Global Head of Sustainability for Investment Management and has 11 years of industry experience.

The Chief Responsible Investment Officer of Calvert reports to the President and CEO of Calvert, and the CIO and Co-Head of MSIM Multi-Asset Solutions, and co-reports to the MSIM Vice Chairman and Head of Strategic Partnerships.

MSIM SUSTAINABILITY TEAM

Led by the Global Head of Sustainability for Investment Management, the MSIM Sustainability team (*Figure 2.2* above, under MSIM Sustainability Expertise) acts as a centralised support resource for MSIM's portfolio managers, investment professionals and Sustainable Investing/ESG research specialists across our independent investment platforms—who are responsible for devising appropriate stewardship and ESG policies for their investment teams and strategies at industry, company and portfolio levels.

The MSIM Sustainability team supports MSIM's collective sustainability business efforts and governance processes, and guides MSIM's investment teams on enhancements to their stewardship and ESG integration practices, on the launch of sustainable funds, and on advising clients on sustainability matters. The team also helps to produce sustainability data, tools and research to support our investment teams. The team partners with the Sustainable Investing leads on each of our investment teams to co-ordinate global Sustainable Investing and stewardship initiatives.

Given the increased focus on stewardship and sustainability within MSIM, our client base and applicable law, and having regard to the growing scale of our business and sustainability offerings, the resourcing of the team was expanded during the reporting period to provide appropriate coverage, support and specialist expertise. In 2022, the Global Head of Sustainability for Investment Management created four specialised verticals (e.g., team heads):

1. **HEAD OF SUSTAINABILITY REGULATION AND POLICY**—leads projects to support MSIM's work in this area, including implementing key regulatory and industry ESG frameworks, representing MSIM in the related ESG-focused industry forums, and developing MSIM's approach to key sustainability themes. The Head of Sustainability Regulation and Policy also chairs (with the support of the Sustainability team) the Sustainability Product and Regulatory Working Group described below;
2. **HEAD OF SUSTAINABILITY STRATEGY AND SOLUTIONS**—focuses on strategic implementation, regulatory and product-related sustainability initiatives, including new products and existing strategies, supporting investment teams on product positioning, ESG labels, developing frameworks and content generation. The Head of Sustainability Strategy and Solutions also chairs the Sustainability Team Leads meetings (please see below for more details) and coordinates the Sustainability Council meetings;
3. **HEAD OF PROXY VOTING AND STEWARDSHIP (INCOMING OCTOBER 2022 HIRE)**—will lead MSIM's existing Stewardship team (please see below for more details), overseeing legacy MSIM's proxy voting and legacy MSIM engagement and stewardship-related activities, supporting investment teams. Responsibilities also include corporate governance research and analysis, monitoring and developing legacy MSIM stewardship strategies.
4. **HEAD OF SUSTAINABILITY DATA AND TECHNOLOGY**—leads all aspects of sustainability data due diligence and selection, quantitative analysis of portfolios and technology innovation to address use case in research, portfolio construction, and regulatory and client reporting. The Head of Sustainability Data and Technology also chairs the ESG Data and Technology Council.

Two additional junior hires (Sustainability Content and Quantitative Analysts) have also been made to support the Heads of Sustainability Strategy and Solutions, and Sustainability Data and Technology.

The build-out of the four verticals further enhances the team's centralised function across MSIM by providing:

- efficient coordination of specific sustainability issues, functions and tools that have utility to all of MSIM;
- sustainability expertise that seeks to ensure quality, consistency and integrity across asset classes and products, enabling investment teams to achieve their objectives;
- collaboration across Morgan Stanley businesses (Global Sustainable Finance—please see Principle 4, Institutional Securities Group and Wealth Management) to leverage internal synergies, delivering the best of One Firm into MSIM; and
- further support to MSIM-level reporting, policies and communications.

The MSIM Sustainability team also includes the MSIM *Global Stewardship team*, consisting of five stewardship analysts with an average of eight years of experience in corporate governance and proxy voting. The Global Stewardship team co-ordinates our stewardship and investee engagement agenda and activities alongside our investment teams, with help from our proxy advisors (please see Principle 8 for further details). The Global

FIGURE 2.3

Team-Level Sustainability Expertise[8]

JOHN STREUR

President and Chief Executive Officer for Calvert Research and Management (DC) | 35 years industry experience

EMILY CHEW

Chief Responsible Investment Officer, Calvert Research and Management (NY) | 11 years industry experience

MONA BENISI

Head of Sustainable Investing, Real Assets (NY) | 15 years industry experience

MARTE BORHAUG

Head of Sustainable Outcomes, International Equity (London) | 12 years industry experience

SANDRA LAUTERBACH

Head of ESG, Morgan Stanley Infrastructure Partners (NY) | 17 years industry experience

VIKRAM RAJU

Head of Impact, Private Market Solutions (London) | 26 years industry experience

LI ZHANG

Head of ESG Investment, Global Balanced Risk Control (London) | 14 years industry experience

DANA PHILLIPS

ESG Specialist, Emerging Markets (CA) | 15 years industry experience

ERIC CARLSON

Managing Director - Head of Sustainability Emerging Markets Equity (NY) | 26 years industry experience

MARC FOX

Managing Director, Global Opportunity (Toronto) | 17 years industry experience

JOHN WILSON

Director of Corporate Engagement for Calvert Research and Management (DC) | 25 years industry experience

HELEN MBUGUA

Director of Research for Calvert Research and Management (DC) | 13 years industry experience

JADE HUANG

Director of Applied Responsible Investment Solutions for Calvert Research and Management (DC) | 17 years industry experience

VLADIMIR DEMINE

Head of ESG Research, International Equity (London) | 20 years industry experience

GWEN LE BARRE

Director, Responsible Investing for PPA (Seattle) | 19 years industry experience

HARRISON JAMIN

ESG Data Specialist, Emerging Markets (NY) | 2 years industry experience

THOMAS KAMEI

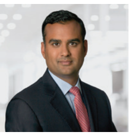
Executive Director - Sustainability Research at Counterpoint Global (NY) | 10 years industry experience

BARBARA CALVI

Executive Director - Sustainable Investing Fixed Income (London) | 12 years industry experience

RACHEL SMITH

Analyst Sustainable Investing Fixed Income (London) | 1 year industry experience



ANUJ GULATI

Managing Director, Head of Corporate Strategy, Calvert/MSIM Fixed Income (NY) | 21 years industry experience

CHIARA SIRANI

ESG Analyst, Global Balanced Risk Control (London) | 3 years industry experience

CANDY CHAO

Engagement Lead and ESG Specialist Emerging Markets (NY) | 3 years industry experience

KIAN MASTERS

ESG Senior Associate, Global Balanced Risk Control (London) | 7 years industry experience

VICTORIA ASHWORTH

ESG Lead, Impact, Private Market Solutions (London) | 3 years industry experience

[8] Team-level sustainability expertise as of 30 June 2022. Select members of investment teams across the MSIM platform that have sustainability expertise

Stewardship team is responsible for ensuring shareholder meetings are voted, and supports the investment team to vote in the best interest of the client, consistently applying the MSIM Proxy Voting Policy. Investment teams may collaborate with the Global Stewardship team when undertaking engagements to utilise their expertise on broader industry stewardship trends, amplify a sustainability message and/or provide supplemental resources in approaching specialist or systemic issues. Prior to engagement, the investment teams may work closely with the MSIM Global Stewardship team to assist in structuring engagement dialogues. The majority of engagements led by the Global Stewardship team focus on shareholder meetings and take place during proxy season.

It is the investment teams' responsibility to define their approach to stewardship and ESG integration. Each of our largest investment teams has appointed at least one dedicated Sustainable Investing/ESG research specialist to co-ordinate and support this work for that investment team (please see Principle 1 for further details in respect of specific investment teams). We believe that this model helps drive accountability for stewardship and ESG integration at investment team level, and ensures that each investment team is appropriately resourced and equipped to further its stewardship priorities and efforts, in a manner that it considers would best serve its clients' interests. As appropriate, investment teams will also expand sustainability coverage and expertise within their headcount. Please see below and Principle 7 for investment team-specific examples.

2022 Case Study – IE Team Resourcing

The International Equity team appointed its Head of Sustainable Outcomes last year, who reviews and contributes to ESG strategy for the team; liaises with Morgan Stanley, MSIM and external ESG and impact resources; contributes additional sustainability expertise to the investment debate and engagement with companies; has introduced external specialist research resources; and co-ordinates ESG matters for the team. The team's Head of ESG Research works closely alongside investment team members, focusing on the analysis of thematic material and relevant ESG issues, which can supplement the investment team's fundamental and ESG analysis of a company. The Head of ESG Research also works on company engagement topics and liaises with MSIM's Global Stewardship team as necessary.

A key responsibility of these investment team specialists is to work with the portfolio managers in their respective teams to help encourage ESG integration, in line with each team's investment philosophy and strategy. Other elements of the role include supporting investment staff in their stewardship efforts and continuously enhancing ESG integration in investment processes through research, training and knowledge-sharing; helping define methodology and resourcing for dedicated Sustainable Funds (where relevant); engaging with investee management teams; and representing their asset class/team in client meetings, consultant meetings and other forums and groups as necessary.

PROXY REVIEW COMMITTEE

The Proxy Review Committee oversees MSIM's Equity Proxy Voting Policy and Procedures ("MSIM Proxy Voting Policy," which is updated annually), including vote execution and voting operations, record retention and conflicts of interest in voting. The Proxy Review Committee consists of investment professionals who represent the different investment teams and geographic locations of MSIM, and is chaired by the director of the Proxy Voting team, which reports to the Global Head of Sustainability for Investment Management. The Committee meets at least quarterly and reviews and considers changes to the MSIM Proxy Voting Policy at least annually, with input from our Morgan Stanley Funds Board. Portfolio managers and other members of investment staff play a key role in proxy voting, given that proxy voting is an investment responsibility and impacts shareholder value, and because portfolio managers have in-depth knowledge of the companies and markets in which they invest. Please see Principle 3 for further details on the activities performed by the committee, particularly with respect to the management of conflicts in the context of proxy voting.

ESG TECHNOLOGY WORKING GROUP

The ESG Technology Working Group is comprised of technology leads from MSIM and Calvert, who work to define, develop and integrate technology expertise, projects and proprietary ESG data programmes to support client needs and the overall MSIM Sustainable Investing and stewardship strategy. This includes, and is not limited to, regulatory and bespoke client ESG reporting solutions, ESG portfolio management and analytics, ESG research, and proxy voting and engagement management tools. The ESG Technology Working Group reports to the Head of Global Sustainability for Investment Management and the Chief Responsible Investment Officer of Calvert Research and Management.

MSIM SUSTAINABILITY DATA & TECHNOLOGY COUNCIL

Our MSIM Sustainability Data and Technology Council supports business and client needs for ESG data governance and technological controls, and consists of a group of senior, cross-functional business leaders, including: (1) the Global Head of Sustainability for Investment Management and Chief Responsible Investment Officer of Calvert Research; (2) the Head of Data and Analytics for Investment Management; 3) Heads of Operations and Technology for Investment Management; and 4) Senior leaders from MSIM Legal and Compliance.

The Sustainability Data and Technology Council advises on high-level ESG data and tech operational priorities, including: Selection and sourcing of third-party ESG data; establishing and maintaining the ESG data governance framework in accordance with Firm standards; promoting continued innovation of ESG data and applications across the business; and ensuring technology readiness for evolving client/regulator demands.

SUSTAINABILITY RISK MANAGEMENT AND CONTROLS

We recognise that various sustainability factors can pose actual or potential material risks to our investments at the individual asset and portfolio levels. The Investment Management Risk Committee is appointed by the Firm Risk Committee to assist in the oversight of MSIM's risk management framework. The scope of this Committee includes all risk types and MSIM businesses, including sustainability risks, market risks, credit risks and other risks relevant to our investment management and stewardship approach. Within our Risk function, the Global Risk and Analysis team leads sustainability risk monitoring and analysis. Further details of how we manage sustainability risks, in particular, are outlined in Principle 4 – Promoting Well-Functioning Markets.

MSIM SUSTAINABILITY OVERSIGHT

As part of MSIM's 2022 sustainability and resource enhancements, the Global Head of Sustainability for Investment Management, in collaboration with the MSIM EMEA COO team, created a dual-hatted lead, responsible for Sustainability Oversight for MSIM by establishing an ESG control framework, which seeks to ensure processes are in place to capture and monitor product/investment commitments made. The objectives are partly to provide enhanced sustainability governance oversight and minimise greenwashing risk by MSIM, addressing regulatory and market concerns. Though build-out of this team is still in progress, it will be partnering with investment teams to help secure their respective ESG obligations and commitments. As part of existing oversight responsibilities, it also provides senior management transparency and regular updates on MSIM's ESG control environment.

THE SUSTAINABILITY REGULATORY AND PRODUCT WORKING GROUP

As noted above, this working group is chaired by the Head of Sustainability Regulation and Policy with support from the Sustainability team. This working group monitors and tracks global ESG legal/regulatory developments, including the EU Sustainable Financial Disclosure Regulation ("SFDR"), and rules published by the U.S. Securities and Exchange Commission ("SEC") and the U.K. FCA. The group meets with internal cross-functional teams, including Legal and Compliance, on a regular basis to coordinate and prioritise resources to respond to ESG-related regulations and consultations.

How Our Governance Structure Promotes Effective Oversight and Accountability of Stewardship

Enhancements made to our governance structure this year have been in response to our regular assessment of stewardship and sustainable investing capabilities and needs, resources and alignment with our products, and commitments to clients, taking into account regulatory requirements and market developments. In this regard, we have also taken steps to ensure that stewardship activities and corresponding governance and oversight are appropriately resourced at different levels in terms of headcount and seniority.

INVESTMENT TEAMS

As noted previously, each of the larger investment teams has appointed at least one dedicated Sustainable Investing/ESG research lead to take accountability for and coordinate stewardship and sustainability efforts at the investment team level. The stewardship and sustainability efforts of these investment teams are then supported by the MSIM Sustainability team, and overseen by MSIM control and sustainability oversight and governance functions on a day-to-day basis. The MSIM Sustainability team, in particular, provides centralised support to the investment teams and helps promote consistency, transparency and accountability across our different investment platforms (having regard to MSIM's Sustainable Investing Policy and Engagement and Stewardship Principles) and, through the Global Stewardship team, helps in structuring engagement dialogues and coordinating the engagement agenda across MSIM, as required. As noted above, the specific investment teams will also evaluate and, where appropriate, enhance their coverage and/or resourcing of sustainability matters.

SUSTAINABILITY TEAM AND SUSTAINABILITY COUNCIL

The Sustainability team (including our Stewardship team) is overseen by the MSIM Sustainability Council, which, as noted above, is made up of senior individuals from our investment teams and is co-chaired by the Global Head of Sustainability for Investment Management (who is also the Global Head of Sustainable Investing for MSIM Fixed Income and Liquidity) and Chief Responsible Investment Officer of Calvert Research and Management. This composition helps ensure that stewardship and sustainability matters are effectively prioritised, coordinated and overseen across our different business lines. The Sustainability team will also provide reports and updates on relevant stewardship and ESG matters to the boards of our regulated entities within EMEA.

SUSTAINABILITY OVERSIGHT AND GOVERNANCE

As mentioned above, our MSIM Sustainability Oversight function will be led by our current MSIM Head of EMEA and Asia Portfolio Surveillance in a dual-hatted capacity. This appointment capitalises on the MSIM Head of EMEA and Asia Portfolio Surveillance's experience managing our existing MSIM portfolio surveillance framework, monitoring product-specific and/or client-specific, ESG-related investment guidelines, both pre-trade and throughout the mandated life cycle. Developments on top of this framework will serve to strengthen oversight on product-related binding ESG commitments, such as in legal/offering documentation, to ensure, on the one hand, investment teams continuously work towards achieving and delivering such commitments, and, on the other hand, MSIM is able to report/disclose on progress and achievements as a result of this.

EXAMPLES OF OUR GOVERNANCE AND CONTROLS IN PRACTICE

1. PRODUCT DEVELOPMENT & NEW PRODUCT APPROVAL

By way of practical example, when an investment team seeks to launch a product with ESG/sustainability characteristics, the Sustainability team and Risk will be the first stakeholders involved in the review process. The ESG features and aims of the product will be assessed as part of MSIM's New Product Approval process based on an internal workflow specifically developed for reviewing any product with sustainability characteristics. This review involves various stakeholders across MSIM, who perform an independent assessment of the product, from a sustainability perspective, before it is brought to market. Please see *Figure 2.4* below for a broad overview of this review process:

ESG Checklist

A key feature of this workflow is the use of our internal ESG Checklist, which documents the proposed new product's ESG characteristics/objectives and methodologies used to attain these characteristics/objectives. It also covers existing products that seek to revise ESG characteristics/objectives

FIGURE 2.4

General Workflow for Review of Sustainability Products

INVESTMENT TEAMS	SUSTAINABILITY + RISK	PRODUCT	LEGAL & COMPLIANCE	PORTFOLIO SURVEILLANCE
• Propose investment idea and methodology • Identify target fund classification (using internal and external frameworks)	**SUSTAINABILITY** • Advise on sustainability issues • Review proposals against relevant classifications **RISK** • Opine on sustainability risk issues • Model identification (as relevant)	• Initiate and coordinate prospectus review and filing process • Gather competitor product intelligence and review	• Advise on drafting and regulatory requirements • Opine whether the proposed disclosure/ approach is clear and reasonable • Review relevant marketing documents • Agree oversight model with Portfolio Surveillance	• Identify relevant control framework (in collaboration with Risk and Sustainability) • Implement control framework with Risk

and methodologies. This Checklist is owned by the MSIM Sustainability team and has been further expanded this year, requiring investment teams to document specifically how their proposed or revised ESG characteristics/objectives/methodologies align with relevant regulatory classifications and requirements; e.g., SFDR and, where relevant, the rationale for any regulatory classification conversions.

Once the Checklist is reviewed by and signed off by the MSIM Sustainability team, it is then included in the broader product development process for presentation to Product Committees, such as the EMEA Product Governance Committee (as appropriate for specific fund ranges) with responsibilities for reviewing regulatory documentation, target market assessments and pricing, and, ultimately, the New Product Committee, which consists of senior functional stakeholders across MSIM and MS, who review, vet and sign off prior to product launch or formalisation of proposed material product changes.

Once a product with sustainability characteristics has been approved by the New Product Approval process and the workflow described above, our Portfolio Surveillance team will monitor ESG-related investment guidelines throughout the mandate. Sentinel, our guideline compliance system, assists equity portfolio managers in ensuring that trades are executed in compliance with client guidelines. The Sentinel system provides pre- and post-trade account guideline assessments for all equity accounts. All investment guidelines, including ESG-related investment guidelines, are coded in Sentinel to seek to ensure compliance with portfolio guidelines. Systematic ex-post checks are performed to ensure that stocks meet the fund's screening criteria, and automated IT systems prevent investment managers from investing in excluded stocks or those that do not meet positive screening criteria.

2. PATHWAY FOR INTERNAL REVIEW OF MSIM ESG-RELATED PROPOSALS

To provide more governance over our non-product ESG commitments, we have recently established an internal process to review proposed commitments from an MSIM and/or investment team perspective, given the number of cross-industry engagement/stewardship memberships and initiatives we sign up for. The scope also covers responses to ESG-related regulatory consultations (where relevant and appropriate) and industry-related proposals. The objective is to facilitate a consistent approach for internal review by relevant stakeholders of MSIM and across the Firm to ensure that proposed actions and/or memberships align with MSIM, the Firm, and clients' objectives and interests based on our fundamental philosophy of being client-centric and of being active and good stewards of our clients' capital.

3. THREE LINES OF DEFENCE

Stewardship and engagement activities are also assessed and monitored in accordance with our MSIM control and monitoring frameworks. MSIM operates a "three lines of defence" model (First Line is our business unit, key Second Lines of defence are Firm Risk Management and Compliance, and the Third Line is Internal Audit) to provide independent, objective and timely assurance about the effectiveness of the Firm's risk, governance and internal controls.

The MSIM Internal Audit coverage team is part of the Firm Internal Audit Department ("IAD"), which reports directly to the Firm's Board Audit Committee. Internal Audit is an independent and objective assurance function that is guided by the philosophy of adding value by improving the Firm's risk management, and helping the Board and executive management protect the assets, reputation and sustainability of the Firm. IAD assists the Firm in achieving its strategic and operational objectives by identifying and assessing risks facing the Firm, and providing independent, objective and timely assurance to stakeholders about the effectiveness of the Firm's risk management, internal controls and governance processes. Additionally, IAD may provide forward-looking insights about risks and control matters related to the Firm's strategic agenda. In so doing, IAD provides perspectives to both Senior Management and the Audit Committees for their consideration in discharging their legal, fiduciary and oversight responsibilities.

To fulfil its purpose, IAD maintains a professional staff with sufficient knowledge, skills and experience to meet these requirements.

IAD's mandate is to evaluate the design, implementation and operating effectiveness of the system of internal control across the Firm using a variety of tools and techniques at its disposal. Every activity (including outsourced activities) and every entity of the Firm (including subsidiaries, affiliates and branches) are subject to IAD coverage. IAD identifies and assesses key risks associated with the Firm's products, services and activities ("auditable universe") to inform its coverage for the assurance plan activities, and evaluates the adequacy and effectiveness of the Firm's system of internal control. IAD will consider the key aspects of a business's control framework, including evaluating the key processes of other control groups that work with the business, such as Compliance, Operations, Technology and Finance.

IAD conforms with the Institute of Internal Auditors' ("IIA") International Standards for the Professional Practice of Internal Auditing, which is validated by an independent third party every five years.

Internal Assurance of Stewardship

Good stewardship practices require periodic reviews of existing policies/procedures, governance frameworks, and sustainability/stewardship-related practices, to assess effectiveness, vis-à-vis MSIM and client requirements, but also to incorporate uplifts where appropriate, given the evolving regulatory and industry landscape. In Q4 of 2021, our MSIM Compliance team completed an ESG Testing review to assess whether relevant ESG disclosures complied with investment team practices, documentation and applicable regulations, and in Q3 of 2022, IAD commenced an ESG audit on our sustainability and stewardship governance, reporting and select portfolio management processes.[9] Though Firm policy does not allow external disclosure of results of internal reviews/audits, we continue to review, assess and enhance our overall approach holistically, as identified in our previous 2021 report. Progress is provided throughout this report in Principles 5, 6, 7 and 10.

Gifts and Entertainment; Confidential Information

Additionally, recognising the risk of inside information or inducements being received in the context of stewardship activities, all employees engaging in engagement and stewardship activities will be subject to MSIM's Global Gifts, Entertainment & Charitable Giving Policy, Global Confidential and Material Non-Public Information Policy related controls.

MSIM's Focus on Diversity and Inclusion

As evident from the membership of our Sustainability team above (as of 30 June 2022), we strive to ensure that principles of diversity and inclusivity are reflected within the individuals who lead and resource our stewardship framework. At MSIM, workforce diversity is both a priority and opportunity for our clients, employees and business. By valuing diverse perspectives, we can better serve our clients while we help our employees achieve their professional objectives.

Our MSIM Diversity Council therefore seeks to foster a diverse and inclusive culture across our entire business. We believe that this makes our employees feel appreciated and valued, makes us better investors by bringing to bear a plurality of perspectives, and helps us to deliver more innovative solutions to clients. The Diversity Council is comprised of senior executives from across MSIM (diversified by investor/non-investor and geography).

In addition to our existing Diversity and Inclusion initiatives, examples of new initiatives and developments made over the past year include, but are not limited to:

- **INVESTMENT STRATEGIES** – expanding our product suite of investment strategies with an emphasis on diversity; for example, an equity diversity fund that invests in companies that demonstrate leadership or meaningful improvement in terms of a diverse workforce and an equal and inclusive work culture;
- **INDUSTRY INITIATIVES** – Joining industry initiatives supporting gender diversity and ethnic minorities; for example:
  - 30% Club, a U.K. investor group that campaigns to increase gender diversity at board and executive-committee levels. As part of the Investor Group, MSIM seeks to drive diversity, equity and inclusion ("DEI") change in companies we have a share in
  - Black Women in Asset Management, a professional U.K. network we joined last year focusing on advancing and retaining Black, female professionals in the asset management industry
  - Robert Toigo Foundation – our MSIM Vice Chairman, Head of Strategic Partnerships, and a member of MSIM's Operating Committee sit on the Board. We have made commitments to double the number of Toigo alumni, supporting career advancement and increased leadership presence of under-represented talent
- **PROVIDING JUNIOR/MID-LEVEL EMPLOYEES A SAY IN DRIVING DIVERSITY** – in Q2 of 2022, our MSIM Diversity Council launched "Diversity Champions," an initiative to drive DEI focusing on four workstreams: (1) representation and recruitment; (2) advancement and culture; (3) commercial outreach and communications; and (4) DEI and investments
- **MENTORING** – launch of our first reverse mentoring programme earlier this year, pairing senior management with junior employees where the latter acted as mentors. The programme had a female and ethnic-minority focus with the goal of helping senior management better understand issues faced by these groups of employees, both at work and in daily life
- **TALENT DEVELOPMENT** – continuing to build on multiple talent-nurturing programmes, including *Women's Leadership Circles*, which focus on high-potential, female Executive Directors and seeks to create connectivity amongst senior female talent;

[9] The ESG Audit is still in-progress at the time of writing this report.

and *Emerging Leaders Programme*, which focuses on engaging and developing high-potential VPs by providing visibility, networking opportunities and leadership-focused development sessions

  – Externally, we have continued partnering with *Girls Who Invest* ("GWI"), led by the Founder of the NGO who has joined the MSIM leadership team. We have increased our involvement, commitment level and number of interns with GWI

- **DIVERSITY AND CULTURAL TRAINING** – unconscious bias and inclusive leadership training, including leadership conversations focusing on outcomes

Additionally, our Calvert business has a long history and emphasis on diversity over the years by engaging to encourage Board diversity at companies, developing the Calvert Women's Principles on which the U.N. Women's Empowerment Principles are based and has made diversity, inclusion and equity a strong engagement priority.

Engagement and collaboration with external industry organisations to further our commitment to Diversity and Inclusion can also be found in Principle 10.

Resourcing Stewardship Activities: Investment in Systems, Processes, Research and Analysis

In addition to the governance structure, processes and resources we have outlined earlier in this Principle, we continue to build upon our existing systems (where appropriate and feasible) to support our stewardship activities and efforts, and also as we progress in our integration with EV.

ENGAGEMENT RESOURCES

1. **ENGAGEMENT TRACKING:** The majority of engagements are tracked at the team level. Investment teams may utilise various systems to assist with tracking, such as Provosys and Aladdin Research. Through tracking engagements, investment teams are able to evaluate the success and progress of their interactions, in addition to identifying areas for further engagement or escalation, consequently pushing for better sustainability outcomes.

   Examples of fields tracked in engagement systems include: geography; issuer type; sector; engagement theme and summary; whether it was a satisfactory engagement; impact of engagement on investment strategy and type of sustainable bond (for Fixed Income only).

   Over the past year, the main upgrade made was an enhancement to enable Provosys to document and execute split votes within the automated workflow. Our Global Stewardship team will also be working on enhancing the engagement module in Provosys to enable improved documentation and reporting capabilities.

   Our EV affiliates operate similarly to our independent MSIM investment teams, and so our mid-term goal for the next two to three years is to integrate the different engagement tracking systems used into one, to allow for holistic monitoring and governance. As part of these efforts, our near-term goal is to provide an overview and training for relevant stakeholders on MSIM frameworks and systems, in order to obtain feedback on what and how the combined structure/system should look and operate.

2. **INTERNAL VOTING PLATFORM:** Our internal voting platform notifies portfolio managers when there is a meeting for one of their holdings, and they are given the opportunity to input on the Global Stewardship team's analysis and voting recommendations prior to finalising the investment team's voting decision. This interactive process facilitates ongoing discussion between the Global Stewardship team and portfolio teams about a holding's material ESG and related stewardship issues. The platform also enables a semiautomated control process to ensure eligible holdings are voted at shareholder meetings.

   As with our engagement tracking systems, our mid-term goal over the next two to three years is to align voting platforms across MSIM and EV affiliates, with the near-term goal of sharing our best practices to gain a better understanding on potential options and ways of combining internal voting platforms.

3. **MSIM'S GLOBAL STEWARDSHIP TEAM:** MSIM has a dedicated Global Stewardship team (as mentioned above) to help coordinate and execute stewardship activities across MSIM and provide support to investment teams. Coupled with the incoming Head of Proxy Voting and Stewardship who will lead the team, this serves to strengthen the overall success of engagements and focus on specific thematic areas; e.g., climate, which is a key priority for the Firm. Our Head of Proxy Voting and Stewardship will work closely with engagement experts in both legacy MSIM and our EV affiliates to synchronise such efforts.

ESG DATA RESOURCES

Investment teams may supplement their proprietary ESG research and analysis with third-party ESG data. ESG data is utilised in various ways; for example, some investment teams use it to inform their own fundamental

SPOTLIGHT NO. 1

Progress on the Development of Our ESG Proprietary Database/System

The centralisation of the ESG data stack (consisting of data sets across the ESG spectrum of approaches, across asset classes and data providers) at Morgan Stanley has allowed for product innovation and applications enhancements across the Firm, including MSIM. In close collaboration with interested business units, the Global Sustainable Finance ("GSF") team constructed a set of application prototypes enabling portfolio analysis across a range of sustainability factors. Importantly, we believe that assessing a portfolio on ESG risks and opportunities relies on using multiple sources of information, and, in most cases, from different third-party providers to allow for cross-comparability. These include, and are not limited to:

1. **Climate Analytics**
   Our analytics have a heavy focus on climate, where we engage clients and internal teams around carbon emissions, portfolio earnings at risk from carbon price scenarios, corporate science-based target analysis, power generation mix, exposure to stranded assets and physical risk.
2. **Geospatial Capabilities (Under Development)**
   We continue to expand our geospatial capabilities in order to ingest publicly available weather and hazard information, as well as vendor solutions. This increased flexibility allows for a more complete climate picture.
3. **ESG Screening and Analytics**
   On the ESG side, we focus our analytics on portfolio exposures to a range of more than 50 screening criteria, an assessment of performance across ESG ratings providers, an analysis of impact alignment to a range of sustainability themes from a corporate revenue perspective, and additional proprietary analysis, including an increased focus on diversity, equity and inclusion, where we mapped granular data to an existing framework on inclusive growth. These tools and analytics are actively being deployed across a range of platforms, both internally and with clients.

In the last 12 months, there has been an increased focus on creating data-driven tools for portfolio analysis and reporting on EU regulations. In particular, MSIM acquired third-party data sets for regulatory reporting, and created internal tools for monitoring the EU SFDR's Principal Adverse Sustainability Indicators; MSIM is also expanding the solution to address reporting requirements for the EU SFDR more broadly. Client requests for TCFD metrics are also becoming increasingly common, and we are actively building solutions to address client reporting needs in this area.

There is a steady pipeline to develop more ESG analytics modules. We will gradually shift the focus towards ex-ante portfolio ESG modelling and issuer-level ESG analysis as we progress in our proprietary ESG database/system build-out.

research, while other teams integrate third-party data into proprietary models and scoring frameworks. In turn, the use of ESG data helps to identify material ESG risks or issues, consequently supporting investment teams in identifying areas for future engagement and stewardship.

Third-party ESG data providers are generally selected based on how effectively they will meet our stewardship needs and particularly on the depth and breadth of coverage required for regulatory reporting and disclosures. For example, when evaluating an ESG data provider, we take into consideration the applicability of the data of a particular topic (e.g., climate, biodiversity) and use case (e.g., research, reporting), breadth of coverage, robustness of the vendor's methodology, and feasibility of implementation.

Once sourced and onboarded, MSIM leverages this data to support individual teams with ESG integration and client reporting. Driven by strong internal demands, increased volume of client interests and changing regulations, MSIM has been further enhancing its ESG analytics dashboards this year to help investment teams to view ex-post portfolio exposure to a broad spectrum of ESG metrics, in areas such as climate, screening and controversies, corporate ESG ratings and sustainable revenues.

For more information on how each investment team incorporates third-party ESG data into their investment process, please see Principle 7. For more information on how we monitor our service providers, activities and progress during the reporting year, please refer to Principle 8.

USE OF SERVICE PROVIDERS

MSIM views proxy voting as one of the key stewardship activities and obtains information on corporate governance, proxy voting, issuer research and selected environmental and social issues from its investment teams' own research, as well as two independent advisors, Institutional Shareholder Services ("ISS") and Glass Lewis, who provide vote execution, reporting and record-keeping services.

ISS and Glass Lewis were selected in this space as, currently, only these two service providers have the capacity to handle our global portfolio of voting in more than 65 markets. In addition to extensive coverage, both of these providers exhibit good levels of due diligence in their research and are responsive when we identify errors in their research.

As active managers, we take a more engaged and direct approach on stewardship, and our use of services provided by ISS and Glass Lewis is more supplementary and administrative in nature (please see Principle 8 for more details). On the supplementary side, MSIM retains ISS and Glass Lewis as research providers to provide company-level reports that summarise key data elements contained within an issuer's proxy statement. This timely research includes data points on thousands of companies, which are useful for us to make voting determinations. While we are aware of their voting recommendations (given our active stewardship approach), these recommendations are not determinative of our vote nor is any potential vote prepopulated based on their research. MSIM votes all proxies over which it has voting discretion based on its own proxy voting policies in the best interests of each client or, where relevant, in accordance with client instructions.

The research provided by ISS and Glass Lewis give our Firm insight into emerging global trends and best practices in global governance. In addition to voting, we may also leverage data points from these providers (e.g., data points around board diversity) when engaging with issuers. These data points help us to target specific holdings and determine our strategy to methodically engage and exercise our stewardship duties.

Further information relating to our use of service providers can be found under Principle 7 and Principle 8.

Performance Management and Reward Programmes

MSIM remains an employer of choice by offering competitive compensation programmes to our employees. A primary objective in designing compensation programmes for MSIM employees is to ensure that compensation incentives are aligned with our business strategy of driving performance and adding value for clients, shareholders and other Firm employees. Additionally, the Firm ensures that our programmes are highly competitive in the industry, and well communicated and understood internally. MSIM employs the services of a variety of compensation consultants globally to ensure that our compensation methodology for investment professionals is competitive, objective and transparent.

Further, the Firm has a Global Incentive Compensation Discretion ("GICD") Policy, which is reviewed at least annually and amended, as needed, in advance of the annual incentive compensation decision-making process. The GICD Policy requires and directs compensation managers to consider only legitimate, business-related factors when exercising discretion in determining incentive compensation. Such factors include adherence to Morgan Stanley's core values, conduct, disciplinary actions in the current performance year, risk management and risk outcomes. The GICD Policy also requires and directs compensation managers to escalate circumstances that may warrant cancellation or clawback of previously awarded compensation for further investigation. Compensation managers are required to certify their compliance with the GICD Policy in advance of exercising discretion in determining incentive compensation, and Morgan Stanley's HR coverage team works directly with compensation managers to ensure that they understand their responsibilities.

Where required by regulation, such as the EU SFDR, the UCITS[10] Directive or MiFID II,[11] our local entities have adopted remuneration policies to promote sound and effective risk management with respect to sustainability risks, including discouraging excessive risk-taking with respect to sustainability risks. Risk is considered at every stage of the compensation planning process, from the initial determination of the bonus pool to individual compensation decisions. Remuneration policies adopted according to regulations are publicly available for MSIM Fund Management (Ireland) Limited, Morgan Stanley Europe SE and Morgan Stanley SGR S.p.A.

Though the implementation of stewardship is currently not a formal part of employee development plans, we are currently exploring options to enhance and formalise this as part of internal governance and regulatory expectations to ensure stronger linkage and correlation between stewardship in employees' work activities and performance, and reward programmes.

Based on our current framework, the ongoing integration of stewardship across MSIM is broadly considered in the appraisal process for some staff. In addition, several investment teams have committed to third-party stewardship/ESG training for investment analysts and portfolio managers. Dedicated Sustainability professionals also have ongoing training included as part of their professional development plans. Furthermore, portfolio managers are incentivised to outperform their respective benchmarks over a multiyear time horizon. Given our view that there is a link between stewardship/ESG and performance, portfolio managers are implicitly incentivised to consider this, with a view to generating long-term value and returns in the portfolios they manage.

One of the ways in which we look to strengthen stewardship in employee development plans is through mandatory sustainability training. We are currently in the process of launching an MSIM-wide training

[10] Undertakings for Collective Investment in Transferable Securities Delegated Directive (EU) 2021/1270.

[11] Markets in Financial Instruments Directive (EU) 2014/65 and Markets in Financial Instruments Regulation (EU) 600/2014—collectively known as MiFID II.

programme, which seeks to provide baseline knowledge across related front, middle and back office functions on a range of topics, including, but not limited to: market and regulatory landscape (including greenwashing risk), client ESG/stewardship requirements and interests, MSIM Sustainability and Stewardship framework, governance, conflicts of interest and risk management.

In creating this programme, detailed analysis was conducted to ensure bespoke buy-side sustainability training based on MSIM's global business, stewardship responsibilities, respective industry memberships and Stewardship Codes it is a signatory to, and key applicable global regulations. Additionally, topical training is currently being provided to relevant stakeholders in areas such as EU SFDR Regulations, MiFID Client Suitability Assessments and Sustainability Preferences, etc.

By providing baseline training to both MSIM investment teams (including EV affiliates) and supporting functions, we also seek to ensure our employees feel valued as we continue to invest in their development.

Notwithstanding the upcoming initiatives, individual performance is and will still be based on a combination of quantitative and qualitative factors, taking consideration of contribution to the performance of the whole business. The review process is regular with clear feedback. Factors currently considered include culture, broad contribution to the organisation, as well as performance and asset growth. Stewardship plays a role in each of these factors in different ways.

Effectiveness of Governance Structure and Processes

Our stewardship and sustainability governance structure and processes have been set up to align with our MSIM business values and purpose, and to ensure accountability and effective oversight of our stewardship efforts across MSIM.

We believe that our multidimensional approach—our Sustainability leadership, Sustainability Council, core Sustainability team, Global Stewardship team and other related working groups—allows flexibility to adapt our MSIM stewardship programme, given our independent investment teams' structure. By embracing our diverse investment strategies, this allows for adaptation which will ensure our Sustainability programme's relevance to our clients and the changing global economic climate. It can also generate employee engagement.

As part of this adaptation and flexibility, we continuously seek to improve and enhance weaknesses in our stewardship methods and framework. As noted in the preceding section, over the reporting period, we have made progress in enhancing our governance structure and processes, expanding people and technical resources, updating corresponding policies and procedures, advancing on our collaboration efforts and sharing best practices with EV affiliates, including Calvert and Parametric and technology and infrastructure integration across the board, to support increasing efforts on the stewardship front:

- Resources
  - *Specialists* – To support a growing business, expanding stewardship activities, client needs and regulatory requirements, we have further defined specialist verticals and added key expert resources to our MSIM Sustainability team while in the process of creating new Sustainability Oversight and Governance roles. Given that this is still a work in progress, effectiveness of such measures has yet to be fully assessed; however, specific objectives and goals have been set, and progress will be measured and reported in our next U.K. Stewardship Report
- Governance Framework
  - *ESG Oversight/Governance Framework* – In-line with the above, implementing an enhanced holistic ESG framework will be a key priority over the next six months.
  - *Products/External Commitments/ESG-related Proposals* – Combined with a more granular review of new products and existing products (per our product development process), and a formal review pathway for external commitments and ESG-related proposals, this enhances control and oversight, which will in turn allow for better tracking and monitoring of actions and outcomes
- Policies & Procedures
  - *MSIM Proxy Voting Policy* – In line with our commitment to revise annual updates to the first quarter of each year as opposed to the third quarter to ensure the policy is updated ahead of each proxy season, we implemented this change in Q1 of 2022, including clarifications on our expectations with regards to board diversity and accountability for boards failing to meet this expectation. In doing so, we also clarified our general approach to voting on environmental and social issues, highlighting certain key elements and the expectation for enhanced transparency. The rationale for these updates is based on evolving best practices, hence it clarifies our expectation on certain key elements to guide companies in which we invest towards better

governance practices, which we believe produce long-term, sustainable returns. Such updates will further integrate our governance and proxy voting policy with clients' investment goals, using votes to encourage portfolio companies to enhance long-term shareholder value and to provide a high standard of transparency such that equity markets can value corporate assets appropriately

- *ESG Amendments to Regulatory-Related Policies* – As part of the MiFID II, UCITS and AIFMD[12] amended regulations to incorporate sustainability into existing policies and processes, we have reviewed and assessed requirements against our internal functional areas and processes, performed gap analyses and made relevant internal updates to our Suitability Process, creating a framework capturing clients' Sustainability Preferences, reflecting these updates in our Conflicts of Interest Register and related EMEA entity Conflicts of Interest policy, and others—to incorporate sustainability risks and factors into our existing processes, and provide guidance to relevant stakeholders who interact closely with our clients. Please see Principle 3 for more details.
- *Stakeholder Input* – We continue to seek input and consensus from a wide range of MSIM stakeholders, including EV affiliates, as well as input from other relevant functions with MSIM (e.g., Legal and Compliance, etc., where appropriate)

- Collaboration and Stewardship Know-How
  - *External Collaboration* – Our MSIM investment teams generally take a one-to-one direct approach in engaging with our portfolio companies. Over the reporting period, we have taken a more targeted approach in collaborating with external industry groups and organisations, carefully selecting the ones that provide the most potential for impact and outcomes aligned with our client interests. For example, as outlined in Principle 1, we joined the U.K. Chapter of 30% Club, further extending both MSIM and the Firm's commitment to diversity and inclusion. We also submitted an application to join the U.N. PRI Advance, a new stewardship initiative where institutional investors will work together to take action on human rights and social issues. Our application was submitted in collaboration with several of our investment teams, who jointly came together for a common cause (please see Principle 10 for more details on outcomes of our collaborative efforts).
  - *Leverage Calvert/Parametric Strengths* – We continue to share stewardship knowledge and best practices with our EV affiliates, including Calvert and Parametric. We recently embarked on two product collaborations between our MSIM Global Listed Real Assets team and Calvert, launching a Climate Transition Fund and a Global Real Estate Fund. With other product collaborations in our pipeline, we endeavour to create a Sustainability powerhouse, marrying our diverse MSIM investment platform with Calvert's strengths and Parametric's rules-based customised solution capabilities.
- Enhance Technology/Infrastructure To Support Governance and Growing Stewardship Efforts
  - *Resources/Systems* – As we continue to grow and further our Sustainability agenda, we are in the process of building our data and technology capabilities (please see Principle 8) to better track, monitor and use ESG data analytics, including a centralised engagement tracking system that covers both our public and private investing platforms. As detailed earlier in this Principle, we hired a Head of Sustainability Data and Technology for the MSIM Sustainability team as well as a Quantitative Analyst to help facilitate and lead efforts in this area—in line with last year's commitments. To complement our increase in headcount and support, our Calvert colleagues have also expanded their Data and Technology team to better coordinate integration with MSIM and to meet increasing technology needs as a result of stewardship developments from our business as a whole.

[12] Alternative Investment Fund Managers Delegated Regulation (EU) 2021/1255.

PRINCIPLE 3

Conflicts of Interest

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

MSIM Conflicts Management Framework

As part of a diversified global financial services firm that engages in a broad spectrum of activities, MSIM may encounter potential or actual conflicts of interest between: (i) MSIM (including connected persons such as our affiliates and employees) and our clients; and (ii) different clients.

MSIM is conscious of the need to manage our clients' assets in our clients' best interests and has put in place a framework for managing these conflicts of interest. All MSIM employees must comply with Morgan Stanley's Global Conflicts of Interest Policy, which outlines principles and standards, including: (1) policies and procedures for identifying and addressing conflicts; (2) a framework for escalation of conflicts; (3) periodic review of significant conflicts-related issues; (4) policy assurance methods; and (5) governance. We have disclosed a summary of Morgan Stanley's Global Conflicts of Interest Policy in the Appendix of this report.

Along with Morgan Stanley, MSIM has established procedures intended to identify and mitigate conflicts of interest related to business activities on a worldwide basis. A conflict management officer for each business unit and/or region acts as a focal point to identify and address potential conflicts of interest in their business area. When appropriate, there is an escalation process to senior management within the business unit, and ultimately, if necessary, to Firm management or the Firm's franchise committees, for potentially significant conflicts that cannot be resolved by the conflict management officers or that otherwise require senior management review.

All MSIM employees must also comply with Morgan Stanley's established Firm-wide policies and procedures, such as: the Firm Code of Conduct, Global Gifts, Entertainment & Charitable Giving Policy, Global Employee Trading and Outside Business Activities Policy, Global Confidential and Material Non-Public Information Policy (covering information barriers) and the Firm Conflict Clearance Policy, which identify the various activities that Business Units must notify or clear through the Firm's Conflict Management System (the "Conflict File") governed by the Global Conflicts Policy before proceeding with those activities.

All employees receive appropriate training to ensure that they are fully aware of their responsibilities and obligations. As part of the conflicts management framework, MSIM has a Conflicts of Interest Committee, chaired by a Conflicts Management Officer, with a remit that includes reviewing and evaluating transactions and business practices identified as posing conflicts of interest; evaluating, in aggregate, matters brought to the Committee to assess consistency of resolution and potential themes or trends; and maintaining the Conflicts of Interest Register (as mentioned above). MSIM also has in place an escalation process, both to senior management within the business unit and to Firm Management, or the Firm's franchise committees, for potentially material conflicts.

In 2022, the MSIM Conflicts of Interest Registers was updated to reflect our evolving understanding of situations that could conflict with the sustainability preferences/interests of our clients. We did this in the context of new ESG conflicts rules that began to apply to MSIM Ltd's European affiliates.

Approach to and Examples of Stewardship Conflicts and Outcomes

MSIM recognises the importance of identifying and managing conflicts in the context of stewardship, which are addressed through the wider conflicts management framework set out above. Our conflicts management framework enables us to identify and manage actual and potential conflicts of interest in the context of stewardship. Such conflicts may arise , for instance, as a result of MSIM's commercial relationships with clients or third parties who may be issuers of securities held on behalf of accounts managed by MSIM, or from cross-directorships of MSIM staff. MSIM is also part of Morgan Stanley, a global financial services group, and, as such, MSIM faces potential conflicts due to the role of other Morgan Stanley divisions, which represent companies in which MSIM may invest.

In addition to the above, our approach to identifying, managing and mitigating other potential stewardship-related conflicts is as follows:

PROXY VOTING

Material Conflict Management

MSIM takes a targeted approach[13] in pre-identifying conflict of interest as part of the voting process. The MSIM Proxy Voting Policy provides guidance for identifying actual or potential material conflicts of interest in voting situations, a process maintained by MSIM's Sustainability team and Global Stewardship team. A potential material conflict of interest could exist in the following situations, among others:

1. The issuer soliciting the vote is a client of MSIM or an affiliate of MSIM and the vote is on a matter that materially affects the issuer;
2. The proxy relates to Morgan Stanley common stock or any other security issued by Morgan Stanley or its affiliates except if echo voting is used;
3. One of Morgan Stanley's independent directors or one of MSIM Funds' directors also serves on the Board of Directors or is a nominee for election to the Board of Directors of a company held by an MSIM Fund or affiliate; or
4. Morgan Stanley has a material pecuniary interest in the matter submitted for a vote (e.g., acting as a financial advisor to a party to a merger or acquisition for which Morgan Stanley will be paid a success fee if completed).

If the Global Stewardship team determines that an issue raises a potential material conflict of interest, the following process will be followed as deemed appropriate:

- If the matter relates to a topic covered by the MSIM Proxy Voting Policy, the proposal will be voted as per the Policy;
- If the matter is not covered by the MSIM Proxy Voting Policy or the Policy indicates that the issue is to be decided on a case-by-case basis, the proposal will be voted in a manner consistent with the recommendations of the Research Providers,[14] provided that a) all the Research Providers consulted have the same recommendation, b) no portfolio manager objects to that vote and c) the vote is consistent with the objective of maximising long-term investment returns;
- If the Research Providers' recommendations differ, the Global Stewardship team will refer the matter to a Special Committee to vote on the proposal, as appropriate;
- Where it serves the best interest of our clients, MSIM will vote against management;
- 'Echo Voting'[15] may be used where shares are instructed to be voted in the same proportion as the vote of all of the other holders of the fund's or company's shares, where feasible; and
- Where Morgan Stanley or MSIM hold shares in MSIM-managed funds, MSIM may use the voting rights conferred by those shares to vote at the General Meetings of those funds provided its votes are in line with the recommendations of at least two research providers

CASE STUDY 3.1: PROXY RELATING TO SECURITY ISSUED BY MORGAN STANLEY OR ITS AFFILIATES

CONFLICT	• The proxy relates to a security issued by Morgan Stanley or its affiliates.
CONFLICT DESCRIPTION	• In May 2022, MSIM, in its capacity as investment manager of client portfolios invested in a Morgan Stanley fund, had to vote on resolutions relating to that fund. • Situations of this nature represent a potential conflict because of the risk that the vote would be motivated by the interests of the Firm; e.g., passing a contentious increase in remuneration, rather than the interests of MSIM's clients.
MANAGEMENT	• Since the shares voted amounted to under 2% of all shareholder votes, the way we managed this risk was by ensuring that we followed the vote recommendations of independent research providers, in this case, both ISS and Glass Lewis, who recommended in favour of all resolutions. • This was done to ensure compliance with the MSIM Proxy Voting Policy.
CONFLICT OWNER(S)	• MSIM Proxy Voting Team & MSIM Conflicts Officer

[13] Targeted approach in the context of the conflict of interest identification involves specific meeting level monitoring for conflict scenarios which represent a potential conflict of interest.

[14] ISS and Glass Lewis.

[15] Echo voting refers to a practice when one votes shares in the same proportion as the vote of all of the other holders of the fund's shares.

Special Committees are comprised of the Global Stewardship team and at least two portfolio managers (preferably members of the MSIM's Proxy Review Committee), as approved by MSIM's Proxy Review Committee. The Global Stewardship team may request non-voting participation by MSIM's General Counsel or their designee and the Chief Compliance Officer or their designee. In addition to the materials from Research Providers, Special Committees may request analysis from MSIM Affiliate investment professionals and outside sources to the extent deemed appropriate.

The MSIM Proxy Review Committee has overall responsibility for the Policy. The Committee consists of investment professionals who represent the different investment disciplines and geographic locations of MSIM, and is chaired by the director of the Global Stewardship team.

The MSIM Global Stewardship team tracks actual and potential conflicts of interest arising in a proxy voting context, and how these issues are handled. All such issues are also reported to the Proxy Review Committee, and, on a quarterly basis, to public fund boards for relevant portfolio companies. MSIM memorialises conflict-of-interest issues in the minutes of Proxy Review Committee meetings and will disclose them to clients that hold the affected securities in their accounts if requested.

The EMEA IM Conflicts of Interest Committee monitors quarterly metrics on exceptions to the MSIM Proxy Voting Policy and procedures across these four conflicts categories.

In the period 1 July 2021 to 30 June 2022, all potential conflicts of interest related to proxy voting were considered and resolved with either a vote against a management recommendation or application of voting policy. There were no policy overrides at meetings identified with a potential conflict of interest.

DIFFERENCES BETWEEN INVESTMENT TEAMS ON VOTES

As a result of MSIM's independent investment team structure, a situation may emerge whereby different investment teams have different views on a particular vote for a company. At all times, we aim to stay true to our stewardship philosophy in seeking to maximise long-term investment returns for each client. Under these

CASE STUDY 3.2: VOTING WHERE MORGAN STANLEY IS AN ADVISOR TO AN M&A TRANSACTION

CONFLICT	• Voting where Morgan Stanley's Investment Banking Division (sell-side) is an advisor to an M&A transaction
CONFLICT DESCRIPTION	• In June 2022, MSIM voted in favour of the merger of a U.S. electronics company and a multinational communication technology company, for which transaction Morgan Stanley Investment Banking Division was serving as financial advisor. • Situations of this nature represent a potential conflict because of the risk that the vote would be motivated by the interests of the Firm; e.g., completion of the transaction and receipt of associated revenue, rather than the interests of the clients.
IDENTIFICATION	• The resolution was identified as part of the standard Shareholder Meeting review process.
MANAGEMENT	• The way we managed this risk was by ensuring that we followed the vote recommendations of independent research providers, in this case ISS, who recommended in favour of the transaction. • This was done to ensure compliance with the MSIM Proxy Voting Policy. • MSIM took further actions to manage this potential conflict: – MSIM assessed the merits of the transaction objectively. We considered this vote consistent with the objective of maximising long-term investment returns since the merger consideration was fair and provided both liquidity and certainty of value. – We ensured that Morgan Stanley buy-side and sell-side divisions continue to operate on an arm's-length basis, with physical segregation between divisions. Interactions between the divisions are subject to Compliance monitoring. There was therefore no influence from the Investment Banking Division on this vote.
CONFLICT OWNER(S)	• MSIM Proxy Voting Team & MSIM Conflicts Officer

circumstances, different views on a particular vote will result in a conflict, which we seek to manage through split votes. For example, when different clients have varying economic interests in the outcome of a particular voting matter (such as a case in which varied ownership interests in two companies involved in a merger result in different stakes in the outcome), the votes will be cast on a split basis (in proportion to the votes held by the relevant clients).

We also may split votes at times based on differing views of portfolio managers (e.g., based on what they consider would generate better value for their investment strategies). These generally apply to cases where the policy item is determined on a case-by-case basis. Where policy guidelines are clear on the voting matter, the policy is generally followed, and hence a split vote should not arise.

ARM'S-LENGTH APPROACH

In addition to the controls and mitigants set out above, MSIM deals with other group companies within the Morgan Stanley Group at arm's length. By doing so, we minimise the risk that we will act towards our portfolio companies in line with the interests of other divisions; e.g., Institutional Securities rather than the interest of our clients. Further, trading in Morgan Stanley securities by accounts managed by MSIM is prohibited by MSIM's policy and procedures.

EMPLOYEE PERSONAL TRADING AND OUTSIDE BUSINESS ACTIVITIES

MSIM has also put in place processes to identify and manage situations where an employee's personal relationships and outside business interests might compromise MSIM's duty to act in the clients' best interests. Employees are subject to the Firm's Global Employee Trading and Outside Business Activities Policy, which establishes a duty to declare and seek prior approval for in-scope outside business interests and dealing on personal accounts. MSIM conducts e-communications surveillance to undeclared outside business interests. MSIM requires employees to confirm personal dealing accounts annually. As mentioned above, the Firm's Code of Conduct applies to all MSIM employees.

PORTFOLIO MANAGEMENT

As our portfolio managers are involved in stewardship and engagement efforts, we are mindful of the risk of them acquiring inside information in the process or undertaking personal account dealing that would conflict with client interests and result in potential client detriment. Accordingly, all portfolio managers (and other personnel involved in stewardship and engagement activities) must comply with the Global Gifts, Entertainment & Charitable Giving Policy, Global Employee Trading and Outside Business Activities Policy, Global Confidential and Material Non-Public Information Policy and related controls.

Additionally, when an advisor manages multiple portfolios ("side-by-side management") with different structures (e.g., registered funds and unregistered funds) and/or fee structures (e.g., performance-based fees versus asset-based management fees), certain perceived or actual conflicts may arise. Potential conflicts include favouring one account over another in investment decisions or the exercise of investor rights; taking conflicting positions in the same security for different portfolios; or favouring an account where performance fees are awarded over an account that is charged an asset-based fee. To minimise potential conflicts and protect the interests of all MSIM clients, the Global Side-by-Side Management Policy and Procedures (the "Policy and Procedures"): (i) provide that allocation decisions are not influenced by fee arrangements or other incentives; and (ii) allocate investment opportunities in a manner that treats all clients fairly and equitably over time.

The Policies and Procedures set out specific guidelines to mitigate potential conflicts that may arise in connection with side-by-side management, including conflicts around trading practices, performance fees, security selection, investment in MSIM funds and consistent investment viewpoint (e.g., long/short).

All portfolios actively managed by the same investment team (e.g., the same portfolio manager exercising ultimate discretion over an account) must generally take the same directional viewpoint (e.g., short or overweight) in a particular security (e.g., a consistent investment viewpoint). Within the same investment team, opposite direction investment decisions are not permissible except where they fall within a consistent investment viewpoint, as delineated in the Policy and Procedures.

MSIM has established the Side-by-Side Subcommittee, which meets on a regular basis and comprises representatives from business areas and control functions, including Compliance, and has overall governance responsibility for helping to ensure adherence to the Policies and Procedures.

DIFFERENCES IN STEWARDSHIP APPROACHES ON THE SAME SECURITIES

In some cases, there may be differences in opinion and priorities in engagement approaches between investment teams across asset classes for the same security (e.g., Fixed Income vs. Equities).

For example, our Fixed Income team may be more focused on governance issues or controversies that could impact the price or liquidity of bonds in the near term, whereas Equity investors may be more focused on sustainability issues that might have longer-term implications for valuation. Accordingly, any such divergences will be appropriately escalated, considered and resolved in accordance with our policies and procedures.

MSIM investment teams work closely with each other (where relevant and where circumstances permit) with the support of the MSIM Global Stewardship team to pursue our thematic priorities.

PRIVATE MARKETS-RELATED CONFLICTS

Examples of potential conflicts that may arise in the private markets context include co-investment situations where more than one strategy pursues, is involved with, or has an existing relationship with parties in a specific transaction. Other potential conflicts could include scenarios in which investment teams invest in companies with poor sustainability practices in conflict with any sustainability preferences expressed by clients or where larger fund investors are given the opportunity to co-invest alongside MSIM funds.

These conflicts will be managed in accordance with the conflicts policies and procedures summarised above, but MSIM has put in place additional controls to deal with conflicts in the private markets context. Private investment activities need to be cleared through the Firm's Global Conflicts Office, an oversight function housed within the Firm's Legal and Compliance Division that oversees the Firm's Conflict File (a confidential database that tracks all past and potential transactions being pursued by the Firm's various business units). Furthermore, private investment transactions are brought to the Private Transaction Review Committee housed within MSIM for additional review, particularly in scenarios such as the co-investment scenario noted previously, to ensure that there is independent input and oversight in the process to promote fair outcomes for investors.

Allocation of Investment Opportunities

The Private Markets Solutions team seeks to ensure that all investment opportunities are allocated on a fair and equitable basis, consistent with each advisor's fiduciary obligations, the investment strategy of the relevant client and the governing documents of each client. The Private Transaction Review Committee, comprised of senior professionals from MSIM, the Legal and Compliance Division, and the Global Conflicts Office, reviews investment opportunities that are allocable to more than one client. The following nonexclusive factors are considered, as appropriate, in connection with allocation decisions:

- Any existing rights of first-offer provisions in favour of a client;
- Overall risk profile;
- Investment guidelines, goals or restrictions of the client;
- Available capital of the client;
- Existing allocation to similar strategies and the diversification objectives of the client;
- Tax, legal or regulatory considerations; and
- Other relevant business considerations.

PRINCIPLE 4

Promoting Well-Functioning Markets

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

Overview

Identifying and responding to market-wide and systemic risks is a priority for Morgan Stanley. As such, we have staffed appropriate governance and controls, escalation protocols, and management and remediation processes to ensure our business and stewardship activities not only meet clients' interests and requirements but help promote a well-functioning financial system. We take a globally harmonised approach across MSIM and the Firm, adopting a three-lines-of-defence model—although most risks are identified and managed at the business level (First Line), we believe that risks should be independently monitored by our Firm Risk Management and Compliance teams (Second Line) and Internal Audit (Third Line), which performs a range of assurance activities commensurate with the risk exposure across the Audit Universe, which may include reviews of key risk management processes.

Our MSIM and Firm Risk Committees serve to oversee, manage and address risks that are escalated from First and Second Lines of Defence. Our Entity Boards (please see Principle 2) provide Board-level oversight and Firm leadership with input from our business heads as the identification and management of such risks. These include, but are not limited to, investment and enterprise risk report updates, which are provided periodically to Boards. These include, but are not limited to, Investment, Enterprise and ESG risk report updates, which are provided periodically to Boards. The Investment Risk report is presented quarterly and includes a number of Key Risk and Performance Indicators with reporting thresholds. These metrics include, but are not limited to, key person risk, investment breachers, leverage, counterparty risk, liquidity risk and stress testing. The Boards are provided with RAG-rated updates each quarter, in addition to commentary on focus areas and emerging risks. The Enterprise Risk report is also presented quarterly and includes updates on emerging regulatory and external events, as well as detail on Operational Risk Incidents above Firm-established thresholds for that period. Further, on an annual basis, the Boards review and approve the Risk Appetite Statement for their entity, which documents the appetite for key risks, including operational, earnings, compliance, reputational and conduct risk, as well as other risks facing the entity, including credit, liquidity, market and model risk. Additionally, an ESG Risk report is presented quarterly and includes updates on the risk monitoring of sustainability objectives and restrictions in investment strategies under the Sustainable Finance Disclosure Regulations. The report's metrics include, but are not limited to, portfolio carbon footprint and board diversity, and it also includes findings from position screenings for business involvements, ESG controversies and global compact compliance. The Board is provided with RAG-rated updates on the ESG risk report and commentary on any emerging risks for the funds.

The types of market-wide and systemic risks we work to mitigate include, but are not limited to, macroeconomic, market, credit and currency risks—but, most importantly, with respect to sustainability—e.g., climate change, physical/transition risk, social and governance risks. This year, in response to the evolving industry trends and regulatory developments, we have also enhanced our internal ESG governance framework to minimise greenwashing and stewardship-washing risks (please see Principle 2 for more details on policy, process governance and resource uplifts to combat greenwashing and stewardship-washing). Internally amongst our employees, upholding our Firm's core values (Principle 1) is critical in addressing market-wide and systemic risks. We provide further details in the sections below.

MSIM Risk Management Overview

At MSIM, we believe that effective risk management is vital to the success of our business activities. Accordingly, we employ a risk management framework to integrate the diverse roles of our risk departments into a holistic enterprise structure and to facilitate the incorporation of market-wide and systemic risk evaluation into decision-making processes across our division. The cornerstone of our Risk Management philosophy is the pursuit of risk-adjusted returns through prudent risk-taking that protects our Firm's capital base and franchise.

We have implemented systems, controls and procedures to identify, monitor and manage risks at security, portfolio and MSIM levels. As a fiduciary of client assets, MSIM also manages client assets in accordance with clients' risk tolerances (which are defined in fund offering documents and in client investment management agreements) which are reflected in our systems and controls.

Our MSIM Risk function is led by our Chief Risk Officer, who chairs our IM Risk Committee ("IMRC"), which provides a regular forum for representatives of our different functional groups to identify and discuss key risk issues and make recommendations to senior managers on actions necessary to manage those risks. Our IMRC is appointed by our Firm's Risk Committee to assist in the oversight of our divisional risk management, including all risk types and businesses, as well as our [MSIM Risk Management Policy](#).

EMPLOYEE CONDUCT AND CONDUCT RISK

Our employees are our Firm's key resources in implementing risk management frameworks and controls. Morgan Stanley strives to adhere to the highest standards of ethical conduct. As such, our employees must uphold the Firm's commitment to ethical conduct, abiding by the letter and the spirit of applicable laws and regulations. These principles are hallmarks of Morgan Stanley's culture and reflect our pledge to Do the Right Thing and Put Clients First.

Conduct Risk is the risk arising from misconduct by Firm personnel. It includes conduct related to business activities, as well as other conduct that could harm the Firm and, in certain regions including EMEA, includes conduct where the outcome is an adverse impact on clients or markets.

Each member of staff at Morgan Stanley is responsible for addressing Conduct Risk by:

- Complying with relevant local conduct standards, including acting with integrity, due skill, care and diligence at all times and observing proper standards of market conduct;
- Refraining from any act, on or off Firm premises, that threatens the reputation of the Firm or any of its clients;
- Being alert to any potential adverse consequences that our actions or the actions of others might have for our clients, the markets or Morgan Stanley; and
- Identifying and escalating potential Conduct Risk incidents.

We believe that employee conduct, effective risk identification and management are integral parts of a robust stewardship strategy. As stewards of our clients' capital, we need to be able to hold ourselves to the highest standards, and anticipate, identify and track the risks faced by our investments (and these may be risks specific to the particular investment/asset or may represent wider market-wide/systemic risks) to ensure that they inform our engagement strategies, initiatives and dialogue.

Market-Wide and Systemic Risks

As noted above, our risk management frameworks have been designed to identify, assess, monitor and manage all significant risks involved in our business and investment activities, including market-wide and systemic risks relevant to our client portfolios and assets. This section provides an overview of how MSIM, at an organisational and investment team level, identified and responded to key market-wide and systemic risks during the reporting period.

MSIM's Global Risk & Analysis ("GRA") team performs ongoing monitoring for emerging geopolitical and financial risks in the market. These risks are identified by the market risk team at both the portfolio level and aggregate business line level, and they are assessed using measurements such as exposure analysis, beta analysis and scenario analysis. The team assesses the business's top exposures to identified risks and the implied stress profit and loss across different hypothetical market-driven scenarios. Findings from this analysis are then shared with the investment teams and management, and they are also escalated to the IMRC, which is the forum for representatives across different functional groups to discuss key risk issues and make recommendations on actions necessary to manage those risks. Additionally, GRA discusses market trading volume and liquidity with portfolio managers and traders to assess potential trading disruptions, and it performs screenings for issuers that may be impacted by sanctions, working with its partners across the firm to mitigate these risks.

A key market-wide event during the reporting period was the invasion of Ukraine by Russia and the related sanctions that were imposed on Russian securities by international regulators. In anticipation of such events, a cross-functional working group was set up to ensure that MSIM would be able to react in a timely manner to developing events and to ensure the firm's ability to comply with all applicable sanctions. This group considered risks arising from these events, including liquidity risk, risk of contamination, regulatory risk and compliance, and stayed in regular contact with external stakeholders, including clients, trading counterparties and regulators. The investment teams within MSIM worked closely with this working group to enable an open flow of information that was essential to ensure that prompt and appropriate investment actions could be taken with respect to the accounts and funds managed by MSIM.

From a trading perspective, all orders were scanned through our order and compliance management tool to avoid risk of trading in sanctioned names.

On the engagement side, our fund custodian stopped supporting meetings based on sanctions applied, in line with other custodians in the market. MSIM did not make any significant changes in our voting approach; we voted where we were eligible and able to, barring cases in which our custodian did not support meetings due to sanctions applied.

CLIMATE CHANGE – INCLUDING TRANSITION AND PHYSICAL RISKS

At MSIM, we continue to believe that climate change is a key systemic risk, and that climate transition and physical risks should be effectively incorporated into our risk management process. At a Firm level, we have conducted workshops with representatives across business lines to identify and measure future climate risks according to their business activities, as summarised in the graphic below. The workshop culminated with the development of firm-wide scenario narratives, as shown in *Figure 4.1* below:

Our MSIM GRA team conducts scenario analysis to monitor the climate risk of portfolios across asset classes. These scenarios are forward-looking and aim to measure the financial impact of hypothetical transition or physical risks. The stress testing results are monitored for changes over time and factored into portfolio construction, composition and investment decisions made by some investment teams (as appropriate) to ensure that climate risks across client portfolios are appropriately identified, tracked and managed. Additionally, our GRA team conducts its own research regarding climate change and other topical ESG risks, and develops our own proprietary scenarios. This work to create new scenarios ensures that the stress testing remains relevant and an effective tool for risk management as market conditions change.

Topical ESG risks (including climate change) are also discussed in the regular weekly meetings of our Market Risk team. Once identified, risks are measured through several different kinds of analysis. For example, exposure screening may be conducted at both the individual portfolio and aggregated business line levels. New stress tests may also be developed to measure the financial impact of hypothetical scenarios. Changes in risk levels, scenario analysis results and exposures are monitored at the portfolio and aggregate business line levels, and the trend line over time is analysed by the team and used to influence strategy, portfolio and investment-level decisions.

GRA identifies risks through its regular processes for monitoring climate metrics. The GRA team may then engage directly with portfolio managers across certain of our investment teams on potential risks and escalates them during risk committee meetings, which include members of senior management. Periodic ESG risk updates have also been provided to Board Risk Committees.

In order to better identify, respond to and mitigate climate risks, we are still developing further climate portfolio analytics—that are currently in the testing stage with select investment teams on the public markets front. These include:

- **SCENARIO ANALYSIS OF CARBON EARNINGS AT RISK** – projecting carbon price impacts across regions and sectors using various climate scenarios to estimate the impact of future possible carbon price on a company's earnings ("EBITDA");
- **SCENARIO ANALYSIS ON ENERGY TRANSITION FOR POWER GENERATION** – for portfolios which may invest in companies with power generation activities;
- Carbon footprint (as measured by carbon emissions intensity);
- Climate scenario analysis (transition risk climate scenarios including Carbon Tax and U.S. Green Plan); and
- Position screening for business involvements and controversies.

Recognising that climate change is an economic reality and a growing risk that businesses and investors are learning to address, we seek constantly to develop better analyses on climate change to provide our clients and

FIGURE 4.1

Phases of Climate Scenario Development and Testing

1. FORCES SHAPING THE FUTURE	2. DEFINING CRITICAL UNCERTAINTIES	3. SCENARIO MATRIX	4. TESTING THE BUSINESS STRATEGY
Identify relevant: • Megatrends • Future Factors and Trends • Signals of Change	Uses research from Phase 1 to workshop *critical uncertainties* to the business, including at least one that is strongly climate focused	Chart the critical uncertainties on a set of *scenario axes* and develop accompanying *scenario descriptions*. Integrate climate data	Test the business/strategy against the scenarios narratives in a workshop

other stakeholders with more information to enable better investment decision-making and increase awareness of the impact of climate change as a systemic risk.

MSIM/Morgan Stanley Firm-Wide Climate Strategy

MSIM also works in collaboration with the GSF division, the Morgan Stanley Institute for Sustainable Investing and our Environmental Social & Risk Management ("ESRM") team to help strategically inform and engage the appropriate internal partners across the Firm on emerging climate change-related risks, where relevant to the Firm's activities.

Morgan Stanley adopts a Four-Pillar Climate Strategy that consists of: (1) Transition to a Low-Carbon Economy; (2) Climate Risk; (3) Operational Resilience; and (4) Transparency. This is outlined in our [Morgan Stanley 2021 Climate Report], where we detail a multidisciplinary approach in implementing our Climate Strategy, Governance, Risk Management and Metrics and Targets.

Identifying, assessing and managing climate risk is an evolving science and a moving target. The financial industry is investing significant resources in testing methodologies for how to best address climate risks, yet accurate data and relevant tools remain inadequate in the near term. Appropriate corporate disclosure, supported by common definitions and standards, has an important role to play in improving the data necessary for the industry to appropriately quantify and manage climate risk. Morgan Stanley was an early supporter of the TCFD disclosure framework, which distinguishes two main types of climate risk—transition risk and physical risk—and encourages corporations to consider and report their climate exposure this way.

TRANSITION RISKS

We select transition risk scenarios based on the Firm's risk profile, emerging changes in policies (such as carbon pricing) and the economic impacts of global warming. The scenarios are conducted for time horizons ranging from two to 30 years, and consider exposure concentrations by region, sector or industry. The Firm's Risk Analytics Group leverages existing economic scenario forecast models used for stress-testing exercises as a starting point to develop climate scenario forecasts. This approach has

FIGURE 4.2
Morgan Stanley Four-Pillar Climate Strategy

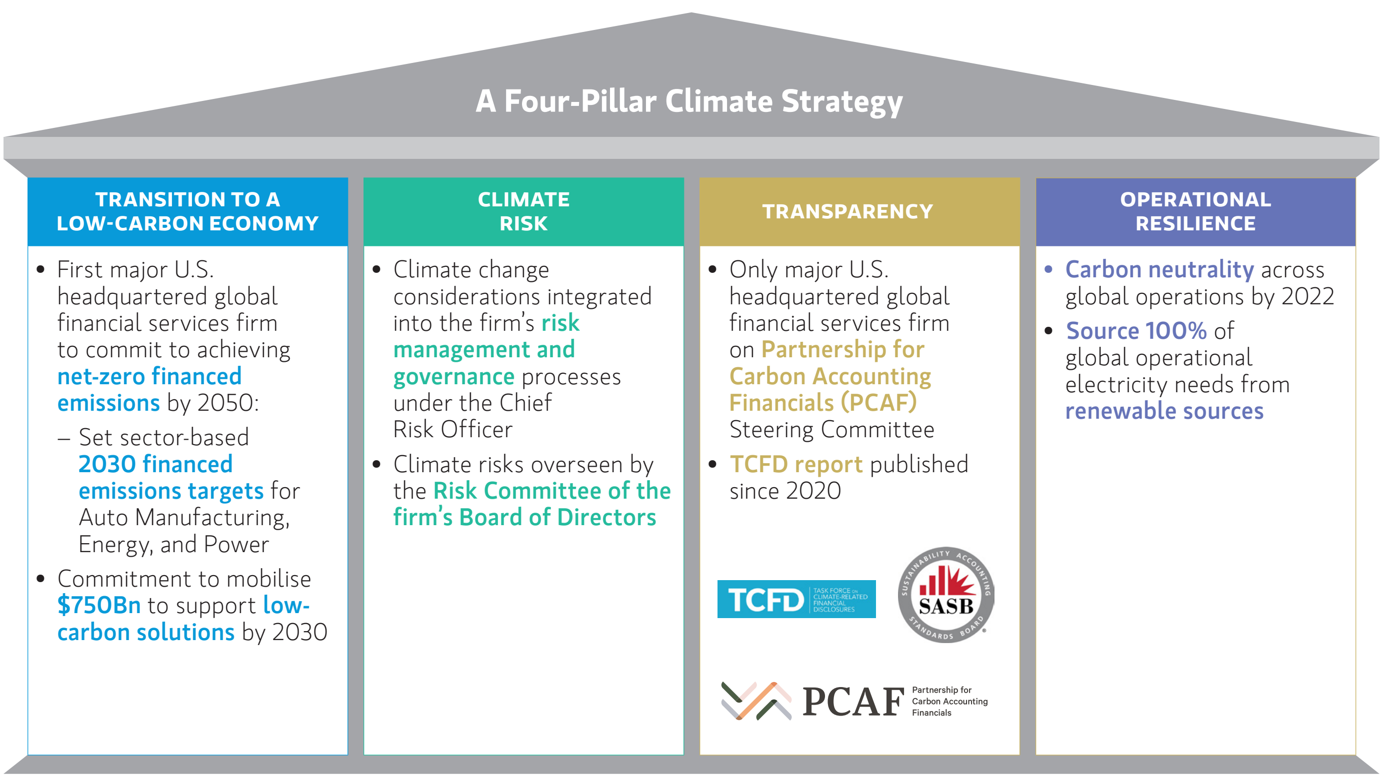
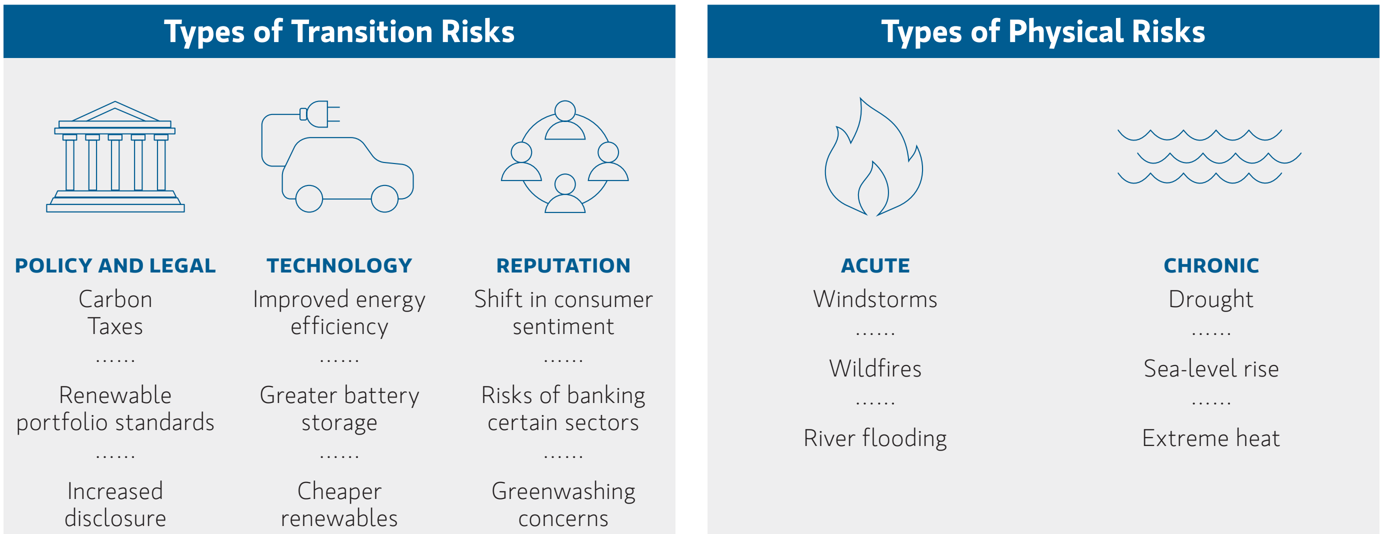


FIGURE 4.3

Types of Transition and Physical Risks



advantages, including an ability to model statistical relationships between variables and an existing global structure that captures key macroeconomic and financial market variables across regions. Climate-specific variables are then added to the forecast, with the latest models better able to meet the particular requirements of climate scenario analysis. Firm Risk Management ("FRM") has enhanced climate risk transition scenario capabilities over the past two years, in consultation with GSF and our Credit Risk and Market Risk teams.

PHYSICAL RISKS

FRM selects physical risk scenarios based on a combination of the latest science and risk identification, identifying potential near-term events and matching them to portfolio concentrations. We identify and map a range of physical risks, focusing on potential extreme events, such as storms, rather than long-term developments, such as sea level rise. In our first physical stress-testing forecast, we focused on risks that might generate the largest credible loss for the Firm from an extreme short-term weather event. This year, we are expanding our range of physical scenarios.

DEVELOPING GLOBAL REGULATION

Regulatory authorities are using the TCFD recommendations to issue guidelines for relevant sectors. Globally, financial regulators are exploring potential mandatory disclosures of Scopes 1, 2 and 3 greenhouse gas emissions, which could include financed emissions reporting for the financial sector. In 2021, our Firm engaged with U.S. financial regulators to explain the PCAF initiative and methodology, and its potential supporting role in helping financial institutions measure, track and report emissions from financing and lending. Our leaders and experts will continue to engage with policymakers and other key stakeholders globally, as opportunities arise, to support the development of effective public policies that accelerate the transition to a low-carbon economy.

From a U.K. perspective, regulatory authorities are using TCFD recommendations to issue guidelines for relevant sectors, and beginning 1 January 2022, the U.K. FCA rules require TCFD reporting for asset managers and asset owners with first public disclosures to be made by 30 June 2023. In line with the Firm's commitment to climate change, MSIM is in the process of preparing to publish its inaugural TCFD report by the regulatory effective date next year. In doing so, we worked with an external consultant this year to conduct a gap analysis to assess our business and disclosure readiness with regard to the TCFD's four pillars: Governance, Strategy, Risk Management and Metrics & Targets. Our consultant reviewed relevant documentation and conducted interviews with relevant MSIM stakeholders to assess our existing business practice against the 33 sector-neutral TCFD recommendations and nine asset manager-specific guidance points. A TCFD Readiness Report was ultimately produced, outlining areas and further steps that could be taken to strengthen our framework to support a high-quality, initial TCFD disclosure in 2023. Though per Firm Policy, we do not disclose results of such assessments, the gap analysis did not highlight any significant deficiencies. Work has begun to strengthen and formalise governance processes (Principle 2) and set timescales to define, collect and measure required data to meet the 2023 regulatory effective date.

TOWARD CARBON NEUTRALITY AND CLIMATE-RESILIENT OPERATIONS

In 2017, the Firm set an ambitious target to achieve carbon neutrality across our global operations by 2022, and we are well on our way to achieving this goal. Our approach combines sourcing 100% of global operational electricity needs from renewable sources and offsetting any remaining GHG emissions.

Key strategies to reduce emissions include increasing the efficiency of our infrastructure and using renewable electricity on-site. Through our capital improvement planning, we enhance the efficiency of our heating, air-conditioning and ventilation systems ("HVAC"); strive to reduce the water intensity of our HVAC; focus on plug load management to reduce parasitic losses; and leverage daylighting to improve the employee workplace while reducing lighting loads. Where feasible, we build on-site renewable energy systems and procure certified green energy for local electricity loads.

SENIOR MANAGEMENT SPONSORSHIP

The Morgan Stanley Institute for Sustainable Investing plays a unique role in our Firm and sector. For nearly a decade, it has worked to accelerate the adoption of sustainable investing and finance by fostering innovation, empowering investors through actionable analysis, and developing the next generation of leaders in the field. It also drives strategic sustainability initiatives across Morgan Stanley. Founded in 2013 by the Firm's CEO and Chairman, the Institute is chaired by the Firm's Vice Chairman and Head of External Affairs and is guided by an advisory board of prominent leaders from business, academia and leading nongovernmental organisations.

Through the Institute, we also regularly engage with industry and sustainability issue experts in an effort to encourage innovative approaches to solving sustainability challenges, including climate change. We consider the Institute's findings in our own practices. An example of specific engagement on this point is that both MSIM and Calvert are members of the Sustainability Account Standards Board ("SASB") Investor Advisory Group (Calvert being a founding signatory), where we frequently engage with fellow investors to promote SASB reporting standards.

OUR COVID-19 RESPONSE

Morgan Stanley continues to closely monitor developments related to COVID-19, including the emerging variants, informed by public health authorities, including, but not limited to, the U.S. Centers for Disease Control and Prevention ("CDC") and the World Health Organization ("WHO"), and guidance from national and local governments. Our Firm continues to focus on the health and safety of all employees, contingent workers and their families. As such, the return-to-office plan is constantly evolving and adjusting as appropriate, in line with local and national government and public health authority guidance. We continue to remain vigilant, monitoring the environment for any further developments.

GREENWASHING AND STEWARDSHIP-WASHING RISKS

Greenwashing is a key concern and priority to address for regulators, governments and the industry. Ultimately, it involves strategic, legal, compliance, reputational and regulatory risks—more far-reaching at a systemic level. The erosion of client trust and brand reputation—not to mention exaggerated or lack of environmental/social benefits of product claims—negates industry efforts towards greater sustainability. In the same vein, stewardship-washing is also cause for concern. Not all engagements are created equal, and a higher volume of engagement does not necessarily mean better engagement or that it will lead to more impactful outcomes. There is still a lack of industry consensus on what constitutes meaningful engagement, and based on what standards, given the different types of investment products and strategies used.

We highlighted in Principle 2 detailed enhancements made to our sustainability oversight and governance process, adding expert resources and formalising review and approval pathways for our products and external commitments. Our goal is to ensure transparent disclosure of what we do—commitments, activities and achievements, in line with our objectives, and so we can demonstrate progress and outcomes in a fair and objective manner, understandable by our clients and external stakeholders.

Our commitment to minimising greenwashing and stewardship-washing risks is an ongoing one; we seek to ensure our employees are well-equipped in not only "dos and don'ts", but broader industry and regulatory developments and implications for MSIM. We are preparing to launch greenwashing training for our MSIM employees during Autumn 2023.

Investment Team Approaches

We have set out below examples of the approaches adopted by some of our investment teams in identifying and responding to market-wide and systemic risks.

INTERNATIONAL EQUITY

The International Equity team specifically focuses on factors (ESG or otherwise) that may materially influence the sustainability and resilience of future returns. This includes understanding the risks that may threaten returns, as well as the opportunities that may exist to improve them. Thematic research on, for example, carbon, the circular economy, or diversity and inclusion contributes to the team's understanding of thematic risks.

The team captures ESG risks and opportunities using its proprietary screening framework, the Material Risk Indicator ("MRI"), a tool designed to capture the portfolio managers' ESG company assessments in a consistent and comparable way over time. The MRI helps to:

- Identify material ESG risks and opportunities at the company level;
- Reflect these risks and opportunities in valuation and portfolio construction, if appropriate; and
- Identify priority areas for future company engagement.

The fundamental question that the portfolio managers must then consider is whether the factors in question can significantly impair or enhance a company's long-term returns on operating capital employed (which is the primary quality metric used by the team). The nature of ESG factors on market-wide and systemic risks can make it challenging to quantify their impact. As such, the team employs a range of methods to reflect the outcome of its ESG analysis in the portfolio.

If the risks assessed by the MRI are too high, the team may choose not to invest in the candidate company. Where feasible, the team runs scenario analyses; for example, forecasting the impact of an ESG factor on the company's growth rate, profits or capex and the resulting change in fair value—for instance, modelling the impact on profits and valuation of consumer staples companies switching to more sustainable packaging. The team may:

- Adjust the weighted average cost of capital ("WACC") to reflect the higher or lower risk; and/or
- Reflect potential risks by adjusting the position size, in addition to any model or WACC changes.

A high MRI grade does not automatically suggest a large position, and a relatively low MRI grade does not automatically trigger a reduction or divestment of a holding. The assessment is an important component of the research process, not the sole driver of investment decisions.

Climate Change

In response to climate change, the International Equity team conducted a detailed carbon transition engagement programme, with the aim of assessing the climate risks and opportunities for each holding in the team's global portfolios, gain understanding of the companies' climate profiles, and encourage improvement. The team's purpose when engaging was to ascertain its portfolios' resilience to a low-carbon future. The team engaged with 95% of all the companies it holds across its global portfolios. As an example, as part of this programme, the team urged one of their holdings, a fintech services company, to set formal carbon reduction targets and improve ESG disclosure. Although it is a carbon-light company, the team believes that every company in their global portfolios should seek to contribute to decarbonisation. It also highlighted the reputational and commercial risks of not having a clear climate action plan. The team was encouraged by the company subsequently announcing targets of 100% renewable electricity and Scopes 1 and 2 emissions neutrality by 2025, and a commitment to set science-based Scope 3 targets. In a follow-up engagement, the team explored how these targets will be achieved. The team will continue to engage with the company to monitor and encourage its progress.

Positive outcomes followed. Six out of seven companies the team own that initially did not have targets are preparing to set them or have them in place, and nine companies advanced their existing target ambitions to be carbon neutral or net zero. Broadly, at the outset of 2021, an average 54% of the team's holdings across its global strategies had set net-zero targets or better. By the end of the year, this average had risen to 63%. Conversations around climate change continued in 2022, as the team has followed up on the progress made by companies it engaged with in 2021, and begun engagements on decarbonisation with new holdings.

COUNTERPOINT GLOBAL

Risk Defined as Potential for Permanent Loss of Capital

For Counterpoint Global, as an active fundamental investor, the biggest risks are unexpected macro shocks, or market rotation in and out of sectors, when fundamentals are, in the short term, less relevant. For these reasons, the team defines risk as the potential for permanent loss of capital.

Risk Assessment & Management Approach

In an absolute sense, Counterpoint Global seeks to own big ideas that win over time. The team's investment horizon is three to five years. Counterpoint Global attempts to avoid permanent loss, which the team defines as selling a position at a loss, by buying high-quality businesses. The team considers the risks inherent in each position by evaluating what could go wrong and by evaluating company developments in the context of the investment thesis. For example, this could include assessment for potential loss in value of an investment due to increasing competition, mismanagement of the business or financial insolvency. The team manages these potential risks through the rigorous analysis of business fundamentals and the evaluation of an investment's risk/reward based on free cash flow yield, optionality and end game.

Counterpoint Global maintains objectivity by referring to the investment thesis, which clearly states why the team owns a stock, and when circumstances occur that violate the thesis, it sells, and does not modify the thesis. The team manages portfolios that are well diversified as a way to help control risk at the portfolio level.

Resources Managing Risk

The investment team is responsible for risk across their strategies, with ultimate responsibility lying with the team's lead investor and Head of Counterpoint Global. In this task, the team is supported by MSIM's GRA team, which uses quantitative and qualitative tools to analyse investment risk by product area. The GRA team produces in-depth reports for each investment programme on a monthly basis, concentrating on tracking error, R-squared, Beta, Information Ratio, and absolute and relative exposures versus the benchmark. The team uses a range of vendor-based and proprietary systems to conduct this analysis. Reporting for each investment strategy is available to the lead investors and portfolio specialists, as well as to divisional management and the Firm-wide risk committee.

While risk analysis is provided monthly, they have the capability to run intra-month analysis. The investment team does not manage to specific limits, and the GRA team cannot overrule investment decisions made by the team.

GLOBAL OPPORTUNITY

For Global Opportunity, risk management is an integral part of the team's investment process. In an absolute sense, Global Opportunity seeks to own big ideas that win, over time. Their investment time horizon is five years. The investment team attempts to avoid permanent loss, which it defines as selling a position at a loss, by buying high-quality businesses. The team considers the risks inherent in each position by asking what could go wrong and by evaluating company developments in the context of the investment thesis. The investment team maintains its objectivity by referring to the investment thesis, which clearly states why they own a stock, and when circumstances occur that violate the thesis, it sells, and does not modify the thesis. Global Opportunity manages portfolios that are well diversified as a way to control risk at the portfolio level.

The investment team believes that idiosyncratic risk can be reduced by addressing what matters at the company level:

- Valuation risk is mitigated by not paying a price that exceeds the team's estimate of value;
- Sustainability risk is mitigated by analysing the threat of disruption, financial strength and ESG externalities; and
- Fundamentals risk is mitigated by analysing the threat of deteriorating competitive advantage and growth opportunities.

Portfolio risks are mitigated by reducing correlated factor exposures with the support of monthly reports from Portfolio Attribution and Risk teams. Market and principal risks are measured at the portfolio level by monitoring portfolio volatility attributed to movements in the market and determining the impact of a realised loss on the total portfolio. The investment team manages this risk through the diversification of investments.

Global Opportunity is responsible for risk within the Strategy, with ultimate responsibility lying with the Head of Global Opportunity.

In this task, the team is supported by the MSIM's GRA team, which uses quantitative and qualitative tools to analyse investment risk by product area. The GRA team produces in-depth reports for each investment programme on a monthly basis, concentrating on tracking error, R-squared, Beta, Information Ratio, and absolute and relative exposures versus the benchmark. The team uses a range of vendor-based and proprietary systems to conduct this analysis. Reporting for each investment strategy is available to the portfolio managers and portfolio specialists, as well as to divisional management and the Firm-wide risk committee. While risk analysis is provided monthly, however, it has the capability to run intra-month analysis.

EMERGING MARKETS EQUITY

For Emerging Markets Equity, ESG materiality is considered across the investment team, in investments and engagements, which are an important part of their research process.

Macroeconomic Risks
EME's dedicated macro-thematic team conducts original research on such issues as economic growth, credit penetration levels and currency valuations. This team works in partnership with EME's Portfolio Managers and the EM sustainability investors team to consider the dynamics driving equity markets, including, more recently, global sustainability topics such as greenflation, the energy market transition, electric vehicles, copper, lithium and decarbonisation.

At the country level, EME seeks to understand the environmental, social and governance drivers that may affect a country's growth pathway, pose policy risks or otherwise impact company earnings. Some of the metrics they follow to inform their comprehensive view of the country include decarbonisation pathways, energy sources, labour force participation and diversity rates, unemployment, income inequality and human rights.

Environmental Risks
Climate-related risks are an important part of EME's research process. They analyse the GHG emissions of their portfolio companies, and seek to understand the implications for corporate strategy, competitive positioning, contingent risk and potentially incremental market opportunities. They engage with companies on their GHG disclosures (including Scope 3), and if there is a strategy for decarbonisation, how they plan to achieve it, and are their targets reasonable and achievable. To this end, they encourage companies to set more short- to mid-term quantifiable targets to effectively measure and evaluate their progress towards their long-term goals. When EME engages with companies, they seek disclosure on these targets so it can compare them against the Transition Pathways Initiative ("TPI") carbon intensity below 2°C scenario.

For products that strive to align with the objectives of the Paris Agreement, the team is focused on a decarbonisation pathway at the aggregate portfolio level. This includes creating a decarbonisation tracker that allows them to track portfolio-level and company weighted average carbon intensity ("WACI") numbers, utilising both company-reported and MSCI greenhouse gas emissions data. The tracker also uses company emission reduction targets to project portfolio WACI over the next 10 years and includes a 10-year Paris-aligned benchmark for comparison. The team calculates WACI for Scopes 1 and 2, as well as Scopes 1, 2 and 3 emissions due to the increased focus on and scrutiny of Scope 3 emissions, although Scope 3 calculation is not universally reported or estimated, making Scope 3 difficult to assess.

Additionally, EME believes an important part of the energy transition is investing in those companies that need to fundamentally change how they operate in order to lower emissions or that will be global enablers of a sustainable energy transition. Key to this is investing with companies that are willing to engage with investors and change. The team engages with the top emitters in their portfolios, evaluating each decarbonisation plan using the TPI and comparing against best practices per industry. It also tracks the percentage of the portfolios with climate targets, including Science-Based Targets, net-zero and climate pledges, which helps them understand how the portfolio may change over time.

Social Risks
Accidents and injuries in the workplace are principal risks that EME pays close attention to, particularly in heavy industries within emerging markets. Not only are accidents and injuries detrimental to victims and their families, but they also speak to the broader culture of a company generally, and can have consequences, including loss of labour, reputational damage, tighter regulations and fines, and loss of social license to operate.

EME incorporates human rights through their engagements on labour conditions and health and safety. Though it is very challenging to get data and disclosure on human rights, as violations of human rights typically occur deep in the supply chain more than in the directly listed entities in the team's universe, EME has created a framework to analyse potential supply chain risks using well-known think tanks, such as Know the Chain.[16] This framework is used in the team's company analysis and engagements where they may suspect human rights issues. EME is also particularly concerned in situations where government policy may be enacted in response to perceived human rights issues and how this may affect market opportunity for these companies and/or cost of capital. For now, social factors remain difficult to materially quantify, and therefore remain an engagement topic for the team.

Governance Risks
A key criterion of EME's philosophy in investing is strong governance, both at management and the board levels. As long-term investors, it is imperative that they understand the management's strategic goals and key targets.

[16] 'Know the Chain' is a resource for companies and investors to address forced labour in global supply chains. Their benchmarks and practical resources help companies operate more transparently and responsibly while also informing investor decisions.

As responsible managers, the team actively examines and vote their proxies. Voting represents the direct participation of shareholders in the overall governance of a corporation and offers shareholders a voice on important issues, such as director independence and executive compensation.

Cybersecurity

While cybersecurity tends to be a more material issue in select sectors, such as internet services and communications companies, EME sees the need for robust cybersecurity practices across all sectors. Any company without proper data protection measures is at a higher risk of experiencing a data breach that can materially impact the business and its long-term reputation. Throughout the team's engagements, it will continue to address this issue to ensure that portfolio companies have proper data privacy infrastructure and protocols in place.

GLOBAL FIXED INCOME

Our Global Fixed Income team's objective is to construct durable portfolios so that the team is not a forced seller at distressed prices during extremely illiquid periods in the market brought on by systemic risk events. Systemic risk is extremely difficult to hedge and anticipate as it impacts the very structure of the market. Therefore, the structure of a portfolio is a first line of defence adopted by the team—taking account of factors such as diversification, position sizing, minimising correlation risk and liquidity is important.

Our Global Fixed Income team recognises that environmental and social risks, such as climate change, global pandemics and geopolitical conflicts, can represent systemic risks, and takes them into consideration when assessing sectors and issuers' level of exposure, risk management and resilience, and whether those are reflected in the price of their bonds. An example is the energy crisis that stemmed from the Russia-Ukraine conflict, which has had major repercussions on the global and especially European economy. Whilst the crisis represented a short-term opportunity for mining companies, energy and utility companies to leverage high fossil fuel prices, our Fixed Income investment team continued to engage with these high-risk sectors to ensure they would not delay their coal phase-out and decarbonisation investment plans, and maintained a positive outlook on those companies with a stronger focus on renewables, hydrogen and carbon-capture development strategies. The team also conducted targeted meetings with European banks, in particular, those with exposure to Russia and/or Ukraine, and those with significant fossil fuel lending portfolios, to assess the extent to which the energy crisis may impact their netzero, financed emissions commitments.

Governance risk, particularly in the form of lack of management transparency associated with family ownership, board entrenchment and overpaid executives, has been a central focus in the investment team's engagement with high-yield companies throughout the past twelve months.

Overall, when market-wide and systemic risks appear, they are discussed by the Asset Allocation team, which is led by the CIO of MSIM's Global Fixed Income team and is comprised of the heads of each Portfolio Management team. While the Asset Allocation team is responsible for identifying and assessing the probability of systemic risks, portfolio managers are responsible for determining implementable trades, in line with the portfolio investment opportunity set and client guidelines. Additionally, systemic risk events are highlighted by the independent Risk Management team via stress tests and scenario analysis.

Morgan Stanley is also a member of the International Capital Market Association ("ICMA"), and a supporter of their Green and Social Bond Principles ("GBP/SBP"). MSIM looks at ICMA's principles and guidelines as best practice frameworks in the sustainable bond market, and some members of the Fixed Income Sustainable Investing team take part in selected meetings of the GBP/SBP working groups, such as the Impact Reporting working group, alongside other investors and market participants. The Global Fixed Income team uses this forum, as well as their bilateral dialogues with issuers and structuring advisors of sustainable bonds, to proactively share feedback in order to increase the transparency and quality of these instruments in the market, and to provide the responsible investor perspective in the ongoing development and evolution of these industry standards.

In their proprietary Sustainable Bond Evaluation framework, the Global Fixed Income team rewards/penalises sustainable bond issuers for alignment/misalignment with the GBP/SBP. For example, where they see a tendency amongst some U.S. companies in the real estate or utility sectors to issue green bonds that do not align with the disclosure and external verification recommendations of the GBP/SBP, the team usually assigns lower scores to such bonds, and proactively shares feedback with the issuers on expectations for them to provide greater transparency.

GLOBAL BALANCED RISK CONTROL

From an asset allocation perspective, the team's investment process focuses on trying to achieve a given volatility target, plus the optimal return for the risk taken. Central to the team's process is the aim of identifying potential systematic risk events, the analysis of which will aim to help the team understand the volatility environment in the near-medium term. This in turn will lead the team to adjust the broad asset mix of global equities, global fixed income and cash, with the aim of maintaining the overall portfolio's realised volatility, in line with its target. Examples of previous systemic and market-wide events through which the team has previously guided its portfolios include the eurozone crisis, the Greek debt crisis, commodity price extremes, plummeting Chinese equities in 2015, the U.K.'s 2016 "Brexit" referendum, multiple political and geopolitical events, U.S.-China trade tensions, the COVID-19 pandemic, and, most recently, the Russian invasion of Ukraine, soaring inflation and tightening monetary policy.

Climate Change

GBaR also categorises climate change as a potential systemic risk, which could threaten the stability of financial markets. The way the team looks to respond to climate risk is by tilting its portfolios towards companies that are more resilient to climate change whilst tilting away from carbon-intensive industries. The team also seeks to increase investments in solution-type companies that stand to benefit from opportunities arising from climate transition. Last but not least, the team actively engages with companies in hard-to-abate sectors to make sure they take into account the risks associated with climate transition and set up ambitious decarbonisation measures.

Russian Invasion of Ukraine

February 2022 was marked by the escalating tensions and a full-scale Russian invasion of Ukraine. Many asset classes were already on a downward trend since the beginning of 2022, given inflation pressures, concerns over rate hikes and deterioration in investor sentiment. While GBaR entered 2022 already cautiously positioned, their view was that the military conflict in the Ukraine was unlikely to end quickly, hence volatility was expected to persist. In fact, the team felt it prudent to further reduce exposure to risk assets. GBaR monitored portfolio holdings commitments to divest Russian operations closely. They also kept a list of companies and performed qualitative analysis on any laggards.

Currency Risks

Given the GBaR team's multi-asset investment focus, currency risk is an ongoing market-wide risk that the team actively monitors and manages based on its internal analyses and objective indicators. This is because the team generally invests in the native currency of each asset it holds and generally manages its funds with unhedged currency exposures unless it has a specific currency view. The goal is to have asset returns, not currency moves, as the primary driver of performance.

PRIVATE CREDIT & EQUITY

PC&E as an asset class has always focused on identification and consideration of material risks in any category prior to making an investment and during the holding period, given the long-term nature of its strategies. Systemic risks, such as climate change, may precipitate an increased focus in a particular area (e.g., emissions) and become an important factor considered during the investment process.

With regard to company engagement as it relates to systemic risks, the control strategies under PC&E have the ability to influence strategic direction and major company decisions through board positions and, when appropriate, may use that influence to address one of MSIM's four engagement priority areas (Principle 9): (1) Decarbonisation & Climate Risk; (2) Circular Economy & Waste Reduction; (3) Diverse & Inclusive Business; and (4) Decent Work & Resilient Jobs. For example, under the ownership of Morgan Stanley Energy Partners ("MSEP"), a strategy that targets control investments in the energy sector, a resource management company acquired the technology to offer full-cycle water management solutions, which resulted in the avoidance of approximately 275 million barrels per year of wastewater disposal.

In order to address climate risk, PC&E is exploring several different approaches to understand the carbon footprint of its portfolio across the platform. For example, Morgan Stanley Capital Partners ("MSCP"), one of the strategies under PC&E, has engaged an external vendor to conduct emissions calculations for all the portfolio companies in their most recent vintage funds. For PC&E strategies where portfolio companies do not, or cannot, calculate emissions themselves or partner with a vendor to do so, a proxy approach has been developed based on sectoral emission estimates of public market companies to approximate carbon emissions across all strategies. This proxy approach is intended to help teams identify potential areas of climate risk and opportunity in advance of portfolio companies calculating their own emissions and developing comprehensive climate strategies. They are directional indicators and can serve as a basis to encourage and support portfolio companies towards a path of decarbonisation.

Within PC&E, in our last report, we detailed the Private Markets Solutions team's commitment to catalysing private sector capital to address some of the most critical systemic risks faced by the planet and people in need—through the launch of its Climate Impact Solutions Fund, where every dollar invested will seek to have a concrete climate impact measurement, ranging from tonnes of CO_2e emissions offset and litres of water saved, to reduction in air pollution levels, in addition to generating compelling private markets returns. The Climate Impact Solutions Fund was launched in a first-of-its-kind collaboration with the U.S. Congregations of Dominican Sisters to find investment solutions that focus on climate change and aid marginalised communities that are disproportionately impacted by global warming.

Continuing its efforts this year, the Private Market Solutions team launched a new climate impact-focused product that seeks to catalyse the avoidance of 1 gigaton of CO_2e emissions from the earth's atmosphere while generating attractive financial returns for investors by targeting companies at a growth inflexion point. Underscoring their conviction in the strategy, the team has designed a carried interest compensation structure tied to achieving both the substantial climate impact goal and generating robust private equity returns (thereby contributing to mitigating systemic risks).

Additionally, last year, PC&E partnered with the Multicultural Innovation Lab to launch the Next Level Fund, an impact-focused strategy with the objective to generate long-term capital appreciation generally through privately negotiated venture capital investments in primarily early-stage technology and technology-enabled companies with female or diverse members of the founding team. In addition to a financial investment, portfolio companies benefit from access to select partners, including Microsoft, Hearst and Walmart, which, together with Morgan Stanley, provide strategic assistance and operational value in order to improve economic outcomes and accelerate business results.

GLOBAL LISTED REAL ASSETS

The Global Listed Real Assets team believes ESG factors and a company's approach to sustainability will significantly influence its future risk and total return prospects. Given this view, the team believes it is imperative to focus on analysing sustainability factors and integrating these risks and opportunities into an assessment of value.

GLOBAL LISTED REAL ESTATE: The Global Listed Real Estate team's investment philosophy and portfolio construction process is focused on three distinct pillars: relative valuation, risk integration and high-conviction position sizing.

1. **Appreciation of relative valuation:** Appreciation of relative valuation: Proprietary valuation tool ranks each security in the investment universe on both net asset value and earnings multiple standardized for future growth. The importance of each metric varies by property sector in the final determination of relative value rank.
2. **Integration of risk analysis:** Assessment of common factor exposure is important in portfolio construction, and we are looking to optimise risk contribution from idiosyncratic factors as opposed to macro components. The team is focused on alpha contribution versus beta to limit downside and maximise upside capture.
3. **High-conviction position sizing:** Each security in the portfolio should have relative value support and a fully vetted investment thesis/identification of critical factors; capital is precious and each security is expected to meaningfully contribute in a prudent risk adjusted manner; focus on active share is important for portfolio construction.

The investment philosophy of the Strategy incorporates equity multiples and cash flow growth estimates, in addition to a real estate net asset value approach. In addition, risk analysis is an integral part of the investment process, including the assessment of common factor exposure, as the team looks to optimise risk contribution from idiosyncratic factors as opposed to macro components. The team is focused on alpha contribution versus beta to limit downside and maximise upside capture. Importantly, the objective of the investment philosophy is to outperform, irrespective of the underlying market environment, by having a more robust definition of value and a strict adherence to risk integration into the portfolio construction process to minimise common factor and macro exposures.

ESG Risks and Opportunities

We believe climate change, ESG factors and a real estate company's approach to sustainability are important factors to consider for the real estate sector, which will significantly influence a company's potential future risk and total return prospects. Existing buildings face chronic and acute physical risks, including intensifying hurricanes, floods and wildfires, as well as economic, social and regulatory changes necessary for decarbonisation. To limit the global temperature increase to 1.5°C in this century as required by the Paris Agreement, it has been estimated that real estate's direct carbon emissions will need to be cut in half by 2030, compared to 2020 levels, and reach net zero by 2050.

Publicly traded real estate companies hold a significant share of the building stock globally. As such, they are in a unique position to play an important role in achieving global sustainability targets. As public market investors, understanding how companies can influence and achieve net-zero targets is important, as is assessing the financial implications and, importantly, the capital expenditures required to reach such targets.

GLOBAL LISTED INFRASTRUCTURE: The Global Listed Infrastructure team leverages third-party ESG research, including MSCI ESG data and Sustainalytics ESG Reports. Each industry faces a variety of ESG challenges and opportunities. As part of the team's fundamental analysis that seeks to understand the material challenges facing each company, they may reference these research tools to help identify controversies or further assess the relevant ESG concerns that could undermine the long-term sustainability of a company's returns. The team may then, if relevant, discuss them with a company's management.

The team's approach can be summarised as follows:

1. Regular review of ESG scoring (based on MSCI ESG, Sustainalytics and GRESB reports) in conjunction with the MSIM Global Stewardship team;
2. Identification of areas of portfolio company ESG weaknesses, including analysis of reputational risks, potential litigation and other exposures; and
3. Engagement with a company's Corporate Sustainability Officer, or equivalent, as part of our standard periodic due diligence or a separate, standalone meeting;
   - Generally speaking, the team looks to highlight potential areas of risk and encourage companies to improve their ESG scores
   - Also, note that, given infrastructure's role as a provider of essential services, the fact that the companies have highly regulated operations, and the prominence they have amongst consumers, most management teams put a great emphasis on the environmental and social aspects of operations—where companies tend to be more at risk on the governance side.

PRIVATE INFRASTRUCTURE

Morgan Stanley Infrastructure Partners

MSIP seeks to minimise the potential impact of financial and market risks on investment returns through a proactive currency and interest rate hedging programme. MSIP believes that the benefits of mitigating these potential risks favourably outweigh the cost of executing a hedging programme afforded by MSIM's scale in the relevant currency and interest rate markets. MSIP works with our MSIM Private Funds Hedging team whose sole focus is to provide MSIM Private Funds, such as those managed by MSIP, with hedging strategy and execution support.

MSIP's private funds execute fund-level hedges with third parties that are subject to MSIM's Counterparty Risk Policy (in accordance with the Volcker Rule, no fund-level hedging transactions are executed with Morgan Stanley).

Interest rate risk is an ongoing market-wide risk that the team actively monitors and manages. Given volatility in underlying interest rates, MSIP's strategy is to typically hedge 80% to100% of underlying base interest rates for portfolio company bank term loans or other fully funded floating interest rate exposure.

CALVERT RESEARCH AND MANAGEMENT

Climate Change

Calvert has long recognised the significance of identifying the risks that industries or sectors face and has then sought information on how an issuer addresses such risks. Calvert believes carbon and other greenhouse gases are currently largely externalities to the cost of doing business, and that the markets are at the initial stage of pricing those externalities. The price ultimately must reflect the value society places on a stable environment and climate versus a more volatile world generally more hostile to the human species over a particular time period. In that context, to price such future scenarios and direct capital to better outcomes, and to protect investment portfolios from downside risk from climate change, investors must have accurate information disclosure on climate change.

The team also believes climate change poses a systemic risk to markets, the economy and society, and intersects with a wide array of ESG issues. While it may not be possible to price these many interconnected issues, Calvert upholds the responsibility of companies to be forthcoming with investors and other stakeholders on how these issues are being met and addressed. As such, the team believes it is essential to incorporate such information as part of its financial materiality approach as climate risk may have a strong financial or strategic impact on its business.

Calvert has multiple internal experts that address climate change issues across its ESG research, engagement and applied solutions departments. This allows the team to focus on and consider climate risks across the business and in their portfolios as they seek to mitigate climate and other ESG risks across industries. Calvert believes substantive impacts would be those that would significantly impact a business or cause the firm to change its internal approach to manage such a risk. The team believes its financial materiality approach, in conjunction with consideration of climate-risk issues, has allowed them to address and manage such risks effectively.

The process for climate change risk and opportunities starts with Calvert's proprietary research process focusing on identifying the financially material ESG risks to which issuers are exposed, and evaluating management teams' ability to navigate those risks. As part of this process, Calvert ESG analysts develop a research thesis on each industry. Through this thesis work, Calvert analysts develop a deep understanding of the potential environmental impacts, including climate change, of an industry.

Calvert identifies potential operational risks, regulatory risks and reputational risks tied to the various issues, such as the environment, and the impact of these risks or opportunities influence a company's revenues, expenses and cost of capital. By incorporating all this into the team's thesis work, users can then weigh the climate change and environmental risk alongside other risks associated with each industry.

Calvert's analysts identify how best to evaluate each company's management on key issues, including climate change. Each Calvert analyst ultimately recommends companies that are taking appropriate steps to manage climate change and other risks for inclusion in portfolios. Calvert also evaluates annually its own climate risk impacts directly from its operations in terms of Scopes 1, 2 and 3, and has determined that it primarily has Scopes 2 and 3 operations, which the team has chosen to offset in full for the past few years, in order to become carbon neutral.

Legal, Regulatory and Compliance Risk

Legal, regulatory and compliance risk includes the risk of legal or regulatory sanctions, material financial loss, including fines, penalties, judgments, damages and/or settlements, or loss to reputation we may suffer as a result of our failure to comply with laws. MSIM's Legal & Compliance Division advises the Firm on managing legal risk and monitors teams' compliance with current and emerging regulatory and legal requirements, including climate-related regulations where applicable. Our Government and Regulatory Relations teams represent the firm's public policy views, and engage with governments and regulators on behalf of the firm on existing regulations, including those related to climate regulations. We expect companies to comply with all relevant local and national laws, including laws that implement international agreements.

Regulation has impact on the valuation of the companies and business activities, including on the potential selection and the need to decarbonise. For companies where the risks are determined to be material, Calvert considers them in the ESG assessment. Such risks also impact existing and new products since the team needs to ensure that it is in compliance with the specific regulations in the markets where Calvert offers products. In addition, changes to regulations may alter relations with key suppliers.

Changes in policies, such as carbon taxes, renewable fuel standards or building energy-efficient standards, may impact our firm directly or indirectly through our investments. Calvert tracks climate-related regulations to assess potential transition risks to its business and investments. Similar to current regulation, emerging legal, regulatory and compliance risk includes the risk of legal or regulatory sanctions, material financial loss including fines, penalties, judgments, damages and/or settlements, or loss to reputation it may suffer as a result of failure to comply with laws or being associated with companies that failed to comply. Such emerging regulations may influence asset valuation and our future performance due to the potential cost of complying with future regulations and adjustment to existing business. Calvert also recognises that it may provide new opportunities.

In June 2021, Calvert responded to the SEC's request for comments on the regulation of climate change disclosures as the Commission considered disclosure rules and potential new disclosure requirements. Currently, climate change disclosures are largely voluntary, unverified and idiosyncratic. Calvert suggested that such disclosures be similar to current financial disclosures—so they can be historical, auditable and comparable against peers—required to appear in annual reports, at a minimum, with quarterly updates as appropriate. Calvert suggested using both qualitative and quantitative data, subject to third-party standards and verified by auditors. In addition, Calvert leveraged the SEC request on climate change disclosure to provide subsequent input on broader ESG disclosure to stress the importance of "consistent, comparable and complete disclosure" on human capital metrics. Subsequently, when the SEC asked for comments in 2022 to its Proposed Rule on Climate-risk Disclosures, Calvert provided a second set of comments on climate-related risks.

Technology Risk

Calvert recognises the significant impact technology can have on asset valuation and the climate strategy. However, there are many new opportunities for technological development to align with a net-zero world but that also raises risks regarding existing technologies. Calvert seeks to identify those risks and opportunities as they can have an influence on the performance of its products.

PRINCIPAL ADVERSE IMPACT ("PAI") MONITORING

Given our role as a global investment manager, we recognise that an unintended consequence of some of our investments may include some level of adverse impact on broader systemic sustainability factors, such as environmental matters, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters.

We acknowledge that the systemic nature of sustainability issues, where, relevant to a given investment strategy, needs to be addressed in a coordinated and concerted manner across the value chain. Through our Sustainability team and GRA team, we look at the portfolio holdings in all MSIM's long-term funds and assets to facilitate this holistic approach and, based on the balance of exposures and potential market influence, periodically define areas of potential principal adverse impact which may require attention and discussion with the relevant investment teams. For example, these include potential contributions to:

1. the increase of greenhouse gas emissions and systemic climate risk;
2. the increased use of finite natural resources;
3. the volume of hazardous and non-recyclable waste; and
4. violations of social norms and employee rights.

Where relevant, investment teams use reasonable efforts to obtain the required data to monitor these potential impacts and to understand any remediation efforts undertaken by companies. Portfolio managers maintain discretion over the extent to which the outcomes of this due diligence affect buy/sell decisions, portfolio construction, and ongoing engagement and asset stewardship.

We look to mitigate such potential adverse impacts through a combination of actions, including investment teams' engagement with investee management, our global stewardship programme, our thematic research and our collaborative efforts in the broader investment industry, as set out below. Moreover, we strive to adhere to several normative business conduct codes and standards. For example, our Portfolio Surveillance team monitors potential violators of the principles enshrined in the United Nations Global Compact and OECD Guidelines when this requirement is disclosed in the investment policy of a fund. If a potential violation occurs, the Portfolio Surveillance team will consequently reach out to the investment team and Sustainability team. The investment teams can then engage with these companies on remediation strategies.

In line with our commitment to transparency and reporting our activities to our clients and per regulatory requirements (e.g., SFDR, MiFID II, etc.), our investment teams have begun disclosing the different types of PAI indicators they consider, where applicable to their investment products in the European ESG Template ("EET"), providing intermediaries and hence end-clients with more information when determining which products meet clients' sustainability preferences, as well as preparing for SFDR Level 2 disclosures, which come into effect on 1 January 2023, and will require more detailed disclosure on our PAI consideration.

Stakeholder Collaboration to Promote Continued Improvement of Functioning of Financial Markets

We maintain memberships and affiliations with organisations that help to validate our stakeholders' range of perspectives, influence and encourage the adoption of consistent and clear industry standards, and which serve to reinforce our sustainability commitments and priorities. We also dedicate time and effort to collaborating with our peers on addressing systemic risks and advancing the industry's role in promoting sustainability as a key investment theme. We do so through our active participation in various industry bodies and forums, which is also highlighted in detail with examples in Principle 10 – Collaboration.

MSIM is currently a signatory to:

- the Principles for Responsible Investment ("PRI");
- the 2020 U.K. Stewardship Code;
- the Hong Kong Stewardship Code;
- the Japan Stewardship Code.

MSIM participates in the following industry initiatives:

- the European Leveraged Finance Association ESG Working Group (through our Fixed Income team);
- PRI's ESG in Credit Risk and Ratings Initiative;
- the Ceres Private Equity Working Group (through our PC&E team);
- the Sustainability Accounting Standards Board ("SASB") Investor Advisory Group;
- the Global Real Estate Sustainability Benchmark ("GRESB"), participating as an investor and asset member;

- the One Planet Sovereign Wealth Fund ("OPSWF") asset manager initiative, which was formed to advance the understanding of the implications of climate-related risks and opportunities within long-term investment portfolios through the sharing of investment practices;
- the working group convened by the Chartered Financial Analyst Institute ("CFA") to create a global product disclosure standard for sustainability-focused products;
- the U.K. Investment Association's working group on Fund-Level Communication of Responsible Investment, which is focused on fund disclosure requirements applicable to U.K.-based asset managers;
- the Real Estate Roundtable;
- the National Association of Real Estate Investment Trusts;
- National Association for Real Estate Investment Management;
- the NCREIF-PRE reporting standards working group; and
- the European Public Real Estate Association.

Our Calvert business has a long history of joining with like-minded investors and industry groups to further the advancement of material ESG issues and responsible investing, which include addressing and mitigating market-wide and systemic risks to ensure a well-functioning financial system. For example, this may involve co-filing resolutions and actively participating in engagement campaigns and responsible investing-related convenings.

Calvert also frequently responds to regulators' invitations for feedback on investor regard for climate and human capital issues. For example, Calvert's President and CEO testified to the Committee on Banking Housing and Urban Affairs of the United States Senate in 2019 on "The Application of Environmental, Social and Governance Principles in Investing and the Role of Asset Managers, Proxy Advisors and Other Intermediaries." His testimony outlined several data-driven arguments for the important role that responsible investing plays in ensuring that our financial system achieves the most sustainable future possible.

Often, Calvert partners with other investors and NGOs to advance common objectives, especially when it comes to addressing and mitigating market-wide and systemic risks to promote sustainable capital markets. Calvert believes there is power in numbers when it brings different voices and interests to the table with common objectives; for example, as demonstrated in its collaborative role in the Net-Zero Asset Managers' Initiative, joining others in the climate change campaign and was an original signatory. Calvert also regularly collaborates with members of the Interfaith Center on Corporate Responsibility, the Investor Network on Climate Risk/Ceres, U.S. SIF,[17] the Principles for Responsible Investing (PRI), and CDP.[18] As noted above, Calvert has a long history of partnering with the UN and its related entities. As it relates to the PRI, Calvert[19] was a founding signatory and has served on various committees over the years. Calvert currently serves on the Investor Reference Group on Corporate Reporting and the Global Policy Reference Group, and collaborates on engagements. Additionally, the Calvert Women's Principles were adopted as the UN Women's Empowerment Principles. Calvert also strives to promote the Sustainable Development Goals through the companies it invests in, through its engagement efforts with corporations and governmental agencies, and through its own operations.

In summary, the role we collectively play across our MSIM business and our participation depend on different types of industry initiatives. Our contribution spans:

- Sharing feedback regarding impact of and complying with upcoming policies and regulations;
- Enhancing awareness of systemic issues, such as climate, physical and transition risks;
- Sharing sustainability knowledge and investment best practices;
- Leveraging networks to increase our impact and improve our ability to work with companies; and
- Acting as the voice of our clients to further all of the above.

Notwithstanding industry collaboration to promote well-functioning financial markets, we also partner with our colleagues in Morgan Stanley's Global Capital Markets team as part of the ICMA Green & Social Bond Principles Working Groups and, as noted previously, our Firm is a member of the Global Impact Investing Network ("GIIN"), the Ceres Investor Network, the TCFD and the Steering Committee of the Partnership for Carbon Accounting Financials ("PCAF").

We also actively collaborate with external industry peer groups to address the risk of "greenwashing" related to sustainability-focused products. In this regard, we have actively participated in regulatory consultations relating to the EU SFDR, and MiFID II, among others,

[17] U.S. Social Investment Forum.

[18] Carbon Disclosure Project.

[19] Calvert was a founding signatory of the PRI in 2006 and has continued to be a member ever since.

aimed at increasing the transparency of how investment managers integrate sustainability issues and risks into their investment decision-making process. Our Head of Sustainability Regulation & Policy is a member of the Irish Funds' ESG Policy and Legal workstream, representing MSIM in such discussions to agree to best practices and also to contribute our views and learning to promote greater disclosure in a manner that mitigates the risk of greenwashing, and to assist industry peers to respond to relevant policy initiatives in a meaningful and impactful manner.

Another challenge that our industry faces is the availability, consistency and comparability of ESG data (which we also discuss in Principle 8 regarding ESG Data Providers). The poor data quality has the potential to impede the effective identification and assessment of ESG risks, as well as our ability to provide transparency and reporting to investors on ESG matters. These challenges are industry-wide, impacting us, our peers and our clients. We have actively participated in regulatory forums and initiatives to voice these challenges alongside our peers, with a view to reaching an industry-level solution.

Our engagement and participation with industry groups allow us to collectively share not just best practices and know-how, but also our experiences and challenges. We do so on behalf of and in the best interests of our clients (Principle 6) to ensure the continued improvement of functioning of financial markets, especially in cases where our industry working groups provide feedback to regulators on the feasibility of regulatory requirements, as well as advancing the industry's role in promoting sustainability investment, practices and standards.

Further details of collaboration and key industry initiatives are provided in Principle 10.

Effectiveness in Identifying and Responding to Market-Wide/Systemic Risks, and Promotion of Well-Functioning Financial Markets

We outline below a high-level summary of the key groups and committees involved in addressing market-wide and systemic risks on behalf of clients, the Firm and within financial markets.

We consider that our risk management and engagement approaches have been, and continue to be, effective in identifying and responding to market-wide and systemic risks, as well as promoting well-functioning financial markets.

MSIM RISK FRAMEWORK

Our overall MSIM risk framework is reviewed and updated on an ongoing basis by our Risk team, to ensure that MSIM is appropriately identifying and managing the risks (including systemic and market-wide risks) that it faces in its business, or which could cause harm to clients or financial markets. Consideration of market-wide and systemic risks, as well as MSIM's effectiveness in responding to them, are considered in the risk assessment which informs the annual plan of assurance activities for IAD. Please see Principles 2 and 5 for more details on IAD's current review of MSIM's ESG/Sustainability governance and control frameworks, investment activities and commitments

MSIM SUSTAINABILITY OVERSIGHT AND GOVERNANCE

As outlined in Principle 2, we have enhanced our ESG control framework and governance, with the addition of subject matter experts and additional monitoring and controls throughout the life cycle of products and regarding external commitments. We continue to strengthen our organisational readiness from controls, reporting and regulatory perspectives—which, in turn, enables more robust cross-functional timely communication and coordination in all aspects of ESG/ sustainability. Though these enhancements are still in the process of being implemented before effectiveness can be fully assessed, we have set specific objectives and milestones which we continue to report to our various stakeholders (see Table 4.1 above) and aim to disclose in more detail in our next U.K. Stewardship Report.

MSIM INVESTMENT TEAMS

From an investment perspective, despite the lingering effects of COVID-19, and volatility and market disruption arising from geopolitical crises and challenges (e.g., Russia/ Ukraine crisis), we consider that our investment teams responded in a considered and long-term focused manner (as outlined in our select investment team examples above) during the reporting period. Our response was also well supported by our ongoing focus on identifying and managing ESG risks, which contributed to the resilience and performance of our portfolios during this volatile period, as companies with stronger ESG credentials weathered market upheavals better. We continue to focus on minimising greenwashing and stewardship-washing risks as part of our client-centric commitment, providing transparency and reporting on investment progress and outcomes of our engagement and stewardship/ collaboration efforts (Principles 3, 9 and 11).

TABLE 4.1

Summary of Key Groups/Committees Addressing Market-Wide and Systemic Risks

	SUMMARY OF KEY GROUPS/COMMITTEES ADDRESSING MARKET-WIDE AND SYSTEMIC RISKS*	
	ROLE & PROCESS FOR ESCALATION	**TYPES OF MARKET-WIDE/SYSTEMIC RISKS**
MSIM		
First Line of Defence **Investment Teams** **MSIM Risk/GRA/ IM Risk Committee** **Portfolio Surveillance**	• Investment teams are ultimately responsible for addressing and mitigating risks associated with their respective products and strategies, working with the MSIM Sustainability team and other MSIM/Firm stakeholders (including MSIM LCD, MSIM Risk (and GRA), Portfolio Surveillance, etc.). Periodic meetings with the Sustainability Team Leads, Sustainability Regulatory & Product Group, Sustainability Council and Investment Oversight Committees ensure ongoing communication and escalation of potential/actual risks • MSIM Risk/GRA identify, monitor and manage risks at security, portfolio and MSIM levels, working with investment teams and MSIM Sustainability and Sustainability Oversight teams. Updates (including escalation) to IMRC and other regional MSIM Risk Committees are made on a periodic basis • Portfolio Surveillance oversees and ensures all ESG screening and monitoring guidelines are agreed to between investment teams and clients at the outset of client onboarding, implemented and continuously monitored throughout the mandate.	• All relevant market-wide and systemic risks to the extent they are relevant to specific investment strategies and products, including those which may have wider implications (please see above) • Specific focus/priority on greenwashing, stewardship-washing, environmental (including climate change), social (including human rights, controversies) and governance, etc., as appropriate and relevant to the strategies/ products they manage
Subject Matter Expertise **MSIM Sustainability Team** **MSIM Stewardship Team** **MSIM Sustainability Oversight**	• The MSIM Sustainability and Stewardship teams provide subject matter expertise, supporting the Investment teams holistically, and work with MSIM/ Firm stakeholders (including MSIM LCD, MSIM Risk (and GRA), Portfolio Surveillance, etc.) to address product, regulatory, strategy, stewardship and data-related areas (Principle 2) • The MSIM Sustainability team hosts and coordinates the Sustainability Team Leads, Sustainability Regulatory & Product Working Group and Sustainability Council meetings • MSIM Sustainability Oversight ensures processes are in place to capture and monitor product/investment commitments made (Principle 2) • Stakeholders above also periodically update Board-level members, given ESG is a standing agenda topic at quarterly meetings	• All relevant market-wide and systemic risks relevant to investment teams and their respective products including wider implications for MSIM as a whole (pls see above) • Specific focus/priority on greenwashing, stewardship-washing, environmental (including climate change), social (including human rights, controversies) and governance etc.
Second Line of Defence **MSIM Compliance**	• MSIM Compliance works with investment teams and the MSIM Sustainability, Stewardship, Sustainability Oversight team to: advise on ESG-related regulatory and industry consultations; advise on ESG-related policies and procedures; and conduct periodic reviews of the MSIM businesses' compliance with laws, regulations and policies, including with respect to ESG investing approaches, disclosures and practices	• All relevant market-wide and systemic risks relevant to investment teams and their respective products, including wider implications on MSIM as a whole (please see above) • Where appropriate, there is a specific focus/ priority on greenwashing, stewardship-washing, environmental (including climate change), social (including human rights, controversies) and governance, etc.

SUMMARY OF KEY GROUPS/COMMITTEES ADDRESSING MARKET-WIDE AND SYSTEMIC RISKS*

	ROLE & PROCESS FOR ESCALATION	TYPES OF MARKET-WIDE/SYSTEMIC RISKS
FIRM-LEVEL		
Firm Risk Committee (Global, Regional)	• Oversees Firm-level risk, based on divisional business activities, provides guidance on management and mitigation of potential/actual risks • Reports to various Boards	• All relevant market-wide and systemic risks relevant to the Firm as a whole (please see above)
Firm Operating Risk Committee (Global, Regional)	• Oversees Firm-level operating risk based on divisional business activities, provides guidance on management and mitigation of potential/actual risks • Reports to various Boards	• All relevant market-wide and systemic risks relevant to the Firm as a whole (please see above)
Regulatory Oversight	• Oversees, guides and ensures Firm-level regulatory compliance and disclosures, working with functional stakeholders across divisions • Reports to various Boards	• All relevant market-wide and systemic risks relevant to the Firm as a whole (please see above)
Subject Matter Expertise **Global Sustainable Finance** **Environmental & Social Risk Management**	• GSF provides subject matter expertise across sustainable market trends, product innovation, ESG analytics and key themes, including climate, plastic waste and inclusive growth. Support all Firm Business Units, including close collaboration with MSIM. GSF reports to the Firm's Chief Sustainability Officer • ESRM provides subject-matter expertise on E/S risks, conducts diligence on relevant transactions, engages with stakeholders, and monitors emerging risks and developments in partnership with MSIM Private Credit & Equity and Real Assets businesses and GSF	• Sustainability-specific areas/priorities concerning MSIM, including, but not limited to: environmental, climate change, biodiversity, social, governance, regulatory, including greenwashing, etc.
Third Line of Defence **Internal Audit**	• IAD is an independent and objective assurance function reporting directly to the Firm's Board Audit Committee. • IAD assists the Firm in achieving its strategic and operational objectives by identifying and assessing risks facing the Firm, and providing independent, objective and timely assurance to stakeholders about the effectiveness of the Firm's risk management, internal controls and governance processes	• All relevant market-wide and systemic risks relevant to MSIM and the Firm as a whole (please see above)
BOARD-LEVEL		
Various Board Committees (MSIM (including Investment Oversight)/Firm-Level, Entity-specific, Product-specific, Global, Regional etc.)	• The role of Boards is to execute on their respective Board Charters, which include but are not limited to: ensuring businesses comply with their respective objectives and operate within appropriate governance and control frameworks, discussing and providing guidance on managing potential/actual risks upon escalation etc. • The main functions of Boards are to protect the Firm and business units	• All relevant market-wide and systemic risks relevant to MSIM and the Firm as a whole (please see above)

* The above is a non-exhaustive list of stakeholders involved in identifying, managing and mitigating market-wide and systemic risks. Further details can also be found in Principles 2, 3, 5, and 7-12.

FIRM-LEVEL AND BOARD GOVERNANCE STRUCTURES

Our Firm-Level and Board Governance Structures (as summarised in Principle 2 and in *Table 4.1* above) oversee the identification and management of risks by MSIM, including market-wide and systemic potential/actual risks.

MORGAN STANLEY HORIZON SCANNING

The Board of our U.K. holding company, Morgan Stanley International Limited, carries out a horizon scanning exercise on a biannual basis to identify medium- to long-term external factors that have the potential to impact the Firm's business and operations.

MORGAN STANLEY AS A SYSTEMICALLY IMPORTANT FINANCIAL INSTITUTION

The Dodd-Frank Act, as amended by the Economic Growth, Regulatory Relief and Consumer Protection Act ("EGRRCPA"), establishes a systemic risk regime to which certain large Bank Holding Companies ("BHCs"), including Morgan Stanley, are subject. Under rules issued by the Federal Reserve to implement certain requirements of the Dodd-Frank Act's enhanced prudential standards, such large BHCs must conduct internal liquidity stress tests, maintain unencumbered, highly liquid assets to meet projected net cash outflows for 30 days over the range of liquidity stress scenarios used in internal stress tests, and comply with various liquidity risk management requirements. These large BHCs must also comply with a range of risk management and corporate governance requirements. Pursuant to these requirements, Morgan Stanley has put in place arrangements within its business to monitor and respond to systemic risks.

The Federal Reserve also imposes single-counterparty credit limits ("SCCL") for large banking organisations. U.S. Global Systemically Important Banks ("G-SIBs"), including us, are subject to a limit of 15% of Tier 1 capital for aggregate net credit exposures to any "major counterparty" (defined to include other U.S. G-SIBs, foreign G-SIBs, and nonbank systemically important financial institutions supervised by the Federal Reserve). In addition, we are subject to a limit of 25% of Tier 1 capital for aggregate net credit exposures to any other unaffiliated counterparty.

MORGAN STANLEY FIRM RESILIENCE AND FUSION RESPONSE & RECOVERY

Morgan Stanley's Firm Resilience team maintains global programmes for Business Continuity Management ("BCM"), Disaster Recovery ("DR") and Third-Party Resilience designed to protect the Firm during a business continuity incident. A business continuity incident is an interruption with potential impact to normal business activity of the Firm's people, operations, technology, suppliers and/or facilities. These include, but are not limited to, cyber and fraud technology incidents, weather events, terror attacks, geopolitical unrest and pandemics. The BCM programme's core functions include business continuity planning, testing and crisis management. The programmes are governed by the Business Resilience Governance Committee and a Risk Oversight Committee. In addition, a Committee of the Board of Directors and senior management oversee the programme.

The Fusion Response and Recovery team lead rapid and comprehensive response and recovery operations in order to minimise impact from a broad range of business-disrupting threats and incidents. When such events are identified, the Firm leverages recovery strategies documented within Business Continuity Plans, such as transference or remote, to recover critical business processes. During 2022, the Fusion Response and Recovery Crisis Management Operations team monitored and reacted to 310 incidents globally, ranging from severe weather/natural hazards (e.g., cyclones, winter storms, wildfires, earthquakes, tornadoes and flooding), external vendor outages, security and life safety, and technology incidents. 105 of such incidents related directly to weather/natural hazards and only 10 of the total 310 resulted in business impact.

LOOKING AHEAD

Effective risk management and identification is, however, an ongoing journey, and, as indicated by the increasing importance of ESG risks, market concerns on greenwashing and stewardship-washing, and events such as COVID-19, climate change, geopolitical crises such as the Ukraine-Russia war and rising inflation, the universe of potential risks will continue to expand. We therefore intend to continue evaluating and adapting our risk modelling, forecasting, management and engagement frameworks and strengthening our organisational readiness on an ongoing basis to ensure that we can continue to respond appropriately to market-wide and systemic risks and promote the effective functioning of financial markets.

PRINCIPLE 5

Review and Assurance

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

Review, Oversight and Continuous Improvement of Policies and Processes Ensuring Effective Stewardship

Ongoing review, assessment and reflection of our policies, processes and frameworks are crucial in ensuring the effectiveness of our stewardship approach in response to the evolving industry landscape and, most importantly, ensuring that our stewardship activities continue to deliver outcomes aligned with our clients' interests.

Though our internal processes guide the frequency of review and updates of different types of policies, we take a pragmatic approach and may conduct ad hoc reviews/ updates, if and when there are time-sensitive drivers, such as material incidents or regulatory amendments, the effective dates of which may precede our regular review and update cycles.

Notwithstanding the above, we follow a robust governance review and sign-off process by relevant functional and senior stakeholders (based on the type of policy, process & framework). This is not generally without feedback, as the different types of stakeholders involved (e.g., cross-functionally, where applicable) can often lead to diverse opinions, new perspectives and better decisions.

Examples of these include:

MSIM PROXY VOTING POLICY AND PROCEDURES

As described in Principle 2, our MSIM Proxy Voting Policy was updated earlier this year, in line with our commitment to revise annual updates to Q1 of each year as opposed to Q3, to ensure the policy is updated ahead of each proxy season. Our MSIM Proxy Review Committee ("Committee") has responsibility for overseeing the implementation of the MSIM Proxy Voting Policy.

The Committee meets at least quarterly and reviews and considers changes to the MSIM Proxy Voting Policy at least annually. Regular review of the MSIM Proxy Voting Policy by the MSIM Sustainability and Global Stewardship team has led to ongoing incremental improvements and clarifications to the existing policy—and during this reporting period, in particular, we actively engaged to seek the views of our public-side investment teams to ensure that our proposed amendments are aligned with their proxy voting strategies and ultimately our end-clients. These were then incorporated and presented to the Morgan Stanley Funds Boards of Directors/Trustees for Board Approval. Key updates included:

- Clarification of our general approach to voting on environmental and social issues, highlighting certain key elements and the expectation for enhanced transparency
  - Potential implication/effect: to stay in line with evolving best stewardship market practices based on our investment teams and client feedback
- Provision of additional language on policy and gender and racial diversity
  - Potential implication/effect: potentially recommend against nominating committee members in cases of lack of gender and racial diversity
- Provision of additional language on environmental and social issues that we expect will be prominent in proxy season
  - Potential implication/effect: support shareholder proposals focused on enhanced disclosures and/ or improvements related to climate, and other environmental and social risks
- Provision of additional clarifications to reflect the increasing importance of close consultation with the investment teams through proxy season, and increased specificity of client sustainability mandates
  - Potential implication/effect: greater collaboration with investment teams and potentially additional split votes

Looking ahead, we will continue to actively incorporate our investment teams' views, as they provide crucial intelligence on guiding companies in which we invest towards better ESG practices, which we believe produce long-term, sustainable returns. Future updates will further integrate our governance and proxy voting policy with clients' investment goals, using votes to encourage portfolio companies to enhance long-term shareholder value and to provide a high standard of transparency such that equity markets can value corporate assets appropriately.

ESG CHECKLIST AND PATHWAY FOR INTERNAL REVIEW OF MSIM ESG-RELATED PROPOSALS

We similarly adopted a multi-stakeholder and multidimensional approach (please see our Sustainability

Organisational Structure in *Figure 2.1*, Principle 2) to reviewing our ESG Checklist, which aims to document and provide oversight on product/investment-level objectives and methodologies, as well as proposals to respond to external industry consultations and/or commitments, respectively (Principle 2).

Both the Checklist and Pathway for Internal Review were first presented within MSIM at the Sustainability Team Leads and Sustainability Product & Regulatory Working Group to gather feedback from the "first sphere" of stakeholders that are directly impacted by the corresponding revisions/proposals. In doing so, we also sought the views of our EV affiliates to ensure that the proposals are relevant to their respective strategies, businesses and operations. At the same time, our MSIM and EV affiliate, Legal & Compliance and Risk teams assessed the parameters of our proposals to ensure they comply with and operate within our existing controls and governance framework. The "second sphere" of stakeholders involved the Sustainability Council whose role is to provide MSIM-level sustainability leadership and guidance, and thereafter, the "third sphere" of stakeholders involved appropriate firm-wide functional management, including, but not limited to, GSF, ESRM, Regulatory Relations, Corporate Communications, etc. (the latter sphere was more applicable to the Pathway for Internal Review, given the external reputational angle).

As a result of this multi-stakeholder and multidimensional approach, key suggestions that were incorporated include:

- **ESG Checklist** – consideration of U.S. SEC ESG proposals, which, though not final, brings to the investment teams awareness of such proposals on the horizon and how to position their proposed investment strategy/methodologies, product names etc.
  - Potential implication/effect: provides a comprehensive view for investment teams in considering different regional regulations/proposals and impact on global investment strategies distributed in jurisdictions
- **ESG Checklist** – product conversions, whether regulatory or from a commercial perspective e.g., enhancing ESG characteristics or adding specific sustainability objectives
  - Potential implication/effect: brings into scope existing products thereby expanding oversight and governance, which does not just include new products
- **Internal Review of MSIM ESG-Related Proposals** – clarifying and assigning ownership roles within MSIM, EV, Calvert and Parametric e.g., proposer, central coordinator and respective delegates
  - Potential implication/effect: ensures a streamlined process in escalating proposals for review, including accountability and transparency for each business segment

SUSTAINABILITY OVERSIGHT AND GOVERNANCE

As mentioned in Principle 2, we are in the process of implementing enhanced Sustainability Oversight and Governance, also as part of our ongoing reflection to further develop our stewardship activities and client commitments. Given this is still in-progress, we aim to evaluate our efforts vis-à-vis our core objectives over the next six – twelve months. These will also include the need to ensure we accurately report and disclose to clients our activities and that we deliver on our commitments, ensuring that our overall stewardship reporting is fair, balanced and understandable, supported by accurate data and metrics.

MSIM SUSTAINABLE INVESTING POLICY AND ENGAGEMENT AND STEWARDSHIP PRINCIPLES

As mentioned in Principle 1, our MSIM Sustainability team is responsible for maintaining the Sustainable Investing Policy and, in conjunction with the Global Stewardship team, overseeing our MSIM Engagement and Stewardship Principles as part of that effort, collaborating closely with the Sustainability Team Leads, the Global Stewardship team and other functions. The Sustainability Council is responsible for reviewing and approving the Policy and Principles, ensuring that it accurately reflects the philosophy and processes that govern MSIM's sustainability strategy as well as the practical experiences and insights of our investment teams.

We are currently in the process of reviewing our Sustainable Investing Policy to determine appropriate updates, given the enhancements to our Sustainability Oversight and Governance, ESG Checklist and Pathway for Approval process. The goal is to reflect and report our strengthened oversight, which directly correlates with our stewardship activities. Once we arrive at a consensus for updates, these will be implemented, subject to our governance review and sign-off process, and a summary will be included in our next U.K. Stewardship Code Report.

Regular updates to global stewardship codes, beyond the U.K. Code, such as the Japan and Hong Kong Stewardship Codes, also encourage us to revisit our Engagement and Stewardship Principles regularly.

Internal and External Assurance; Continuous Improvement of Stewardship Policies and Processes

Assurance of our sustainability and stewardship policies, processes, activities and reporting is important in ensuring we continue to deliver on our client commitments, in line with internal and external regulatory and industry requirements, and that our reporting and communications are an accurate reflection of this and are fair, balanced and understandable.

INTERNAL

In addition to our business unit stakeholders, our MSIM Compliance team conducts periodic reviews of the MSIM businesses' compliance with laws, regulations and policies, including with respect to proxy matters and ESG-related investing approaches, disclosures and practices. As referred to in Principle 2, an ESG Compliance Test was conducted in Q4 of 2021 to assess whether relevant ESG disclosures comply with investment team practices,[20] documentation and applicable regulations. The goal was also to ensure disclosures are sufficiently robust to minimise greenwashing. The scope of the review included internal policies and procedures, as well as external-facing documentation, such as marketing materials and reports. Though internal policy does not allow for external disclosure of results of internal reviews, MSIM continues to review and assess its approach in all ESG-related areas and implement enhancements per regulatory and client requirements, and in line with industry standards, as appropriate.

In our last U.K. Stewardship Report, we made reference in this Principle to focusing on three key area enhancements: (1) disclosures and marketing materials; (2) ESG data provider due diligence; and (3) oversight and governance of products, which have been noted by the Internal Audit Department as an area of regulatory focus and included in the audit risk assessment to inform the annual plan of audit assurance activities. As a result of this, in Q3 of 2022, IAD commenced an audit of the MSIM ESG investing framework, including sustainability governance, monitoring over sustainable investing, ESG integration in portfolio management activities, sustainable investing reporting and the use of exclusionary screens.[21] IAD is also performing a separate audit, which focuses on the inclusion of sustainability factors in the product governance process and disclosures related to the EU SFDR Level 1 requirements. Morgan Stanley believes this assurance approach provides an objective assessment of the effectiveness of MSIM's policies, processes, activities and reporting, as IAD is fully independent of the business, with the Chief Audit Officer reporting into the Firm Board Audit Committee. IAD also has full accessibility to Morgan Stanley and possesses a deep knowledge of the business and applicable regulations. ESG is a focal area for IAD across the firm, with multiple audits being conducted across business units between 2022 and 2023 focusing on climate risk, sustainable finance and ESG investing.

Though the audit is still ongoing as of the date of this report, through our continuous and ongoing review and reflection of our stewardship controls and processes, we seek to ensure effective stewardship reporting so that it is fair, balanced and understandable. This can be further enhanced following our audits as well.

IAD conforms with the Institute of Internal Auditors' ("IIA") International Standards for the Professional Practice of Internal Auditing, which is validated by an independent third party every five years.

MSIM LTD BOARD

Our MSIM Ltd Board is ultimately responsible for overseeing the business of the entity, including its stewardship activities. As noted previously, the Board has approved the issuance of this report.

EXTERNAL

While our external consultant engaged to conduct a TCFD readiness assessment (Principle 4) did so from a TCFD and climate perspective, given the regulatory requirement for U.K. asset managers to publish TCFD reports by June 2023 next year, in doing so, our policies, processes and internal frameworks were assessed comprehensively. We therefore benefit from understanding, from a climate change and TCFD perspective, the development areas needed to strengthen our internal frameworks to support a high-quality, initial TCFD disclosure in 2023. This will, in turn, help support our clients' respective TCFD reporting requirements as well. Case in point, U.K. pension schemes that are also required to publish TCFD reports. Knowledge of areas we can continuously improve on will also serve to fortify effective stewardship.

On proxy voting, an external auditor also performs an external SSAE-18 audit of the proxy voting process and procedures as part of the Firm's annual Sarbanes-Oxley review. We have passed this audit in each of the last seven years, indicating that our process continues to be robust and effective.

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[20] Applicable to legacy MSIM investment teams only, given the timing of the test plan and actual test itself.

[21] The ESG Audit is still in progress at the time of writing this report.

MSIM maintains voting records of individual agenda items at company meetings in a searchable database on its website on a rolling 12-month basis. As a result of wanting to provide greater transparency to clients, we have enhanced and improved this reporting to include vote rationales for items voted against management and rationales for voting on shareholder resolutions.

OTHER REVIEWS TO ASSURE PROCESSES AND ASSESS EFFECTIVENESS OF STEWARDSHIP ACTIVITIES

As part of MSIM's ongoing oversight of third-party providers, MSIM performs periodic due diligence on service providers used to support our stewardship and investment activities. Topics of the reviews include, but are not limited to, conflicts of interest, methodologies for developing their policies and vote recommendations, and their resources. Where necessary or appropriate, MSIM also conducts on-site due diligence meetings and meets with research staff, compliance and information technology teams to review policies and procedures.

LOOKING AHEAD

Notwithstanding the above drivers, MSIM will take steps from time to time to review its own ESG frameworks and processes in an effort to identify areas for continuous enhancement, and to seek opportunities to increasingly develop a more globalised strategic approach to MSIM's investment practices and risk management related to ESG products. With integration progressing with our EV affiliates, this calls for more collaboration and opportunities to design a more streamlined and holistic MSIM ESG/stewardship approach across all businesses. To achieve this, complete integration of infrastructure, operations and systems between MSIM and EV needs to occur, but this will not come at the cost of inaction, as we believe that good ESG practices, sustainability and stewardship are not static or end-destinations but an evolving journey, complemented by our philosophy as active owners and good stewards of clients' capital.

Over the next 12-24 months, we will continue to strengthen the following:

1. **SUSTAINABILITY OVERSIGHT AND GOVERNANCE**
   - Fully implement the new functions, roles and responsibilities outlined previously. Expand the framework to EV affiliates. Please see Principles 2 to 4 for more details
2. **PRODUCT/INVESTMENT OBJECTIVES AND EXTERNAL INDUSTRY COMMITMENTS**
   - In part to maintain transparency in regulatory, client and stewardship reporting, but also to minimise greenwashing and stewardship-washing. Please see Principles 2, 4, 6, 7, 9 and 10
3. **ESG DATA PROVIDER DUE DILIGENCE**
   - To ensure fair, balanced and understandable reporting, our data needs to be objective, comparable and relevant. We continue to analyse and monitor our ESG data providers and due diligence to support investment teams. Please see Principle 8 for more details on our due diligence process; and
4. **HOLISTIC REPORTING SOLUTION FOR MSIM AND EV, CATERING TO RESPECTIVE CLIENT BASES**
   - Our ongoing integration with EV affiliates demonstrates the need to ensure regular sharing of best practices and stewardship approaches. Given the different types of client bases, this indicates differing client requests for various types of metrics and reporting based on their respective requirements. Our goal is to integrate our systems and expand our centralised database consisting of multiple modules that can be customised per investment team, and align the use of data providers and metrics to ensure good stewardship reporting. Please see Principle 8 for more details

SECTION 2

Investment Approach

PRINCIPLE 6

Client and Beneficiary Needs

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

Understanding and Meeting our Clients' Needs

MSIM has a diverse portfolio of clients with a broad spectrum of needs. We believe that our independent investment teams' structure and our overarching focus on responsible investing give us the agility and perspective to understand and meet the plurality of our clients' needs and investment objectives. Our diverse client base also benefits from the advantage of having global teams of investment professionals in major hubs, including, but not limited to, New York, Boston, Washington D.C., London, Mumbai, Singapore, Hong Kong and Tokyo, which seek to leverage their in-depth knowledge and expertise to capitalise on investment opportunities in all major markets across the globe. The charts below provide a breakdown of our AUM across our four investment platforms and regions of investment, as well as a breakdown of our diverse client base. We seek to embed Sustainable Investing into our investment strategies, where relevant.

FIGURE 6.1

MSIM Investment Capabilities and Assets Breakdown[22]

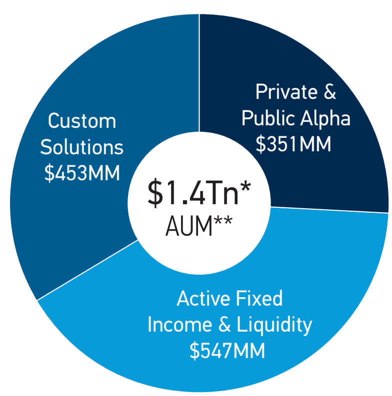
As of 30 June 2022

Leadership Across Investment Capabilities

SUSTAINABLE INVESTING

- HIGH-CONVICTION EQUITIES
- ACTIVE FIXED INCOME AND LIQUIDITY
- ALTERNATIVE INVESTMENTS
- CUSTOM SOLUTIONS

Assets By Investment Capabilities ($Bn)



* For the purposes of AUM consolidation, Eaton Vance AUM (including its four investment brands—EV Management, Calvert Research and Management, Parametric Portfolio Associates and Atlanta Capital) has been included within our total MSIM AUM and asset class breakdowns

** Assets under management (AUM) includes all discretionary and non-discretionary assets of Morgan Stanley Investment Management (MSIM) and all advisory affiliates. MSIM Fund of Fund assets represent assets under management and assets under supervision. MSIM direct private investing assets represents the basis on which the firm earns management fees, not the market value of the assets owned.

[22] "Sustainable Investing" does not represent a separate investment team, but is a term used to refer to our other investment teams when acting with a sustainable investing focus.

FIGURE 6.2

AUM by Region of Investment

As of 30 June 2022

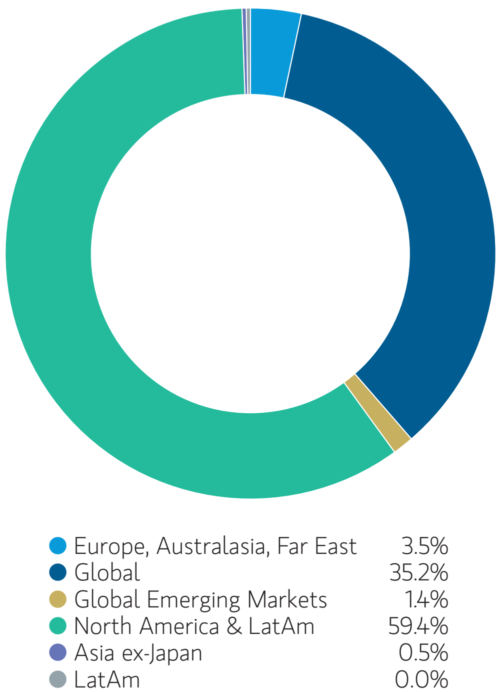


FIGURE 6.3

MSIM AUM Breakdown by Client Geography

As of 30 June 2022

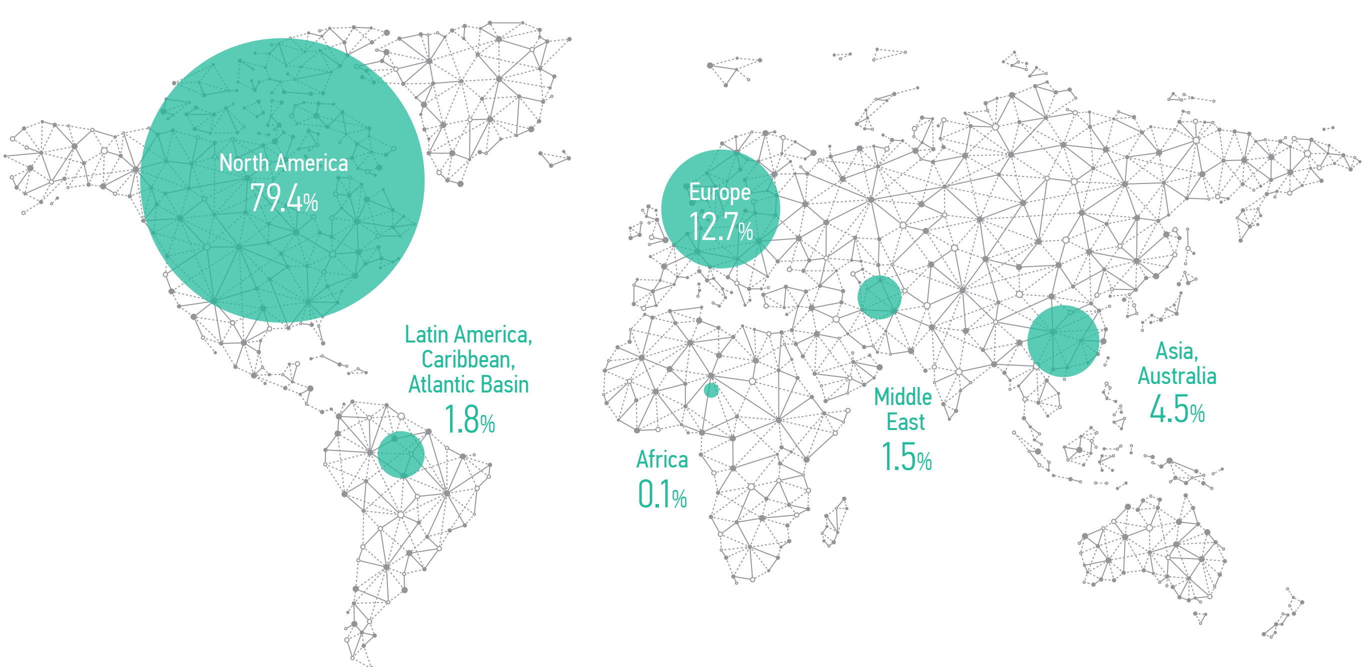


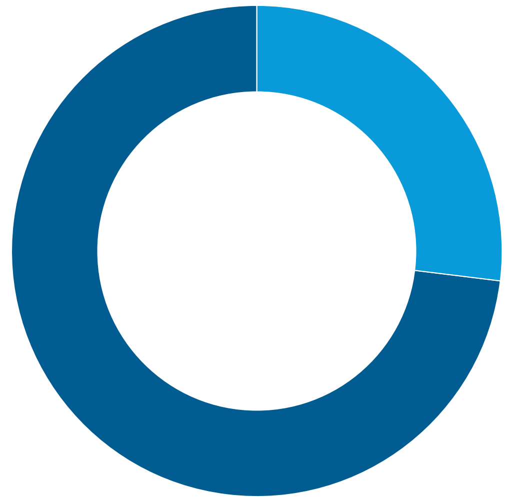
FIGURE 6.4

MSIM AUM Breakdown by Client Type *As of 30 June 2022*

Institutional	45%
Retail	55%

FIGURE 6.4B

MSIM AUM Breakdown by Product Type *As of 30 June 2022*

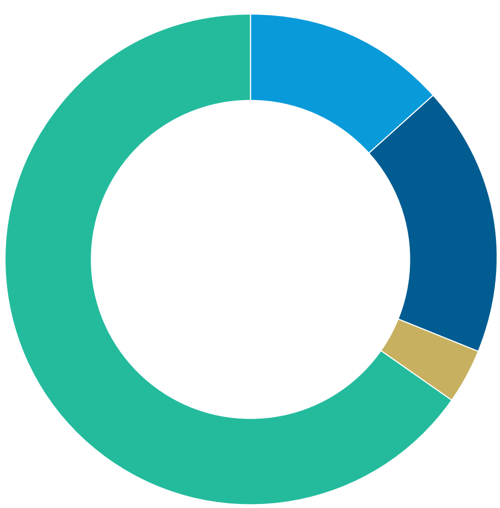


Separate Mandates	27%
Pooled Funds	73%

FIGURE 6.5

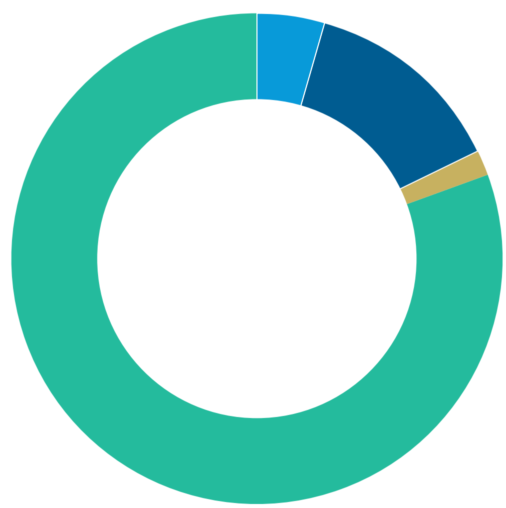
MSIM AUM Breakdown by Asset Class and Geography *As of 30 June 2022*

High-Conviction Equities



Asia	13.4%
EMEA	17.9%
Latin America	3.5%
North America	65.3%

Fixed Income & Liquidity

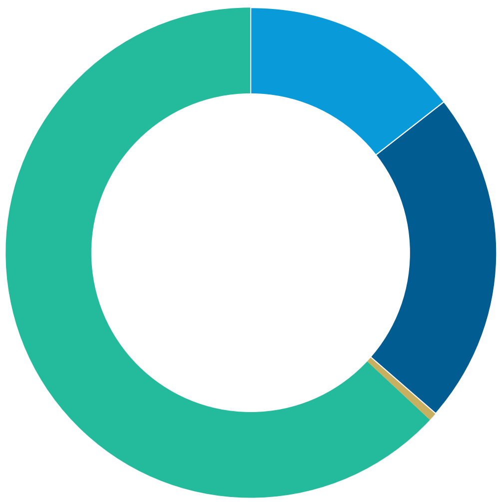


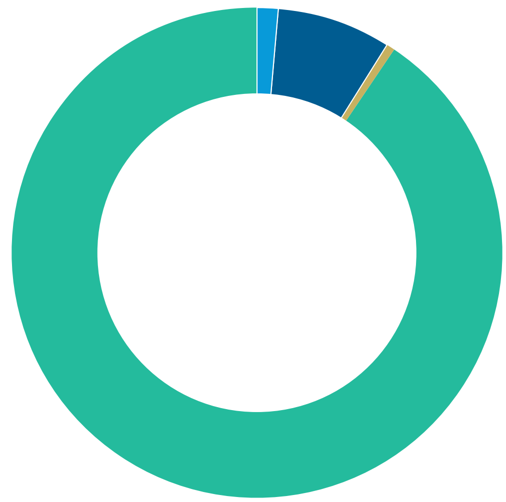
Asia	4.7%
EMEA	13.3%
Latin America	1.6%
North America	80.3%

FIGURE 6.5

MSIM AUM Breakdown by Asset Class and Geography

As of 30 June 2022





Investment Horizons

The investment horizon of our clients varies depending on their individual financial goals, objectives and liabilities. MSIM works with clients to ensure that the investment horizons of the strategies and solutions we are providing align with their needs. While investment horizons vary across our independent investment groups and platforms, on average, most MSIM investment teams consider a three- to five-year investment time horizon, with some teams being below or above that range. For example, some of our concentrated global equity portfolios have held certain companies for decades, while our money market, liquidity and asset allocation funds consider much shorter time horizons.

The investment horizon also varies depending on the asset classes and investment strategies pursued—for example, some of our private asset funds could have an investor lock-in period of up to eight to 10 years, whereas our Liquidity funds tend to have an investment horizon of one year or less—as well as market conditions, that in turn are impacted by factors such as investor confidence, geopolitical events (e.g., the Ukraine-Russia conflict) and market-wide risks (e.g., inflation and the cost-of-living crisis).

Obtaining Clients' Views

It is our goal to help our clients address their particular investment issues, as well as regulatory and reporting needs. Over the past 12 months, in anticipation of regulatory deadlines and effective dates (e.g., SFDR Level 2, MiFID II Sustainability Preferences, TCFD, etc.), we have proactively reached out to end-clients and intermediaries, ahead of time, to understand the scope of additional and/or bespoke regulatory reporting we can support, in line with our client-centric commitment. As a result of this, we have implemented a number of internal processes in collecting specific types of data for clients and/or incorporated their needs in our data and technology build-out, including further assessments on third-party data providers on coverage, understanding future enhancements and how these may support our clients' needs (please see Principle 2 for more details).

Our teams of experienced professionals aim to set industry standards for investment expertise and client service, striving to:

- Work with our clients to understand their business, investment and regulatory needs, offering a range of tailored services and a diverse selection of top-tier investment products; and

- Partner with our clients to achieve their investment goals and take pride in our ability to provide best-in-class service, combined with the global resources of Morgan Stanley.

STRATEGIC RELATIONSHIP MANAGEMENT AT MSIM

Our dedicated Strategic Relationship Management ("SRM") team, established since 2019, continues to go above and beyond our existing client service support functions. The SRM team is dedicated to fostering meaningful relationships with our clients and, with our EV integration, their remit has expanded, working and collaborating with key EV affiliate stakeholders in building one MSIM. The team specialises in developing unique and holistic partnerships with clients, which are customised to a client's specific investment needs, interests and goals, which often include specific sustainable investing objectives.

Our various client interactions provide us with an opportunity to better understand how to meet their investment needs. Our investment teams have published research and thought leadership in response to specific client inquiries and areas of interest, and also joined investor coalitions or industry organisations that are important to our clients. We strive to be responsive to our clients' needs holistically, above and beyond their specific investment objectives and targets.

Incorporation of Client Views, Stewardship and Investment Policies Into Asset Management

The incorporation of clients' views, stewardship and investment policies is generally conducted by individual investment teams corresponding to their specific clients.

GLOBAL OPPORTUNITY

For example, one of our equity teams, Global Opportunity, ensures that its client mandates take into account clients' stewardship policies through consultation during the onboarding process based on open dialogue and consensus on Investment Management Agreement ("IMA") guidelines, agreed to by each client. In 2020, through the incorporation of one large client's sustainable investment objectives, the Global Opportunity team partnered with the client to launch Global Change, a customised global equity strategy, which currently has over $5.8 billion in assets as of 30 June 2022. This demonstrates both the success of incorporating a client's sustainable investment objectives and stewardship policies, as well as collaboration/partnership to achieve the client's specific goals.

The Global Opportunity team also continuously obtains client feedback, which is integrated in the team's annual ESG and Sustainable Investing Report that discusses ESG integration within the investment process. For example, clients have previously requested company engagement case studies and information relating to the carbon footprint of portfolios, which the team incorporated in its annual report. The Global Opportunity team continues to innovate and evolve its process, and believes that integrating ESG within its investment analysis improves the risk and reward profile of client portfolios. To do this, client feedback is incorporated in the team's future plans, including ESG reporting and potential product launches.

INTERNATIONAL EQUITY

Our International Equity team works with clients to customise their portfolios with additional client-specific exclusions. Given the shared investment beliefs between the International Equity team and its clients, the team frequently publishes thematic insights on the MSIM website, communicating its understanding and outlook on relevant ESG topics, such as single-use plastic and decarbonisation. These pieces are also emailed directly to its clients. Additionally, the International Equity team publishes a biannual Engage report, outlining the team's engagement activities and voting statistics. This is in part to update its clients, but also enables clients to report to their own stakeholders, recognising their corresponding duties to report on certain ESG topics and/or metrics. Finally, the team produces quarterly ESG fact cards for all of its global SICAV funds, as well as for the Global Sustain OEIC and the Global Sustain strategy. These are available on the MSIM website and can also be emailed directly to investors.

PRIVATE CREDIT & EQUITY

Separately, our PC&E teams implement client-specific stewardship requirements (through side letters or negotiation of the fund documents) such as: (1) excuse rights or investment restrictions (e.g., tobacco, alcohol, weapons); (2) client-specific reporting; and (3) enhanced due diligence or portfolio-monitoring procedures.

EMERGING MARKETS EQUITY

The EME team adds value to clients' stewardship and investment policies through engagements with corporates on sustainability issues on clients' behalf, portfolio-level sustainability reporting and through detailed reviews with clients on their stewardship practices. The team also publishes a yearly report with detailed ESG metrics and engagement examples. Customised reporting on EME's ESG progress is provided to clients throughout the year. In addition to this, the team customises portfolios for clients who wish to implement specific exclusions or additional ESG standards. Client reporting on fund-level ESG and Stewardship metrics varies based on fund strategy. These portfolio reports may be available to clients, both regularly or upon request.

EME also engages with clients on sustainability and ESG topics to understand their investment policies and stewardship activities so that we can partner with them and ensure we are aligned with client interests.

CALVERT RESEARCH AND MANAGEMENT

Calvert Research and Management combines deep industry experience, a principled approach, global reach and active corporate engagement to help meet clients' needs and goals, implemented across a range of investment strategies and asset classes.

For example, the Calvert Applied Responsible Investment Solutions ("Applied Solutions") team works with clients to build custom solutions to help them meet their financial and responsible investing goals. In consultation with clients, the Applied Solutions team has been able to leverage their in-depth knowledge of ESG data to build investment solutions that support both clients' environmental and social impact goals. Throughout the portfolio construction process, the team members engage clients in discussions to ensure alignment between the investment portfolio and the client's stated goals.

As a part of our client service offerings, the Applied Solutions team provides periodic updates on company engagement, proxy voting and outcomes. In addition, a client may also receive ESG impact reporting. They also conduct periodic calls, as needed, based on the client's request, to discuss their investment portfolio(s).

PARAMETRIC PORTFOLIO ASSOCIATES

Parametric believes that responsible investing is done best when it is directed by the client, rather than the manager imposing their own view. For this, Parametric subscribes to and offers hundreds of specific environmental, social and governance metrics that clients can utilise in the management of their portfolio, as well as the option to utilise client-provided data. This data can be applied to any of the exposures offered at Parametric to screen based on client criteria while striving to provide as similar a risk/return profile as the original exposure. Parametric's proprietary systems are designed to provide clients with a high degree of customisation and allow account-specific restrictions to be enforced and monitored on an ongoing basis. This flexibility applies over the life of the account, and clients may change exposures or ESG criteria at any time. Parametric also offers dedicated, responsible investing indexes from Calvert and a number from third parties as well.

In addition to client-driven, specialised portfolio construction, Parametric votes and engages with companies in a manner to encourage high environmental, social and governance standards. Parametric also offers clients the opportunity to participate in filing shareholder resolutions, should they choose to do so.

GLOBAL FIXED INCOME

While the Global Fixed Income team runs an engagement programme that spans across multiple fund holdings, they also manage multiple client mandates with tailored sustainability objectives and/or criteria, which include specific requirements on engagement, such as conducting a minimum number of meetings with portfolio companies per quarter, thematic priorities aligned with the client's ESG policy, or bespoke engagement reporting formats. As an example, a large European client requested the team to engage with carbon-intensive investee companies, in support of the mandate's low-carbon objective, to ensure the companies' emissions reduction targets are aligned with the Paris Agreement and that the companies abide by their commitments.

GLOBAL LISTED REAL ASSETS

The Global Listed Real Assets team actively works with separately managed account clients to customise investment guidelines and requirements through the client onboarding process, taking into account a number of factors, including client sustainability and proxy voting needs. For example, one client's mandate includes an ESG-based exclusion list provided by the client, and a commitment for the Portfolio to have less carbon exposure relative to the Reference Index, with a further goal of reducing this exposure relative to the Reference Index over time. In addition, the team provides clients with the flexibility to vote proxy themselves if that is their preference or to have MSIM vote proxy on their behalf according to the MSIM Proxy Voting Policy.

The Global Listed Real Estate team has also published several papers, which discussed sustainability in part, including sections on how REITs can make a difference in the context of sustainability.

PRIVATE REAL ESTATE

Building operations and construction account for approximately 40% of global energy-related CO_2 emissions, according to the United Nations Environment Program.[23] In order to keep global warming limited to 1.5°C by 2050, aligned with the Paris Agreement, it is

[23] World Economic Forum.

estimated that real estate's direct carbon emissions will need to reduce by 50% by 2030.[24] Morgan Stanley Real Estate Investing ("MSREI") seeks to manage the environmental footprint of assets in a way that enhances financial value and reduces negative impacts while maximising value to investors and the communities in which the funds operate. Interest in transitioning investment portfolios to net zero by 2050 is accelerating among the investor community. Select MSREI funds have set 2050 net-zero aspirations and interim Scopes 1 and 2 carbon reduction targets.

PRIVATE INFRASTRUCTURE

MSIP is a founding participant of the Global Real Estate Sustainability Benchmark ("GRESB") Infrastructure Assessment and has participated in its surveys since inception in 2016. GRESB participants are scored on their ESG policies, management practices and performance. The GRESB Infrastructure Assessment covers a range of asset types, including energy generation, energy transmission and distribution, transportation, telecommunications, water and waste treatment, and social infrastructure. It is an investor-led benchmark, not an industry network/initiative, which provides the type of credibility its clients require. Given the importance of GRESB benchmarking assessments to clients, these are shared with MSIP clients upon request.

In addition, MSIP contributes to the Infrastructure Module of MSIM's UN PRI annual survey, which looks at responsible investment implementation during fundraising, pre-investment processes and post-investment processes. Given clients' interest in PRI, which is a widely recognised framework for responsible investing, PRI infrastructure reports are shared with MSIP clients upon request.

MSIP also publishes an annual ESG Report for its investors, which highlights MSIP's approach to ESG integration throughout the investment life cycle and provides an annual update on MSIP's ESG focus areas and key accomplishments.

Bespoke Client Requirements

Bespoke client portfolio monitoring and screening requirements are also taken into account, once agreed, when we take on board new clients. As mentioned in Principle 2, our Portfolio Surveillance team oversees and ensures all ESG screening and monitoring guidelines are agreed to between investment teams and clients at the outset of client onboarding, implemented and continuously monitored throughout the mandate. This means working with different functional stakeholders; e.g., our investment teams, who share the client requirements to be implemented for the management of the client account, and Technology/Data teams to ensure our system capabilities and coding of ESG rules/requirements are created/feasible. A few examples of onboarding new ESG rules and guidelines for client mandates include:

- **Equities strategy: Client's restriction requirements regarding specific controversial sectors**
  - Under this scenario, the client described what they wanted to restrict, and relied on MSIM to suggest the most appropriate method of monitoring
  - The Portfolio Surveillance team discussed with the relevant investment team and the Sustainability team and came to an agreed monitoring framework best suited to the client's restriction requirements
  - For requests like these, at times, MSIM may need to feed new data points into our system to capture client specifications, and these data points may come from third-party ESG data providers
- **Fixed Income strategy: Customised restriction and monitoring requirements**
  - In some cases, the team agrees with clients to implement an automated monitoring mechanism using vendor data within our Compliance tools; however, on rare occasions, we also agree to monitor based on the clients' own restricted list and methodology
  - Some clients prefer the latter option if they are dealing with multiple sub-advisors and want to ensure that all are excluding the same list of companies

To monitor and ensure that client requirements are properly adhered to, an escalation process is in place, where issues are immediately raised to the investment team as part of protocol that includes MSIM Compliance, MSIM Risk, and the MSIM Sustainability team and Sustainability Oversight. Any confirmed issues would be further escalated to senior management through a specific escalation channel.

Communicating With Our Clients About Our Stewardship Activities and Continuous Reviews

From a broader MSIM perspective, consistent with our pledge to have a clear investment process, we also pride ourselves on being available to our clients and providing them with regular and timely information on our services and stewardship activities. Collective stewardship and sustainable investing updates are consolidated and

[24] Global Alliance for Buildings and Construction – 2021 Global Status Report for Buildings and Construction.

SPOTLIGHT NO. 2

Portfolio-Level Sustainability Reporting

Client reporting on fund-level ESG and Stewardship metrics varies based on both the investment team and fund strategy. These portfolio reports may be available to clients, both regularly or upon request. Examples from various investment teams include:

INTERNATIONAL EQUITY

- The International Equity team produces quarterly ESG fact cards for its Global Sustain strategy, as well as for the Global Brands/Global Brands Equity Income and Global Quality SICAV funds. As noted above, the International Equity team also publishes a biannual engagement report, Engage, detailing its engagement activities. All of these documents are available to clients on the MSIM website.
- Additionally, the team works closely with clients to meet their bespoke ESG reporting needs, as well as providing in-depth data and reporting to U.K. pension fund clients for use in their TCFD reports, Statement of Investment Principles and annual Implementation Statement requirements.
- The team meets regularly with its clients, providing a platform to respond to their individual questions. Engagement and proxy voting activities are covered in the team's quarterly client calls. In addition to the previously mentioned thematic insight papers, the team also uses its monthly Global Equity Observer piece to provide updates to clients on ESG-related activities; for example, this year's articles on the team's carbon transition engagement programme, on DE&I, and on proxy voting.

GLOBAL FIXED INCOME

- The Fixed Income team recently published an inaugural 2021 Engagement Report, providing insight on how the team engages with companies, governments and other organisations on ESG issues, in alignment with MSIM's Engagement Thematic Priorities (please see Principle 9 for more details).
- The team provides quarterly reporting on its Fixed Income engagement programme to existing clients, either as part of periodic portfolio reviews or upon request, highlighting the thematic nature of the team's dialogues, its impact on the team's investment strategy and ad hoc case studies.
- The team also provides clients with a detailed portfolio-level ESG report, which includes a detailed dashboard with ESG KPIs, as well as charts on portfolios' carbon footprint and other climate-related characteristics, in alignment with the UN Sustainable Development Goals (SDGs), and exposure to green/sustainable bonds, among other characteristics. ESG reports are generally made available to clients on a quarterly or, if required, monthly basis.

GLOBAL BALANCED RISK CONTROL

- For the Global Balanced Sustainable Fund, GBaR monitors the ESG and Carbon Risk for its direct holdings using third-party ESG data. For this fund, the team is able to report to clients on various metrics, such as ESG ratings, Low Carbon Transition scores and Weighted Average Carbon Intensity.
- GBaR is also able to provide additional metrics that are not directly associated with its investment process, such as reputational risk, governance risk, fossil fuel reserves and exposure to high water risk.
- Additionally, the team publicly reports on its Stewardship activities on an annual basis.

PRIVATE CREDIT AND EQUITY

- PC&E recently published its inaugural 2021 ESG Report, which details how ESG is integrated throughout the investment life cycle across strategies (where relevant), PC&E's governance structure, ESG-related partnerships around ESG, and select case studies that highlight the impact PC&E has had through its work with portfolio companies.
- Clients may request that the PC&E teams take further action in the form of increased transparency and reporting (e.g., according to IFC principles, in alignment with TCFD or specific reporting pertaining to modern slavery). These requirements are discussed and agreed upon through side letters with clients when the LP commitment is made to the strategy.
- PC&E will typically include a panel discussion addressing relevant ESG topics during its annual investor conference, and strategies may provide LPs with significant ESG updates during their annual meetings.

PRIVATE REAL ESTATE

- Morgan Stanley Real Estate Investing participates in the annual GRESB Real Estate Assessment, an investor-led, global ESG benchmark used to measure the ESG performance of individual real estate assets and portfolios based on annual self-reported data. The data is validated by GRESB, awarded a score per entity and benchmarked against peers. The benchmark report may be shared with clients, given increased demand to analyse ESG performance.

PRIVATE INFRASTRUCTURE

- Morgan Stanley Infrastructure Partners publishes an annual ESG report for its existing Limited Partners ("LPs"), which highlights MSIP's approach to ESG integration in addition to updates on the team's ESG focus areas and key accomplishments.
- The team also shares with clients GRESB benchmarking assessments on portfolio companies' ESG performance,

as well as the team's infrastructure PRI reports upon request.

CALVERT RESEARCH AND MANAGEMENT

- Calvert reports on its annual firm-wide stewardship activities in its annual Tools of Change report, which outlines the challenges companies face today, and how Calvert ascertains how they are positioned to respond to these challenges and to allocate capital in a manner that drives positive change.
- To better align marketing documents globally, given Calvert's product launch into EMEA in 2022, Calvert's impact (ESG) fact sheets, which are distributed for its U.S. mutual funds, will soon be extended to all its public mutual funds (where data permits).
- In addition to this, Calvert makes specific tools available for clients and/or financial professionals to analyse and compare products and metrics. These include:
  - the Calvert Impact Tool, which allows users to measure the impact of their investment in a Calvert index as compared to the broad market index (e.g., carbon emissions, water, waste exposures); and
  - the Calvert Transparency Tool, which allows financial professionals to compare open-ended mutual funds and ETFs across traditional financial characteristics, ESG metrics and proxy voting.
- Calvert also offers in-depth, custom ESG reporting to separate account clients, tailored to the portfolio's specific themes and objectives.

PARAMETRIC PORTFOLIO ASSOCIATES

- Currently, Parametric offers ESG reporting on firm-wide stewardship activity (annually) and client-driven portfolio construction incorporation (quarterly).
- Examples of other custom client reporting include carbon footprint/emissions reporting, Sustainalytics ESG risk ratings, Sustainalytics portfolio reporting, modern slavery reporting and proxy voting reporting.
- Parametric has industry-leading, digital reporting platform experience, which is available to clients, and also includes ESG reporting metrics. The team receives and implements feedback from clients on aspects of this platform that can be enhanced and evolved.

integrated into regular communications with our clients. These regular touchpoints include: annual or biannual client meetings; our annual client conference; quarterly conference calls (in the case of certain strategies); portfolio-level sustainability reports; and monthly information packages.

Client relationship managers and investment teams are also available to connect with clients outside these scheduled touchpoints. Through their regular client interactions, our investment teams have observed the increasingly prominent role that stewardship plays in our asset owners' investing objectives and that has informed the magnitude of our efforts in this space. Our investment managers enjoy access to global research and company management, and have firsthand experience in the world's capital markets, which translates to more opportunities for our clients.

Our annual client conference, IDEAS, increasingly includes dedicated sustainable investing forums and panels that showcase our portfolio managers' approaches to stewardship. We also have MSIM Mini IDEAS in Amsterdam, Paris, Madrid and Canada for a smaller, regional conference format. These forums provide an opportunity for client dialogue on important and emerging governance and sustainable investing topics, and our portfolio managers may use these opportunities to inform their stewardship agendas.

In 2022, we hosted additional events continuing to build on these important client relationships, by catering to topics that are most meaningful to our clients. Some of these were/will be conducted cross-divisionally with our Firm colleagues to deliver a holistic One MSIM, including, but not limited to:

- **MSIM Institute** – a training programme targeted for members and representatives of institutional investors, such as sovereign wealth funds and central banks
  - This provides an opportunity for our clients to engage with our global investment experts on a number of front-of-mind topics and themes across asset classes; e.g., the Rise of Intangibles: Strategic and Financial Implications; 10 Key Themes for Investing in Global Equities; Managing Credit Risk in Portfolios; Overview of Private Markets; Navigating Sustainable Investment Trends in 2022 and Beyond; and Sustainable Investing in Practice, etc.
- **ESG in Action Workshop Series** – The Three I's Approach and Framework to Engagement in Fixed Income, a virtual ESG workshop by the MSIM Head of Sustainable Investing
  - This focused on the Fixed Income team's "Integrated, Insightful and Influential" engagement approach, and how effective engagement with bond issuers can drive change; and
  - Bond issuer engagement case studies on tackling ESG challenges and carbon transition risk were also shared.

- **Morgan Stanley Sustainable Investing Summit –** including a dedicated MSIM half-day virtual event featuring ESG capabilities and thought leaders across our investment teams and businesses
  - The goal is to gather industry leaders to share ideas and insights about innovations in sustainable finance.
- **Morgan Stanley Executive Women's Conference –** where women business leaders presenting more than $5 trillion in market cap and $40 trillion in assets gathered to discuss at the nexus of change to share ideas, lessons and inspiration
  - This year's discussions included the pandemic and its economic consequences, the importance of social justice, greater boardroom diversity, navigating the metaverse economy, and leading with authenticity and purpose
- **Morgan Stanley Asia Pacific Summit** – the firm's flagship client event in Asia (since 2002) bringing clients together with policymakers, industry experts, thought leaders, corporate leaders and senior global investors exchanging views and sharing insights on topics that will shape the future. There were 4,700 attendees globally, including 550 corporate representatives and 3,000 investors at our last event in November 2021
  - Dedicated ESG sessions were conducted with keynote track presentations, fireside chats and panel discussions on developments in Asia and key industries, including countries' net-zero/carbon neutrality goals and measures governments implement to achieve this
  - The success of the Summit reflects the Firm's ranking as the No. 1 Best Asia Corporate Access Provider in Institutional Investor 2021

In addition to these dynamic client touchpoints, our MSIM U.K. Stewardship Report itself is the most comprehensive report on our collective global sustainability/ESG, engagement, proxy voting and stewardship activities across our investment platforms. Our last U.K. Stewardship 2021 report was shared with clients after receiving the FRC's approval with positive client feedback on our progress, activities and outcomes. As mentioned above, individual investment teams may also publish team- or strategy-level engagement reports for clients, and provide engagement information and case studies on request.

All of these regular touch points by MSIM, as well as individual investment teams, also serve as opportunities to address client queries, such as impact of certain geopolitical or market events impacting portfolio holdings; portfolio managers' outlook on certain asset classes, companies or industries; as well as details on portfolio performance. We continuously seek client feedback on all communication fronts (outlined above) to ensure that we deliver the highest level of client satisfaction through our sustainability/ESG and stewardship approach, investment products, client relationship management and client reporting solutions. Our Strategic Relationship Management team leads the development of meaningful relationships, customised per individual client needs.

Effectiveness of our Client Communication Methods

We have assessed the effectiveness of our chosen methods to communicate with and understand the needs of our clients, using factors such as direct client feedback, the scale and spread of our AUM across different regions and investment platforms (for example, due to increased ESG priorities and preferences across our investor and client base, we are seeing increased demand not only for our Sustainable Investing products but for bespoke reporting that will assist our clients' respective regulatory and stakeholder reporting/transparency requirements) and our ability to access our client and investor base (ranging from separate account clients with dedicated MSIM relationship managers to investors in our funds who are able to communicate with us through investor forums and conferences).

We consider that our chosen communication channels and approaches have been effective in taking into account clients' sustainability and stewardship needs. We believe this is demonstrated firstly in the successful implementation and scale of our bespoke investment solutions, custom portfolios, multi-asset strategies and outcome-oriented accounts for clients—which, as of 30 June 2022 consists of $703 billion in AUM, half of our overall AUM.

Secondly, the expansion of our investment platform to launch European Private Credit and ETF businesses is testament to our response to client demand for a broader set of investment capabilities and vehicles to access (Principle 2) and our commitment to aligning our sustainability/stewardship ethos and approach with client interest and requirements.

Thirdly, this is also evident from the long-standing relationships we have with many of our key clients, who have been invested in our strategies for decades—across different investment teams, either within a client capacity or as co-investors, alongside our investment teams. Our oldest legacy MSIM mandates date back to the 1980s, capital we have managed for approximately 40 years.

We intend to continually engage with our clients to get their feedback on both how well we communicate with them and how we reflect their views and priorities in our management of their portfolios. An example of this is our internal sustainability regulatory project workstream, which has been created to:

- Operationalise, document and implement client sustainability preferences as part of client suitability assessments, in response to the upcoming EU MiFID II revisions, which begin to come into effect from August 2022; and
- Prepare, draft, track and report EU SFDR Level 2 product and entity disclosures, which came into effect on 1 January 2023.

This workstream consists of stakeholders across functional teams, including our MSIM Head of Sustainability Regulation and Policy, MSIM Sustainability team, Product Development, Legal/Compliance, Sales Management and ESG Data/Technology teams who work together to ensure relevant MSIM product information and data are tracked, monitored and measured—so that clients can make better and more informed investment decisions when it comes to selecting their sustainability preferences.

We are also aware that due to different regulatory reporting requirements in different jurisdictions, there is potential for asymmetry of reporting and information shared with clients in different jurisdictions. For example, in the EU, SFDR Level 2 enhanced reporting came into effect on 1 January 2023, while in the U.S., the SEC has only released its Statement on ESG Disclosures and ESG Fund Names this year. In the U.K., the Sustainable Disclosure Regulation ("SDR") was proposed late last year, with a further consultation expected in Q4 of 2023. The different types of reporting proposed/required and corresponding regulatory effective dates mean that MSIM will have to prepare different types of ESG reports for investors/clients in different jurisdictions, which could result in information asymmetries on a jurisdictional basis and, in particular, could be challenging for our clients with global mandates and footprints. This remains an ongoing challenge, that we expect will worsen over time as different jurisdictions, regions and regulations are at different stages of the sustainability journey, with some also not seeing ESG as a priority. To this end, we are assessing how we can ensure compatibility and consistency of disclosures across jurisdictions, and are conducting more research into our global client views through various channels, particularly our investment teams in their client communications to gain a better understanding of clients' needs from a global perspective, which will, in turn, better inform and help strategise our global reporting and communications capabilities, supporting consistency and transparency across the board.

It is our ongoing and continuous engagement with clients that enables us to meet their evolving needs in adherence to our Firm-wide core value of "Putting Clients First."

PRINCIPLE 7

Stewardship, Investment and ESG Integration

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

ESG Integration, Portfolio Management and Stewardship

Although issues prioritised during stewardship and investment decision-making vary across different MSIM investment teams, as noted previously, our investment teams will be guided by the MSIM-wide Sustainable Investing Policy and Engagement and Stewardship Principles. Our investment teams act as responsible long-term investors and are particularly responsive to ESG factors that can present both risks and opportunities to investment portfolios.

MSIM adopts a tailored approach to ESG integration and stewardship, whereby public and private investment teams are ultimately responsible for exercising their judgement to identify and integrate materially relevant risks and opportunities into their investment decision-making process, including due diligence and research, valuation, asset selection, portfolio construction, and ongoing engagement and investment monitoring. MSIM assesses materiality in the context of ESG integration and stewardship through the consideration of various factors, such as investment philosophy, asset class, the nature of the issuer, the size of our holding, the exposure to sustainability risk (including both physical and transition risks) and the investment time horizon.

The following examples demonstrate the different types of issues, ESG factors and stewardship methods prioritised by investment teams across asset classes and geographies throughout the investment process generally and during the reporting period.

HIGH-CONVICTION EQUITIES

MSIM's High-Conviction Equities teams comprise generalists, as well as sector or regional specialists, who assess materiality of ESG factors and utilise company-level research to develop investment strategies that seek to create and capture value while reducing risk. The investment teams view engagement with senior management of companies to be an integral component of their role as long-term owners, including engagement on material ESG issues. All equity teams seek to support good governance at portfolio companies through diligent attention to proxy voting responsibilities, for which MSIM provides centralised support.

For our equity teams, stewardship continues to be an integral component of the investment process. As long-term investors, with an owner's mindset, their active engagement is aligned to their long-term investment approach. A key input to their investment selection process is an assessment of the quality of the company's board and senior management. To develop that knowledge, equity teams engage with company management at regular intervals and prioritise active dialogues where positions are significant and issues are viewed as material. Voting decisions in equity portfolios are made in-house by the investment teams, with support from the Global Stewardship team, and in line with the principles addressed in our MSIM Proxy Voting Policy. Further, our equity teams directly engage with their portfolio companies on sustainability topics. As fundamental investors, teams typically take a company-by-company approach to ESG research and engagement, focusing on material issues most important to a particular company. At times, portfolio managers may also address a topic thematically across their portfolios, taking a top-down approach to an emerging systemic risk or area of concern. For example, for our Emerging Markets Equity team, engagement is also shaped by the team's country-level ESG analysis, which may bring into focus specific ESG issues above and beyond what the team's sector-based materiality analysis alone would have indicated.

While engagement and Sustainable Investing approaches differ across our individual High-Conviction Equity teams, all have appointed Sustainable Investing leads who co-ordinate and support their respective team approaches.

The following equities strategies demonstrate the diverse approaches taken with respect to ESG integration in investments and stewardship:

a) International Equity

When integrating ESG analysis into the investment process, the team explicitly focuses on material ESG risks and opportunities and their effect on the sustainability of future returns on operating capital. The team believes that seeking to understand how ESG factors may impact long-term returns has to be rooted in company-specific analysis.

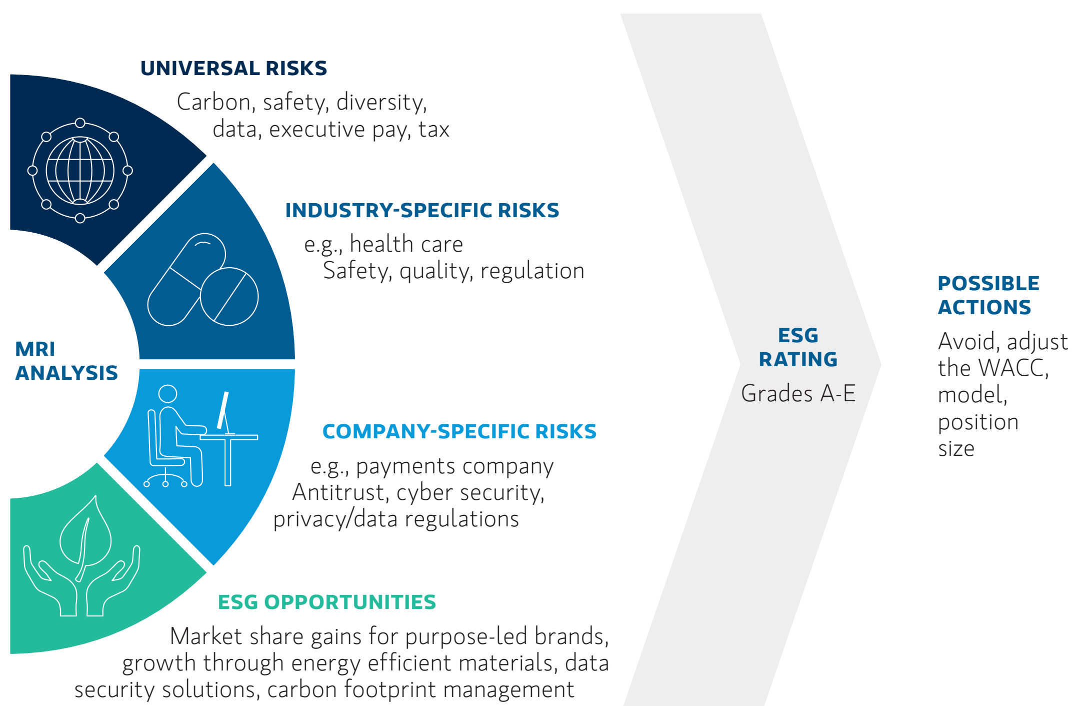
As noted under Principle 4, as part of the team's research process, they have developed a proprietary ESG scorecard, called the Material Risk Indicator (see *Figure 7.1*), which supplements the existing qualitative and quantitative outputs of their research process.

For each company held in their global portfolios, the team attempts to identify both industry-specific ESG factors/risks, such as product safety in Health Care (Portfolio Manager/analyst determined), and key universal ESG factors/risks (team agreed), including greenhouse gas emissions, management compensation and incentives, diversity/culture, safety, data security/privacy and tax. Quantifiable ESG data is also analysed, including the carbon tax impact on EBIT at $100/t of CO_2e, the company's Equileap[25] gender equality score, the impact of normalised global tax rates, and the company's Pay X-ray score. Pay X-ray is the team's proprietary scoring framework for executive pay, used to better compare company pay plans, facilitate team discussions and inform their voting approach. As a streamlined scoring system, it enables the team to flag good and bad practices and rank their holdings' remuneration plans. Elements of the plan receive a positive or negative score, rolled up into an overall company score. The team then uses this score to determine their decisions when voting on remuneration. Should the team have voted against remuneration previously, and observed no change in the company's remuneration plan, they may then escalate their actions, voting against the election of members of the remuneration committee.

FIGURE 7.1

Proprietary ESG Material Risk Indicator Analysis

- Proprietary scoring framework standardises ESG assessment of companies
- Grades are assigned across sectors, rather than intra-sector relative
- Stock-specific analysis allows for ESG engagement and assessment over time



Source: Morgan Stanley Investment Management. The views and opinions expressed herein are those of the portfolio management team, are not representative of the firm as a whole, and are subject to change at any time due to market or economic conditions. There is no assurance that a portfolio will achieve its investment objective or an investment strategy will work under all market conditions.

[25] Equileap is a leading third-party provider of data and insights on gender equality in the workplace.

The MRI helps to identify material ESG risks and opportunities at the company level, and reflect these in valuation and portfolio construction, if appropriate. It also enables portfolio managers to identify priority areas for future engagement with company management. The framework enhances the team's ability to manage downside risk, as well as increase the potential for long-term growth.

Consideration of climate risk is also an important consideration for the team. For example, they monitor the sensitivity of their companies' profits to potential future carbon pricing, which remains very low. Geography, regional allocations and country weightings are not key decisive factors in the integration of ESG and stewardship, as both are products of the team's bottom-up stock selection process.

Information gathered through ESG analysis and stewardship contributes to the team's acquisition, monitoring and exiting decisions. The underlying philosophy (which is also shared across other MSIM investment teams) is to always ensure and maximise clients' portfolio returns, given MSIM's client-centric business purpose. New investment ideas are generally discussed and debated at the weekly investment meetings. A research report outlining the stock's investment case is circulated amongst the investment team prior to the investment meeting, which includes a description of the business, an assessment of the franchise and management quality, strengths and risks to the investment case, insights from meetings with management, historical versus projected key financial ratios under various assumptions, and an assessment of the stock's intrinsic value. ESG risks and opportunities are documented, with reference to ESG data when appropriate.

A stock may be reduced or liquidated if one or more of the following occurs:

- The intrinsic value of the stock has been exceeded;
- Regulatory environment/industry deterioration;
- Absolute risks, including ESG risks (such as climate risk), have exceeded the team's tolerance level;
- The investment thesis has changed materially for the worse, or been proven wrong; and/or
- Another stock idea is more compelling.

Case Study – Sustainable Investments and Third-Party Data

Under the upcoming implementation of Level 2 of the EU SFDR in January 2023, all of the International Equity team's Global Equity SICAVs will be categorised as SFDR Article 8. In preparation for the related disclosure framework, the team has identified minimum commitments for the percentage of each relevant portfolio that will be classified as sustainable investments (as defined by SFDR). The team has created a framework and determined a methodology that it will use to assess its global holdings against the SFDR sustainable investment definition. This has necessitated the identification and use of third-party data sources for this specific purpose. Having assessed and interrogated the ESG data and analysis available from third parties, the team acknowledges that, while some third-party data can be useful, data quality and availability remain a limitation. However, given the need to access such data in order to complete their sustainable investment SFDR disclosure framework, the team seeks to address such limitations by cross-checking different data sources, as well as company disclosures, where necessary.

While, as referenced earlier in this document, the team uses some third-party data sources—for example, Trucost carbon data in its MRI—the team does not rely on third-party ESG conclusions when conducting the in-depth fundamental research that drives its investment process, preferring instead to draw its own conclusions in terms of relevance and materiality, often using engagement as a method of reinforcing its views.

b) Counterpoint Global

As mentioned in Principle 1, Counterpoint Global takes a long-term oriented approach to investing, focusing on identifying differentiated insights on multiyear opportunities. The team believes that environmental awareness and social responsibility are important stewardship issues, and innovative companies can use sustainability initiatives and programmes to differentiate its franchises in the marketplace. Hence the team employs sustainability research additively within their investment process—acknowledging that environmental and socially-oriented initiatives within companies can be drivers of value when those initiatives capitalise on:

- **MOAT EXTENSION**
  Example: increasing the switching costs from smart buildings' efficiency data
- **GROWTH OPPORTUNITY**
  Example: a new market such as mobile-based financial services for the under-banked population
- **EFFICIENCY OPPORTUNITY**
  Example: a profitability enhancer such as energy efficiency practices in cloud computing, and
- **OPTIONALITY**
  Example: making plant-based protein more widely available.

The team's Sustainability Researchers, together with investors on Counterpoint Global that cover different companies, are responsible for sustainability research and integration for respective investments. This way, the team is able to leverage investor expertise to identify opportunities and risks presented by environmental and social trends, and use them as a basis to monitor investments, as well as engage with investee companies. Counterpoint Global believes investing for the long term aligns with interests of long-term shareholders, which often means focusing on disruption and sustainability themes.

c) Global Opportunity

The Global Opportunity team's investment process integrates analysis of sustainability with respect to disruptive change, financial strength, and environmental and social externalities and governance (also referred to as ESG). The investment team views ESG as a component of quality and considers the valuation, sustainability and fundamental risks inherent in every portfolio position.

As bottom-up investors, the Global Opportunity team does not outsource ESG analysis to third-party providers of sustainability ratings that produce scorecards ranking companies versus industry peers. Based on the

FIGURE 7.2

Proprietary HELP ACT Framework

WE CARE HOW COMPANIES HELP & ACT

H ealth: Improve humanity's quality and duration of life
E nvironment: Protect the planet and its inhabitants
L iberty: Human rights, equality, freedom and privacy
P roductivity: Improve our knowledge of how the universe works to make our lives better within it
&
A gency: Skin in the game and incentives to work on behalf of long-term shareholders
C ulture: Encourage a culture of innovation, adaptability and shared values
T rust: Reliability of financial statements and management

FIGURE 7.3

Proprietary HELP ACT Framework—SDGs

HELP & ACT is informed by the Sustainable Development Goals (SDGs) adopted by the United Nations in 2015, composed of 17 goals and 169 targets to be achieved by 2030 with the aim "to end poverty, protect the planet, and ensure prosperity for all."

Source: United Nations The content of this publication has not been approved by the United Nations and does not reflect the views of the United Nations or its officials or Member States. See https://www.un.org/sustainabledevelopment/sustainable-development-goals for more details on the Sustainable Development Goals.

investment team's analysis, such ESG ratings are derived from dozens of metrics and hundreds of ESG data points, thus such approaches may reward corporate issuers with high rates of disclosure rather than businesses with sound operational performance. In the investment team's view, ESG ratings approaches risk leading investors to inconsistent and misleading conclusions. Therefore, Global Opportunity deems disclosure rates to be of lesser importance than potential material risks to company fundamentals.

The Global Opportunity team's quality assessment identifies the key ESG-related opportunities and risks for each prospective investment based on materiality to the long-term fundamental drivers of the business. Using the team's proprietary framework, HELP & ACT (please see *Figures 7.2* and *7.3* above), the Global Opportunity team analyses potential impacts to humanity's health, environment, liberty and productivity, and governance measures to ensure agency, culture and trust, framed by a set of questions applied consistently across companies.

In company engagements, investment team members typically discuss topics specific to each business, such as how an e-commerce platform is implementing a sustainable packaging initiative to reduce waste, how a semiconductor firm is investing in offshore wind power to achieve carbon reduction projects, or how a bank's products and services address financial inclusion in developing economies. Examples of general questions the team typically asks company management teams include:

- What is your most material ESG opportunity?
- What is your most material ESG risk?
- How are management incentives aligned with shareholders?

The Global Opportunity team publishes an annual report that discusses ESG integration within the investment process using the HELP & ACT proprietary framework, company engagement, and the carbon footprint of the portfolios, and summarises participation in collaborative initiatives and relevant MSIM policies.

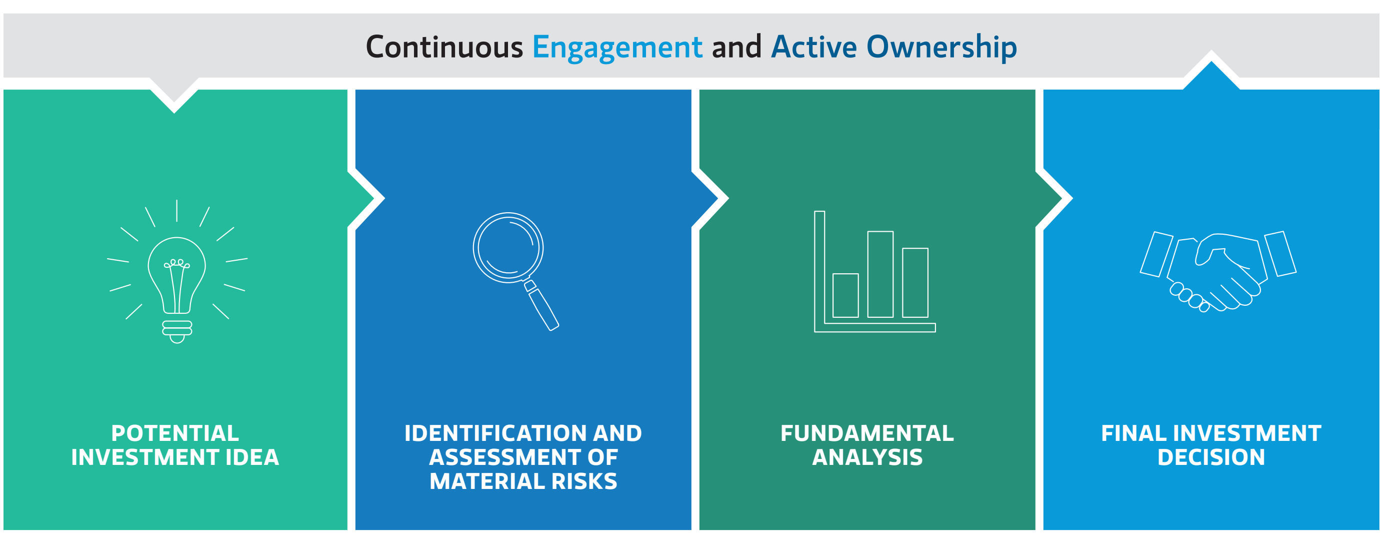
The team also published a white paper titled ESG and the Sustainability of Competitive Advantage, which describes how the team integrates ESG factors into their investment process.

d) Emerging Markets Equity

The EME team manages both funds that integrate ESG as well as Sustainable funds with measurable positive environmental and/or social objectives.[26] Both types of products integrate ESG globally, and do not prioritise certain geographies over others. In addition to this, both also have exclusions based on negative ESG characteristics that are incompatible with the goals of the funds—such as those that do significant harm to humans

FIGURE 7.4

EME ESG Approach



[26] Please see our MSIM Sustainable Investing Policy for more details on our Sustainable Investing framework.

or the environment. EME's Sustainable funds prioritise companies that are aligned to the team's sustainable development themes, and may additionally choose to exclude companies with financially material ESG issues, which may affect the team's sustainability analysis.

The investment team believes companies with forward-looking management teams that have proactive sustainability strategies should be better positioned over the long term, relative to industry peers, to address business risks and opportunities. The team looks for company management teams in quality businesses that understand long-term environmental and social trends and integrate these considerations into their strategies.

The EME team's ESG and sustainability research informs its engagement strategy, which seeks to understand the sustainability strategy and financially material issues for each company, pressing for change where it aligns with long-term shareholder value and tracking progress over time (please see Principle 9 for more details). Furthermore, the team's assessment of the company's sustainability strategy and progress is a key input into their investment decision-making.

For ESG materiality, EME identifies and assesses qualitative and quantitative company-specific factors on environmental impact, social responsibility and governance, including management quality with respect to sustainability. More specifically, factors the team examines can include, but are not limited to, carbon emissions, environmental footprint (e.g., water usage, recycling practices, waste to landfill), worker safety, employee retention and turnover, supply chain management, and board independence and composition. To identify and assess these ESG issues, EME refers to third-party sources (such as MSCI, Bloomberg and ISS), company financial reports and disclosures, as well as the team's own internal research, which can include dedicated company-specific engagements with management on ESG.

Over the past year, EME has undergone three main initiatives: building out its Sustainability team, defining sustainable alignment, and furthering engagement and integration research. In mid-2021, EME named one of its co-lead portfolio managers as the team's Head of Sustainability. EME's Head of Sustainability has been researching EM companies and countries with the team since 1997 and has been a co-lead portfolio manager since 2008. The team also hired a dedicated engagement lead and research associate and, this year, another junior analyst, to focus on decarbonisation pathways and sustainability data. In addition, one of the team's portfolio specialists, who has been with EME since 2011, has been fully dedicated to the Sustainability team, helping to build its sustainability frameworks amidst a complex regulatory environment.

For EME's Sustainable funds, the team has identified several sustainable themes of which it seeks to align the portfolio after the initial negative screening process. EME seeks companies that contribute positively to several sustainable themes, including, but not limited to, responsible energy, access, affordability and sustainable economic growth, decent work and innovation, and sustainable production and circular economy. To identify names in this category, the team looks for businesses that are aligned by revenue exposure and/or business operations to EME's identified sustainability themes. The team uses both third-party data (such as MSCI and Bloomberg), as well as company disclosures, to measure alignment with these themes. From this list, the team also assesses minimum social safeguards and principal adverse sustainability indicators to define the percentage of the portfolios that are sustainable.

Over the last 12 months, EME has deepened integration of ESG into its investment process. The team has further developed its framework of materiality and is moving from baseline engagements, or engagements on a wide array of issues, to more targeted ones. This is evident in the team's engagement data as shown in Principle 9.

ESG Data
In terms of limitations to the team's process, data still remains difficult to assess or quantify, specifically social metrics such as gender pay gap, or climate change scenario analysis. EME engages with third-party vendors and portfolio companies on these data gaps often, and seeks to provide input into tools that might help better assess financially material ESG issues.

ACTIVE FIXED INCOME & LIQUIDITY
The platform has developed proprietary ESG scoring methodologies for corporate credit, sovereign, securitised and sustainable/green bond issuers. Across these methodologies, the focus is on reflecting the relative materiality of E, S and G factors at the sector/asset, class/deal level, rewarding positive sustainability momentum, and penalising exposure to severe ESG-related controversies that can adversely impact bond price or liquidity. These scores inform the portfolio construction process and investment decision-making across the entire Fixed Income platform and for select Liquidity funds.

The team considers meeting management as an integral part of its investment analysis, including within its evaluation of the ESG credentials of issuers. The trading desk maintains relationships with the banks that underwrite and distribute new bond issues. Once a new bond issue is announced, the trading desk is alerted and one of the sector credit analysts is assigned to cover the issue. The analyst will typically review roadshow materials (such as presentations and offering memorandum) and attend a roadshow to meet with the management team. These meetings represent an opportunity for analysts to complement data-driven ESG scoring models with a more qualitative assessment of bond issuers' efforts and progress on sustainability issues. The roadshows offer the analysts the opportunity to ask questions to management relating to the sustainability strategy and targets of the company and/or the new issue, and to clarify any uncertainties within the structure of the issue. Furthermore, team members provide feedback to the issuer during these roadshows, and gain additional ESG insights in particular since the roadshow meetings provide opportunities to align the messaging with other potential investors. The team also regularly engages with issuers of labelled Green, Social, Sustainability and Sustainability-Linked Bonds ("Sustainable Bonds") to promote their alignment with market standards for project/indicators selection and impact reporting.

In addition to regular meetings with company management and treasuries as part of the credit update and investment analysis process, the team also runs a targeted engagement programme that aims to target companies with lagging practices on specific environmental, social or governance issues, in order to set clear expectations around how such concerns can be addressed.

The programme is based on the Fixed Income Engagement Strategy, published in 2020, and focuses on four main themes, in line with *MSIM's thematic priorities* for sustainable investing:

- Decarbonisation & Climate Action;
- Circular Economy & Waste Reduction;
- Diverse & Inclusive Business; and
- Decent Work & Resilient jobs.

Further details on MSIM's thematic priorities are outlined in Principle 9.

In light of regulatory developments, such as the EU SFDR, the team has been increasingly focusing, within these themes, on environmental and social factors that are associated with Principal Adverse Impact indicators, with the intention to mitigate portfolios' exposure to issuers that may do significant harm to such factors. These include, for example, a scale-up in engagement focused on carbon emissions reduction across Scopes 1, 2 and 3, and on the phase-out of fossil fuels, as well as on human and labour rights monitoring along supply chains, in the context of compliance with international norms, such as the U.N. Global Compact or the OECD Guidelines for Multinational Enterprises.

In addition, the Fixed Income team views governance as the pillar from which strong credibility is built across any other environmental and social topic. The team therefore diligences corporate governance, transparency and accountability, and disclosure matters across its dialogues with issuers, also focusing on how they link executive compensation to specific sustainability KPIs and targets.

It is important to note that the team's engagement strategy is defined at a global level, but implemented by the Credit Analysts based on their regional and sectoral coverage, with the Fixed Income Sustainable Investing team supporting them in the preparation of the meetings, attending selected ones and maintaining a centralised tracker of engagement activities for monitoring and reporting purposes.

The team accounts for regional differences in their approach by considering the stage of development of the issuer's country, to ensure that their assessment of their sustainability strategy and targets is contextualised and comparable to peers.

For example, the team recognises that in some emerging markets, a longer glide path might be necessary to achieve desired sustainability outcomes and minimise negative externalities, or there may be a need for engaging in issues related to capital markets policies and processes to facilitate their functioning. This can manifest in the form of a longer phaseout period for fossil fuels in order to continue providing affordable energy to the broader population, more time to improve diversity of a company's board of directors or management team, reflecting the need for a broader change in culture, or trade-offs between job creation and land use, among others.

By way of example, the team engaged with an emerging markets metals and mining company in 2Q22, given serious concerns over tailings disposal (e.g., how waste materials, such as crushed rock accumulated in the process of extracting core minerals, are disposed of) and human rights abuse. The company had outlined some actions they aimed to initiate, such as certification for their copper mining processes; however, these had not sufficiently remedied the extensive environmental damage and negligence towards human rights. The team therefore recommended avoiding investing in this name for portfolios with a sustainability focus.

In the context of Emerging Markets Sovereign Debt, the Eaton Vance/MSIM investment teams, in conjunction, have been engaging with local regulators to simplify foreign exchange and bond trading settlement processes. For example, the teams engaged with and supported an African country's central bank and Ministry of Finance on the successful onboarding and execution of foreign exchange ("FX") trades via third-party FX, which allowed for greater investment flexibility and lower transaction costs. Other investors have started to utilise this model, which helps to lower the liquidity premium to the debt. The teams also petitioned against changes to the taxation regime that would have been unfavourable to clients and would have provided no additional benefits for the sovereign. This is an ongoing engagement, but the team expects this to result in greater investment flexibility, lower transaction costs, and lower liquidity premium, which will benefit both investors and the country's access to and cost of financing.

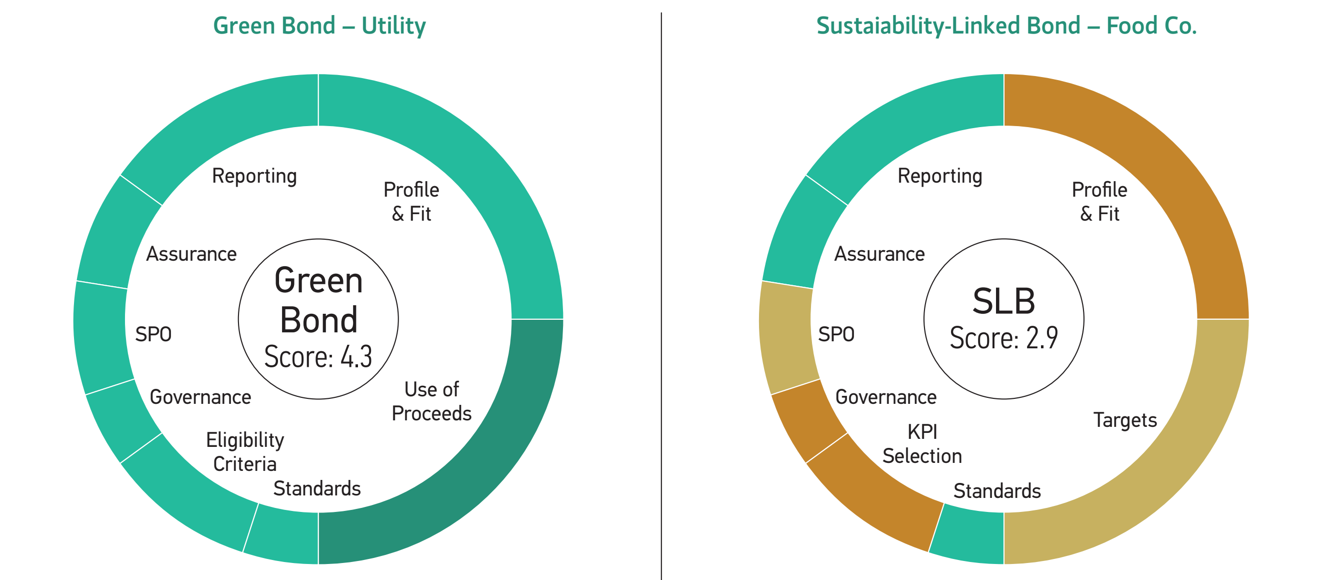
In addition to the points highlighted above, the MSIM and EV Fixed Income teams also have their own team-specific issues/priorities when conducting due diligence and, at times, geographic allocations are not always at the forefront of security selection based on the specific fund strategy.

ESG Data

The main challenge in Fixed Income ESG integration is data gaps, which particularly affect High Yield and Emerging Markets investment teams, and also due to limited resources to fill these gaps across with in-house research, which would require extending coverage to hundreds of additional companies to serve the overall large Fixed-Income investment platform, and the needs of diversified portfolios. The Fixed Income team is taking steps to address this constraint: first, by proactively engaging with some of the companies whose ESG disclosures and data are significantly lacking, to help fill these gaps with qualitative insights from company meetings; and, secondly, by adding Fixed Income ESG research capabilities. Between January and June 2022, the team hired three full-time members (two internal hires, including a senior hire to lead a new team, and one external hire) to address such needs.

FIGURE 7.5

Sustainable Bond Evaluation Model: Sample Evaluations



Rationale
- Company fast-tracked coal phase-out, pivoted its business model towards renewable energy
- Additional commitment to be net-positive on biodiverty
- >90% capex Taxonomy-aligned

Rationale
- Company exposed to litigation on deforestation
- KPIs do not include scope 3 emissions; targets not yet SBTi-verified
- Investment Team engaged with the company

LAGGARD 1 2 3 4 5 **LEADER**

SUSTAINABLE BOND STRATEGIES WITHIN THE FIXED INCOME TEAM

As an active fund manager, the Fixed Income team looks through the labelling and critically assesses sustainable bonds that come to market, to ensure the evaluation of their sustainability characteristics is integrated into the investment process, for the benefit of clients. The team also believes it has a duty to encourage issuers and underwriters to strive to implement best practices to achieve meaningful positive sustainability outcomes through the issuance of robust sustainable bonds, and engage with issuers and participate in industry initiatives to achieve this.

Leveraging the extensive experience of the Fixed Income Sustainable Investing specialists in this market, the team has developed a proprietary model to assess labelled Sustainable Bonds and score them based on the fit of the transaction within the issuer's broader strategy, the additionality of the use of proceeds and robustness of the bond structure, its external verification and the quality of reporting.

The due diligence process includes an evaluation of the extent to which the projects (or targets, for Sustainability-Linked bonds) contribute to specific sustainability objectives and align with selected SDGs that might differ from, or be a sub-set of, those at the issuer level, and can result in positive environmental or social impacts. An overview of the team's Sustainable Bond evaluation is provided below.

Over the past 12 months, the team has also been working with research analysts from Calvert—Eaton Vance's responsible investment arm—to harmonise existing sustainable bond evaluation frameworks, and deploy the resulting aligned model across the fixed income platform.

Global Listed Real Assets

GLOBAL LISTED REAL ESTATE

Within GLRA, the Global Listed Real Estate Securities ("Global Listed Real Estate") team's identification and assessment of risks and opportunities related to sustainability—specifically, the Environment, Social and Governance pillar—are a core element of the team's research process. The team's ESG focus is comparable to its focus on other factors, such as building quality, tenancy, occupancy, strategic business plans and so on.

The team undertakes a mosaic approach to sustainability research, using both quantitative and qualitative data from multiple sources. GLRA's internal research complements and enhances data from company sustainability reports and third-party providers—including MSCI, ISS, Sustainalytics and the Global Sustainability Real Estate Benchmark ("GRESB")—as we focus our sustainability research on the areas shown below.

The team's proprietary research process results in a scorecard that ranks the relative strengths and weaknesses of each company in the investment universe

FIGURE 7.6

GLRA Sustainability Research Areas

ENVIRONMENT

- Energy Usage and Renewables
- Water Usage
- Emissions (GHG)
- Waste Reduction and Diversion
- Supply Chain and Materials
- Tenant Engagement
- Climate Resilience

SOCIAL

- Health and Wellness
- Safety
- Diversity and Gender Equality
- Labor Issues
- Community Impact

GOVERNANCE

- Governance Structure around Sustainability
- Board Diversity
- Compensation Programs
- Government and Regulatory Risk
- Business Ethics
- Sustainability-Linked Financing

on ESG factors. The team then adjusts its valuations of the companies to account for these ESG risks and opportunities, and the impact they may have on a company's net asset value and cash flow forecasts in both the near and intermediate term; ultimately, GLRA seeks to identify real estate securities with the best total expected returns for clients, inclusive of adjustments for ESG risks and opportunities.

Global Listed Infrastructure

The Global Listed Infrastructure Securities ("Global Listed Infrastructure") team focuses on a variety of ESG areas when assessing investments, with priorities varying by sector, given the difference in business drivers/areas of potential ESG improvement. Examples of primary and secondary focus areas by infrastructure super-sector that may be considered are summarised below:

- **Utilities**
  - **Primary** – exposure to clean energy operational business lines, progress on decarbonising existing operational footprint (Environmental).
  - **Secondary** – community relations as it relates to new asset project builds; progress on strengthening minority/female representation within the workforce, management and the Board; increasing direct link between ESG performance and C-suite pay (Social and Governance).
- **Energy Infrastructure**
  - **Primary** – progress on decarbonising existing operational footprint, progress on identifying truly value-enhancing energy transition project areas, rather than just "greenwashing" opportunities (Environmental).
  - **Secondary** – community relations as it relates to new asset project builds; progress on strengthening minority/female representation within the workforce, management and the Board; increasing direct link between ESG performance and C-suite pay (Social and Governance).
- **Communications**
  - **Primary** – progress in improving ESG metrics throughout the company's supply chain, given low direct (Scope 1) emissions footprint; particular focus also on power sourcing (Environmental).
  - **Secondary** – progress on strengthening minority/female representation within the workforce, management and the Board; increasing direct link between ESG performance and C-suite pay (Social and Governance).
- **Transportation**
  - **Primary** – progress in improving ESG metrics throughout the company's supply chain, given significant reliance on third-party contractors for asset upkeep and new build; steps taken to help end customer passengers/freight distributors adapt and utilise lower-carbon alternatives (e.g., a toll road operator's initiatives to incentivise use of EVs).
  - **Secondary** – progress on strengthening minority/female representation within the workforce, management and the Board; increasing direct link between ESG performance and C-suite pay (Social and Governance).

The Global Listed Infrastructure team takes into consideration both the initial state of the business, as well as a company's progress on ESG initiatives, when making new investments or deciding to add or reduce positions. In some instances, companies are early on in their ESG journeys, and in other instances, companies are well-advanced with a high level of experience and very detailed reporting. The team looks for companies to improve in either instance, as its ESG engagement process is about ongoing, continuing improvement. In areas where companies are naturally "green" from an environmental perspective, the team also emphasises the need to be best in class across a number of different ESG elements, not just "E", and to benchmark themselves not just to their immediate peers or industry, but rather to their regional markets more broadly.

ALTERNATIVE INVESTMENTS

The Alternative Investments business consists of Private Global Real Assets and Private Credit & Equity strategies.

a) Private Global Real Assets

The Private Global Real Assets Group believes in being patient, disciplined investors, committed to working with the best operating partners in each market, seeking to generate strong risk-adjusted returns, and always putting clients first. The Head of Sustainability for Global Real Assets supports the Private Real Estate, Infrastructure and Real Estate Credit investment teams to develop and execute sustainability strategies across the U.S., Europe and Asia. The Private Global Real Assets Group has created a holistic ESG Framework to implement the teams' sustainability strategies. As outlined in *Figure 7.7* below, the Framework's four pillars include ESG integration, driving operating and environmental performance across assets, improving ESG engagement and disclosure, and advancing ESG thought leadership.[27]

Private Real Estate
Morgan Stanley Real Estate Investing seeks to integrate material ESG elements throughout the investment process, where appropriate, as part of its approach to responsible investment and risk management. MSREI's Environmental Management System ("EMS") is an internal document that provides best practice, guidance and resources for investment teams to facilitate implementation of funds' ESG elements throughout the entire investment life cycle, to the extent financially and operationally feasible. The EMS, aligned with the ISO 14001 standard, helps investment teams identify and monitor ESG risks and opportunities throughout the investment process from due diligence to asset management. The EMS also includes best practices for new construction and major renovation projects.

Private Infrastructure
Morgan Stanley Infrastructure Partners believes that ESG integration throughout the investment life cycle reduces long-term investment risk and increases the attractiveness of its portfolio companies upon exit. MSIP identifies and assesses various material ESG factors, including environmental and climate change risk, during due diligence and works with portfolio companies on platform-wide ESG initiatives during acquisition and post-close implementation. To ensure effective continued integration of MSIP's ESG programme, investment teams monitor portfolio-level ESG integration and where applicable set and implement strategic ESG goals.

Private Real Estate Credit
The Private Real Estate Credit teams strive to incorporate ESG considerations throughout the investment life cycle, where feasible. However, as a private real estate credit lender, investment teams are limited in their ability to apply ESG practices across all investments (in contrast to that of the borrower/owner of the underlying real estate). As an example, outlined below are select steps to integrate ESG throughout the investment process, where possible.

- **Due Diligence:** The investment teams perform ESG due diligence both prior to and after issuing loan applications in order to analyse ESG implications of the property and sponsorship. Given each loan's unique characteristics, there may be nuances in the due diligence process depending on the loan. There are varied considerations across E, S and G that may be reviewed and may vary by loan structure; select examples are listed below:
  - **Environmental** – This category is particularly relevant for the targeted investment universe, as real estate assets consume energy and water, generate waste, and release greenhouse gas emissions. As a result, ESG due diligence is performed to fully understand the type of asset in the collateral portfolio, its associated activities and its impact on the environment;

FIGURE 7.7
Private Global Real Assets' ESG Framework

ESG INTEGRATION	DRIVING OPERATING PERFORMANCE	ESG ENGAGEMENT & DISCLOSURE	ADVANCING THOUGHT LEADERSHIP
Manage and identify ESG risks and opportunities in the investment process	Improve performance by driving environmental and social initiatives	Create value and differentiation through enhanced collaboration and disclosure	Deepen in-house expertise, and aspire to position Real Assets as a leader in ESG

[27] Select Private Global Real Assets Funds take ESG considerations into account in investment decisions on a **non-binding basis only**. Please refer to the offering documents of any fund prior to investment for details on how, and the extent to which, the relevant fund takes sustainability considerations into account on a binding or non-binding basis

– **Social** – Within the teams' investment universe, social considerations are generally relevant in the context of loan portfolio and collateral management practices. For example, servicing procedures may be reviewed to ensure best practice is followed and applicable legislation is adhered to; and

– **Governance** – Generally, governance factors are evaluated at the sponsor level. Areas considered may include board responsibility and oversight of ESG matters, ESG dedicated individual(s), established ESG committees or taskforces, etc.

While the above provides select examples of ESG considerations, the geographical location, management framework, and type of collateral may influence which ESG elements are considered.

- **Asset Management:** Post-investment, teams may maintain periodic contact with the specific investment sponsors/origination partners to identify any changes to ESG practices and to identify potential exposure to ESG concerns. Where possible, teams strive to follow the performance of the loans and monitor ESG implications to the underlying collateral.

b) Private Credit & Equity

The PC&E business has its own Sustainable Investment Policy outlining investment teams' belief that incorporating ESG factors into the investment process is essential for minimising investment risk and maximising investment return. The identification of ESG risk and opportunity factors early on in the investment process can reduce financial, regulatory and reputational risks and drive value for investors and other stakeholders. While the specific ESG factors incorporated into investment analysis vary depending on what is material to a particular asset class, sector, geography and/or investment opportunity, the areas below generally reflect the sustainable and stewardship approaches that are incorporated into the investment process and assessment of financial impact. Investment strategies that go beyond integration and link ESG criteria to investments may have additional strategy-specific ESG policies.

ESG Investment Integration

PC&E is committed to considering and incorporating material ESG issues when evaluating all investment opportunities throughout the investment life cycle:

- **Pre-Investment**
  – *Screen for sensitive sectors:* In accordance with Morgan Stanley's Environmental and Social Risk Policy, PC&E will generally avoid investing in certain environmentally sensitive sectors and will conduct enhanced due diligence for specific sectors outlined in the policy, employing expert consultants where necessary. The European Private Credit team, in particular, may apply additional sector-based exclusions in a number of business activities/sectors including ammunition, adult entertainment, weapons, tobacco, upstream production of palm oil, and oil and tar sand development.
  – *Operational due diligence:* Conducted by deal teams through review of investment policies, procedures and site visits, and responses to ESG questionnaires. Where MSIM is a limited partner, general partners' internal ESG policies, procedures and documents are reviewed.
  – *Legal due diligence:* Performed in partnership with MSIM Legal to ensure compliance with regulatory frameworks and to identify exposure to long-term liabilities.
- **Investment Decision-Making**
  – *Valuation:* Depending on the results of the pre-investment due diligence process, deal teams may account for these factors in their overall valuation of the company, deal structure and contract negotiations.
  – *Investment Committee:* Last year, PC&E created ESG due diligence questionnaires, based on the SASB Engagement Guide, that are required to be completed for all investment committee meetings. Both private equity and private credit questionnaires cover a comprehensive set of metrics across E, S, and G, and the questions were selected and curated based on their relevancy to the industries that PC&E invests in. Specifically, the private credit scorecard is used to determine an ESG score for each borrower. The score is a composite score based on an evaluation of ESG factors across a standardised set of diligence questions that covers the portfolio company and sponsor. Each component (E, S and G) is measured on a scale and an aggregate total ESG score is calculated. A total ESG score below an established minimum threshold requires additional discussion and consideration by the fund's respective investment committee, and the transaction may be declined if it presents material downside risk. In rare cases, heightened ESG reputational risks may be escalated to the Firm's Franchise Committee.
- **Post-Investment**
  – *Ongoing monitoring:* The investment teams continue to monitor sustainability performance and

risks where possible with the aim of maximising investment value at exit. Material issues identified through monitoring are raised with members of MSIM's Risk team.

- *Stewardship and engagement:* Investment teams engage with the investee and relevant stakeholders to encourage ongoing improvement of sustainable practices, raising issues at the appropriate level (e.g., company management and board of directors).
- *Continuous improvement:* Investment teams may set sustainability goals for portfolio companies and track improvement across a range of ESG factors using Key Performance Indicators ("KPIs") where possible.

To illustrate this in practice, through two of PC&E's strategies, Morgan Stanley Capital Partners and Private Markets Solutions:

i) Morgan Stanley Capital Partners ("MSCP")

MSCP manages a middle-market private equity platform, focusing primarily on North America. For MSCP, deal teams act as a first filter for potential portfolio companies that are being considered. Any company that is associated with material ESG risks that cannot be mitigated or improved on will not be put forward to the Investment Committee for further discussion and approval.

For companies that do make it to the next round in the selection process, the team considers ESG risks and opportunities throughout the investment life cycle, starting in the investment due diligence phase, where it seeks to identify ESG risks and value drivers, and continuing through to the post-investment phase where investment teams partner with investees to maximise ESG opportunities and value drivers.

Case Study

An example of a potential investment that was declined due to ESG considerations is a recent opportunity in the digital advertising space. The MSCP team has been focused on this market within the Business Services sector, as the performance marketing landscape has seen significant disruption due to new data privacy measures and the team believes that well-positioned businesses will outperform in the near-term. The potential investment was a leading performance marketing company that leverages proprietary media, first-party data and AI to drive targeted customer acquisition for advertisers. The company was uniquely positioned as a first-party data provider, rather than relying on third-party cookies and data collection. While the business experienced strong growth and MSCP invested significant time in evaluating the opportunity, the team decided to step down due to qualitative considerations with the business. Following an initial review with the MSCP Partner Group, the team decided to pass on the investment opportunity for ESG reasons as the team felt that the nature of the Company's sites and the method by which user data was sold could potentially be predatory to individuals, which does not align with MSCP's values and desire to invest behind businesses creating a positive net effect.

ii) Private Markets Solutions

The Private Markets Solutions team believes the capital markets can serve as a catalyst for positive change. By endeavouring to advance sustainability, the team aims to support a healthier planet and more inclusive economy while delivering long-term value for clients. Furthermore, the Private Markets Solutions team believes that the integration of ESG considerations into its business activities helps manage risk, enhance capital preservation and deliver more consistent performance to investors. Within this context, the team has long recognised the importance of these issues to the investment programme.

In 2014, the team hired senior personnel from the World Bank Group to build out an impact investment programme and to institutionalise and augment the ESG diligence processes for all investments in the team's core programme, as an additional risk management tool.

In 2015, the team formalised a set of ESG principles that, together with other related Morgan Stanley policies in the area, was adopted by the team in carrying out investment diligence, evaluating and monitoring in all areas of the team's investment programme, not limited to just the impact programme.

In early 2022, the team hired a senior ESG specialist who has helped further the integration of ESG principles into the team's investment process. Prior to joining the Private Markets Solutions team, she was an ESG & Sustainability Consultant at a sustainability specialist asset manager. The hire of the senior ESG specialist brings a wealth of ESG investing knowledge and has further enhanced the team's policies and practices.

The Private Markets Solutions team's approach to ESG encompasses a variety of important criteria (see below).

All investments made by the team are subject to an ESG due diligence process that is embedded in the investment process. The Private Markets Solutions team began conducting ESG due diligence in 2015, and all relevant team members are required to be trained in World Bank standards per the IFC's Sustainability Training & E-Learning Programme, designed to help financial institutions better understand sustainable finance, environmental and social risk management and explore sustainability-related business opportunities.

During the diligence phase, the deal team will assess: (i) the GP's awareness, processes and procedures and (ii) the potential for ESG risks, specifically looking at:

- **Environmental:** Whether the underlying sponsors (i) incorporate ESG considerations into their overall investment life cycle, from initial sourcing and due diligence to portfolio monitoring and exit; (ii) have an appropriate monitoring and reporting capability of ESG-related risks to their limited partners; and (iii) have appropriate ESG resources to implement and enforce their ESG policy and provide relevant training for their staff;
- **Social:** Whether the underlying sponsors (i) have a standard approach to assess, identify and remediate data security risks; (ii) have anti-discrimination and anti-harassment policies; and (iii) have initiatives to enhance diversity, equity and inclusion within the sponsors and across their portfolio companies; and
- **Governance:** Whether the underlying sponsors (i) have a code of conduct, including anti-bribery/anti-corruption policies; (ii) have anti-money laundering and know-your-customer policies; (iii) have an appropriate governance structure and oversight function through executive and investment committees; and (iv) have any ongoing litigations and/or regulatory violations.

Additionally, the team assesses the GP's skill set and portfolio risk with the support of a due diligence questionnaire. The potential (and existing) risk of the

FIGURE 7.8

Private Market Solutions' Approach to ESG

ENVIRONMENTAL, SOCIAL, AND GOVERNANCE (ESG) POLICY SUPPORTIVE OF FIDUCIARY MINDSET

WHAT IS ESG TO PRIVATE MARKET SOLUTIONS?*

ENVIRONMENT	Greenhouse gas emissions
	Energy management
	Air and water pollution
	Circular economy
	Waste management
SOCIAL	Diversity, equity and inclusion
	Employee satisfaction
	Community relations
	Labour standards
	Health and safety record
GOVERNANCE	Board independence
	Business continuity
	Business conduct and ethics
	Remuneration practices
	Legal and regulatory compliance
	Tax strategy

ELEMENTS OF PRIVATE MARKET SOLUTIONS' ESG IMPLEMENTATION

- Private Market Solutions actively began building ESG capabilities and establishing policies over six years ago.
- Private Market Solutions' efforts have been enhanced by strong support from Morgan Stanley, led by James Gorman, including the Firm's Institute For Sustainable Investing and Morgan Stanley Investment Management—a signatory of the UNPRI since 2013
- ESG screening and diligence is fully integrated across AIP Private Markets' investment programs, including:
  - Annual ESG training for each Private Market Solutions investment professional;
  - Active discussion with Investment Committee on ESG diligence findings and skill/risk assessment for each investment put forth for approval;
  - Annual ESG monitoring conducted on underlying fund relationships to ensure ongoing compliance with Private Markets Solutions ESG standards; and
  - Reporting system fro underlying fund managers to notify ESG incidents to Private Market Solutions ESG Incident team for determination whether further escalation and action are necessary.

* The statements above reflect the views and opinions of Private Market Solutions as of the data hereof and not as of any future date and will not be updated for supplemented. There is no guarantee this approach will apply to every investment opportunity Private Markets Solutions reviews. Source: OECD and CFA (2015b) in OECD (2017), "Investment governance and the integration of environmental, social and governance factors."

GP will be categorised formally based on a risk matrix. Complex risk situations will be analysed and discussed during investment committee meetings, with the objective of providing guidance on the next steps.

The Private Markets Solutions team conducts ongoing dialogue with the GP around governance, environmental and social issues as they pertain to a particular investment strategy. As investors, the team believes that ESG matters can pose significant risk factors and may impact long-term performance. The Private Markets Solutions team uses a variety of methods to assess such risks as integral parts of our due diligence approach, as depicted in the illustrative ESG framework graphic below.

ESG Data

The availability and quality of ESG-related data continues to be a limitation and a barrier within private markets. Portfolio companies, especially within the middle market segment, are still in the beginning stages of collecting ESG-related information. While the investment team has greater ability to implement and track KPIs once an investment is made within its control strategies, these portfolio companies often do not have robust ESG data pre-investment. To mitigate this data gap, the team has increased engagements with vendors such as RepRisk, an ESG data science company, that alerts the team of situations where there may be material ESG issues in their portfolio companies. Additionally, the team is in the process of implementing eFront, a portfolio monitoring and management system, across its platform to better collect, aggregate and report on KPIs and data points the team accesses in a more streamlined and consistent manner.

Custom Solutions

Certain of the Multi-Asset portfolios integrate ESG factors contingent on asset class and style of investing. As an example, for quantitative investing, the team may optimise the portfolio by using ratings or scores balanced against other risk/return objectives. For customised portfolio solutions, the team may review ESG factors to assess impact on asset allocation and/or customise a basket of securities or funds according to the particular sustainability preferences of the client. For highly active, concentrated equity portfolios, integrated sustainability

FIGURE 7.9

Private Market Solutions' ESG Framework

	ASSESS AND CATEGORISE THE POTENTIAL (AND EXISTING) RISK IN A PORTFOLIO/DEAL			
	RISK DESCRIPTION	**ENVIRONMENTAL**	**SOCIAL**	**GOVERNANCE**
CATEGORY A HIGH RISK	Potential for significant adverse impacts on the environment or human populations; potential for integrity issues	Large dams, large scale forestry, agro, industrial plants, mining, oil and gas, hazardous/toxic materials, waste disposal, ports	Deals involving large re-settlement of populations	Deals involving public sector and/or politically exposed persons including large contracts or privatizations especially in countries rated lower than 2 on Transparency International ("TI") Corruption Perception Index.
CATEGORY B MEDIUM RISK	Potential serious but not irreversible environmental or human population impacts than can be mitigated through good management; limited potential for integrity issues in certain sectors	Small agro, aquaculture, transmission, small renewables, tourism, construction materials, general manufacturing, water, telecom	Small agro, aquaculture, transmission, small renewables, tourism, construction materials, textiles, general manufacturing, water, telecom	Investments in countries rated 2-7 by TI with emphasis on large scale/ public sector related transactions
CATEGORY C LOW RISK	Minimal environmental or human population impact; minimal impact for corruption	Media, IT, Financial services, other services	Media, IT, Financial services, other services	Investments in countries rated 7 and above by TI

For illustrative purposes only.

FIGURE 7.10

Examples of Progress Made by Portfolio Companies on ESG Issues

FUND	PORTFOLIO COMPANY	ESG ISSUE	STATUS
CONFIDENTIAL FUND 1	Confidential Portfolio Company 1	• Reduce carbon emissions footprint	• Accelerated the company's activity in lower emissions engines and fuels
CONFIDENTIAL FUND 2	Confidential Portfolio Company 2	• Implement ESG policies	• Worked with consultants and other investors to professionalise the business and develop a formalised ESG and Impact framework
CONFIDENTIAL FUND 3	Confidential Portfolio Company 3	• Improve the company's ESG reporting tool which is designed to help building owners and investors better understand how their property can operate more efficiently and sustainably while reducing their carbon footprint	• Supported the expansion of the company's ESG data collection and reporting tools

analysis is conducted based on an ESG materiality framework. The Multi-Asset teams also conduct thematic engagements on materially important environmental and/or social issues facing companies in order to ensure that target companies follow good governance practices. The teams' approaches to stewardship and investment do not generally differ based on geography—although the ESG issues/factors that are prioritised for engagement with specific investments may differ based on regional practices and progress in those areas.

a) Global Balanced Risk Control

Researching risks to the global economy and global markets is integral to GBaR's asset allocation process, and ESG factors such as climate change clearly fall into the team's definition of potential "risk events". The team therefore views the incorporation of ESG factors and stewardship as a natural extension of its philosophy around risk control.

The team believes in the merits of a multi-dimensional approach to incorporating ESG factors into its portfolios. Rather than limit itself to benefiting from a single element of ESG approach, the team aims to combine the benefits of restriction screening (also called exclusions), ESG integration (or "best-in-class"), impact investments and engagement/stewardship.

Each dimension of ESG is incorporated with regard to specific ESG factors, but an overarching area of focus is climate change. Not only does this represent the most significant environmental challenge, but as a result it also represents the biggest ESG-related risk to the companies and securities in which the team invests, for example in terms of reputational, regulatory and financial risk.

Drilling down into the team's ESG multi-asset portfolios, they focus on the following factors within each of the four approaches to ESG that they incorporate:

i) Restriction Screening/Exclusions

- Focusing on the core equity exposures, the team aims to exclude companies involved in activities that are proven, or have the potential, to cause significant harm to the environment and/or society. The team works on an "engage or exclude" basis. If the team believes a company, or broader industry, is open to changing its behaviour, they will seek to engage, in order to help effect that change.
- However, some industries do not, in the team's opinion, offer the prospect of change as a result of engagement, in which case exclusion is the appropriate approach. The team considers the indirect impact of the entire value chain, and apply exclusions in the following areas: ESG controversies, breaches of UN Global Compact, coal and oil sands, tobacco, gambling, controversial weapons and civilian firearms.

ii) ESG Integration/Best-in-Class

- The team aims to enhance ESG quality (in all three pillars) of our core asset class exposures, as distinct from impact investments
- In developed government bonds, the team excludes countries with the lowest ESG rating (CCC), using MSCI ESG Government Ratings scores. Of the

remaining countries, they overweight those with above-average effective ESG Government ratings scores and underweight those countries with below-average scores.

- In equities, the team uses MSCI ESG ratings to optimise securities baskets (sub-portfolios tracking regional equity indices). The team aims to hold securities that in aggregate represent top-quartile ESG performers (again, across all three pillars), within each sector, in each region.
- Given the importance of climate change as an ESG factor, the team has an additional tilt towards stocks that score favourably in terms of the low-carbon transition ("LCT"), using MSCI's LCT scores, which reflect the LCT risks a company faces from its core business (e.g., the risk of stranded assets) and in its value chain, as well as the company's management of those risks.
- The team also incorporates a strategy to reduce the carbon profile of this portion of its portfolio. The team aims to decarbonise its portfolios' core equity exposures according to the 1.5°C scenario, aligned with the most recent IPCC recommendations and targeting net zero emissions for its equity exposure by 2050. In practice, this means the team aims to reduce the core equity portfolio's carbon emissions by 7% per annum, or 1.75% in each quarterly rebalance, until 2030. This will require some degree of tilting to the sector weights within each equity region, although the team will maintain a maximum over/underweight of 5%, relative to each sector's weight in the underlying regional index. The team will continually monitor the results of this strategy, to ensure it remains on the path to achieving its goal.

iii) Impact Investments

- In portfolios that allocate a portion to impact investments, the team targets investments that support potential solutions, such as products and services, to many of the world's most urgent environmental and social challenges. The aim is to generate a measurable, positive environmental and social impact alongside a financial return for the portfolios. The team's impact themes fall broadly into four categories—Climate, Resource Management, Basic Needs and Empowerment.

iv) Engagement/Stewardship

- As active investors and active owners, GBaR believes that it has a duty to be good stewards of clients' capital. The team fulfils this duty by engaging with the companies in which it invests and by effectively exercising proxy voting and other rights as shareholders. These stewardship activities give the team the opportunity to guide companies in which it invests towards better ESG practices, which produces attractive returns for its clients over the long term. GBaR further believes a structured approach to engagement is a powerful tool to keep issuers on track with their commitments.
- Typically, the team's main engagement priorities are guided by top-down thematic-based research and an assessment of material ESG risks by the team's dedicated ESG analysts. GBaR believes this is the best approach for its strategy, as researching risks to the global economy and global markets is integral to the team's asset allocation process. ESG factors such as climate change definitively fall into the team's definition of potential "risk events". This approach therefore ensures that stewardship is seen as a natural extension of the team's philosophy around risk control.

Ongoing Developments

Given GBaR's top-down and diversified approach to investment, the team currently holds a broader set of issuers than other MSIM investment teams, in more concentrated, bottom-up styles and strategies. While GBaR believes its approach to theme selection leverages the team's skills appropriately, it may be more limited than other teams who spend more time researching individual companies and liaising with management teams on a more regular basis.

GBaR has addressed this limitation by building out its ESG team. It has hired staff with direct experience in sustainability-related research and engagement and has increasingly been working with MSIM's Global Fixed Income sector specialists and Global Stewardship team.

GBaR believes it can further enhance its ESG approach by increasing collaboration with sector specialists across MSIM in order to leverage investment teams' combined knowledge and ownership to drive change at portfolio companies. While GBaR has begun to engage more collaboratively, it believes there is scope to grow this practice in subsequent reporting periods. The GBaR team believes this will ultimately serve to enhance the teams' ability to effectively engage with its portfolio companies.

b) Parametric Portfolio Associates

Our Parametric business uses investment science to build and manage investment strategies and to implement custom portfolio solutions, providing clients with targeted investment exposures with control of costs and taxes.

In line with Principle 6 (which is focused on incorporating client needs/requirements), the team's approach to ESG incorporation for the past 20 years is designed to allow each client to implement its own specific views on responsible investing in a very effective, customised manner—rather than accepting a uniform approach—within a separately managed account. The separately managed account structure allows Parametric to customise each underlying account in accordance with the client's individual investment objective and solve for their distinct responsible investing needs. The team's research providers supply its investment teams with a full range of responsible investing metrics: environmental, social or governance ratings; carbon data; and controversies, sanctions and business involvement indicators which are used to inform decision-making and monitoring pre- and post-investment.

Accordingly, the issues the team prioritises for assessing investments prior to investment, and in its ongoing monitoring and exit decisions, tend to be client driven—with a particular focus on ESG considerations. The investment philosophy is firmly rooted in the belief that the team's clients, as responsible investors, want something more than just returns. They want consistency between their principles and the activities of the companies in which they are invested. And they want to be able to use their shareholder rights to effect change.

Many clients request meetings with the team's Parametric Responsible Investing Strategy team on a regular basis for standard updates, discussion around enhancements/evolutions to our approach and, in some instances, recommendations to enhance alignment with the client's individual needs/requirements.

CALVERT RESEARCH & MANAGEMENT

Calvert's research and engagement efforts are built on the foundation of the Calvert Principles for Responsible

FIGURE 7.11

Calvert Principles for Responsible Investment

The Calvert Principles for Responsible Investment (Calvert Principles) provide a framework for Calvert's evaluation of investments and guide Calvert's stewardship on behalf of clients through active engagement with issuers. The Calvert Principles seek to identify companies and other issuers that operate in a manner that is consistent with or promote the following:

E | **ENVIRONMENTAL SUSTAINABILITY AND RESOURCE EFFICIENCY**

- Reduce the negative impact of operations and practices on the environment
- Manage water scarcity and ensure efficient and equitable access to clean sources
- Mitigate impact on all types of natural capital
- Diminish climate-related risks and reduce carbon emissions
- Drive sustainability innovation and resource efficiency through business operations or other activities, products and services

S | **EQUITABLE SOCIETIES AND RESPECT FOR HUMAN RIGHTS**

- Respect consumers by marketing products and services in a fair and ethical manner, maintaining integrity in customer relations, and ensuring security of sensitive consumer data
- Respect human rights, respect culture and tradition in local communities and economies, and respect Indigenous Peoples' Rights
- Promote diversity and gender equity across workplaces, marketplaces and communities
- Demonstrate a commitment to employees by ensuring development, communication, appropriate economic opportunity and decent workplace standards
- Respect the health and well-being of consumers and other users of products and services by promoting product safety

G | **ACCOUNTABLE GOVERNANCE AND TRANSPARENT OPERATIONS**

- Provide responsible stewardship of capital in the best interests of shareholders and debt holders
- Exhibit accountable governance and develop effective boards or other governing bodies that reflect expertise and diversity of perspective and provide oversight of sustainability risk and opportunity
- Include environmental and social risks, impacts, and performance in material financial disclosures to inform shareholders and debt holders, benefit stakeholders, and contribute to strategy
- Lift ethical standards in all operations, including in dealings with customers, regulators and business partners
- Demonstrate transparency and accountability in addressing adverse events and controversies while minimising risks and building trust

Investment (the "Calvert Principles"), which provide a framework for Calvert's evaluation of investments and guide Calvert's stewardship on behalf of clients through active engagement with issuers (see *Figure 7.11*).

Calvert has a team of dedicated ESG research analysts that assess company performance through a comprehensive review of ESG factors. The Calvert ESG research analysts specialise by industry area to rate and rank initial universe components to ensure that companies align with Calvert's Principles for Responsible Investment. As part of its independent research process, the Calvert ESG research team seeks peer review feedback from Calvert's fundamental investment analysts to identify the most material ESG criteria and data indicators by sub-industry.

The Calvert ESG research process focuses on identifying the financially material ESG risks to which issuers are exposed, evaluating management teams' ability to navigate those risks, and recognising opportunities for companies to improve their ESG performance. Calvert parses thousands of ever-evolving data points to differentiate issuers based on financially material ESG issues, which inform both its investment decisions and corporate engagement efforts. Calvert's research process takes the following steps:

In the first step of the process, Calvert focuses on financial materiality—the ESG factors most likely to influence company performance. Materiality, however, differs by industry and sub-industry, so the process begins by refining established classifications into custom peer groups based on common ESG risks. This allows the team to make more relevant company comparisons, which it believes lead to better investment decisions. Calvert currently uses approximately 200 of these custom peer groups in evaluating issuers.

The second step is to develop an ESG investment thesis with the goal of identifying industry trends, emerging ESG issues and—most importantly—ESG risks and opportunities that are financially material to a particular set of companies.

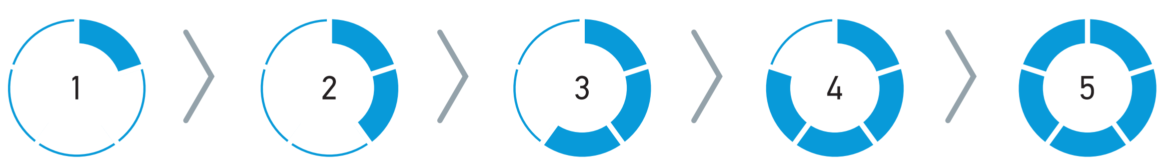
In the third step of the process, Calvert builds a Structural Model for the peer groups that measure issuer results against Key Performance Indicators ("KPIs"). Calvert uses nearly 20 external ESG data providers to source KPIs. Accordingly, Calvert has access to thousands of KPIs. When Calvert believes vendor KPIs are lacking, it creates custom indicators from underlying data, with an emphasis on coverage, dispersion and data integrity.

Calvert winnows the vast number of data points to focus on financially material ESG risks that it believes affect company performance. The team then uses a proprietary scoring model that rates and ranks companies within their sub-industry peer groups. Calvert ESG research analysts further evaluate the final scores, drawing upon their industry-specific sustainability expertise.

The final peer group rankings help support Calvert's identification of issuers that are adequately managing their financially material ESG risks and opportunities, and which are therefore deemed eligible for Calvert's investment strategies. This process is the same across

FIGURE 7.12

Calvert Research Process



	DEFINE PEER GROUP	DEVELOP INVESTMENT THESIS	BUILD STRUCTURAL MODEL	RATE AND RANK ISSUE	MONITOR PROCESS
RESULT	Refine classifications into custom peer groups based on shared, financially material ESG risks.	Develop investment thesis to identify current and emerging ESG risks and opportunities over our investment horizon.	Evaluate performance on financially material ESG issues using select Key Performance Indicators (KPIs)	Determine overall ESG decision for each issuer based on analysis of three material exposures: company level, industry level and execution level.	Robust governance ensures the oversight of investment theses updates, continuous maintenance of models and investment decision changes.

asset classes. When disclosure is more limited, a more qualitative approach is taken. Qualitative reviews follow the same governance process and this results in the analyst preparing a write-up that indicates whether or not the issuer is adequately managing its material ESG risks, and which is also approved by the Responsible Research Review Committee or its delegated working group.

Once minimum investment eligibility has been established, additional steps are taken by Calvert portfolio managers to further integrate ESG information into the investment thesis and ultimately into portfolio construction. This occurs in both a fundamental investment process and a more systematic risk-managed investment process, depending on the investment strategy.

ESG Data

Barriers to Calvert's existing approach include the lack of adequate data availability for small cap and unlisted (fixed income) securities, which results in a more qualitative and less data-driven approach to our analysis. The team continues to see new sources of data at scale to resolve these gaps. Further, Calvert continues to refine its views on the appropriate application of ESG financial materiality concepts to emerging markets securities.

SUSTAINABLE INVESTING[28]

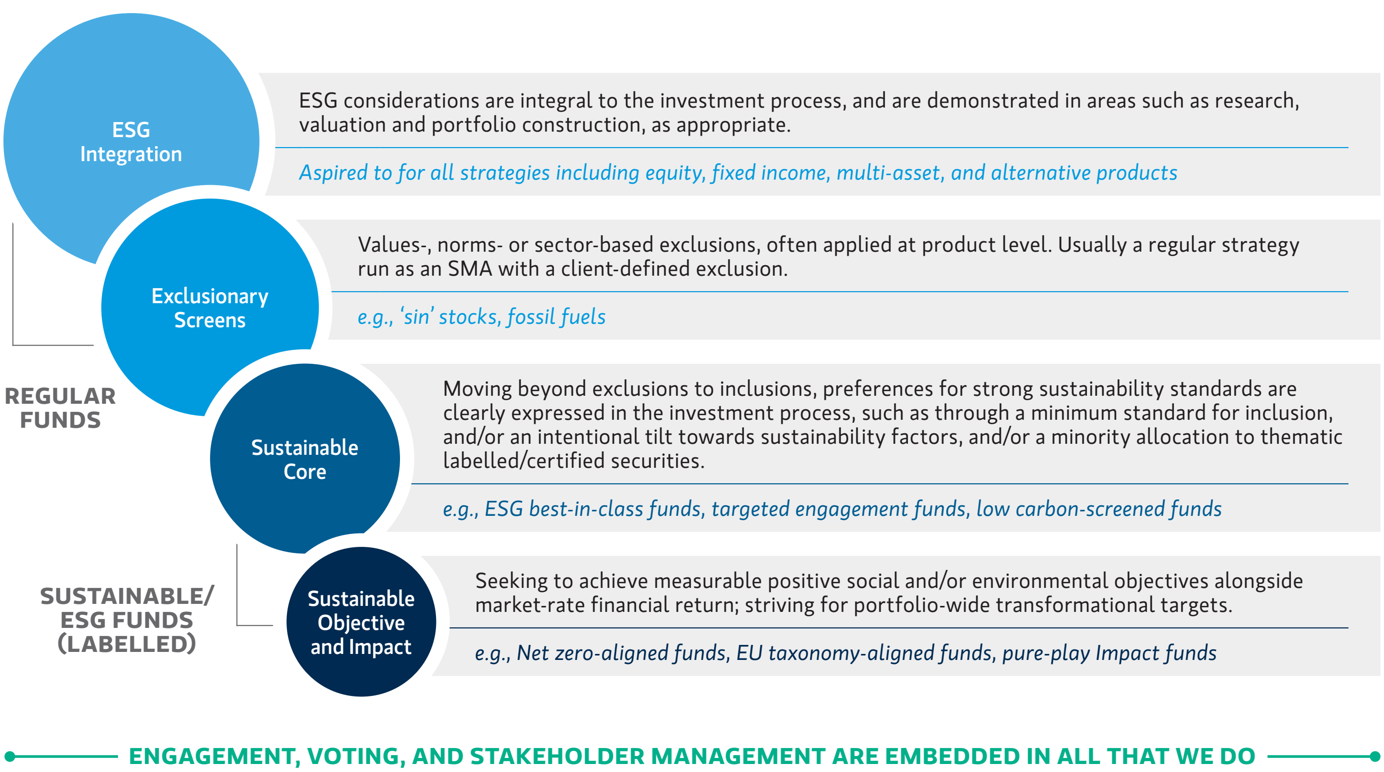
MSIM offers a variety of "Sustainable Investing" products, and we define "Sustainable Investing" as a spectrum of practices that use ESG information and criteria to deliver returns for clients and shape dedicated investment solutions.

Our framework below articulates how Sustainable Investing can be implemented across various investment strategies to provide a clearer view of what it does for its clients and stakeholders.

MSIM defines a labelled "Sustainable Fund" as a portfolio that is driven, in part, by a strong philosophical conviction in sustainability as a secular economic growth trend or as a source of investment performance and implemented

FIGURE 7.13

MSIM Sustainable Investing Spectrum



[28] "Sustainable Investing" does not represent a separate investment team, but is a term used to refer to our other investment teams when acting with a sustainable investing focus.

through a pooled vehicle and/or a separately managed account structure. The team's MSIM Sustainable Funds demonstrate this through the following implementation levers:

- **Inclusionary approaches** based on relevant sustainability factors. This could be implemented using fundamental ESG data or derived ESG ratings/scores/rankings in a variety of ways—for example, selecting relatively stronger or best-in-class investees/assets, setting a minimum performance standard for investees/assets, identifying thematic exposures or using ESG information to define a target set of investees/assets with potential for improvement;
- **Baseline exclusions** for controversial or sensitive sectors or assets, with some of the more concentrated Sustainable Funds applying relatively more extensive exclusions; and
- **Strong and active engagement and stewardship activities**, where explicit objectives are set and outcomes tracked.

MSIM is committed to providing clients with a broad spectrum of thematic Sustainable Funds across both public and private markets. MSIM strives to provide quantifiable metrics and reporting for Sustainable Funds, as data access and discoverability improve over time.

STEWARDSHIP AND SERVICE PROVIDERS

MSIM views proxy voting as a key component of stewardship activities and obtains information on corporate governance, proxy voting, issuer research and selected environmental and social issues from its investment teams' own research, as well as independent advisors (ISS and Glass Lewis), to provide vote execution, reporting and recordkeeping services.

Notwithstanding the appointment of ISS and Glass Lewis as proxy advisors (ISS is also MSIM's proxy voting administrator), as noted earlier in the report, MSIM does not outsource proxy voting, hence does not rely on either firm to implement a custom stewardship policy. As active managers and owners, our stewardship philosophy is enshrined in performing stewardship directly in companies it invests in, in order to promote long-term shareholder value, which is in line with the views of its clients.

That said, MSIM communicates with both service providers at least monthly to discuss research and other operational voting issues to ensure that both service providers are kept well aware of its stewardship and voting needs and its expectations of them. In the event the team discovers a potential discrepancy in the underlying service provider's research, it generally escalates and contacts the firm's Head of Research to resolve the issue.

HOW INFORMATION GATHERED THROUGH STEWARDSHIP INFORMS INVESTMENTS, MONITORING AND DIVESTMENTS

In addition to the commentary provided above, the following case studies show how stewardship methods and information gathered during the stewardship process contribute to decisions relating to investments, ongoing portfolio monitoring and divestments and/or addressing multiple ESG topics and engagements.

CASE STUDY 7.1: FIXED INCOME

Investing to Support Energy Transition

The MSIM Fixed Income team engaged with an Italian utility company that has an extensive gas transmission network, to encourage increased CapEx spending into upgrading its gas pipelines for hydrogen use. The company has significant leverage in transitioning the national energy transmission network towards transporting more renewable sources, and the team therefore sought to recommend more aggressive investments in this area.

The engagement was highly satisfactory, given that the company is an early mover in the energy transition space, and a key player in the preparation of a European hydrogen network. The company has shifted its strategic goals from improving the efficiency of its traditional gas network towards setting a long-term target to transport entirely decarbonised gas, and has recently developed partnerships with railway operators to improve the possibility of hydrogen mobility by rail. The company backed this effort through the issuance of labelled transition and sustainability-linked bonds.

As such, the team considered the company to be exhibiting positive momentum with respect to its efforts to transition towards transporting renewable sources of energy. The company's transition strategy was also beneficial to avoid stranded asset risk, at a relatively low cost. The team decided to invest in one of the company's transition bonds, given the use of proceeds was specifically intended to upgrade the company's gas network and enable hydrogen transport. The team maintains an overweight position on the name, and encourages it to continue the shift towards transporting cleaner fuels.

CASE STUDY 7.2: EMERGING MARKETS EQUITY

First Mover Advantage – Investing to Improve Waste Management

While many EM companies are increasingly engaging with investors on ESG topics, one of EME's portfolio companies had its very first conversation on its sustainability practices with the team recently. This company is a major provider of semiconductor assembling and manufacturing services. EME engaged with it to learn more about the company's approach on minimising negative environmental impact, supply chain management, circular economy and water management. While the company was in the early stages of communicating its initiatives to investors and formalising its overall ESG strategy, the company was already ahead of its peers in emissions and energy management.

In 2021, the company set a science-based target for Scope 1 and 2 emissions and informed EME that it planned to achieve this through optimisation of manufacturing processes and increasing renewable energy use. The company is hoping to achieve 27% renewable energy usage by 2025, from 15% in 2021. In addition, the company proactively committed to reducing its Scope 3 emissions 15% by 2030 from 2020 and will collaborate with its value chain on carbon reduction programmes.

EME pressed the company on implementing circular economy initiatives, including better waste management practices. The company was forthright about its lack of expertise in this area and that it was trying to work towards achieving circular economy but has met some challenges. EME believes that within the semiconductor manufacturing space, there are many opportunities to achieve circular economy through working with suppliers and implementing strong waste management practices. Most of all, through the circular economy model, semiconductor companies can not only reduce emissions but also realise cost savings. As we continue to engage with the company, we will encourage them to adopt the circular economy model and increase materials recycling.

The company has a very strong focus on water management with a recycling rate of approximately 72%. To achieve this, it has built large water reclamation facilities at two of its locations to help treat wastewater and reduce effluents. Its water reclamation facilities utilise multimedia filtration, reverse osmosis and ultrafiltration to process wastewater into purified water that is 20x cleaner than normal tap water. The processed water is then distributed to its surrounding manufacturing facilities for reuse.

As EME is amongst the first shareholders to engage with the company on these issues, the team believes that it is in a unique position to work with the company on improving ESG performance, shaping its strategy and catalysing positive change. EME hopes to maintain an open dialogue going forward and continue to engage on its emissions reduction goals and circular economy initiatives.

CASE STUDY 7.3: CALVERT RESEARCH AND MANAGEMENT

Continuing to Own Portfolio Company; Ongoing Engagement on Climate and Diversity

Calvert has an in-depth ongoing engagement with a financial services company on multiple topics, most recently on EEO-1 reporting and climate risk.

The company publishes EEO-1 data, but was unable to describe how the trends uncovered through the reporting inform human capital strategy. Calvert will continue to ask the company about its strategy and push for connections between data and company actions and diversity decisions.

The climate risk discussion is focused on improving disclosure of climate risk broadly, in line with TCFD recommendations. Such disclosure could address whether and how the physical and transition risks of climate change are incorporated in lending and financing decisions and whether they are integrated into governance and strategy. Ultimately, this may result in changes in lending and financing practices with the objective to protect asset values, improve resilience and make a positive contribution to the low carbon transition by accelerating the shift from brown to green investments.

The company is still developing an approach to measure carbon intensity in its lending. It reports according to the TCFD framework, but this is still in early stages. It does not yet have a well-defined strategy to address climate risks nor goals to decarbonise its lending activities.

Calvert held a meeting with the Vice President of CSR to discuss the company's climate strategy. The company signed up to PCAF in the summer of 2021, but it is not yet ready to disclose details of its methodology for measuring financed emissions. The company also has not yet made a net zero commitment.

Regarding efforts to address physical risk, the company shared that it believes it does a lot of work that is relevant to addressing physical climate risk, but that it needs to improve the public communication of these efforts. The company asked for ideas on potential partners on climate efforts, and Calvert suggested Ceres, the Net Zero Banking Alliance, and UNEP FI's Principles for Responsible Banking. The company was already in discussion with Ceres and a month later both the company and Calvert joined a call with Ceres and other investors to seek feedback on the company's climate strategy. In the meeting, Calvert urged the company to fully commit to net zero and suggested an additional strategic pillar for the strategy—physical risk, resilience and environmental justice.

Calvert will review the company's revised climate strategy when it is made public, watch for improved messaging on physical risk and adaptation efforts, and follow up on the suggestion that physical risk, resilience and environmental justice be considered another pillar of the company's overall strategy, which might set the company's strategy apart from other banks. Calvert will also continue to express support for the company considering joining the Net Zero Banking Alliance and UNEP FI's Principles for Responsible Banking.

CASE STUDY 7.4: EMERGING MARKETS EQUITY

Divestment on Human Rights Grounds

The EME team had invested in a Chinese apparel company, with which the team had an escalation engagement to obtain more information and address its concerns about the company's potential exposure to human rights issues in the supply chain given ties to the region of Xinjiang, China. Dozens of companies including this company were reported to be allegedly linked to suppliers using forced labour in China involving Muslim minorities, Uyghurs. This company also had allegations of sourcing cotton from Nanjing Synergy Textiles, which had been accused of using human rights violations in 2019.

The company denied any ties to suppliers who used forced labour. Using the team's recently formulated supply chain questionnaire, EME pressed for more details around sourcing and auditing/compliance of suppliers with international laws and standards. It was unclear from the call what the breakdown of materials used during manufacturing, including share of cotton, was. While the company's increase in exposure to the Xinjiang region was not the primary concern due to the mass size of the area, the company's lack of effort and initiatives to minimise forced labor risk and reluctance to provide transparency, including around Tier 1 suppliers, concerned the team.

After comparing the company's response with other companies' responses and much internal debate, the team decided to exit its position

PRINCIPLE 8

Monitoring Managers and Service Providers

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

Monitoring of Service Providers to Ensure Services Meet Our Needs

Policies, procedures and controls are in place at different levels within the organisations to manage and oversee relationships with and services received from service providers MSIM utilises in its investment management and engagement activities. This section provides an overview of these controls, how the team monitors its service providers and how they are held to account.

MORGAN STANLEY POLICIES

MSIM adheres to both Morgan Stanley and MSIM-specific policies to select, assess and monitor service providers to ensure we can deliver best-in-class investment solutions and client servicing standards.

Based on Morgan Stanley's Sourcing Guidelines, we engage with suppliers who respect, follow and abide by our Core Values: Doing the Right Thing, Putting Clients First, Giving Back, Leading With Exceptional Ideas and Commit to Diversity & Inclusion. In an ever-changing market, we are committed to evaluating new suppliers to meet our evolving needs as well as those of our clients. We look for strong capabilities, high quality and attractive commercial offerings that build lasting partnerships over time. Engaging with suppliers who share the same core values is key to our success; our global social responsibility is a direct reflection of the Firm's core values and enhances our ability to provide superior service to our clients, our employees and our communities.

Morgan Stanley holds itself to the highest standards and we expect our suppliers and our suppliers' suppliers to adhere to these key values and apply them to how they do business with Morgan Stanley and in general. This is outlined in our Supplier Code of Conduct, which demonstrates our commitment to conducting business honestly and in accordance with our legal and regulatory obligations, including commitments to our suppliers' environmental sustainability, social and ethical business practices. We also ensure Supplier Diversity by working with firms that foster diversity in business, economic development and communities.

Morgan Stanley is committed to being a responsible corporate citizen, respecting and supporting the protection and advancement of human rights. With operations around the world, we strive to uphold global standards for responsible business, including equal opportunity, the freedom to associate and bargain collectively, and the elimination of modern slavery, human trafficking and harmful or exploitative forms of child labour. Please see our Morgan Stanley Modern Slavery and Human Trafficking Statement for more details.

In selecting and monitoring our service providers, the Firm has a Global Third-Party Selection and Engagement Policy that establishes a framework for Morgan Stanley's sourcing activities from external, unaffiliated Third Parties for which our Re-engineering Management ("REM") Sourcing team is engaged. The Policy is designed to help ensure that the sourcing of goods and services by Morgan Stanley is done in a fair, competitive, independent and objective manner, with appropriate due diligence and with substantive involvement from the REM Sourcing team. Additionally, sourcing decisions must be made in accordance with all applicable laws, regulatory requirements and sound business practices. The Policy complements the Global Third-Party Risk Management Policy, which sets forth requirements for identifying, assessing, managing and controlling risks associated with the outsourcing of business processes and contracting for goods and services.

Our Morgan Stanley U.K. Regulated Entities Supplement to the Global Third-Party Risk Management Policy establishes requirements specific to our U.K. Regulated Entities and is designed to enable U.K. Regulated Entities to manage risks within the Morgan Stanley International Group's Third-Party Risk Appetite in compliance with SYSC 8 of the FCA Handbook, the Outsourcing section of the PRA Rulebook, the EBA Guidelines on Outsourcing and other U.K. Regulated Entities-specific regulations and policies listed in Section 6: U.K. Regulated Entities Regulations and Policies.

MSIM POLICIES

MSIM complies with both the Investment Management Public Markets Enhanced Vendor Management Programme Procedures and the Investment Management Private Enhanced Vendor Management Programme Procedures in selecting and monitoring service providers on both our Public and Private investing platforms, including vendors used for stewardship and engagement purposes. The goal of the Enhanced Programmes is to identify, monitor and manage risks associated with vendors that support both the Public Markets and Private Markets businesses. These procedures supplement Morgan Stanley's Global policies (outlined above) and all global requirements must continue to be met in addition to our divisional policies.

While Morgan Stanley's global policies focus on financial stability and information security of vendors, our Enhanced Programme policies seek to ensure that there are specifically identified individuals—Vendor Relationship Owners ("VROs")—in the business or related control/support groups that are responsible for the proper oversight of vendors. Proper oversight includes ensuring that a vendor is providing the services contracted and the invoices for such services are reasonable and consistent with the contractual terms of the vendor arrangement.

A centralised list of key vendor relationships on both Public and Private investing platforms is stored in the Firm's Vendor Repositories and assessed through the Firm's Supplier Portal for Assessing Risk ("SPAR") prior to onboarding. Vendor records must be created and maintained for all vendors in scope. VROs are required to periodically certify as to their periodic due diligence and the ongoing monitoring. Due diligence and ongoing monitoring of vendors (including our proxy advisors and ESG data providers discussed further below) will be conducted through various methods (as appropriate), including:

1. Periodic meetings or site visits and the use of feedback loops to guide these discussions;
2. Review of key risk indicator ("KRI") and key performance indicator ("KPI") reports provided by the vendor;
3. Measuring the service against a service level agreement to ensure contractual expectations are being understood and met by the vendor; or
4. Periodic monitoring of services provided.

Contract renewals are also used as an opportunity to evaluate the services provided and to give feedback to vendors.

Proxy Advisors

As mentioned in Principle 7, MSIM retains ISS and Glass Lewis to obtain information on corporate governance, proxy voting and issuer research; however, we do not outsource proxy voting decision-making to either firm. The primary services they provide to MSIM are vote execution of our proxy decisions, reporting (ISS) and meeting-level research (Glass Lewis). MSIM is responsible for ensuring that all voting instructions from its investment teams and clients are communicated to ISS and we have controls in place to ensure instructions communicated electronically are accurately recorded in ISS systems for execution (including scenarios where votes have been split because of client preference or differing investment team convictions—please see Principle 3 for more details). This includes a confirmation report for every vote data feed sent to ISS and an automated end-of-day reconciliation of votes instructed, between ISS and MSIM systems. Additionally, MSIM reviews on a monthly basis a vote audit report provided by ISS confirming the execution status for all meetings. The Global Stewardship team also conducts ex-post reviews to confirm that ISS has accurately implemented voting instructions.

MSIM performs due diligence reviews on retained proxy advisors on an annual basis and the reviews are conducted onsite by members of the Global Stewardship and Proxy teams and MSIM Compliance. The focus of annual diligence meetings tends to revolve around timeliness and quality of research, particularly on emerging sustainability topics. Though we do not rely on proxy advisors' vote recommendations, we do expect accuracy in the underlying research provided in their proxy reports. When we identify any errors in the underlying research, MSIM's Stewardship team will contact the firms' Head of Research to point out a potential error. If we are correct, the vendor will publish an update to the report to reflect the identified error. We will also seek assurances from vendors that they are taking reasonable steps to reduce the likelihood of such an error recurring in future. We will also provide feedback to our proxy advisors on an ad hoc basis, on how they can improve their services to better suit our and our clients' needs. For example, we recently suggested that one of our primary vendors enhance reporting accessibility on their platform, which it has implemented, to our satisfaction.

If any material issues were to arise in connection with the quality or continuity of service we receive from these providers, we will take steps to escalate and address them in line with the Firm-wide policies and procedures summarised above.

No critical issues were identified during the reporting period 1 July 2021 – 30 June 2022. Notwithstanding this, we continually look to further enhance our stewardship approach and activities. For example, earlier this year our Global Stewardship team communicated with ISS the need to track board diversity metrics specifically related to racial and ethnic diversity, and to flag companies with no representation in their research documents. This was to ensure we meet our voting objectives on this issue as clarified in our Proxy Policy updates earlier this year (please see Principles 2 and 5 for more details). Due to limited availability of these data sets, it is important to gather as much data as possible, and leveraging third-party providers would help bridge the gap while data improves, particularly in the U.S. and U.K..

ESG Data Providers

As noted above, investment teams use ESG data in a number of different ways. Some use it to inform their own fundamental research while other teams are integrating third-party data into factor models and proprietary scoring frameworks.

For ESG data and information, MSIM may leverage third-party data on top of any independent analysis it conducts. MSIM recognises that the lack of standardised ESG disclosures has created a fragmented market, and until such disclosures are improved and systematised it may need to leverage third-party ESG information. MSIM does this through both its own relationships with third-party ESG data providers and those that Morgan Stanley licenses at the Firm-wide level. MSIM can also draw on the expertise of the Morgan Stanley Institute for Sustainable Investing and the GSF division relating to ESG data analysis, to support and inform various approaches to data integration. For example, MSIM partnered with GSF to map individual EU SFDR indicators to third-party ESG data prior to any regulatory datasets being available in the industry. As vendors have come up to speed on EU regulations, MSIM has already integrated its approach with new vendor datasets that address ESG regulations and data points more specifically.

SELECTION AND ASSESSMENT OF ESG DATA PROVIDERS

When selecting ESG data providers, a number of factors are considered, including methodology, coverage, time series availability, transparency, and materiality alignment. An industry-wide assessment of ESG data providers covering several hundred providers was conducted several years ago by our GSF division. This has enabled additional statistical analyses which take place whenever the team onboard or consider new providers or datasets to understand similarities or differences between data providers across a common universe (e.g., any potential biases in datasets).

An example of a recent market-wide dataset assessment relates to the analysis we conducted on third-party vendor solutions for the EU Taxonomy. The team asked each of the vendors under assessment to provide as much granularity as possible on each of the steps of its Taxonomy assessment on the same universe of companies.

In general, our findings from these assessments allow us to make more informed decisions on vendor solutions, understand issues and challenges vendors are facing, and ultimately better assess their respective product solutions to fit our investment and engagement needs.

These analyses are always conducted in parallel to a relevant literature and methodology review. As was the case with some physical risk vendor offerings, our analysis of Implied Temperature Ratings ("ITRs") ultimately led us to the conclusion that some of these third-party vendor solutions are not yet fit for purpose. Significant differences in output results for the same set of locations or portfolio holdings imply that while a vendor solution was available in the market, utilising the solution in a portfolio management context would not be appropriate at this time.

In order to democratise ESG data access, broaden use of these data points and create a consistent set of high-quality and commonly utilised vendors and datasets, the Firm has put in place an "ESG data stack". The ESG data stack contains data sets across the ESG spectrum of approaches, across asset classes, and across data providers. The data stack is constantly being reviewed to ensure the highest quality vendors are used, and new datasets are added when:

1. emerging sources of ESG data are made available (e.g., asset class expansion or specific thematic areas like climate risk or water utilisation);
2. coverage can be improved;
3. a more transparent or granular data set is available; or
4. an improved methodological approach is utilised.

QUALITY CONTROL EXAMPLES AND REMEDIATION PROCESS

In general, third-party ESG data is centralised at Morgan Stanley for broad consumption across the organisation, including the MSIM business. As part of this centralisation process, data is vetted with quality control checks on a recurring basis to ensure data provider feeds are accurate, timely and, where needed, merged with existing firm infrastructure, identifiers and/or expanded to improve issuer coverage.

When quality control checks identify potential issues, the centralised ESG data team at Morgan Stanley that maintains supplier relationships will engage the data provider in a timely manner to ensure revised data is provided, or an explanation regarding the issue is provided. Recent examples include:

- a vendor error which resulted in corporate ratings weight summing to over 100% for a small select group of companies;
- a file transfer error that resulted in an unexpected coverage drop from month to month; and
- a vendor calculation error that resulted in an incorrect scope 3 value being applied to an Oil and Gas company as a result of a barrel of oil equivalent coefficient being incorrectly scaled.

Under these circumstances, data providers will then need to pass further quality control checks upon further granular inspection of the data. If questions still exist, the team will take appropriate action which may range from liaising further with the data provider to resolve the issue, to terminating use of the relevant product or services. In some cases, erroneous data is purged from our centralised ESG data platform and replaced with corrected information. All users of such information are notified via mail groups, at which point revisions to reporting would be made or noted if any of the information was used.

Updates, including new additions or changes to a vendor data feed are handled similarly. The centralised ESG data team works with the vendor to identify the change, assess the downstream impact on technology systems and establish a timeline for the change to be implemented. Relevant teams are notified in advance following best practices associated with change management.

Consistent Framework Across MSIM

The MSIM ESG Technology and Data team follows data governance standards as laid out by the Firm's Global Data Governance Framework. Since the acquisition of Calvert, the team has a dedicated group that is actively engaged in integrating data and technology systems across MSIM and Calvert and ensuring alignment with Morgan Stanley data governance principles.

The policies, procedures and processes we implement in continuously monitoring, working with and assessing service providers such as proxy advisors and ESG data providers demonstrate our commitment to ensuring a consistent framework across an organisation of our size, particularly on data quality, assurance and vendor standards. In particular, we are working towards supporting our activities outlined in Principles 2, 6, 7 and 8, as well as others, with a foundation of centralised and well-governed ESG metrics which will enable consistency and transparency in internal reporting, client reporting and investment engagement.

SECTION 3

Engagement

PRINCIPLE 9

Engagement

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

Engagement Selection and Prioritisation

OUR APPROACH

A key input to our investment selection process is an assessment of the quality of the company's board and senior management. To develop that knowledge, MSIM investment teams engage with company management at regular intervals and prioritise active dialogues where positions are significant and where they view issues as material. Approaches to engagement vary across our investment teams as described in Principle 7 and below but, in general, the investment teams directly engage with portfolio companies, leveraging support from the Global Stewardship team as needed, and having regard to MSIM's Engagement and Stewardship Principles. Our investment teams engage with companies throughout their investment process on a broad range of issues including a company's strategy, financial and non-financial performance, risk management, corporate governance, sustainability initiatives and capital structure. Our investment teams endeavour to engage in constructive dialogue with companies, which encompasses anything from a series of meetings and discussions on a particular issue to multiyear engagements/stewardship on a range of E, S or G topics specific to the company or asset to ensure holistic and resilient enhancement or transformation.

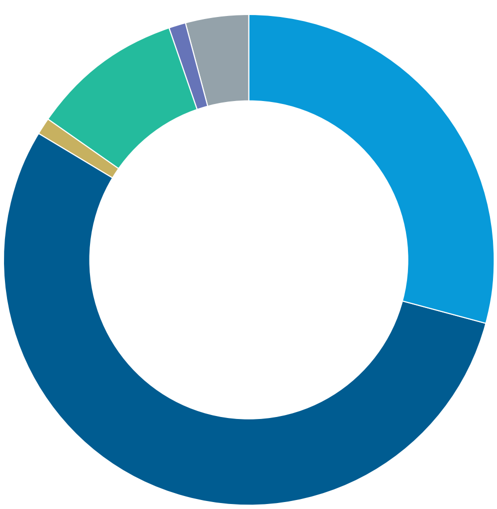
PRIORITIES AND PURPOSE

As part of our MSIM Sustainable Investing/Engagement Philosophy, we focus on four thematic engagement priorities,[30] aligned with the UN Sustainable Development

FIGURE 9.1

MSIM Engagement Statistics (1 July 2021 – 30 June 2022)

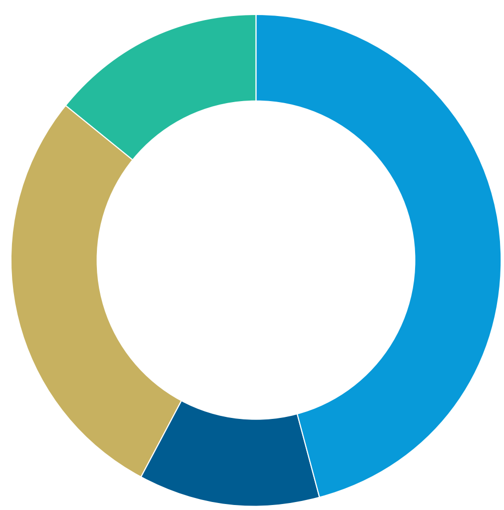
MSIM Engagements by Region



Europe	29%
North America	54%
South America	1%
Asia (Ex Japan)	10%
Japan	1%
Rest of World	4%

Total Engagements[29]: 646

Engagements by MSIM Sustainability Focus Areas*



Decarbonisation & Climate Change	46%
Circular Economy & Waste Reduction	12%
Diverse & Inclusive Business	28%
Decent Work & Resilient Jobs	14%

* This pie chart refers only to the breakdown of MSIM priority engagement themes; other engagement subjects are also covered by investment teams.

[29] Refers to ESG engagements conducted by MSIM investment teams, Global Stewardship team, Calvert, Eaton Vance and Parametric between 1 July 2021 and 30 June 2022. Includes engagements with corporate and non-corporate issuers.

[30] Our legacy MSIM engagement priorities were established in 2020.

Goals ("SDGs"), in recognition that certain environmental and social issues can cause systemic risk to the economy and capital markets, and in some cases pose an existential threat to life on Earth. These views can also be shared by our clients, an often important contributor to the thematic engagement priorities.

As explained in Principle 1 above, our investment teams share an overarching belief that investing responsibly and engaging as long-term owners reduce risks and positively impact returns over time. Accordingly, the four thematic engagement priorities presented below touch all of our investment teams to varying degrees depending on asset class, geography, investment style and strategy. Examples of investment team-specific engagement approaches over the 12 months from 1 July 2021 to 30 June 2022 are outlined throughout the rest of this section.

MSIM investment teams prioritise engagements based on a variety of factors including position size, investment horizon, frequency of annual general meetings, headline events and materiality.

PROCESS AND METHODS

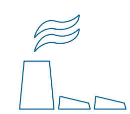
Engagement is a valuable tool for our teams to deepen their insight and understanding of an issuer and the sector or asset class more broadly. MSIM investment teams work to ensure that shareholder engagement is effective and works in the best interests of clients to improve the long-term returns from the companies in which they invest. Although MSIM does not have centralised investment beliefs across asset classes and strategies, there are certain parallels in the chosen approach to engagement across our various investment teams, which reflect our core values as a firm and our determination to act as responsible long-term investors (as described in Principle 1 and Principle 6 above):

Investment teams **generally seek to engage constructively with company management** to encourage improved disclosure, behaviour change and (where appropriate) target-setting.

1. If those efforts prove unsuccessful, they may **escalate their issues or concerns to one or more members of the board of directors.**

FIGURE 9.2

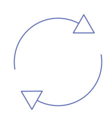
MSIM Thematic Engagement Priorities: Four Key Themes Pursued across MSIM



DECARBONISATION AND CLIMATE ACTION

Supporting the transition to a low carbon economy in line with Paris Agreement goals

- Renewable energy and clean tech
- Energy efficiency
- Physical impact adaptation
- Just transition



CIRCULAR ECONOMY AND WASTE REDUCTION

Supporting business models that reduce impact on natural resources and that innovate to reduce waste generation, with a focus on plastic waste

- Recycling and reuse
- Sustainable sourcing
- Life cycle analysis
- Water stewardship
- Biodiversity

DIVERSE AND INCLUSIVE BUSINESS

Supporting business practices that create a more just and inclusive society

- Affordable access to essential services
- Investing in communities
- Racial justice
- Pay equity
- Board/employee diversity

DECENT WORK AND RESILIENT JOBS

Supporting decent work across the entire value chain and making workforces resilient in the face of innovation and change

- Automation and the workforce
- Supply chain management
- Living wage
- Workforce well-being

This represents how the portfolio management team generally implements its investment process under normal market conditions.

The content of this publication has not been approved by the United Nations and does not reflect the views of the United Nations or its officials or Member States. See https://www.un.org/sustainabledevelopment/sustainable-development-goals/ for more details on the Sustainable Development Goals

2. Following that, they have the **option of voting against management proposals, board directors or supporting shareholder resolutions.**
3. Investment teams **prefer one-on-one engagements directly with senior management/board directors** as they are the most effective way to articulate views to, and engage in constructive discussion with, a company's management.

Notwithstanding one-to-one engagements with senior management/board directors, we are also supportive of collaborative engagement where such engagement appears necessary to materially enhance portfolio values and likely to deliver tangible outcomes in relation to key sustainability or stewardship-related issues, provided we can do so in a manner that is in full compliance with applicable laws, regulations and judicial precedents. More details on our collaborative engagement activities are outlined in Principle 10.

STEWARDSHIP MONITORING AND ENGAGEMENT

MSIM is a predominantly active investment house and investment teams are responsible for monitoring the performance of companies throughout the investment process. The extent and frequency of monitoring varies across investment teams and is dependent on a number of factors including the investment strategy and the size of interest held.

Some investment teams actively monitor at the stock level by evaluating company fundamentals, financials and management, including sustainability management. Others approach portfolio construction using a top-down, macro approach to strategic asset allocation and undertake thematic engagements with select companies across the portfolio, as needed. Investment teams may take different approaches depending on asset class and type of security, and certain issues may be deemed more material for issuers in certain geographies. For example, a minority public equity investor's approach may differ from a private equity investor with a controlling or majority stake. Furthermore, in relation to variance across geographies, teams have observed that diversity and inclusion is a significant topic across Europe, whereas in Asia, companies and investors tend to have a heightened focus on augmenting corporate governance structures and cultures.

Monitoring of companies in which MSIM invests may include, but is not limited to:

1. **Reviewing and analysing relevant public information published by the company** (which may include a company's quarterly financials, earnings calls, general company reporting and/or disclosures, including sustainability-related disclosures);
2. **Developing proprietary quantitative models** to forecast performance, leveraging third-party data services;
3. **Conducting proprietary and reviewing external research;**
4. **Attending company presentations and/or analyst conferences;**
5. Where appropriate, **engaging directly with companies in which MSIM invests** (which can include engagement with company executives and board members through in-person meetings, conference calls and email correspondence); and
6. **Ongoing monitoring of external events that may impact company performance (e.g., regulatory changes, news events).**

These monitoring activities support real-time identification of engagement targets and topics across our Investment teams' portfolios.

SUPPORTIVE FUNCTION OF THE GLOBAL STEWARDSHIP TEAM

The majority of engagements co-ordinated by the MSIM Global Stewardship team focus on shareholder meetings and take place during proxy season. During these engagements, the Global Stewardship team and members of relevant investment teams meet with company management and, when appropriate, a member or members of the board of directors to discuss the issues raised by the company's proxy, including, but not limited to, executive compensation, board structure, ESG issues and shareholder proposals.

Topics of routine engagement focus on governance best practices such as board independence, succession planning, and executive pay. Other topics of consideration include the company's sustainability initiatives and goals, and corporate culture. In consultation with individual investment teams, the Global Stewardship team may request engagement outside the normal proxy process in response to a company headline event or to proactively discuss thematic ESG issues. In these cases, the Global Stewardship team may contact the company and request a meeting with the appropriate management team and/or a member or members of the board of directors. MSIM representatives selectively interact with company boards when the knowledge and experience of the Global Stewardship team may be necessary and beneficial to the engagement process.

Highlights from 2022 Proxy Season

During the 2022 proxy season, MSIM[31] took a focal approach on climate and diversity and inclusion-related proposals, in addition to other sustainability/ESG-related areas deemed material by each investment team based on their respective strategies. Our 2022 activities and approach reflect the implementation of the revisions to our Proxy Policy earlier this year (Principles 2 and 5).

MSIM is supportive of increased disclosure on climate risk and reporting based on the TCFD framework. Certain investment teams use the Transition Pathway Initiative ("TPI") data as a starting point to review before determining our decision, given our belief that TPI has a strong scoring system, having reviewed more than 200 of the world's largest carbon emitters.

For diversity and inclusion, our expectation is at a minimum 30% gender diversity for S&P 500 and FTSE 350 companies. For companies outside of the U.S., we would base our view on the market benchmark, (e.g., for Asian markets, we would require at least one gender diverse nominee). Where we observe a lack of racial diversity and data is readily available, we will recommend against nominating committee members.

Our teams are also supportive of additional disclosures including, but not limited to, human rights risks, supply chain management, workplace safety, human capital management and EEO-1 disclosures.

INVESTMENT TEAM APPROACHES BASED ON MSIM THEMATIC ENGAGEMENT PRIORITIES

As mentioned above, though MSIM has established four thematic engagement priorities, our investment teams prioritise engagement objectives, methods and assessments in varying degrees depending on asset class, geography, investment style and strategy. The following examples demonstrate investment teams' diverse engagement strategies and corresponding rationale:

International Equity

Engagement Approach

The portfolio managers are responsible for engaging with company management, alongside/supported by the team's Heads of Sustainable Outcomes and ESG Research when the engagements are ESG-focused. The team's ESG engagements generally have three key purposes:

1. Assessment of materiality of specific ESG issues relevant to companies;
2. Their strategies to address these issues; and
3. Monitoring of progress and influencing companies towards better practices.

In the case of the latter, the team engages with specific objectives and tracks the company's response and progress including, but not limited to, improved disclosure, behaviour change and (where appropriate) target-setting.

Their engagement can be divided into the following types:

1. **Executive/board level:** The portfolio managers meet with senior management and board members to discuss the fundamental drivers underpinning growth and returns, at which material company-specific ESG issues are frequently raised. They prefer one-to-one meetings with senior executives over group presentations.
2. **Company governance/sustainability team:** The International Equity team's dedicated Heads of Sustainable Outcomes and ESG Research work alongside the portfolio managers to identify and conduct potential engagements which require robust enquiry with the company's corporate governance or ESG/sustainability representatives.
3. **Thematic engagement:** For example, the team's ongoing carbon engagement series with companies across various sectors. Similar thematic engagement activities have been conducted, including on the circular economy with Consumer Staples companies.

The method of engagement is usually determined on a case-by-case basis, depending on the topic that they want to discuss with company management and the timeframe. Dialogue with companies on engagement topics can be prolonged and require multiple engagements. As long-term shareholders with an owner's mindset, the team's active engagement is aligned to their long-term investment approach. Initial engagements may focus on fact finding, building understanding of how the company approaches a particular subject, and the measures and policies they may already have in place.

The team prefers to build an in-depth understanding of what the company is doing by engaging with the company's Sustainability team and Investor Relations. If the team requires more information, or have

[31] Refers to Legacy MSIM.

specific questions that they wish to have answered, as shareholders they have good access to company senior executives, and will engage directly with them on the subject.

ENGAGEMENT PROGRESS MONITORING

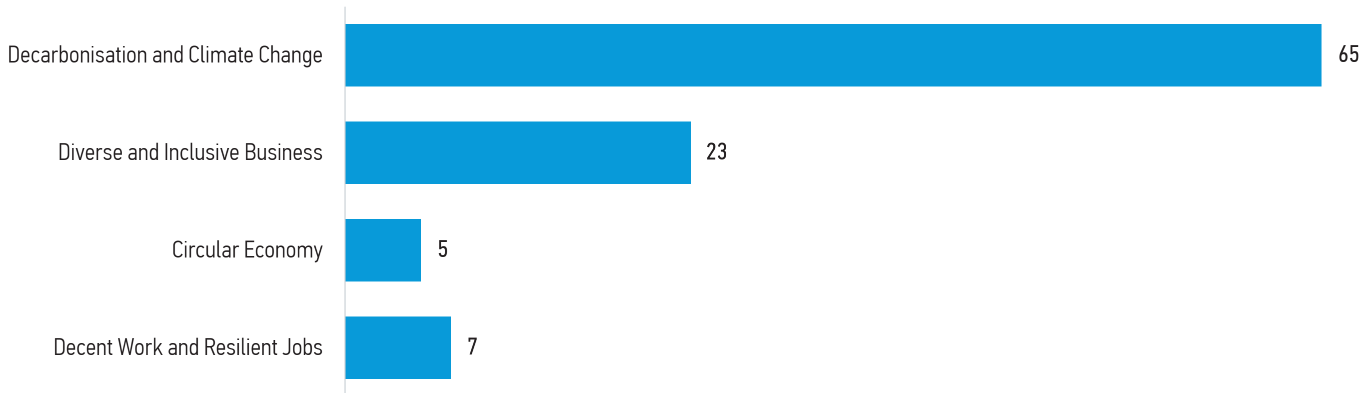
After initial engagement, the team seeks to assess the company's actions, and will monitor progress through continued engagement if they think a company is on the right track, or engage further to encourage change.

ENGAGEMENT CASE STUDY 9.1

ASSET CLASS	• Equity
MSIM ENGAGEMENT THEME(S)	• Diverse and Inclusive Business
TYPE OF COMPANY	• French wine and spirits seller
REASON FOR ENGAGEMENT	• The engagement covered the board make-up and executive compensation, and was the fourth of an ongoing series of engagements on the subject with the company in an effort to encourage change.
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in integrating requirements, delivering sustainable long-term returns through ESG integration, aligning engagement/ investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with company management • Recommending changes and providing strategic advice
DETAILS OF ENGAGEMENT	• Despite being a global company with a major footprint in markets outside Europe, the company had an all-White European board. The International Equity team was concerned about this as they believed the company could benefit from the insight and experience that a more diverse board could offer to the business • The team has always paid close attention to executive compensation and engaged with companies to improve remuneration practices. The team had been seeking changes to the company's executive compensation structure, having reservations regarding their use of options in their long-term incentive plan ("LTIP"). They had also questioned the lack of measurable ESG metrics for key performance indicators ("KPIs")
ENGAGEMENT OUTCOME	• The team was encouraged to learn during the engagement that the company had adopted a number of their suggestions, made during previous engagements • The team was delighted to learn of the appointment of a female board member of Indian heritage who brings business experience from Australia and Asia, including Malaysia and Myanmar. While the team recognises that the company still has further to go, they were encouraged that a start had been made, and consider the board appointment a successful outcome • The company's LTIP is now 100% performance-based (there are no more options), incentivising long-term performance over short-term targets. The company has also set measurable targets for carbon, water, diversity and responsible consumption, enabling management to be held accountable to ESG-related targets over the longer term
INVESTMENT DECISION	• **Continue to hold investment position**
NEXT STEPS/LOOKING AHEAD	• This engagement was satisfying, seeing outcomes the team had been working towards coming to fruition. The team will continue to engage with the company using their Diversity, Equity & Inclusion checklist, pushing for more data and better transparency.

FIGURE 9.3

International Equity Engagements – Corresponding with MSIM Thematic Engagement Priorities



(Please note: more than one subject may be covered in a company engagement, and therefore the total number of engagements may not equal the total number of discussion topics. The chart above is not representative of the full scope of engagement topics covered by the International Equity team during the time period.)

Progress may be monitored through additional virtual or face-to-face meetings, via the telephone or by email correspondence. If the team does not see any progress, they will consider appropriate escalation (please see Principle 11 for the International Equity team's escalation approach and case studies).

The team measures progress as follows:

- Does the company acknowledge the issue raised?
- Has the company come up with a plan and/or specific targets to address the issue?
- Has the company implemented this plan?

Progress may be demonstrated, for example, by the company improving disclosure on a subject, setting official targets, or by linking KPIs related to the issue to management compensation.

INTEGRATING CLIENT SUGGESTIONS IN ENGAGEMENTS

At the client level, if a client has a specific subject on which the team has not previously been engaged, the team will consider bringing that up in future engagements, where relevant and appropriate.

The team's long-term focus on long-term fundamental quality and engagements with companies is continuous, ongoing and robust. The case study below demonstrates this:

From 1 July 2021 to 30 June 2022, the International Equity team had a total of 108 ESG engagement meetings. *Figure 9.3* shows a breakdown of portfolio company engagements that corresponded with MSIM's Thematic Engagement Priorities:

Counterpoint Global

Engagement Approach

The Counterpoint Global team takes a long-term oriented approach to investing, which focuses on identifying differentiated insights on multiyear opportunities. As long-term investors, and active owners, the Counterpoint Global team believes that they have a duty to be good stewards of the capital they manage. The team fulfils this duty by engaging with the companies in which they are invested and by exercising their proxy voting rights. These stewardship activities give the team the opportunity to guide companies in which they invest toward better governance practices, which the team believes will produce long-term, sustainable returns. The Counterpoint Global engagement approach is viewed holistically with their investment activities and they consider their ability to deliver long-term value; hence, they do not actively track their number of engagements, which is not a meaningful statistic that is value-additive to the investment process—each portfolio company is engaged with differently given respective areas of materiality.

Given the team's position as active, long-term owners, they have regular touchpoints with investee companies and have formed relationships with company management. This means that the team's engagement process is iterative, with each engagement providing new information that enhances the team's view of the company and what they regard as its priorities, gaps and opportunities. When the team has provided suggestions or recommendations for companies on their business practices, the team monitors the company's alignment with these suggestions over a period of time. The team's engagement tracking notes allow them to flag issues for follow-up and for monitoring throughout the investment process. The team often goes into engagements with pre-defined topics to discuss with a company, but in some cases they will identify additional issues through an engagement, which then become new issues to monitor moving forward. For companies with significant, ongoing ESG challenges, the team may monitor a company's management of the same issue over an extended period of time and discuss that issue in every subsequent engagement call. For other companies, the topics of engagement may change frequently along with the KPIs and objectives used to monitor them.

Consistent with the approach to engagement across MSIM investment teams, the Counterpoint Global team looks to engage in constructive dialogue with the management teams of portfolio companies in all aspects of the business. The team is increasingly finding that its global, all-sector, all-capitalisation, integrated sustainability research approach is novel to companies and presents the opportunity for partnership, where the team shares strategies with companies to help them capitalise on the sustainability opportunities available to the company. The team selectively offers companies access to its network of other operators, or sustainability practitioners, where they think doing so would create the opportunity for a mutually beneficial dialogue.

The team engages with company management when evaluating strategy and management quality. Where appropriate, the team's portfolio groups engage companies to discuss issues that may include environmental and social policies and practices. The team may also seek support from the MSIM Global Stewardship team when, for example, their expertise on a particular issue is needed. The team generally does not seek out Board-level conversations without substantive concern, as they prefer that Boards remain focused on their core mandates of strategy, management and risk oversight.

The team pays close attention to proxy voting, using their votes and other shareholder rights to promote governance aligned with long-term shareholder interest. The Counterpoint Global team also engages some companies in discussion on various aspects of corporate governance, sometimes as an adjunct to proxy voting.

Counterpoint Global engages with companies in different ways, including:

1. **The Team's Sustainability Lead Working With the MSIM Global Stewardship Team to Directly Engage Current Portfolio Holding Companies** – through the governance channel to discuss ESG initiatives. Most recently, ServiceNow, a U.S.-based holding, engaged with the team to specifically discuss ESG. The conversation included C-level executives.
2. **Regular Meetings with Senior Management of Portfolio Companies** – In regular updates with management teams of our portfolio companies, our investment team members address ESG drivers where there are clear enterprise value implications (e.g., expected dilution from share-based-compensation). Socio-economic empowerment, inclusion, community development, data governance, security and risk management are other areas of high focus.
3. **Global Institutional Conferences Attended by Portfolio Companies' Sustainability Heads** – members from the team attend and/or speak at these conferences, the attendance of which would generally include senior sustainability officers from current portfolio companies and other global organisations.

Based on information obtained via various means outlined above, investment team members create Sustainability Research Engagements Insights which are then distributed to all members of Counterpoint Global following an "SR Engagement", which the team defines as a discussion where it asks its set of questions that are designed to understand the state and sophistication of the company's sustainability strategy and processes. These SR Insights notes synthesise the key insights learned from the discussion, which tend to contextualise the opportunities and risks as well as assess the team's understanding of the long-term alignment of incentives as well as the culture of adaptability, which the team views as often useful in capitalising on Sustainability-related themes. On a quarterly basis, the team's Sustainability Integration Lead highlights the most material and often out-of-consensus insights acquired through that quarter's engagements, giving the senior investors the opportunity to ask questions and prompt new questions for future engagements. These insights are additive to the entire analysis of the company, to give senior investment decision-makers a more complete view into the opportunities and risks facing the company.

The following case studies demonstrate long-term engagement undertaken by the Counterpoint Global team resulting in significant and holistic enhancements in Sustainability:

ENGAGEMENT CASE STUDY 9.2

ASSET CLASS	• Equity
MSIM ENGAGEMENT THEME(S)	• Decent Work & Resilient Jobs: Data; Structural Long-termism • Diversity & Inclusive Business • Others: ESG solutions—enabling others' ESG programmes
TYPE OF COMPANY	• U.S.-headquartered global enterprise cloud computing solutions
REASON FOR ENGAGEMENT	• Position was initiated in the company in 2012 • Counterpoint Global has been a long-term shareholder and partner of the company • Counterpoint Global sees the company as having significant positive Sustainability Optionality • By working with the company, the investment team hopes they can help it to increase its significant positive sustainability optionality
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings/dialogue with the company's various stakeholders including senior management, the company's Head of ESG and Global Impact, the VP and GM for Risk and ESG, General Counsel, etc. • Remediation proposals and sharing of best practices • Thought leadership and strategic advice.
DETAILS OF ENGAGEMENT	• Ongoing engagement throughout the years, including with respect to executive compensation and diversity • Discussed the company's new ESG solution which will enable its customers to better set targets and goals related to ESG, execute on those goals and report out on them. The company's "ESG command center" solution connects people, systems and data and allows its customers to operationalise processes to increase speed, efficiency and scale • Counterpoint Global was able to extend an invite to one of the members of their ESG team to the Aspen Institute's Fellowship Program, which senior management greatly appreciated • Additional discussion topics included diversity metrics across all levels of the organisation and within the Board, where they will continue to look to make progress, and executive compensation and its alignment with long-term value creation.
ENGAGEMENT OUTCOME	• The company incorporated Counterpoint Global's recommendations on executive compensation and long-term incentive alignment (added a three-year TSR metric), removed evergreen provisions, and has since published a sustainability report taking into account Counterpoint Global's input • The company is expected to benefit from Counterpoint Global's introduction to its network of sustainability experts, sharing best practices and ideas • Strategic insights continue to be incorporated in the company's business strategy regarding its ESG solution and long-term sustainability
INVESTMENT DECISION	• **Continue to hold investment** in the company after the assessment given belief it has significant Sustainable Optionality
NEXT STEPS/LOOKING AHEAD	• Continue to engage and partner with the company on growth prospects, brand strength and enabling its customers' ESG programmes—driving a multiplier effect

ENGAGEMENT CASE STUDY 9.3

ASSET CLASS	• Equity
MSIM ENGAGEMENT THEME(S)	• Decent Work & Resilient Jobs: Effective Institutions; Structural Long-termism
TYPE OF COMPANY	• U.S.-headquartered manufacturer and distributor of non-lethal electrical deterrents for personal defence and body cameras to increase public transparency
REASON FOR ENGAGEMENT	• Position was initiated in the company in 2021 • Counterpoint Global sees the company as having significant positive sustainability optionality • By working with the company, the investment team hopes they can help it increase its significant positive sustainability optionality
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with the company's senior management, including the CEO, CFO, General Counsel and Investment Relations and ESG teams • Remediation proposals and sharing of best practices • Strategic advice
DETAILS OF ENGAGEMENT	• Ongoing engagement throughout the years • Discussed the company's Sustainability narrative, in that its products and solutions are protecting lives and reducing the number of deaths from law enforcement encounters, leading to enhanced public safety • Engaged in discussion on shareholder rights and governance structures, including majority voting and declassified boards, to align with long-term value creation as they continue to mature as a public company • Provided opinions on executive compensation, including not overweighting TSR metrics and aligning with operational and profitability metrics, as well as employee compensation to enable employee empowerment and a deeper sense of ownership within the company
ENGAGEMENT OUTCOME	• The company incorporated Counterpoint Global's recommendations on certain structures supporting long-term value creation, including majority voting and declassifying the Board, amongst others • CEO continues to strategise on ways to provide further benefits to the other employees as well as further align their own compensation with sustainability-related outcomes
INVESTMENT DECISION	• **Continue to hold investment** in the company after the assessment given belief it has significant sustainability optionality
NEXT STEPS/LOOKING AHEAD	• Continue to monitor and engage the company on growth prospects, brand strength, and effectively communicating its Sustainability narrative as it is an underappreciated value driver for the company

Global Opportunity

The Global Opportunity team manages highly differentiated, concentrated portfolios. Investing as long-term owners allows the team to concentrate capital in its highest conviction ideas for typical holding periods of three to five years. Over extended time horizons, the team believes that ESG risks are more likely to materialise and externalities are more likely to be priced into the value of securities. Therefore, the team continues to innovate and evolve its process and believes that integrating ESG within its investment analysis improves the investment risk and reward profile of client portfolios.

The Global Opportunity team's investment process integrates analysis of sustainability with respect to disruptive change, financial strength and environmental and social externalities and governance. The team views ESG as a component of quality and considers the valuation, sustainability and fundamental risks inherent in every portfolio position. As bottom-up investors, the team does not apply top-down ESG positive/negative screens to a benchmark. Nor does the team utilise ESG scorecards from third parties which rank companies versus industry peers. In other words, ESG in isolation is not a principal driver of the team's investment thesis;

ENGAGEMENT CASE STUDY 9.4

ASSET CLASS	• Equity
MSIM ENGAGEMENT THEME(S)	• Decent Work & Resilient Jobs • Circular Economy & Waste Reduction
TYPE OF COMPANY	• Korean e-commerce platform
REASON FOR ENGAGEMENT	• To discuss ESG initiatives including human capital management and sustainable packaging
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values.
ENGAGEMENT METHOD	• Meetings with company CEO and CFO • Remediation proposals and sharing of best practices • Strategic advice
DETAILS OF ENGAGEMENT	• Discussions emphasising the importance of improving public relations efforts to address negative publicity and correct false allegations in the media after initial public offering, as well as the use of sustainable packaging • Shared best practices regarding the creation of positive impacts on society, especially in relation to worker benefits, employment opportunities and enabling small- and medium-size enterprises (SMEs) through its platform
ENGAGEMENT OUTCOME	• The company shared more about how its platform enabled SMEs to sell products online which led it to become the leading creator of private jobs in the country, supporting SDG8: to promote decent work and economic growth • The company is the only major logistics company that directly employs 100% of its full-time delivery drivers with an industry-leading five-day work week with insurance, benefits and a minimum of 15 days' paid leave from day 1 of employment • Delivery drivers typically visit the same neighbourhood multiple times per day, eliminating disposable packaging and deploying re-useable eco-bags that are collected and re-used after each delivery • Customers are allowed to return items without requiring boxes, labels or postage, further reducing the resource footprint of their fulfilment process • The company has also eliminated cardboard boxes in over 75% of parcels by re-engineering the end-to-end fulfilment process and is exploring electric vehicle options for delivery trucks that fit its criteria. This company's unique logistics network coverage supports SDG12: responsible consumption and production
INVESTMENT DECISION	• **Continue to hold investment position** in client portfolios
NEXT STEPS/LOOKING AHEAD	• Continue to monitor and engage with the company to ensure that management continues to execute on long-term strategy to build a platform and logistics network that has a positive impact on society

it is but one important component of the team's quality assessment.

Incorporating ESG-related potential risks and opportunities within an investment process is about ensuring long-term stewardship of capital. Over extended time horizons, the team believes that ESG risks are more likely to materialise and externalities not borne by a company are more likely to be priced into the value of securities. Therefore, Global Opportunity continues to innovate and evolve its process and believes that integrating ESG within its investment analysis improves the risk and reward profile of client portfolios.

Engagement Approach

For Global Opportunity, engagement priorities differ by individual company and are not region-specific. The team's research has identified both ESG opportunities as well as risks that may impact the value of a company. In such cases, the team takes an engagement approach to guide/steer the company towards better sustainability practices and strategies that correspond with the company's business. This is demonstrated in the following case study:

Emerging Markets Equity ("EME")

Engagement Approach

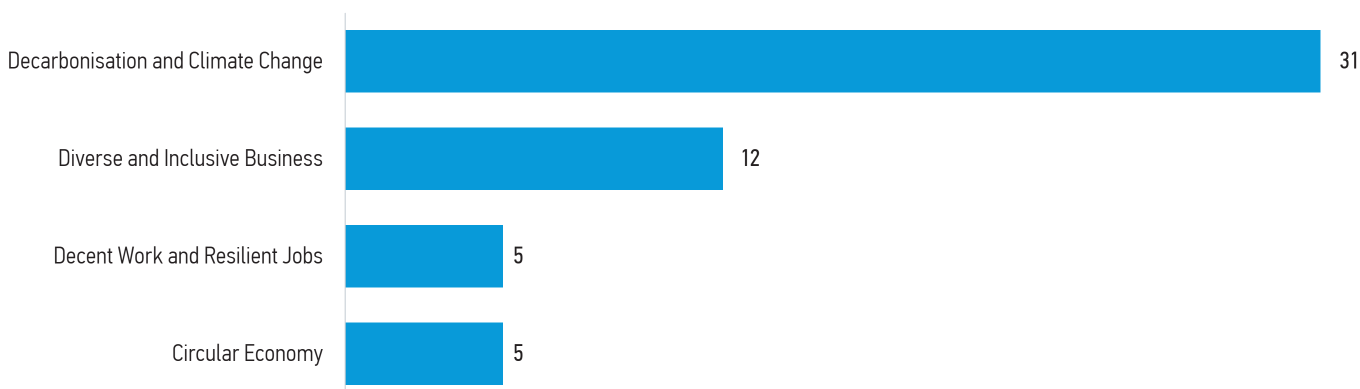
The team's portfolio managers lead their own engagements for respective EME strategies alongside the team's dedicated sustainability team. EME prioritises engagements using a multi-pronged approach, including its thematic agenda, for example where they are currently focused on decarbonisation, or top portfolio holdings or companies where the team has identified that there is a good opportunity for change or companies with material issues they would like to address (e.g., Board composition/diversity) or companies with insufficient disclosure. EME maintains a list of target companies throughout the year with which they engage based on the aforementioned priorities.

EME's engagement process is driven by financial materiality and improving performance through understanding a company's financial and sustainable strategy. As active managers, the team understands that companies' operational performance and ESG strategies are dynamic. Research and engagement allow the team to look beyond an ESG data point and analyse how a company's ESG risks and opportunities are evolving, and how they will impact long-term financial performance. Engaging with management teams allows the team to evaluate whether the company has a clear differentiator and gives them an additional lens into viewing management quality. When engaging, the team seeks to understand how a company's ESG targets and programmes might be embedded in the company's overall strategy and cost structure.

After identifying material risks for a company, the team conducts a baseline engagement meeting with management. EME believes that a company's engagements are a two-way street—the team not only listens and learns about the company's sustainability strategy, but also educates the company on industry best practices and provides guidance, such as encouraging management to set specific emissions targets and communicating the risks which the team believes are most material to the company. EME views a successful outcome as when a material metric improves, or when a company might adopt a suggestion or

FIGURE 9.4

EME Team Engagements – Corresponding with MSIM Thematic Engagement Priorities



(Please note: The chart above is not representative of the full scope of engagement topics covered by the Emerging Markets Equity team during the time period) industry standard, or where the company might disclose an additional metric or put in place more realistic targets.

Post-engagement, EME writes up its assessment of the company's sustainability strategy. For the first baseline engagement, the team focuses most on how the company acknowledges its ESG risks and how they have addressed them so far. EME also wants to understand the company's positioning and evaluate whether or not it is committed to improvement. In its assessment, the team identifies a few key areas and metrics on which they can follow up post-conversation. The team follows up in regular conversations with management.

Should EME not see meaningful improvement on material metrics, the team may put the stock into its escalation

ENGAGEMENT CASE STUDY 9.5

ASSET CLASS	• Equity
MSIM ENGAGEMENT THEME(S)	• Decarbonisation: Responsible Energy Transition
TYPE OF COMPANY	• Materials/Metals and Mining
REASON FOR ENGAGEMENT	• This was one of several engagements on decarbonisation, undertaken by the EME team to understand and assess the credibility and ambition of their portfolio's high-emitting companies' decarbonisation pathways and alignment with international climate goals
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with company management • Strategic and subject-matter expertise advice
DETAILS OF ENGAGEMENT	• The engagement focused on the company's decarbonisation pathway and climate strategy, which in turn influences the company's social licence to operate • Given that this was the EME's first call with the company, the team touched upon other topics as well, including water usage, circular economy, sustainable production and labour management and human rights practices
ENGAGEMENT OUTCOME	• The company has demonstrated significant progress regarding its decarbonisation targets. EME believes that the company has a viable decarbonisation strategy and roadmap, and the company is a strong performer relative to the rest of its industry peers • Having said that, EME takes the view that the company needs to do more work on addressing Scope 3 emissions, but understands that it is a complicated process and this aspect may take time—and will work with the company to assist with this process • The company is also moving steadily towards its goal to achieve 90% water recirculation across all operations by 2025. • While the company has ambitious decarbonisation and water management goals in place, EME believes that it can still make significant progress regarding biodiversity, human rights and Scope 3 emissions • Ultimately, the team believes that the company is an emerging leader and it will continue to engage with the company on their initiatives
INVESTMENT DECISION	• **Invested in the company**
NEXT STEPS/LOOKING AHEAD	• EME plans the next engagement with the company to focus more on water as scarcity risks are increasing, particularly given the company's operations in Chile. EME hopes that the company will also strengthen its framework around biodiversity risks and set more goals on circular economy. The team has communicated these expectations for improvement to the company and will continue to monitor progress on an ongoing basis.

protocols if the team feels that these metrics might impact the competitiveness and growth of the stock, or, if the company's inability to make progress degrades their trust in management, they may exit the position.

EME's approach to escalating engagement does not differ based on strategy or geography but is decided on a case-by-case basis at stock level.

During the full year 1 July 2021 – 30 June 2022, EME held a total 118 meetings with company management teams on a range of ESG topics. Of these, 76 were dedicated ESG meetings across 24 countries. *Figure 9.4* is a breakdown of topics on which the team engaged with portfolio companies based on MSIM's Thematic Engagement Priorities:

Global Fixed Income

Engagement Approach

The Fixed Income team has an important role to play in building a constructive dialogue with issuers and supporting them in pursuing positive sustainability outcomes while enhancing ESG disclosure and price discovery of the proper cost of capital when accounting for ESG risks. While engagement and stewardship have historically been an equity investor remit, the team believes that fixed income investors are uniquely positioned to have a positive influence on issuers, by leveraging more frequent issuance of new capital on primary debt markets for expressing our expectations around the use of such capital, as well as the access to a broader set of organisations beyond the listed companies targeted by equity investors, such as privately or state-owned companies and sovereign bond issuers.

As outlined in Principle 7, Fixed Income engagement efforts are led by Credit Research Analysts, with the support of the Fixed Income Sustainable Investing team. Unlike equity investors, bondholders are not entitled to vote on corporate governance matters or to attend AGMs. Nonetheless, the Fixed Income team is able to exercise effective stewardship and engagement, in particular through rigorous pre-investment due diligence, as well as through ongoing monitoring of KPIs and targeting of some companies that are perceived to be going off-track.

The Fixed Income team establishes an annual pipeline of target companies with which it aims to engage, based on the following criteria: high bondholding exposures across portfolios; laggard ESG scores which may result in the company being screened out from strategies that apply exclusions or best-in-class tilts; high carbon emissions; strong misalignment with SDGs associated with MSIM's thematic focus areas; violations of the UN Global Compact or other very severe controversies. The engagement pipeline is split amongst Investment Grade, High Yield and Emerging Market companies, based on the team's research coverage structure. The rationale for this approach is to establish a dialogue with the companies with which the team potentially has greatest leverage through its bond holdings, whilst also proactively addressing identified material ESG concerns within our investment universe. For example, over the past year the Fixed Income team increased its engagement with High Yield companies from 20% to 26% of the team's total meetings, to help address some of the ESG disclosure gaps they find in this space.

The Fixed Income team approaches issuer engagement constructively and collaboratively. Depending on the impetus for dialogue, the team seeks to set clear expectations from the engagement process. These can include the disclosure of specific data points, promoting the adoption of recognised ESG reporting standards, or suggesting alternative practices where the team is concerned with a certain course of action taken by the issuer.

Example – Setting Specific Targets

Over the course of 2021, the team engaged three times with an investment grade U.S. midstream energy company, soliciting them to set concrete targets related to emissions reduction and diversity. The company had no women on their Board of Directors and was reluctant to set decarbonisation targets—therefore the team sought to maintain a regular dialogue to push for a forward-looking approach to the company's sustainability strategy. Due to lack of progress on the ESG side over the period, the team's Credit Analyst assessed that ESG risk was starting to put downward pressure on the company's bonds valuation, and recommended taking a more cautious position in the name, while continuing to monitor the company's sustainability-related actions closely.

In cases where there is a cross-asset class focus on an issuer's ESG risk both on the equity and fixed income side, or an egregious conduct that warrants escalation by mobilising the broader MSIM franchise, the team may engage collaboratively with other MSIM investment teams and the Global Stewardship team (see Principle 10 for further information and examples of collaborative engagements within MSIM). Engagement efforts are also collaborative beyond MSIM: as members of the PRI's ESG in Risk and Ratings Initiative and of ELFA, for example, the Fixed Income team has participated in multiple workshops with issuers and credit rating agencies in an effort to push for enhanced ESG disclosure. Finally, the team also follows a targeted and thematic approach, as described previously.

Engagements are used as frequently as needed. The team continually monitors controversies across their holdings, and therefore in cases where they identify a material ESG risk or a particular ESG laggard, they aim to engage to assess whether any remediation strategies have been implemented. The Fixed Income team firstly identifies any material issues, for example any controversies or data discrepancies within sustainability reports, before delineating a set of specific questions and expectations. If the team identifies areas for improvement within its engagement, they may request action from the issuer. This can include a specific objective, such as setting a net zero target, and they may set a timeline if the company is lagging behind its peers.

The team's predominant method of engagement is via direct meetings with senior representatives in a company or organisation. These usually include senior Chief Financial Officers and members of the Treasury teams, Heads of Investor Relations and senior representatives from the Sustainability teams. For smaller companies, CEOs are also often attending the sessions. Whilst these meetings are usually intended more for monitoring purposes than for targeted engagement, the team often request one-on-one sessions with the companies as part of their investor outreach, in order to delve deeper into specific ESG issues.

Example – Monitoring Ongoing Progress

Earlier this year, the team engaged with an investment grade U.S. energy company to request an update on progress towards their long-term energy transition goals. The company responded by noting that they are accelerating the transition of their generation one year earlier than planned, and are ceasing coal use in certain locations two years earlier than planned, contributing towards the team's Credit Analyst assigning positive momentum to their sustainability strategy. Additionally, the regulatory landscape had shifted to support the company's emission reduction efforts, such that the company's bond price had increased since the passing of a bill in their jurisdiction to require 70% emissions reduction by 2030, with the Credit Analyst expecting further improvement.

During the past year, with the lifting of Covid-19 restrictions across many countries, the Fixed Income team's Credit Analysts have started meeting companies in person again, which facilitates a constructive dialogue with their management teams. They may use follow-up emails where necessary, for example to ask for specific data or supporting evidence for points covered during a meeting.

The Fixed Income team also deploys other engagement methods, such as thematic series targeting issuers in a specific sector to discuss a selection of topics. The Analysts then conduct follow-up discussions on a regular basis to assess the issuer's progress.

Example – Engagement Series

In late 2021, the team engaged for the second round of automotive engagements, having launched the thematic series in 1Q21, looking into a group of auto manufacturers' and suppliers' practices on supply chain management and investment in electric vehicles and technology. Additionally, in 2022, the team started a new engagement series with selected European high yield telecom companies, focusing on topics such as digital inclusion, data privacy and circular economy initiatives. Whilst the team often engages at the point of issuance, particularly with respect to labelled green/sustainable bond transactions, they also initiate and maintain an ongoing dialogue with issuers of bonds already held in their portfolios.

Engagements are initially constructive, as they aim to understand the company's strategies and identify sustainability momentum. If, after follow-ups, the team identifies that there has been no improvement, or that the ESG risk outweighs any reward, they would escalate the issue to MSIM management. As bondholders, the teams also use their buy/sell decisions as a way of indicating their sentiment to the company on their approach to sustainability.

Progress is monitored through the continual assessment of metrics. MSIM has access to a wide range of third-party ESG data vendors, and therefore they are able to track ESG metrics at the security level. The factors they consider vary based on the issuer and its sector. For example, within their autos engagement series, the teams conducted a materiality-based analysis to identify the most important metrics to monitor over time. These included metrics related to decarbonisation (such as percentage of fleet that are EVs), supply chain management (proportion of suppliers assessed using sustainability factors) and diversity and inclusion (such as gender diversity in the workforce and management).

Dependent on engagement, stakeholders can include: the Fixed Income Sustainable Investing team, Credit Research Analysts, Portfolio Managers, the Global Stewardship team, and MSIM's central Sustainability team.

As mentioned in Principle 7, Fixed Income engagement is defined at a global level, but implemented by the Credit Analysts based on their regional and sectoral coverage, with the support of the central Fixed Income Sustainable Investing team. The teams account for regional differences in their approach by considering the stage of development of the issuer's country, to ensure that assessment of their sustainability strategy and targets is contextualised and comparable to peers.

For example, the teams recognise that in some emerging markets, a longer glidepath might be necessary to achieve desired sustainability outcomes and minimise negative externalities (e.g., a longer phase-out period for fossil fuels in order to continue providing affordable energy to the broader population).

Between 1 July 2021 and 30 June 2022, MSIM Fixed Income conducted 145 ESG-focused engagement meetings. *Figure 9.5* shows a breakdown of topics on which they engaged with portfolio companies based on MSIM Thematic Engagement Priorities, including a detailed case study on multiple engagement topics earlier this year:

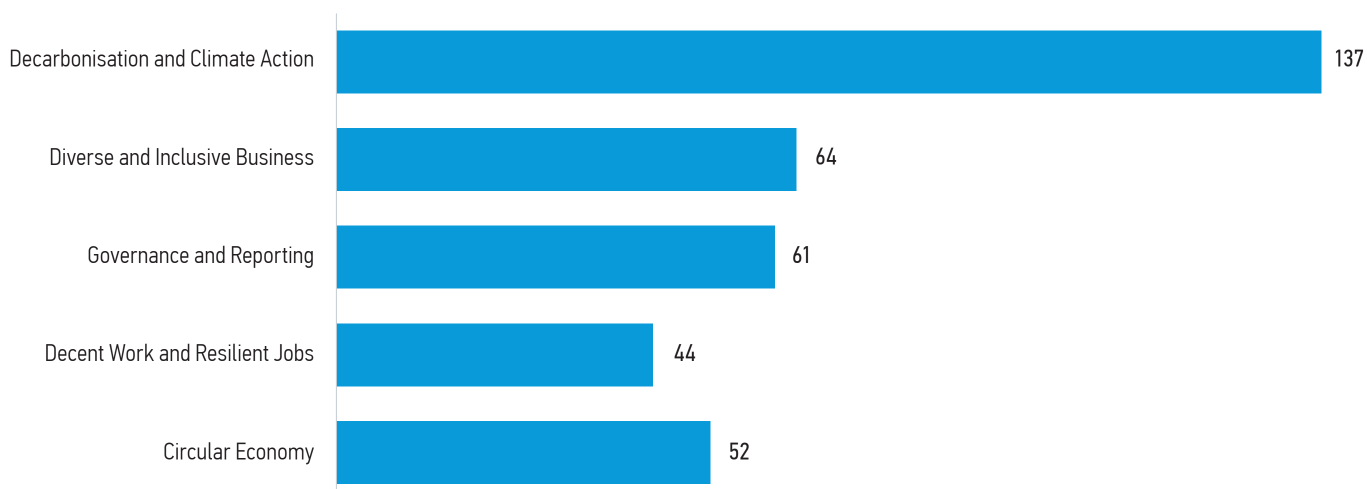
The Fixed Income team aims to re-assess its thematic priorities for engagement over time. In 2022, they started to address the topic of biodiversity more in depth, under the "Decarbonisation & Climate Action" theme, in particular with companies in the agribusiness and food and beverage sectors. For example, the team engaged with an emerging markets meat processing company in 2Q22, to assess the company's response to deforestation and supply chain management controversies. The company had developed a mandatory livestock transparency platform to assess their suppliers, integrating blockchain to prevent illegal deforestation. While the team sees this as a positive first step, it plans to monitor the outcomes of the initiative in the coming months.

Ongoing Developments

The main limitation currently faced by the Fixed Income team relates to the engagement channels and tools available to bondholders to exert and evidence their influence on issuers which may be "softer" when compared to equity shareholders' rights. In fact, whilst the equity investors can leverage resolutions and proxy voting, fixed income investors mainly rely on a "carrot-and-stick" approach, offering issuers the potential benefit of investor loyalty versus the potential penalty of selling bond holdings or not participating in a new debt issuance. The effectiveness of these tools largely depends on an issuer's reliance on debt financing, as well on the magnitude of a single investor's bond holdings in such issuer, which are uses of resolutions and proxy voting. Similarly, although we believe that fixed income investors have a responsibility to engage with sovereign bond issuers to help keep them on track on their climate-related and broader sustainability commitments, the ability of an individual investor to influence a country's policy agenda is very limited, especially in the case of large economies. The team believes that one way to address these challenges is to further enhance their collaborative engagement efforts—both through internal partnerships with other MSIM investment teams, and through external investor or multi-stakeholder initiatives. With regards to sovereign

FIGURE 9.5

Fixed Income Engagements – Corresponding With MSIM Thematic Engagement Priorities



(Please note: The chart above is not representative of the full scope of engagement topics covered by the Global Fixed Income team during the time period)

ENGAGEMENT CASE STUDY 9.6

ASSET CLASS	• Fixed income
MSIM ENGAGEMENT THEME(S)	• Decarbonisation; Corporate Governance (Reporting & Disclosure)
TYPE OF COMPANY	• Northern European Bank
REASON FOR ENGAGEMENT	• The bank had released an updated reporting and sustainable financing framework; however, the Fixed Income team's IG Financials Credit Analyst, together with the Fixed Income Sustainable Investing team, noted that the company had continued to finance fossil fuels, so the team sought to encourage further reductions in fossil fuel financing, in line with the goal of just transition
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values – Doing the Right Thing; Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with bank management in 1Q22 • Sharing of best practices
DETAILS OF ENGAGEMENT	• Focus on Scope 3 emissions reporting and target setting within the company's updated reporting and sustainable financing framework, to encourage continued disclosure (especially given the nature of the sector) • Push for further fossil fuel financing reduction, through concrete targets, and request for additional evidence of initiatives in place to achieve the company's Net Zero 2050 goal
ENGAGEMENT OUTCOME	• The Fixed Income team deemed the engagement satisfactory, given that the bank exhibited a clear intention to continue its progress towards net zero by 2050, alongside proactively working with clients to improve processes and provide financing for sustainable projects • **Fossil Fuel Financing:** Due to the Russia/Ukraine crisis, at the time of the engagement the bank stated that there may be more fossil fuel exposure in the short term, however they would not let their long-term objective be compromised. Following the Fixed Income team's discussion with bank management, the bank announced that they will no longer provide dedicated financing to new oil and gas fields, and that they aim to expand new financing of renewable energy by 50% by end-2025. In addition, the bank also highlighted its target of a full exit of financing coal-fired power plants by 2025. • **Scope 3 emissions:** In response to the Fixed Income team's request for better Scope 3 (financed) emissions reduction and disclosure, the bank committed to steering their whole lending book towards lower carbon profiles, with their entire ~€800bn outstanding loan book in scope for client engagement on decarbonisation. The bank also had interim Scope 3 targets in place (by 2030) for energy intensive sectors • **Climate Risk Analysis:** The bank highlighted their plans to publish further climate pathways to net zero by 2050, by conducting a heat-mapping exercise within their climate risk analysis. The bank also noted that they aim to report progress in their next TCFD report.
INVESTMENT DECISION	• **Continue to hold investment position** given significant enhancements on the topics of decarbonisation, especially from a financed emissions perspective
NEXT STEPS/LOOKING AHEAD	• Plans to follow up on progress in the sustainability areas discussed, particularly following the publication of the bank's next TCFD Report

engagement in particular, they believe that platforms such as the PRI are well-positioned to potentially facilitate this type of policy-focused outreach. More details on this can be found in Principle 10.

Global Balanced Risk Control

Engagement Approach

Our GBaR team defines stewardship as an overarching approach to monitoring, engaging and exercising shareholder rights across their portfolios to promote the long-term success of companies and create sustainable value for their clients, while contributing to environmental and social challenges.

GBaR believes that they have a duty to work with the firms in which they invest, to help improve their ESG performance. The team fulfils this duty by engaging with the companies in which they invest and by effectively exercising proxy voting and other rights as shareholders. These stewardship activities give the team the opportunity to guide companies in which they invest toward better ESG practices, which the team believes produces attractive returns for their clients over the long term. GBaR further believes that a structured approach to engagement is a powerful tool to keep issuers on track of their commitments.

Approach to Prioritising

Typically, GBaR's main engagement priorities are guided by top-down thematic-based research and an assessment of material ESG risks by the team's dedicated ESG analysts. The team believes that this is the best approach for their strategy as researching risks to the global economy and global markets is integral to GBaR's asset allocation process. ESG factors such as climate change definitively fall into the team's definition of potential "risk events". This approach therefore ensures that stewardship is seen as a natural extension of the team's philosophy around risk control.

To maximise the effectiveness of their engagements, GBaR increasingly collaborates with a number of MSIM teams, under appropriate circumstances, including MSIM's Global Stewardship team, who have extensive experience in corporate governance and proxy voting. GBaR finds internal collaboration highly effective in pooling resources and expertise to achieve similar/common goals. Around 15% of GBaR's engagement strategies carried out during the reporting period were collaborative efforts with other MSIM investment teams, an increase from 10% in the preceding period.

Example – Engagement Series on Climate Transition

Carbon- and climate-related risks are a key engagement area for GBaR. During the reporting period, the team initiated a long-term engagement programme with the oil and gas industry and continued their engagement approach with the utilities industry. Over this reporting period, GBaR engaged with eight global oil and gas companies and eight utilities firms.

The team believes that the growing global emphasis on decarbonisation will have profound effects on the most exposed sectors and targeted the industries above based on a materiality-based assessment of risk.

Since 2020, GBaR has engaged regularly with utility companies across Europe, the U.S. and Southeast Asia to encourage a more ambitious decarbonisation plan. Typically, the team's engagement has focused on prioritising renewables over gas in the transition from coal. GBaR has also focused on encouraging a step up in their near-term ambition to align generation portfolios sooner with a net zero pathway.

Over the course of GBaR's initiative, the team met with staff directly responsible for the decarbonisation strategies, as well as with some members of investor relations. Given the scope and scale of this challenge, the team intends to engage with the company over a number of years where they can monitor progress and increasingly step up their engagement requests as necessary.

To date, GBaR is pleased with companies' increasing awareness and prioritisation of the energy transition based on follow-ups with the team's target utility companies. Through dialogue with the companies, GBaR has confirmed its research findings that not only do renewables provide lower carbon electricity, but they are also an increasingly cheaper option compared to coal, and even gas. However, power generation is a highly complex and regulated industry and the team has come to understand the challenges in forcing all coal out of the electricity grid. These challenges are not associated with renewable energy's shortfalls (intermittency, for example), but also related to regulatory requirements to maintain plants, issues around the Just Transition and energy security.

GBaR will continue to work with their target companies to support them in transitioning their businesses. The team believes that those that can decarbonise their portfolios in an efficient manner can reduce their carbon pricing risk, and over the long term the market may reward utility companies that transition away from fossil fuel generation.

ENGAGEMENT CASE STUDY 9.7

ASSET CLASS	• Multi-Asset
MSIM ENGAGEMENT THEME(S)	• Decarbonisation; Circular Economy; Decent Work & Resilient Jobs
TYPE OF COMPANY	• U.K. grocery retailer
REASON FOR ENGAGEMENT	• Continuous and ongoing engagement with a specific focus on the company's response to a shareholder proposal on adopting the living wage standard
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values – Doing the Right Thing, Commitment to Diversity & Inclusion (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values.
ENGAGEMENT METHOD	• Meetings with company chair and CEO • Remediation proposals and sharing of best practices.
DETAILS OF ENGAGEMENT	• **Human Capital Management:** The company was targeted by an investor coalition calling for the company to become a living wage accredited employer. The company's management recommended shareholders vote against the proposal. Management's rationale was that 100% of their direct staff are currently paid on a living wage standard and none of their peers are currently accredited. The company expressed concern that accreditation would take decisions on pay out of their hands and could inhibit their ability to remain competitive. • The GBaR team sought to understand how the company was engaging with proponents and the company explained it was an ongoing discussion for a number of years. While the team commended the company's recent pay uplifts for staff, they disagreed with the company's arguments around accreditation and urged the company to adopt the living wage accreditation standard. Guaranteeing a living wage is an essential aspect of decent work. • GBaR believes that by not becoming accredited and by resisting calls to do so, the company cannot guarantee a living wage. The team pointed out the growing expectation by consumers that staff are paid well and that by adopting the living wage standard they will go a long way towards differentiating themselves. Additionally, GBaR believes this could set a standard that peers could follow.
ENGAGEMENT OUTCOME	• Ultimately, the company disagreed and believed their need to maintain flexibility was paramount and the proposal was against the spirit of competition. • The team escalated the issue by voting for the proposal against the company management's recommendations. Unfortunately, the proposal did not pass
INVESTMENT DECISION	• **GBaR continues to hold investment** in the company. While the team is disappointed with the company's stance, the company is currently paying a living wage to all direct staff and encouraging increased adoption of living wage by contracting firms. Having said that, there is still work to be done and GBaR will continue to push for the company to make progress on this issue.
NEXT STEPS/LOOKING AHEAD	• **2023:** GBaR believes in the importance of paying a living wage. As the cost of living continues to rise, GBaR will monitor the Living Wage Foundation's guidance and seek to ensure that the company continues its established practice of adhering to it through continued engagement with the executive team.

GBaR's oil and gas engagement series is still in its infancy. Given the team's belief that quality engagement takes time, the team has designed a framework to track improvements or deterioration of the companies' practices. The team will continue to monitor their target companies against this framework and plan to supplement this ongoing monitoring with a yearly progress call.

ENGAGEMENT CASE STUDY 9.8

ASSET CLASS	• Multi-Asset
MSIM ENGAGEMENT THEME(S)	• Circular Economy; Decent Work & Resilient Jobs
TYPE OF COMPANY	• Mining company.
REASON FOR ENGAGEMENT	• Follow up on water and community relations-related issues • Discuss the effects of drought and climate change on the company
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in integrating requirements, delivering sustainable long-term returns through ESG integration, aligning engagement/ investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with company management • Strategic advice and sharing of best practices
DETAILS OF ENGAGEMENT	• **Water use:** the team initiated engagement with a global mining company in 2019 and continued to follow up through Q4 2021 on issues such as community relations and water security. Previously, the GBaR team raised concerns that the rollout of water standards at a contentious water-stressed site had to be done delicately, as water played such a key role in the community tensions associated with the development of the site. The team believed that a lack of action could hinder their licence to operate • The team urged the company to continue to release water key performance indicators to allow investors to track progress • **Executive Remuneration:** GBaR also recommended that the company make their CEO responsible for water and to explicitly incorporate water stewardship-related KPIs in their executive remuneration plan, on par with existing safety metrics
ENGAGEMENT OUTCOME	• **Water Use & Community Relations:** In the team's most recent engagement, the company confirmed that they had completed the rollout of water standards and entered into a 30-year water agreement with the affected community • **Executive Remuneration:** The company responded positively to the team's recommendation and has promised to look into this. GBaR is pleased with progress and believes that recommendations put forth should ensure that water stewardship becomes a real strategic imperative • Though progress is positive, GBaR believes that the company should make water conservation a more core part of its strategy by bringing it under the remit of their CEO. This is material due to the locations in which the company operates and their involvement in the aforementioned controversies
INVESTMENT DECISION	• **Continue to hold investment position** given positive commitments made by the company and being receptive to the team's recommendations
NEXT STEPS/LOOKING AHEAD	• Given the above, the team will continue to monitor the company's corporate governance practices on recommendations provided • GBaR intends to check on the company's remuneration structure and CEO responsibilities

Global Listed Real Estate

Engagement Approach

The Global Listed Real Estate team firmly believes that a focus on sustainability within the real estate sector is of utmost importance and will likely serve as one of the biggest differentiators of value for landlords (and investors) going forward. When taking into account both operational emissions and embodied emissions of materials, buildings account for nearly 40% of the world's CO_2 emissions. Moreover, it is estimated that building space is set to grow by approximately 75% through 2050. Without significant decarbonisation efforts within the real estate sector, CO_2 emissions will rise dramatically. At the same time, governments and enterprises around the globe have begun committing to the tenets of net-zero, including setting emissions reduction targets in line with limiting global warming to 1.5°C. With that in mind, the team has already conducted, and plans to continue to conduct, engagements with REITs on committing to net-zero through setting science-based targets, in addition to engaging on other topics such as board gender diversity and executive compensation, as detailed in the case study below:

ENGAGEMENT CASE STUDY 9.9

ASSET CLASS	• Listed Real Estate
MSIM ENGAGEMENT THEME(S)	• Decarbonisation & Climate Action; Diversity & Inclusion
TYPE OF COMPANY	• Singapore REIT
REASON FOR ENGAGEMENT	• Primary objective of working with the company to adopt greenhouse gas ("GHG") reduction targets aligned with science-based targets ("SBTIs") • Working to improve Board gender diversity initiatives
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in integrating requirements, delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with company management • Strategic advice and sharing of best practices
DETAILS OF ENGAGEMENT	• In engaging with the company to adopt GHG targets aligned with SBTIs, the company acknowledged that these are important issues and has set up infrastructure and teams to achieve these goals • Having seen progress where the company had its emissions reduction targets approved by the SBTi initiative, for a "well below 2°C" scenario in November 2020, the team pushed for further steps to be taken by the company to meet this objective
ENGAGEMENT OUTCOME	• Aligned with the team's recommendations, the company acknowledged and saw the need to align with these standards and has committed to providing further updates • This demonstrates positive momentum based on previous engagements and recommendations • With respect to board gender diversity, the Board of the Manager of the company has three female directors in a nine director Board, in line with the team's gender diversity standards
INVESTMENT DECISION	• **Continue to hold investment position**
NEXT STEPS/LOOKING AHEAD	• Continue to closely monitor the company's progress on aligning emissions reduction targets with SBTIs; the team expects further progress updates on the next engagement, including with respect to gender diversity initiatives throughout the company

Global Listed Infrastructure

Engagement Approach

The Global Listed Infrastructure team periodically conducts ESG engagements with listed infrastructure companies. The goal of these engagements is to assess each company's ESG efforts and through their conversations seek information on a variety of ESG topics. Generally speaking, the team looks to highlight potential areas of risk and encourage companies to improve their ESG metrics over time.

ENGAGEMENT CASE STUDY 9.10

ASSET CLASS	• Listed Infrastructure
MSIM ENGAGEMENT THEME(S)	• Decarbonisation & Climate Change; Diversity & Inclusion
TYPE OF COMPANY	• Canadian Energy Infrastructure company
REASON FOR ENGAGEMENT	• Primary objective of working with the company to institute a comprehensive suite of emissions reduction targets • Working to improve gender diversity in the workforce
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in integrating requirements, delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings with company management • Strategic advice and sharing of best practices
DETAILS OF ENGAGEMENT	• In engaging over several meetings with the company, a comprehensive suite of emissions reduction targets, including specifically a net zero component, was implemented • Another engagement effort is to improve female representation in the workforce, where the company recently mandated that all job interviews are to include at least 50% women for every new opening across the firm, which is significant for a company with a large field operation in areas like oil terminals and rail loading docks
ENGAGEMENT OUTCOME	• The company's newly introduced commitment is supported by a detailed roadmap on how they expect to achieve a net zero status by 2050
INVESTMENT DECISION	• **Continue to hold investment position**
NEXT STEPS/LOOKING AHEAD	• Continue to closely monitor the company's progress on aligning emissions reduction targets with SBTIs; the team expects further progress updates on the next engagement, including gender diversity initiatives throughout the company

Private Credit & Equity

Engagement Approach

The PC&E investment teams lead engagement with portfolio companies, based on the business' incorporation of its own Sustainable Investing Policy and ESG/stewardship priorities outlined under Principle 7. Due to the nature of the asset class and diverse strategies, the ability to engage and thus obtain information pertaining to underlying portfolio companies will vary based on the nature of each strategy (e.g., control versus non-control) and type of investment (e.g., private equity versus private credit). To supplement various engagement approaches, PC&E may also leverage third-party diligence to augment the investment team's activities.

Control Situations (Equity)

Control situations enable a high level of regular and ongoing engagement and dialogue with portfolio company boards and management teams. Investment teams collaborate closely with portfolio company management teams in determining 100-day plans for improving operations, expanding business lines, implementing organisational changes, etc., in order to precipitate growth and create long-term value. As a part of that process, KPIs, including those pertaining to ESG, are identified and reported to the investment team as well as the board, where investment teams will have seats, on a regular basis. While there are many common considerations examined across all portfolio companies (e.g., board structure, independent board members, existence of employee policies, the presence of material environmental risks, litigation activities, labour violations, etc.), many other engagement topics are tailored to each industry, given the fairly broad range of sectors and geographical regions in which PC&E strategies invest.

Non-Control Situations (Equity & Debt)

Non-control situations provide more limited opportunities to engage with portfolio companies and accordingly we take steps to carefully diligence and engage with such portfolio companies pre-investment. The level of engagement with portfolio companies where teams do not have control will depend on the nature of their relationship and the willingness of each portfolio company to engage in ESG-related (and other) topics. For equity investments, teams may have board observer rights which provide them with a greater level of transparency; however, this does not enable them to fully engage with companies compared to control situations. For credit investments, teams may have access to information that the sponsor provides; however, the sponsor is the one who determines the materiality threshold of ESG risks and/or incidents and ultimately has control over what is disclosed to investors.

Engagements in the PC&E business are not region-specific but are investment-specific given the long-term horizon and nature of the asset class as well as the opportunistic approach which many of their investment strategies take. This approach aligns with the broader investment objective of MSIM (as explained in Principle 1) to achieve sustainable performance which delivers superior outcomes for clients and markets over the long term.

The following is an example of engagement in an equity control situation:

ENGAGEMENT CASE STUDY 9.11

ASSET CLASS	• Private Equity Control – Equity Investments
MSIM ENGAGEMENT THEME(S)	• Circular Economy & Waste Reduction, Decent Work & Resilient Jobs
TYPE OF COMPANY	• U.S.-headquartered provider of labels and flexible packaging solutions, focused on health care, personal care, food & beverage, and industrial end markets
REASON FOR ENGAGEMENT	• The PC&E deal team identified the labels and packaging sector as a category that requires additional ESG investigation given material concerns for environmental management, worker health and safety, and brand erosion from sustainable packaging competition
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• To help support engagement and gather supplemental information and data, the team engaged Malk Partners (“Malk”), an industry-leading PE due diligence consultant, to perform an in-depth review of the company’s ESG factors and risks • Meetings with company management also took place to share strategic advice and best practices
DETAILS OF ENGAGEMENT	• The deal team and Malk identified the expansion of the company’s sustainable packaging line as an opportunity to de-risk the company while improving top-line and bottom-line growth • It was also discovered that the company did not have any material ESG concerns, favourable turnover rates compared to industry average, and a respectable start on sustainable packaging product lines
ENGAGEMENT OUTCOME	• As a result of the deal team’s engagement efforts, supported by Malk, the company expanded sustainability efforts (accelerated commercial momentum of sustainable products portfolio and established a supplier sustainability programme) • The company also implemented ethics, diversity, and safety initiatives (established a code of ethics and DEI, consolidated enterprise resource planning systems to strengthen IT security) • Worked to improve transparency and reporting (established key sustainability metrics to revisit consistently (e.g., waste reduced, carbon footprint)
INVESTMENT DECISION	• **Invested in the company** and engaged with management to incorporate ESG opportunities into the Value Creation Plan (“VCP”)
NEXT STEPS/LOOKING AHEAD	• The deal team also further engaged with management to incorporate ESG opportunities into the VCP, and will continue to partner with management to improve sustainable packaging and other relevant ESG considerations

Private Markets Solutions

The Private Markets Solutions team sends annual ESG questionnaires to its portfolio companies or GPs to obtain updates on ESG policies, processes and performance reporting. This approach is different from other PC&E teams as the Private Markets Solutions business consists mainly of Fund of Funds, and since they are not active owners of assets, they rely on active partners (external managers) to engage with portfolio companies (although this varies by partner/strategy/country). ESG questionnaires are a way of obtaining information prior to deciding on next steps with respect to each GP or investment.

The team are in the process of launching an Article 9 fund under SFDR that has a sustainable investment objective focused on climate change mitigation (through the avoidance of CO_2 emissions). To support this sustainable investment objective, the Private Markets Solutions team has implemented an enhanced ESG policy including additional engagement protocols. Engagement activity will predominantly be outcomes-based, seeking to drive positive change by engaging with the key influencers and decision-makers within a portfolio company, with whom the team typically have direct lines of communication.

Key influencers will differ between portfolio companies, and the team therefore takes a flexible and tailored approach in terms of which issues are addressed specifically, while recognising the importance of senior manager buy-in to drive commitments to sustainability-related initiatives from the top down.

While there is no formal schedule for following up on company engagements, it is expected that this will occur on an ongoing basis, with follow-ups scheduled quarterly at a minimum. Depending on the ESG-related objectives and company management's desired level of collaboration, this may occur on a more frequent basis. Where applicable, goals will incorporate quantitative targets against which progress may be measured.

In the event that the deal team identifies a situation in which the portfolio company's management of one or more material ESG-related risks or opportunities does not meet satisfactory levels or has been deteriorating over time, or where a company within the Article 9 fund has been identified as potentially causing significant harm through the impact of its operations on an ESG theme or principal adverse impact indicator, the team will enact an enhanced engagement protocol. Under this enhanced engagement protocol, the portfolio company and deal team work to resolve this over the course of 12 months from the date of identification. In such an instance, the frequency of engagement activity will likely increase and may involve other resources, such as MSIM's central sustainability resources or third-party specialists. At the end of this 12-month period, the team will review the situation and take appropriate next steps.

In connection with this Article 9 fund, the team will also track and update engagement activities in an Engagement Database, which will assist in tracking progress against targeted outcomes and ensuring that portfolio companies remain on track.

ENGAGEMENT CASE STUDY 9.12

ASSET CLASS	• Private Equity Fund of Funds
MSIM ENGAGEMENT THEME(S)	• Decent Work & Resilient Jobs
TYPE OF COMPANY	• A U.S.-based venture capital manager (GP) focused on making early- and mid-stage investments in technology companies across the Pacific Northwest and North America.
REASON FOR ENGAGEMENT	• Operational Due Diligence – identifying notable business and operational factors and promoting best business practices • The GP was a growing venture capital manager whose corporate governance policies and procedures were not up to the requisite standard expected by institutional investors, including MSIM • As part of its operational due diligence, the Private Markets Solutions team needed to obtain more details as to the extent of corporate governance gaps before deciding whether to invest in the GP
HOW ENGAGEMENT ALIGNS WITH MSIM/ CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/ investments with shared ESG and investment values
ENGAGEMENT METHOD	• Meetings and discussing key issues with the GP • Conducting calls with the GP's key service providers • Requesting and reviewing various documents, including policies and procedures as well as fund-related documents • Discussing remediation proposals and sharing of best practices
DETAILS OF ENGAGEMENT	• The Private Markets Solutions team identified gaps that the GP could remediate and worked together to improve the GP's overall governance model and operational infrastructure • Although the GP maintained a basic employee trading policy within its employee handbook, it allowed employees to trade in public securities held by the GP's funds. Given the increased potential of employees coming into possession of material non-public information as well as the potential conflicts of interest with regards to employees acting in the best interest of and/or front-running the funds' limited partners, the team recommended the GP to improve its personal trading policy by restricting trading in any public securities held by the funds as well as formalising a restricted list and requiring employees to disclose their quarterly transaction report and annual holding report to the GP for review. The GP understood the team's concerns and agreed to implement their recommendations by improving its personal trading policy • The GP did not formalise certain policies around several business functions, including policies related to cash movement, anti-money laundering/know-your-customer, and investment and expense allocation. In the Private Markets Solutions team's view, it is important for the GP to maintain a full set of formal policies to ensure that appropriate procedures are established, documented and communicated to employees, because failure to prepare such documents generally reflects an investment manager that has not created an institutional- style infrastructure. As such, the team recommended the GP to consider formalising these policies and/or to engage a third-party compliance consultant for assistance. The GP agreed to such recommendation • Except for when hiring Managing Directors, the GP did not perform formal background checks on its staff; instead, their process has been limited to conducting reference checks on candidates. The team recommended that the GP conduct more robust checks and verifications on employees joining the organisation, as well as implementing a recurring schedule for performing update background checks (upon each new fund launch or every three to five years on senior front- and back-office staff, including those with cash signing authority). As best practice, the GP should validate potential employees' educational history, professional qualifications, employment history, legal claims and actions and credit and financial history. The GP was open to the team's feedback and agreed to begin performing formal background checks on employees going forward
ENGAGEMENT OUTCOME	• The GP agreed to take remedial actions by implementing a number of corrective measures and best practices that the team proposed in its engagement, as described above
INVESTMENT DECISION	• **Invested in the GP** after the GP agreed to the team's recommendations
NEXT STEPS/LOOKING AHEAD	• Follow up with the GP on the progress of implementing corrective measures and best practices • Continue to assist the GP in strengthening its corporate governance as it grows and becomes more institutionalised

Private Real Assets

Private Real Estate

Engagement Approach

Morgan Stanley Real Estate Investing strives to engage relevant stakeholders to gain an understanding of what topics matter most and how MSREI can adapt efforts to better align with these needs. MSREI recognises that it is better able to generate exceptional ideas that develop innovative solutions to complex issues by soliciting feedback and listening to the different perspectives of our stakeholders, such as tenants. As such, select MSREI funds have established a tenant engagement programme which includes providing tenant sustainability guides to tenants, conducting tenant engagement surveys and tenant events focused on increasing sustainability awareness at selected assets where appropriate across the portfolios.

Additionally, MSREI requires property managers to consider ESG items in their day-to-day work in managing properties. MSREI strives to include ESG items in its Property Management Agreements where feasible. Clauses may outline requirements for cooperation between landlord and property manager to identify and assist with execution of various sustainability measures including improving energy efficiency, obtaining green building certifications, etc.

ESG issues are discussed frequently by the portfolio management teams and generally in conjunction with asset management. Additionally, for select funds, MSREI may conduct an annual property management survey to help assess risk, monitor compliance with a diverse set of policies and track improvements, where possible. This survey includes questions to determine if and how the property management and leasing management teams are conducting reviews to ensure compliance with all leasing terms and conditions by their tenants, including those highlighted in green lease clauses.

Private Infrastructure

Engagement Approach

Morgan Stanley Infrastructure Partners is committed to sustainability through its ESG approach, which calls for active management of ESG issues throughout the investment life cycle for each portfolio company. MSIP believes that ESG integration throughout the investment life cycle reduces long-term risk and increases the attractiveness of its portfolio companies.

As part of the investment life cycle, the team performs due diligence on ESG topics, collaborating with internal and external ESG specialists. As part of acquisition and ownership, MSIP works to ensure continued integration and implementation of the ESG programme, including by engaging with portfolio companies to report against the GRESB Infrastructure Assessment.

Additionally, MSIP looks to engage with key stakeholders on ESG issues which helps shape the team's ESG efforts by sharing valuable feedback on new ideas, best practices and industry trends, where applicable.

ENGAGEMENT CASE STUDY 9.13

ASSET CLASS	• Private Infrastructure
MSIM ENGAGEMENT THEME(S)	• Decent Work & Resilient Jobs – Health & Safety
TYPE OF COMPANY	• Data Infrastructure Company
REASON FOR ENGAGEMENT	• The company owns and operates a large European independent fibre network. • Since the company was formed from an asset carve-out from a larger telecom operator, it had no stand-alone ESG management processes, policies/procedures or key performance indicators (KPIs) • After investment, the MSIP team worked closely with company management to implement ESG management processes, policies/procedures or KPIs tracking • Specifically in 2021, MSIP worked with the company to focus on its health and safety approach
HOW ENGAGEMENT ALIGNS WITH MSIM/CLIENT VALUES (PRINCIPLES 1 AND 6)	• MSIM Innovative Investment Solutions; Commitment to Sustainability and MSIM Sustainable Investing Policy (Principle 1) • Morgan Stanley Core Values of Doing the Right Thing, Leading With Exceptional Ideas (Principle 1), Putting Clients First (Principles 1 and 6) in delivering sustainable long-term returns through ESG integration, aligning engagement/investments with shared ESG and investment values
ENGAGEMENT METHOD	• MSIP formed a working group and scheduled biweekly meetings with the company's management to discuss and implement ESG programme improvements • The team also worked with the company to co-develop policies, assessments and datasets
DETAILS OF ENGAGEMENT	• In 2021, MSIP ensured that health and safety was included on the monthly board agenda as a recurring topic, and engaged company management on a health and safety workshop to share best practices • MSIP worked with the company to initiate a deep dive on health and safety metrics (including for contractors), followed by a root-cause analysis and a review of the health and safety framework, policies and procedures
ENGAGEMENT OUTCOME	• As a result of the above, clear health and safety metrics and targets and consistent tracking and reporting (including near misses) were established. A formal framework was established to increase transparency • ESG metrics were adopted into executive incentive plans • The company identified roles and responsibilities for relevant parties (including contractors) at the company's construction sites to confirm execution and compliance with the company's standards.
INVESTMENT DECISION	• **Continue to be invested in the company as part of MSIP's broader portfolio**
NEXT STEPS/LOOKING AHEAD	• Continue to apply this approach to improve ESG and health and safety programmes and processes of future portfolio companies

Calvert Research and Management

Engagement Approach

Calvert seeks to strengthen capital markets by ensuring that corporate engagement is a core investment function. Rooted in proprietary ESG research, collaboration with active managers, coordination with other shareholders and a commitment to incorporating the perspectives of diverse stakeholders, Calvert seeks to influence companies to better align with the [Calvert Principles for Responsible Investment].

As an investor, Calvert has a responsibility to engage in the oversight of companies to ensure that management is acting in clients' long-term interests. As a complement to Calvert's research, structured engagement in pursuit of improving environmental and social outcomes—as well as long-term shareholder value—is a core component of Calvert's investment approach. As the connection between a company's ESG practices and its financial success becomes clearer, engagement aimed at improving corporate ESG performance increasingly aligns with the creation of shareholder value. Calvert believes that this approach to engagement contributes to better financial returns, better markets and a better world.

Calvert prioritises its engagements using a variety of considerations:

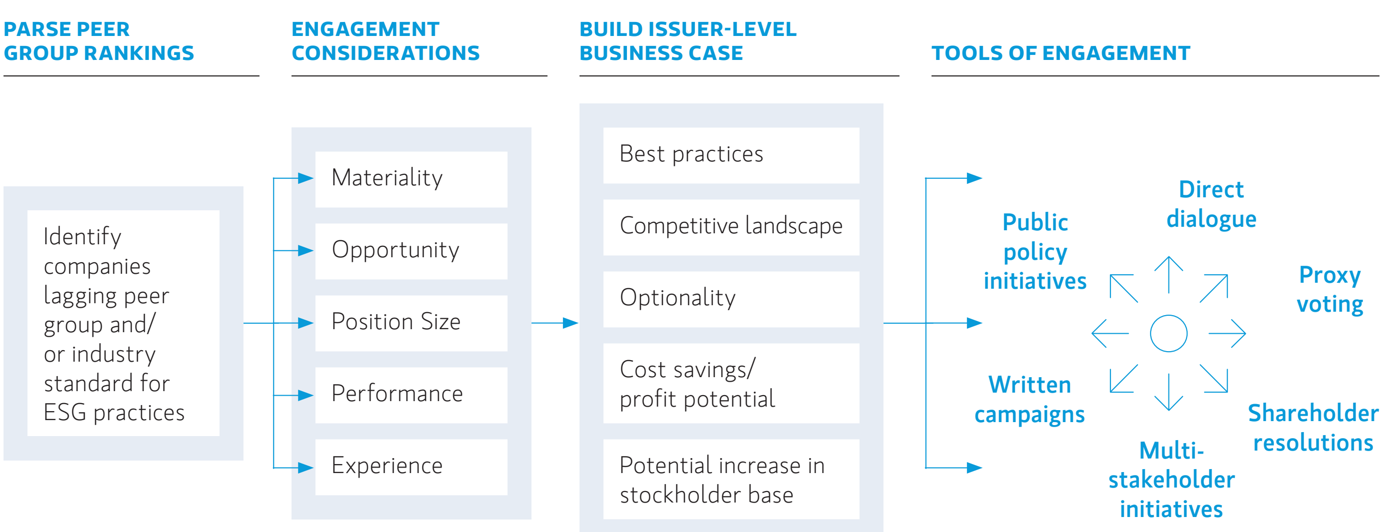
- **Materiality:** based on the team's internal research, they look for concerns about the company's ESG performance that may have a material impact on their position as an investor or an emerging issue that may raise concerns in the future.
- **Opportunity:** where the team believes that there is a reasonable likelihood of successful engagement, and that the company has practical options to improve performance.
- **Position Size:** primarily engaging with companies where the team has an active position or a relatively large stake in the index, or where they believe that successful engagement will allow us to increase our ownership stake.
- **Financial Performance:** prioritising engagements with companies that are lagging financial performers.
- **Experience:** Calvert has expertise in an area that allows the team to credibly engage the company and/or the possibility of collaboration that complements their strengths.

The target engagement selection process is shown in *Figure 9.6* below:

Calvert typically sets engagement objectives following an initial meeting with the company. Calvert sets objectives that are structured around the current positioning of the company, the degree and nature of the risks or opportunities, the positioning of peer companies, the investment significance of the issue, and an assessment of a realistic expectation for the company given management, culture, resources and other factors relevant for the company circumstances.

FIGURE 9.6

Calvert Engagement Selection Process



As with all objective-setting, objectives set are specific, measurable, achievable, relevant and timely. As objectives are met over time, engagement analysts may choose to update the objectives or to move the engagement to a monitoring phase.

In general, company objectives usually fall into these categories:

- Acknowledge and appropriately frame the concern;
- Conduct a substantive risk analysis, including reasonable worst-case scenarios;
- Encourage development of a structured internal dialogue of the issue;
- Commit to disclosures aligned with leading peers;
- Commit to adopting or helping to achieve best practices, consistent with company circumstances;
- Commit to tangible performance improvements;
- Develop governance and management systems consistent with managing the issue;
- Align public engagement with internal management or strategic efforts to the address the issue; and/or
- Integrate the issue into strategic planning.

Depending on where Calvert sees the most opportunity to make an impact and to the extent that the team notes similarities in issues and material risks faced by a set of companies, they may choose to approach an engagement in a stewardship, thematic, structured (deep) or supportive (collaborative) manner.

Stewardship engagements are usually one-off engagements where the team discusses a specific proxy voting outcome from the company's annual meeting or a related article pertaining to the company in news flows.

Calvert belongs to several investor coalitions that work on a variety of topical issues. In instances where a particular company may resist bilateral engagement with us, supportive (collaborative) engagements are helpful to leverage coalition members' expertise and contacts, add weight behind our engagement objectives, and potentially improve the likelihood for successful outcomes.

When Calvert's research acknowledges that there may be similar ESG themes, issues or material risks facing an industry or a group of companies—such as climate change and diversity—they will likely undertake a thematic engagement approach for a group of companies in our holdings. Thematic engagements seek to set new market norms. Having identified and explored the theme, the team determines the industries with both high exposure and optionality with respect to the theme. Within those industries, the team targets those companies that either can help develop business norms around the issue or whose lack of policy or disclosure around an issue may result in suboptimal performance relative to peers.

Structured engagements are deep, extended engagements with companies on material ESG risks and opportunities. With these engagements, companies undergo an exploratory phase, where we use a combination of research and initial dialogue with individual companies to establish a differentiated engagement approach appropriate for each company's unique circumstances. Following that, these companies will go through a Reconciliation phase, which uses the tools of shareholder engagement to bridge the gaps between company strategy, governance, operations and disclosure and its material ESG risks and opportunities. In this phase, Calvert may use shareholder proposals, company dialogue, collaborations or public engagement to meet the team's objectives. Finally, once the team's objectives for the company have been met, they enter the Reporting and Assessment phase, in which they remain engaged with the company to ensure that commitments are met, assess what worked and did not work, and consider whether to establish new objectives for the company.

Calvert has historically engaged primarily in the U.S. because of the importance of this market for its funds, and is increasingly engaging with companies headquartered globally.

Examples of Calvert's engagement priorities are below, but the team also engages on other topics consistent with the Calvert Principles for Responsible Investment described previously:

- **Climate Change** – promote policies to hasten energy transition to clean and renewable sources of energy and to address the physical risks of climate change;
- **Diversity** – advance women and minorities at board and management levels, and promote diversity and inclusion at all levels of the workforce;
- **Labour and Human Rights** – strengthen performance in company operations and supply chains; and
- **Disclosure** – improve disclosure of material ESG matters.

Between 1 July 2021 and 30 June 2022, the team performed 121 structured engagements.

ENGAGEMENT CASE STUDY 9.14

ASSET CLASS	• Equity
ENGAGEMENT THEME(S)	• Climate Change
TYPE OF COMPANY	• REIT focused on senior housing and medical office spaces
REASON FOR ENGAGEMENT	• The company is the current largest weight in Calvert's Global Real Estate Fund and has the 10th highest carbon emissions • The company's current energy efficiency programme has yielded mid-teen internal rate of return with attractive annual energy savings. The company has completed around 20% of LED retrofit projects with annual utility savings of around $7.2 million. • A full rollout of LED retrofits could save the company more than $40 million annually, which would be available for reinvestment and or dividends
ENGAGEMENT METHOD	• Meetings with company management • Setting an objective for the company to take a specific action related to climate change
DETAILS OF ENGAGEMENT	• Calvert engaged the company on setting environmental targets and they shared their renewable energy approach for onsite and offsite and not using offsets. The team shared that it was critical for the company to target an initial goal of 4-5% annual GHG reduction between now and 2030. • The company also shared progress on building certifications with a focus on Energy Star. Additionally, every renewal or new lease will have an ESG clause or be considered a green lease. The company stated that there has been some interest from tenants in sharing the cost of energy efficiency and they are also beginning to ask for EV charging stations. • Calvert inquired about governance at the company, specifically on ESG. The company had just formed an ESG Steering Committee involving operating teams and capital market teams.
ENGAGEMENT OUTCOME	• On the back of Calvert's engagement, the company has committed to adopting GHG reduction targets aligned with a 1.5oC scenario, and Calvert expects an official announcement by the end of 3Q23
INVESTMENT DECISION	• **Continue to hold investment** given its commitment to incorporate Calvert's recommendation
NEXT STEPS/LOOKING AHEAD	• Review the company's next upcoming sustainability report, expected by 31 July 2023, to measure progress on GHG reductions and LED retrofits.

Parametric Portfolio Associates

Engagement Approach

The scope of Parametric's engagements is global. The team directly engages with companies using a two-pronged approach: (1) letter writing and (2) virtual meetings. These engagements are proactive, thematic, stewardship-team led. Depending on the topic, engagements can initially include staff specialists, senior leadership or board members.

In the public equity space, the team currently has a formal engagement programme that covers board gender diversity, EEO-1 disclosure, human rights and climate change. The team is also participating in climate-related collaborative engagements with Climate Action 100+.

The team determines a list of target companies for each engagement initiative and reaches out to companies either with a formal letter (board gender initiative and EEO-1) or an email (human rights) to initiate a conversation. Companies can either write back or schedule a meeting to discuss the issues outlined.

From 1 July 2021 to 30 June 2022, Parametric had 26 company engagements focused on diverse and inclusive businesses, human trafficking and climate change. Given the nature of their customs solution business, engagements are not always directly tied to or do not always result in an investment decision but are instead dictated by client preferences and specifications.

ENGAGEMENT CASE STUDY 9.15

ASSET CLASS	• Public Equity
ENGAGEMENT THEME(S)	• Human Rights
TYPE OF COMPANY	• Large-Cap U.S.
REASON FOR ENGAGEMENT	• Accusations on the use of forced/slave labour
ENGAGEMENT METHOD	• Letter to the Board of Directors
DETAILS OF ENGAGEMENT	• A global household products company has long used a large Southeast Asian palm oil supplier alleged to use child and forced labour. Though the company discloses its standards and frameworks to the SASB, the Carbon Disclosure Project (CDP) and the Task Force on Climate-Related Financial Disclosure (TCFD), these allegations warranted PPA's outreach • The team was concerned that supplier monitoring appears to be more reactive than proactive and that third-party supply chain audits necessary to validate company statements appear inadequate. PPA also found that worker-complaint mechanisms seem insufficient, such as online complaint forms that are only available in English • PPA encouraged the company to expand their SASB reporting to include supply chain labour standards
ENGAGEMENT OUTCOME	• The company now plans to offer worker-complaint mechanisms in local languages, and they agreed to hold further discussions on these issues of increased reporting
INVESTMENT DECISION	• N/A; no investment was made
NEXT STEPS/LOOKING AHEAD	• PPA is requesting another meeting to evaluate progress in September 2023 through the team's continuation of its human trafficking engagement initiative

ENGAGEMENT CASE STUDY 9.16

ASSET CLASS	• Public Equity
ENGAGEMENT THEME(S)	• Diversity, Equity & Inclusion
TYPE OF COMPANY	• Large-Cap U.S.
REASON FOR ENGAGEMENT	• EEO-1 Data Disclosure
ENGAGEMENT METHOD	• Letter to the Board of Directors
DETAILS OF ENGAGEMENT	• PPA asked a large U.S. clothing manufacturer to disclose EEO-1 data, as well as their pay equity review process and board diversity policies. The team also suggested that the board's nominating committee adopt a Rooney Rule, which requires at least one candidate of an underrepresented gender, race or ethnicity to be considered for every director position
ENGAGEMENT OUTCOME	• Though PPA was the first prospective investor to engage the company on EEO-1, they agreed to disclose the data because of the ease of reporting and the team's explanation of its importance to investors
INVESTMENT DECISION	• N/A no investment was made
NEXT STEPS/LOOKING AHEAD	• PPA will monitor the progress of this firm moving forward to ensure further implementation and execution of PPA's recommendations

Collaboration Amongst MSIM Investment Teams

Engagement Approach

Notwithstanding our independent investment team's structure and decentralised approach to investment management, MSIM investment teams will engage collaboratively where a cross-asset class stewardship issue arises (e.g., if there is focus on an issuer's ESG risk or egregious conduct that warrants escalation by mobilising the broader MSIM franchise).

SPOTLIGHT NO. 3

Case Study

In the second half of 2021, the MSIM Fixed Income team, together with the GBaR investment team, collaboratively engaged with a high-yield U.S. energy company. The company had been involved in controversies relating to diversity and inclusion practices, in particular with respect to age and gender discrimination, as well as their use of corporate political donations. Additionally, the company was lagging from a climate and emissions-reduction perspective, and therefore the teams aimed to engage on their broader sustainability strategy.

The engagement was a collective effort across both investment teams to leverage the broader MSIM franchise and speak with a single voice to present our expectations on behalf of our clients. The teams held a preparatory session ahead of the engagement to define priorities and expectations, particularly given the sensitive nature of the discussion topics.

The company highlighted that their next sustainability report would include an increased level of disclosure on diversity metrics, rather than setting quotas, and that it aimed to actively promote diversity and an inclusive culture through its employee networks. The MSIM teams pushed for a response regarding the discrimination allegations, which the company strongly rejected, providing a detailed explanation of the events and internal investigation. The company also clarified the process for their political contributions and highlighted their inability to influence the ultimate allocation of funds once donated.

On the emissions-reduction side, our collaborative engagement identified that the company was working on setting more ambitious methane emission- reduction targets, and had initiated collaborative efforts with industry peers to improve the standardisation of environmental data reporting.

OUTCOME

The MSIM investment teams assessed the meeting to be satisfactory. The company had also recently been upgraded by a third-party ESG rating provider, which alongside the engagement insights, contributed towards the Fixed Income team's decision to continue to hold existing positions in the name.

The teams are seeing further positive progress from the company since the meeting, in particular on the diversity and inclusion front: For example, they have included their workforce gender mix for all of their global locations in their latest sustainability report, as well as a broader set of workforce and leadership demographics metrics, in line with our recommendations; they have reached almost 100% participation rate on the company-wide diversity and inclusion training programme launched a year ago; and they have tripled the membership of their black professionals employee network. On the climate front, the company has achieved, as of the end of 2021, their goal of ending routing flaring in the U.S., and has established a new goal to also substantially reduce flaring in their main emerging market hub.

PRINCIPLE 10

Collaboration

Signatories, where necessary, participate in collaborative engagement to influence issuers

As outlined under Principle 9, MSIM's investment teams frequently engage with portfolio companies and generally find that one-to-one discussions are the most effective way to articulate our views to a company's management. However, we are supportive of collaborative engagement where such engagement appears necessary or useful to materially enhance portfolio values and where we can do so in a manner that is in full compliance with applicable laws, regulations and judicial precedents. Other factors that we will consider before participating in collaborative actions include, but are not limited to: potential conflicts of interest, materiality of the issue and the likelihood of delivering tangible outcomes in relation to key sustainability or stewardship-related issues. In addition, at the request of our investment teams, our Global Stewardship team joins selective collaborative efforts to enhance our understanding of a company or to amplify our message, as well as broader initiatives that promote the sustainability and stability of the global financial system.

Notwithstanding the mode of collaboration that we adopt, we always approach collaborative engagement from the perspective of being fiduciaries of our clients' assets, acting on behalf of and in the best interests of our clients (Principle 6), and therefore living by MSIM's Core Value of Putting Clients First (Principle 1).

As mentioned in Principle 1, this past year we have been more selective in collaboration, targeting new initiatives (e.g., 30% Club, FAIRR, WBA, etc., outlined below) where we can directly influence or contribute to influencing material causes aligned with our fiduciary duties and client interests and focusing on obtaining real outcomes. To support this, we are in the process of further enhancing our oversight and governance of collaborative engagements, conscious of anti-trust regulations and undue and/or unfair pressure exerted on companies as a result of collective engagements. Depending on the type of external collaborative proposal, those that seek to join external organisations need to go through the Pathway for Approval process (detailed in Principles 2 and 5) while one-off collaborative engagements will need to obtain approval by the Firm's Antitrust Counsel.

A select summary of the types of collaborative engagements both at an MSIM organisational level and through our individual investment teams over the 12 months from 1 July 2021 to 30 June 2022 are detailed below:

1) Industry Networks – Disclosure/Reporting Frameworks

Objectives
Policy Engagement; Feedback on Global Sustainability Regulations and Requirements; Address Systemic Issues; Enhance Sustainability Knowledge and Share Best Practices; Act as the Voice of Our Clients

i) Principles for Responsible Investment ("PRI")

MSIM has been a signatory to the PRI since 2013. We are also proud of our recent acquisition of Eaton Vance including Calvert, particularly given that Calvert was a founding signatory of the PRI in 2006 and has served diligently on various PRI committees over the years.

Our membership allows us to pool resources, share information and enhance our influence on ESG issues. It is also a hub for us to connect and engage with other PRI signatories and to contribute our voice and practical experiences to a widely recognised responsible investment framework.

We have also considered best practices of other industry stakeholders and incorporated these with our own observations to improve our reporting capabilities, to include new indicators such as board independence and diversity on the governance side, to reflect the increasing availability of governance data.

ii) Sustainability Accounting Standards Board ("SASB") Investor Advisory Group; Taskforce for Climate-Related Financial Disclosures ("TCFD")

MSIM promotes disclosures aligned with SASB and TCFD, in our direct engagements with portfolio companies. Morgan Stanley signed up to the TCFD in 2017, and published its first TCFD report in 2020, with the 2021 report released recently. As a consequence, two-thirds of companies engaged through our SASB efforts have agreed to implement reporting according to the SASB standards.

MSIM is expecting to publish its own TCFD report in 2023 to align with the U.K. FCA's proposal to extend TCFD reporting to asset managers beginning in January 2022. To learn from and discuss best practices on climate strategies and risk management with peers our MSIM Head of Sustainability Strategy and Solutions (from the MSIM Sustainability team) joined the Ceres

SPOTLIGHT NO. 4

ESG IN CREDIT RISK AND RATINGS INITIATIVE
Our MSIM Fixed Income team is also a member of the PRI's ESG in Credit Risk and Ratings Initiative, through which we contribute our knowledge and views on the materiality of ESG factors in credit analysis across sectors. In 2022, MSIM Fixed Income participated in two collaborative workshops with issuers in the banking and insurance sectors, alongside more than 20 other market participants including credit rating agencies and investors. Topics covered during the workshops included the integration of environmental and social consideration in financial institutions' governance structures, climate risk horizons for scenario analysis, and the societal cost of the energy transition. MSIM's Credit Analysts attended the sessions, contributing their views on the topics above as well as on the materiality of other ESG factors in the credit analysis of the sectors under discussion, with the aim of encouraging transparent and valuable ESG-related disclosure.

OUTCOME
As a result of our participation in the Initiative's workshops, the PRI published summary notes outlining the best practices we shared. This is an example of our many contributions to share best practices with industry stakeholders to enhance awareness of the importance of standardisation of sustainability disclosures in the Fixed Income space. We have since aimed to continue growing collaboration efforts, placing our Credit Analysts at the centre of dialogues, with the Fixed Income Sustainable Investing team as a support mechanism.

Paris Aligned Investment Working Group earlier this year as part of efforts in preparation for MSIM's first TCFD report. Calvert also has representation on this Working Group.

Since 2012, MSIM has also been a member of SASB, where we frequently engage with fellow investors to promote SASB reporting standards.

2) Investor Coalitions – Leverage Networks; Improve Ability to Engage With Companies

Objectives

Access Broader Range of Expertise; Leverage Engagements To Increase Our Impact; Seek Out Specific Expertise (Academic, Industry, Non-Governmental Organisations) To Improve Our Ability To Work With Companies; Act as the Voice of Our Clients

i) Climate Action 100+

Our Calvert business has been an active member of Climate Action 100+ since 2018, when the initiative began. Climate Action 100+ provides an opportunity for us to engage with like-minded external partners who share similar sustainability objectives and methods. Collaborations with other investors can be a valuable approach to shareholder engagement. Peer collaboration provides several benefits to our engagement strategy, including: (1) increasing the number of shares represented, (2) leveraging relationships that our peers may have with companies, and (3) pooling knowledge and resources.

Through our participation in Climate Action 100+, we have joined a collaborative investor initiative that seeks to enhance corporate governance of climate change, curb emissions and strengthen climate-related financial disclosures at companies with great opportunities to tackle climate change. By bringing together the views and values of diverse asset managers and asset owners as a singular voice, the Climate Action 100+ initiative has the power to influence and drive better climate responses and behaviours by investors. The initiative has been engaging with the 166 companies that represent over 80% of global industrial emissions and are, as a group and individually, critical to progressing the global economy to net-zero emissions by 2050.

In 2021, Climate Action 100+ released its first-ever Net-Zero Company Benchmark, assessing the world's largest corporate greenhouse gas emitters on their progress in the transition to the net zero future.

Progress Update

The 2022 iteration of the Company Benchmark Assessment was published in March 2022 and includes assessments for 166 focus companies. 69% (compared to 43% in the 2021 Assessment) of companies have set a net zero by 2050 target or ambition in some form, which is an important signal to investors that companies understand and are preparing for the transition. This represents a 17% year-over-year increase compared to the 2021 Assessment. However, only 17% of companies have set medium-term targets aligned with limiting global warming to 1.5oC, moderately improving from 10% last year. Calvert will be sure to focus on improving this and continue to actively participate in this collaborative engagement.

SPOTLIGHT NO. 5

Calvert is currently leading engagement with one electric utility company and one major transportation company on behalf of Climate Action 100+. Calvert has also played a role in dialogues with four other companies. The efficacy of the Climate Action 100+ engagements is strengthened by the collaborative approach of participating investors that call for progress from the target companies. The Climate Action 100+ benchmark provides a roadmap for corporate progress toward net zero that is agreed by a broad coalition of investors in NGOs. Bringing the collective voice to these engagements can lead to increased pressure for corporate change.

During dialogue with the companies, individual investor institutions can weigh in on the most relevant factors from their perspective, allowing greater participation and saving company and shareholder time. Furthermore, as leaders of these engagements and participants in strategic planning conversations, Calvert is able to shape broader engagement objectives and focus on areas that apply across Climate Action 100+ target companies.

PROGRESS

In 2021, the Climate Action 100+ investor group had shared with the company plans for the next iteration of the Climate Action 100+ Company Benchmark Assessment, encouraging the company to give feedback on preliminary assessments, provide new disclosure information and engage with Ceres on questions about the process. Soon after, on 1 November 2021, the company announced a net zero carbon goal for its natural gas business, becoming the first utility company to adopt an enterprise-wide net zero carbon target covering gas and electric operations. The company now has a stated goal to reduce greenhouse gas emissions attributed to its electric utility business by 80% by 2030 and plans to be carbon-free by 2050. In addition, we asked it to align climate lobbying policy and human capital management policies, including Just Transition, to support the achievement of net zero targets. The investor group met with the company in Q3 2021 to review Climate Action 100+ benchmarking results, explore opportunities for improvement and discuss questions around Scope 3 emissions. Calvert asked that it consider including its natural gas utility operations in its net zero commitment. The investor group will follow up with the company to discuss its decarbonisation plans, particularly as they relate to investment in renewable energy and other technologies, in more detail.

At the same time, Calvert and other Climate Action 100+ investors' engagement with a transportation company has focused on encouraging the company to commit to greenhouse gas reduction goals and to increase its commitment to serving the market for zero-emission trucks. Discussions have also covered climate lobbying, product strategy and investments alignment with climate goals. The investor group met with the company in Q1, Q3 and Q4 2022 to discuss its readiness to serve the zero-emissions truck market, its emissions reduction goals and lobbying. The company has published more ambitious plans to serve the zero-emissions truck market, has begun to lay out its approach to climate policy engagement and has added resources to its sustainability team to drive further progress.

OUTCOME

As per above, the utility company became the first integrated U.S. utility company to commit to an enterprise-wide net zero target. Calvert is continuing to monitor its progress toward meeting its net zero commitments, in particular how capital allocation will support the company's goal to cut emissions in the electric and gas utility businesses by 80% and 25%, respectively, by 2030; seeking better transparency regarding how its decarbonisation plans link to the company's current and projected financial results; and asking the company to develop and disclose a comprehensive Just Transition policy to include workers and communities in transition planning.

Given that Calvert's engagement as part of the Climate Action 100+ coalition is ongoing, work is in progress and full outcomes have not yet transpired as of the submission of this U.K. Stewardship Report.

ii) Institutional Limited Partners Association ("ILPA") – Diversity in Action

Our PC&E business is a signatory to ILPA's Diversity in Action initiative, which involves GPs and LPs committed to advancing diversity, equity and inclusion ("DEI") in the private equity industry, which is also one of Morgan Stanley's core values—Commit to Diversity & Inclusion. The goal of the initiative is to motivate market participants to engage in the journey towards becoming more diverse and inclusive and to build momentum around the adoption of specific actions that advance D&I over time.

Outcome

Given MSIM's membership in ILPA's Diversity in Action, our PC&E business commits to specific actions that advance diversity and inclusion, both within our business, our portfolio companies and the industry more broadly. As a signatory, we undertake four essential DEI actions that span across talent management, investment management and industry engagement. Last year, PC&E, with other ILPA Diversity in Action signatories was involved in discussions on diversity-related definitions and metrics for due diligence questionnaires. Following this, ILPA issued draft templates for public commentary, which, upon consolidation of feedback, culminated in an updated due diligence questionnaire and diversity metrics template last year. These documents aim to standardise the key areas of inquiry posed by investors during their diligence of manager and provide a framework for ongoing monitoring of progress related to DEI.

iii) Ceres Private Equity Working Group

Our PC&E business is also a member of Ceres' Private Equity Working Group, which supports GPs and LPs transition private equity portfolios towards a sustainable net zero economy. Our contribution has included facilitating and participating in sessions that provide GPs and LPs with the latest climate-centric and sustainable investment practices, policies, frameworks and tools to assess, manage and mitigate ESG and climate risks.

Ongoing Progress

Through this forum, PC&E has been able to make a positive contribution by sharing our insights with GPs and LPs on best practice within the private equity space with respect to: (1) investment strategies aligning with the Net Zero Investment Framework, (2) consideration of environmental and social impacts of investments to support sustainable development, and (3) developing and implementing investor climate action plans.

PC&E's relationship with Ceres is also reinforced by the fact that Morgan Stanley is a member of the Ceres Investor Network on Climate Risk and Sustainability, and the CEO of Ceres is a member of the Morgan Stanley Institute for Sustainable Investing Advisory Board.

iv) 30% Club (U.K. Investor Group)

MSIM joined the 30% Club earlier this year, as part of its efforts to extend both MSIM and the Firm's commitment to diversity and inclusion (Principle 1). The Head of Sustainable Outcomes for our International Equity team is Co-Chair of the 30% Club Investor Group, which includes asset managers and asset owners, and represents MSIM Ltd in Investor Group and Steering Committee meetings.

The U.K. Investor Group's priority areas include building investor knowledge and awareness on diversity through training and research, engaging firms on the 30% Club's targets and driving gender diversity globally within our investments. Promoting more ambitious targets includes encouraging beyond 30% representation of women on boards, executive committees and new board appointments within the FTSE350, and senior management within the FTSE100, as well as extending Parker Review goals of "at least one board member from an ethnic minority by 2021" to include board and ExCo seats for women of colour.

Progress

Race Equity Statement and Engagement – in collaboration with representatives from the Investor Group, the Head of Sustainable Outcomes for our International Equity team led a working group that published this Statement emphasising that the group's 40+ investors with $11 trillion of AUM could choose to vote against U.K. companies not showing sufficient progress to address racial and ethnic inequality. The Statement requested U.K. firms to go beyond delivering the Parker Review recommendations, also taking into consideration the representation of their executive committees. It also asked firms to advance diversity and inclusion efforts, to disclose racial diversity data where permitted, and to establish a level of transparency on par with current gender diversity disclosure, as well as set out how they plan to increase racial diversity and inclusion in their workforces. The Group also sent letters to targeted companies that failed to meet the Parker review targets, urging them to accelerate their delivery of greater representation and inclusion of ethnic minorities.

Global Engagement – we also supported collaboration with the 30% Club's Canadian Chapter to engage North American companies considered laggards in board diversity. Again here, the Head of Sustainable Outcomes of our International Equity team has a continuing focus on DEI policies, representation, engagements and voting within the companies the team holds as part of their ESG integration and engagement. They also promote awareness of the topic, publishing "Diversity – Asking Difficult Questions" in March 2022, which summarised portfolio progress, and contributing to MSIM's "The Path to Gender Diversity" in May 2022, as well as participating in the Diversity inclusion summit.

Recently, MSIM hosted 30% Club Investor Group representatives in person at our London office, supporting the Group's knowledge sharing aim by having Morgan Stanley Research present their Holistic Equal Representation Score ("HERS") findings on the stock market impact of diversity within companies to the Group.

v) Thirty Percent Coalition (U.S.)

The Thirty Percent Coalition has an extensive membership including public companies, private equity and professional services firms, government officials, senior executives and women's nonprofit organisations.

Its 90-plus members come from diverse sectors across the U.S. and are from three principal groups—institutional investors, corporate leaders and public policy and outreach. Investor members represent $7 trillion in assets under management. Committee members work directly with companies without women directors and public officials to support passage of state, city and federal resolutions to encourage stronger gender diversity, and business leaders to help facilitate their involvement with influencing their peers.

As a member of the investor working group, Calvert participated in a Call to Action asking companies to strengthen governance policies by embedding a commitment to diversity, inclusive of race and gender and including women and minorities in candidate pools of selecting board nominees and senior corporate leaders.

Since 2012, the Coalition's institutional investors have collaboratively engaged with more than 180 companies that have added women to their boards of directors. Corporate leaders explore strategies to promote greater diversity on corporate boards, using their influence and networks, while the Public Policy and Outreach Group continues to explore and implement ways that the Coalitions can engage with public officials. The coalition has broadened its scope to focus no longer just on women, but on representation of racial and ethnic diversity on boards.

Ongoing Progress; Outcomes

Calvert presented at the Coalition's 4Q21 quarterly meeting on the team's EEO-1 initiative, including progress on having Calvert's top 100 holdings disclose or commit to disclosing their EEO-1 reports publicly (91 companies out of 100 as of June 30, 2022). Calvert shared the discussion on the shareholder proposal it had with one of the few remaining companies that was refusing to disclose, and encouraged coalition members to support its proposal, and then went on to receive increased support from independent shareholders as compared to when Calvert filed it in 2021. Finally, Calvert also discussed engaging ISS on EEO-1 data disclosure and incorporated policies to vote against directors into its own voting guidelines as a result of those discussions. This remains a focus for the team going forward.

3) Engaging/Collaborating With Issuers – Setting Industry Standards

Objectives

Improve Industry Practices and Disclosure Standards; Share Feedback on Structuring Sustainable Products/Securities; Increase Transparency and Quality of Market Instruments; Act as the Voice of Our Clients

i) Farm Animal Investment Risk and Return ("FAIRR")

MSIM joined FAIRR in 2022 with the objective of forging new partnerships and delivering sustainable outcomes. FAIRR is a leading collaborative-engagement non-governmental organisation focusing on delivering a sustainable food system, helping investors identify and prioritise ESG risks and opportunities through cutting-edge research, which can then be integrated into investors' active stewardship and decision-making processes.

In May 2022, our International Equity team joined a collaborative engagement with FAIRR, meeting with a Norwegian seafood company held in their international portfolios. Concerned with managing biodiversity and climate risks in aquafeed, the engagement took place as part of FAIRR's engagement on sustainable aquaculture, which targets eight global salmon companies, asking them to develop and disclose strategies for diversifying feed ingredients towards lower-impact and more sustainable alternatives to enable production growth, reduce climate risk exposure and ensure that the risks associated with sourcing fishmeal and fish oil and soy are adequately managed.

Progress

The current phase of the engagement series is focused on increased transparency, and the aim of this particular engagement was to understand the company's strategy, targets and performance milestones. While the company in question was the first to set a target for emerging feed ingredients by 2030, during the engagement they were pushed for further disclosure on their strategy to reach their feed target, and the milestones that will be used to measure progress. Encouraged to provide more disclosure around the research and development of novel feed ingredients they were conducting, including risk assessment studies, the sustainability credentials of the ingredients and spending, the company provided further information during the engagement, although it argued some of the requested information was proprietary.

They did disclose they had spent €2.8 million on developing emerging feed ingredients. At present, the FAIRR collective engagement is only in Phase 2. Once this has concluded they intend to publish a report of their findings, with next steps yet to be discussed. The International Equity team continues to support this initiative and remains open to joining further collaborative engagements where they can add value and where the initiative aligns with the team's philosophy of in-depth bottom-up research, constructive discussion and encouraging change rather than making moral judgements.

ii) World Benchmarking Alliance ("WBA")

MSIM joined the World Benchmarking Alliance in 2022. The WBA is a global organisation that works to drive change within 2,000 of the world's largest companies by assessing and ranking them publicly on their performance. They focus on seven key areas, including climate change and just transition, social, biodiversity, food, digital, urbanisation and finance. Our goal in joining WBA is to cooperate with other investors on key issues across the Sustainable Development Goal (SDG) Space. The WBA also provides an excellent benchmarking tool to use to drive changes with companies and a network for partnership and community building.

Progress

The Head of ESG Research for our International Equity team attended the WBA Assembly in July 2022, which addressed the theme of "Community Building," exploring the potential of global and diverse partnerships to drive action on sustainable development. As it is still early stages, no significant outcomes have transpired; however, MSIM plans to continue taking part in roundtables and events with key global sustainability stakeholders.

iii) European Leveraged Finance Association ("ELFA")

MSIM joined ELFA as a member in 2021, led by our Fixed Income team, to help promote sustainability awareness and best-practice reporting amongst high-yield bond issuers. It is active on several ELFA committees, including those focusing on ESG and on Diversity and Inclusion.

Progress; Outcomes

As part of this process, the Fixed Income team provided input to a number of ELFA publications, including an ESG Fact Sheet for the Autos sector to help standardise the disclosure of material E, S and G considerations for the sector; an insight report *(SFDR's Disclosure Challenges: How Credit Investors and Corporate Borrowers Can Prepare)* to help high-yield issuers and smaller investors understand the implications of the EU SFDR and prepare for its implementation; and a summary report from the team's participation in ELFA's ESG engagement workshop, during which they shared their views on the importance of engagement focused on ESG topics with high-yield companies, main objectives and best practices to track progress. Smaller, often non-listed companies operating in the leveraged finance space tend to have limited resources to dedicate to sustainability reporting; hence the guidance and reference frameworks that we help provide them through ELFA contribute to making their disclosure process more efficient, transparent and targeted.

iv) Municipal Issuer Racial Equity & Inclusion Engagement Framework With JUST Capital

MSIM (led by the Fixed Income team) has an ongoing collaboration with JUST Capital, a nonprofit sustainability research organisation. Along with four other large asset managers, a Racial Equity and Inclusion Engagement Framework for U.S. Municipal issuers was launched in September 2021. This initiative is being implemented in collaboration with two minority-owned underwriters.

Progress

The framework is facilitating the opening of a constructive and voluntary dialogue between Municipal issuers and investors on diversity and inclusion (one of MSIM's thematic engagement priorities). By encouraging issuers to publicly disclose data in line with the framework, the initiative enables access to more transparent information across the market, helping stakeholders make more informed investment decisions.

One of the emerging challenges we see around collaborative engagement is the risk, for asset managers, of being involved in antitrust allegations, in particular in the U.S., by jointly participating in initiatives that target specific sectors or companies. MSIM has been mitigating this risk by involving its Legal and Antitrust Counsel when preparing for external collaborations, and by promoting maximum transparency in the context of these initiatives, e.g., by ensuring that statements of expectations for the companies are made clear from inception, and that any data or information collected by participating investors is shared publicly on platforms approved for the coordination of these collaborations.

v) Better Building Partnerships ("BBP")

In 2022, Morgan Stanley Real Estate Investing became a member of the Better Buildings Partnership ("BBP"), a group of leading commercial property owners who work together to improve the sustainability of existing commercial building stock.

Progress

As part of MSREI's membership, the Global Real Assets Sustainability team participates in working groups, such as Net Zero Carbon and Climate Resilience, and other BBP initiatives. Given the team has recently joined BPP, progress is still being made.

vi) National Council of Real Estate Investment Fiduciaries ("NCREIF") Pension Real Estate Association ("PREA") Reporting Standards ESG Working Group

The NCREIF PREA Reporting Standards (Reporting Standards) is an industry initiative co-sponsored by the National Council of Real Estate Investment Fiduciaries (NCREIF) and the Pension Real Estate Association (PREA) with a mission to establish, manage and promote transparent and consistent reporting standards for the real estate industry to facilitate informed investment decision-making. The three main areas of reporting are Valuation, Performance and Fair Value Accounting.

Progress

The Head of Sustainability for Global Real Assets participated in the NCREIF-PREA Reporting Standards ESG Working Group, which developed a set of global voluntary reporting standards for non-listed real estate investment vehicles in late 2021/early 2022.

vii) Electric Vehicle Automaker

Calvert is a member of a large group of investors that engaged with an electric vehicle automaker for their 2021 annual meeting after the company made no meaningful action against Calvert's engagement objectives around diversity, equity and inclusion.

At the company's 2021 annual meeting, a majority (57%) of shareholders supported Calvert's resolution asking the company to provide more quantitative data about its diversity, equity and inclusion efforts, which also included asking the company to disclose its EEO-1 report publicly. Despite receiving majority support from independent shareholders, the company did not commit to following through with the ask of Calvert's resolution.

Inaction and unresponsiveness followed the 2021 annual meeting, and upon further collaborative engagement with other investors Calvert decided to file a repeat resolution at the company's 2022 annual meeting.

Progress

Following Calvert's filing, the company informed the team they would be publishing EEO-1 data. Calvert withdrew its shareholder proposal for the company's 2022 annual meeting when the EEO-1 report was published in May 2022 as part of their greater ESG report.

Throughout the process, Calvert collaborated with other investors who shared the same concerns and difficulties in engaging with the company, corporate governance concerns, and significant controversies involving human capital management and DEI. Calvert will continue to work with the company and collaborate with other investors in the company in order to build on and improve EEO-1. In particular, the current report shows workforce diversity on a relative percentage basis, and the team ideally would like to see these reported on an absolute number-of-employees basis.

4) Giving Back to the Community: NGOs; Talent Development

We aim to contribute to our communities, including NGOs as part of our Morgan Stanley Core Value – Giving Back (Principle 1). We believe there is power in numbers when we bring different voices and interests to the table with common objectives.

We also embarked on an important talent development and recruitment initiative during the reporting period:

i) Sponsors for Educational Opportunity ("SEO") – Alternative Investments Fellowship Programme ("AIFP")

Last year, our PC&E business became a partner of SEO's Alternative Investments Fellowship Programme, which aims to connect historically excluded talent to career opportunities in the alternatives sector through interview preparation, a curated alternative investments curriculum, mentorship and private networking sessions. As one of 50+ partners, PC&E helps in educating, developing and providing access to first- through third-year investment banking analysts and management consultants who are looking to pursue careers in the alternatives.

Outcome

Through this partnership, PC&E has completed one cycle of the mentorship programme with two SEO fellows and is currently participating in another cycle of the mentorship program, again with two SEO fellows. In this mentorship programme, SEO fellows are paired up with a number of junior and senior investment professionals across PC&E's different strategies to help prepare them for on-cycle private equity recruiting. Additionally, PC&E is exploring opportunities to potentially hire SEO fellows into its investment teams full-time.

As outlined above, through their various businesses and internal functions, MSIM and Morgan Stanley belong to and take a leading role in many ESG-related organisations.

Overall

We regularly bring together investors, policymakers, NGOs and thought leaders to share lessons and promote innovative solutions to environmental and social challenges. Our priority is to always act in the best interests of our clients (Principle 6), as good stewards of their capital. This also includes participating in industry conference panels, exploring joint research and supporting the work of groups focused on ESG-related issues.

MSIM and Morgan Stanley are active participants in a number of external sustainability initiatives including, but not limited to, the following:

- U.K. Investment Association
- CDP (formerly the Carbon Disclosure Project)
- U.S. Partnership for Renewable Energy Finance
- Global Impact Investing Network ("GIIN")
- Sustainability Accounting Standards Board
- International Emissions Trading Association
- Principles for Responsible Investment ("PRI")
- PRI's ESG in Credit Risk and Ratings Initiatives
- Irish Funds Industry Association
- Ceres Investor Network on Climate Risk and Sustainability
- Business for Social Responsibility
- Emerging Markets Private Equity Association
- The Financial Stability Board Task Force on Climate-Related Financial Disclosures
- C2ES
- One Planet Summit Asset Managers Initiative
- Council for Institutional Investors
- Partnership for Carbon Accounting Financials ("PCAF")
- Black Women in Asset Management
- Net-Zero Banking Alliance
- European Leveraged Finance Association ("ELFA")
- The Impact Investing Institute and The Carbon Trust
- Ceres Private Equity Working Group
- Entrepreneurs In Action (EIA)
- Ceres Paris Aligned Investment Working Group
- 30% Club – U.K. Chapter
- FAIRR
- WBA

Calvert is involved in the following sustainability organisations and initiatives:

- The 30% Coalition
- Access to Medicine
- Access to Nutrition Index
- Human Capital Management Coalition
- Investors and Indigenous Peoples Working Group Principles for Responsible Investment (PRI)
- AHC Group
- As You Sow
- CDP
- Ceres
- Ceres Paris Aligned Investment Working Group
- Chemical Footprint Project
- Climate Action 100+
- Interfaith Center on Corporate Responsibility (ICCR)
- The Investment Company Institute
- Investor Agenda
- Farm Animal Investment Risk and Return (FAIRR)
- Global Network Initiative
- Investor Network on Climate Risk
- Net Zero Asset Managers Initiative
- U.S. SIF: The Forum for Sustainable and Responsible Investment
- UN CEO Water Mandate
- UN Global Compact
- UN Women's Empowerment Principles

PRINCIPLE 11

Escalation

Signatories, where necessary, escalate stewardship activities to influence issuers

Our regular engagements with company management provide an opportunity to monitor and track the performance of our investments. Both investment teams and the Global Stewardship team regularly monitor and engage with companies throughout the investment process and maintain detailed engagement records to track progress and to allow engagement insights to be incorporated in investment and proxy voting decisions.

We consider an engagement to be successful when a company is receptive to our viewpoints and suggestions and takes concrete steps to implement them. In cases where a company is not receptive or where our engagements do not lead to desired results, we may escalate our engagement by, for example, casting votes against management, requesting meetings with board members, or writing letters to boards and management. In some cases, repeated, unsuccessful engagements in relation to a material issue may contribute to a decision to decrease or exit a holding. Additionally, we may consider collaborative engagement or filing a shareholder proposal as an escalation method in appropriate cases.

Our portfolio managers are ultimately responsible for interpreting and integrating information gained through engagements into their investment decision-making process and for prioritising further engagement or escalation, as appropriate. Hence the need for escalation and types of escalation methods used depends on the investment, prior engagement activities, outlook and a judgement call made by the portfolio manager as to the materiality of the issue at hand, whilst always putting our clients' interests at the forefront of decision-making (in line with our Core Value to Put Clients First). As active owners, we already have regular engagements with portfolio companies/issuers. However, we also appreciate that each engagement is unique to the particular company and therefore we do not rely on a prescriptive engagement escalation framework. Therefore, in some cases, it may take years to effect substantive change on certain issues.

The following examples demonstrate the different types of escalation approaches taken by investment teams across asset classes based on individual team and portfolio investment circumstances:

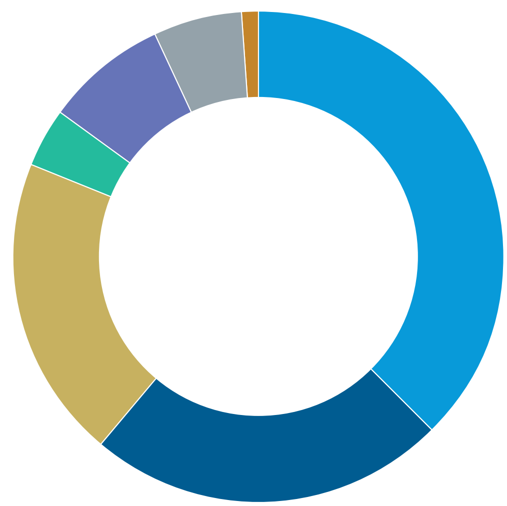
International Equity

Bringing issues directly to the company CEO is one form of escalation used by the International Equity team, as is voting. *Figure 11.1* below outlines the team's voting activity between 1 July 2021 and 30 June 2022:

FIGURE 11.1

International Equity Voting Activities

% Votes against management by topic 12 months to 30 June 2022 (across International Equity team's strategies)



Compensation	38%
Directors Related	24%
Shareholder Proposal - ESG	20%
Capitalisation	4%
Anti-Takeover Related	8%
Routine/Business	6%
Other Shareholder Proposal	1%

- In the 12 months to 30 June 2022 we voted on 1,634 proposals across our strategies, of which 9% were against management
- 26% of votes on 209 pay proposals were against management

Source: Morgan Stanley Investment Management. The views and opinions expressed herein are those of the portfolio management team, are not representative of the Firm as a whole, and are subject to change at any time due to market or economic conditions.

MSIM and the International Equity team did not vote one meeting due to shareblocking implications.

Over two-thirds of the votes were related to executive pay, director appointments and ESG-related shareholder proposals. In instances when the team has long-standing unresolved concerns, further escalation will see them vote against the election of committee members. For example, with companies whose pay plans they have voted against a number of times, the team votes against members of remuneration committees to make their message clearer. The team also votes against nomination committee members where they have concerns over diversity. In total the team voted against 30 directors in the last 12 months, as of 30 June 2022.

Voting on shareholder proposals is another form of escalation. While the companies the team owns receive fewer shareholder proposals than an average company, reflecting, they hope, fewer underlying issues, when they do, the team analyse them carefully and engage with companies on them. During the same time period they have voted in support of 31 shareholder resolutions, and against management 56% of the time, on a broad range of topics, including ESG issues such as decarbonisation, diversity and human rights.

CASE STUDY 11.1: ESCALATION TO EXISTING PORTFOLIO COMPANY ON EXECUTIVE COMPENSATION

Scenario	• The International Equity team believes incentives need to reward behaviour that is in the interest of shareholders. Owning companies for the long term, which they aim to do, means they are wary of incentive schemes that rely too heavily on earnings per share (EPS) as an evaluation metric. If management are paid on EPS, it can be tempting to manipulate earnings using short-term tactics—such as increasing debt or making acquisitions—at the expense of shareholders' long-term returns. They are also wary of schemes that award high pay for ordinary or even poor performance. Instead, the team likes to see management compensated for achieving return on capital targets, as well as progressing environmental and social objectives. • The team has been engaging with one of their U.K.-based consumer staples holdings on the subject of executive compensation for a long time. In previous engagements, they had argued that the preoccupation with EPS in management's long-term incentive plan ("LTIP") was not conducive to long-term performance, and that the lack of measurable environmental and social metrics would likely hinder progress in these areas. They also expressed their concern over the quantum of pay—given the potential value of the options package—which they felt was misaligned with the corporate's recent performance. Previously, they voted against the company's pay plan to signal their dissidence.
Outcome	• In their engagement with the Head of the Remuneration Committee earlier this year, the team was pleased to hear that EPS targets have been dropped from the pay plan, and that targets for decarbonisation and sustainable product promotion now constitute a meaningful portion of the LTIP. Furthermore, the company has reduced the maximum LTIP opportunity available to executive directors, meaning the quantum of pay has come down.
Reflection	• The International Equity team recognises that there is still a way to go, and they intend to keep pushing for more sensible operating metrics that should help share price performance in the long run. • This occasion has allowed the team to take stock of the company's progress. To signal their encouragement for the meaningful progress that has been made, they voted in favour of this year's pay plan.

Emerging Markets Equity

GENERAL APPROACH

Proxy voting has always been an important part of the Emerging Markets Equity team's active portfolio management and engagement and stewardship process. It is indeed the right of shareholders to vote and partake directly in corporate governance. The team actively reviews all proxies and will vote against management on proposals that they do not believe are in the best interests of shareholders on material financial, governance and sustainability issues. The team will also review past votes prior to their engagement meetings with management teams in order to ensure their messaging with companies remains consistent and to raise any issues the team found important during voting.

The EME team's escalation policy is based on a five-step process outlined below:

- **First conversation:** When the EME team has a concern around a company's approach to a certain material ESG risk, the team will first request a call with the company to discuss the issue, implications/negative effects on the business and our expectations. Afterwards, the team will monitor the company for the next 6-12 months for improvements.

- **First escalation:** If the team is not satisfied with the company's progress or feels that the company is unreceptive/unresponsive, they will raise this issue with the board or senior management and ask for a plan.
- **Second escalation:** Following EME's first escalation, they will follow up with management on the remediation plan and next steps and assess for measurable progress.
- **Vote:** If the team remains unsatisfied with the company's actions or feels that the company remains unreceptive, they will vote against directors responsible for this business area.
- **Consider divestment:** Given that divestment could remove options for further interactions and engagements, the investment team often tries to continue engaging with companies on the specific concern. In the case that the issue could have an adverse effect on the business model and/or stock price, and the team loses confidence in management or their ability to manage the issue, they may exit the company.

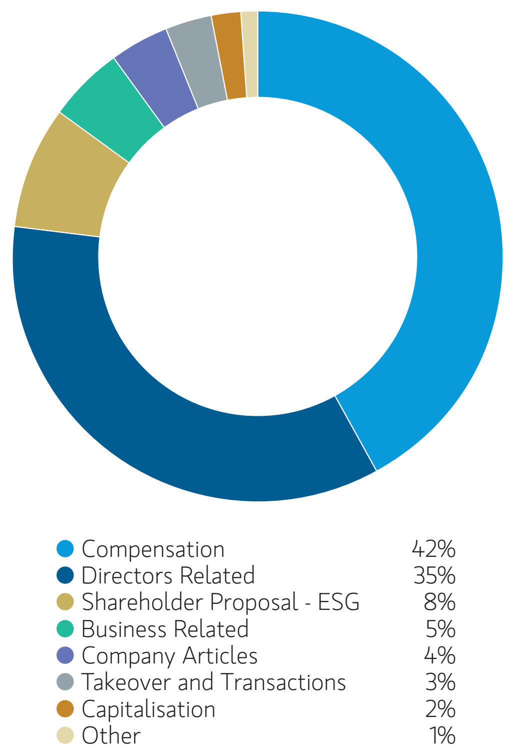
Over the past year, EME has prioritised a few themes for engagements based on current events. For example, given the news flow around human rights in the supply chain earlier in 2022, they engaged companies in apparel and electronics manufacturing where the team felt there might be increased risks of exposure (in this example the team assessed companies operating in the Xinjiang region of China). The EME team has followed this with a focus on human rights in metals and mining companies more recently. They are also prioritising engagements with their highest carbon emitters given the changes in emissions profiles expected in 2022.

Between 1 July 2021 and 30 June 2022, EME voted at 571 meetings and on 6,322 proposals. Overall, the team voted against management in 9% of the cases, and 46% of meetings had at least one vote against management. The most common reasons for voting against management were related to non-salary compensation, board structure and shareholder proposals—mostly on social items such as more disclosure on human rights and racial/gender equity issues. In the 2022 season, the investment team has continued to focus on board independence and remuneration plans.

FIGURE 11.2

Emerging Markets Equity Voting Activities

% Votes against management by topic 12 months to 30 June 2022 (across EME team's strategies)



- In the 12 months to 30 June 2022, EME voted on 559 proposals against management

Source: Morgan Stanley Investment Management. The views and opinions expressed herein are those of the portfolio management team, are not representative of the Firm as a whole, and are subject to change at any time due to market or economic conditions.

MSIM and the International Equity team did not vote one meeting due to shareblocking implications.

CASE STUDY 11.2: ESCALATION TO PERSUADE EXISTING PORTFOLIO COMPANY TO COMBAT DEFORESTATION

Scenario	• The EME team recently escalated its engagement with an existing portfolio company (global consumer goods company) to persuade them to explore initiatives in sustainable paper product sourcing and encourage more action to combat deforestation • The company currently targets an increase in the percentage of supply with the most stringent Forest Stewardship Council certification • While they are committed to 100% recycled or third-party certified packaging content, they were reluctant to introduce recycled paper into their actual products as they believe that would be detrimental to product performance (e.g., absorption)
Outcome	• After initial discussions with the company on this topic, EME was not entirely satisfied with the company's answers and actions, and supported a shareholder resolution on deforestation, which was passed • It was a partially achieved objective, with the company promising action in line with the resolution
Reflection	• The team will continue to monitor and assess the company's progress—to ensure that its objectives are fully met and determine feasibility of future progress • This occasion allows the team to determine whether to continue the engagement, to escalate further or to step back to monitor the company's ongoing progress

MSIM Fixed Income

GENERAL APPROACH

The Fixed Income escalation process is generally the same across geographies. However, as engagement priorities may differ based on sector and location, the factors influencing teams' escalation approaches may also differ. The team also aims to consider each issuer with respect to their level of regional development, which feeds into these differences in factors influencing escalation. For example, a persistent lack of a coal phase-out plan might be a trigger for escalation in the engagement with an energy or mining company operating and distributing mainly in a developed market, given the risks associated with new low-carbon regulation. However, the Fixed Income team might concede a longer time buffer for a company with most of their coal-related operations and distribution in emerging markets, taking into consideration the issue of access to affordable power. They would not apply the same flexibility with respect to issues related to human and labour rights as they believe issuers have to abide by established international norms. Governance standards may also differ across geographies, with certain countries or regions being more prone to company family ownership, for example, which in some instances can be associated with less transparent remuneration practices. The Fixed Income team has, on multiple occasions, escalated concerns around executive overcompensation within these types of companies.

Whilst the ownership rights conferred by equity tend to permit better corporate access and therefore more options with respect to escalating engagements, in the fixed income context the Fixed Income team typically escalates engagements by either voting against a bondholder resolution or raising relevant issues with other stakeholders in order to facilitate a collaborative engagement.

CASE STUDY 11.3: ESCALATION RESULTING IN DECISION NOT TO INVEST

Scenario	• The Fixed Income team engaged with an Indonesian mining company following the issuance of several new bonds after a period of inactivity. The company did not have a third-party ESG rating; however, the parent companies were either rated poorly by MSCI, at B in one case, or associated with severe pollution, biodiversity-related and community relations controversies. As a result, the team was concerned about the company's environmental damage and social risks and demanded the company provide evidence of entity-level mitigating policies and initiatives. • The engagement was in line with the Fixed Income team's targeting of companies, especially in emerging markets, which are deemed to be involved in severe sustainability controversies, to encourage adherence with international standards where available, and to support affected communities and landscapes.
Outcome	• On the environmental side, the company noted that the tailings from their mine continue to be disposed into the surrounding rivers, posing risks to both the environment and communities. The tailings are estimated to accumulate at a rate of 87 million tons per year, demonstrating extensive negative impact. • A key mine for the company is located in a politically sensitive area, resulting in clashes between employees and the armed forces. There have been over 20 deaths and 75 injuries between 2009 and 2020 as an alleged result of the company's negligence, both with respect to safety and human rights abuses. • As a response, the company outlined several strategies they planned to initiate, including starting the Copper Mark certification process. • However, the Fixed Income team Credit Analyst considered the response to be insufficient, highlighting the concerns to the Fixed Income Sustainable Investing Specialists. Whilst the company has a strong cost structure, and has implemented some sustainability strategies (such as a 2030 emissions reduction target, and plans to initiate a third-party human rights impact assessment), issues continue to persist with respect to their controversial mining practices, which outweigh current initiatives. • The company had not yet implemented tangible changes, and had only outlined future plans, without detailing concrete steps towards improvement. As a result, the Credit Analyst decided to recommend a more cautious position on the name across portfolios, and not to invest in this company's bonds.
Reflection	• An area the Fixed Income team could have improved in this case was the scope of collaboration for escalating engagement: By trying to join forces with other investors focused on addressing human rights or tailings issues in mining practices, the Fixed Income team might have persuaded the company to provide clear, detailed steps towards remediation of their controversies, across both environmental and social factors. We intend to focus more on the possibility of collaborative engagement going forward.

CASE STUDY 11.4: ESCALATION RESULTING IN DECISION TO DIVEST

Scenario	• In Q2 2022, the Fixed Income team engaged with a U.S. high-yield construction company, due to concerns relating to their governance and board structure • The Credit Analyst covering the company had identified significant issues relating to the plurality voting method of the board, and therefore aimed to encourage and assess the company's willingness to change their voting process • However, the company noted they had no plans to change plurality voting, and given the company is family owned, future changes were unlikely • The company also claimed that all members of the board are legally deemed independent; however, the team noted that one board member is not deemed independent by a third-party ESG data provider.
Outcome	• The company did not respond proactively to changing their voting process, which would continue to result in three entrenched board members, all of whom are on the Compensation Committee, with the CEO being overpaid compared to peers • The Fixed Income team considered the engagement outcome unsatisfactory, and considered the entrenchment of board members a persistent issue that impacts the use of additional cash, highlighting the priorities of the family-owned company • Given the CEO owns 15% of shares (family-owned), and with no succession plan discussed, the Fixed Income team decided to sell the company's bonds
Reflection	• Fixed Income research analysts will monitor the company's approach to their governance, particularly in relation to their board structure, to see if there will be any positive developments in the near future

Calvert Research and Management

GENERAL APPROACH

Escalation is a tactical decision made by Calvert's Engagement Analysts to increase pressure on a company to respond to requests to address our stewardship concerns. Shareholder proposals are the most common escalation tactic. Calvert uses escalation strategies when a company ignores or refuses our invitation to engage or takes no action or no meaningful action to address concerns, or the Engagement Analyst concludes that additional discussions are unlikely to move the discussion forward.

Shareholder proposals must be preapproved by the Calvert Director of Corporate Engagement and the Calvert Proxy Voting and Engagement Committee. Following the filing, the Engagement Analyst should generally seek to negotiate an agreement to withdraw the proposal on terms that advance our objectives with the company and lead to more collaborative dialogue. Calvert will proceed to a vote if terms for withdrawal offered by the company are not sufficient to meet Calvert's expectations for progress.

Calvert's Engagement team does not typically vary its approach across different asset classes when deploying this escalation strategy. Historically, Calvert's filing of shareholder resolutions has primarily been in the U.S.. Calvert also considers whether shareholder proposals are binding or advisory on a market-by-market basis. When a proposal is advisory in nature, it makes it easier to support a resolution knowing that if the ask of the proposal is a tall ask, companies have some flexibility in how much or the way they respond to the passed proposal. When a proposal is binding in nature (which is the case in many global markets), supporting and filing a shareholder resolution can be more complicated, knowing that a company is bound to satisfy the ask of the proposal, even if it means potentially compromising the strategy of the business or may affect supply/production costs and therefore result in a financial risk to shareholders.

The following escalation examples relate to Calvert's Diversity & Inclusion engagement priority, in which it seeks to encourage companies to publicly disclose their Equal Employment Opportunity Commission ("The EEO-1 Report"), which is submitted to the U.S. Equal Employment Opportunity Commission ("EEOC") on an annual basis. Since 1968, companies have been required to report the demographics of their U.S. workforce to the EEOC, disclosing the number of employees in each of 10 job categories (e.g., executive, management, professional, administrative and labour) categorised by race, ethnicity and gender. The report provides the most detailed perspective on the diversity of a company's workforce, but individual company reports are not available to the public unless the company chooses to disclose theirs voluntarily.

At the outset of Calvert's initiative, only 4% of Russell 3000 companies disclosed this report, though among the largest companies 15% disclosed as of 2019. Calvert contacted the top 100 names in its Calvert Indexes to encourage the publication of EEO-1 data. The team wrote to the 18 companies that were already publishing this report, thanking them and asking them to continue doing so. Calvert engaged with the other 82 to address their concerns and to encourage disclosure. As of 30 June, 2022, 91 out of the top 100 names in the Calvert Indices have disclosed or have committed to disclose their EEO-1 reports publicly.

CASE STUDY 11.5: ONGOING ESCALATION WITH CHALLENGES; OUTCOME NOT REACHED YET

Scenario	• Beginning in H2 2020, Calvert sent a letter to the Chair of the Board and Chief Diversity Officer of a communications company to express the need for and the importance to shareholders of the Company making its EEO-1 report publicly available. Calvert requested a call to which they never responded. • The company's current disclosure shows a percentage breakdown of female, Black/African American, Hispanic/Latin-x, Asian and Veteran employees, but this breakdown is listed merely as a percentage of all full-time and part-time employees. • Instead, Calvert believes that effective diversity reporting should show the breakdown of employees by race and gender clearly delineated by job classifications, which is what the EEO-1 report shows. Corporate commitments to diversity are credible only if the company releases full EEO statistics on its workplace demographics. • Due to the lack of response to Calvert's engagement, the team filed a shareholder resolution at the company's 2021 annual meeting. • Calvert had their initial opportunity to engage with the company only after the proposal received 40.7% support in 2021. The team also followed up that call with a letter to board members to which they did not respond. • Calvert filed again for the company's 2022 annual meeting. This year, the company became more receptive and offered to have a dialogue with the team. They offered some incremental disclosure (not the full EEO-1) to see if Calvert would consider withdrawing the proposal. • Calvert's proposal then went to a vote this year and received 45.5% (up 5 percentage points from 2021).
Ongoing Escalation Process	• As the company was not willing to engage with Calvert and their existing disclosures did not meet the standard as appropriate, Calvert escalated the issue by filing a shareholder proposal at consecutive annual meetings • The company is closely held by an affiliated entity that votes in line with management. That entity held 30% of the company's outstanding shares and voting power in 2021, and that percentage increased to 40% in 2022. Despite this being a challenge to the shareholder proposals Calvert filed at both annual meetings, support for their proposal actually increased from 40% to 45% year-over-year, demonstrating an increasing number of independent shareholders believe that this diversity disclosure is critical.
Reflection	• Over time, the company is becoming more receptive to engaging with Calvert on this issue. Compared to the lack of response to the team's initial outreach in the second half of 2020, most recently, the company has offered to disclose some incremental amount of diversity information in order for Calvert to consider withdrawing their most recent shareholder proposal. • This engagement is one where Calvert has not yet achieved their objective but has made incremental progress, which can be demonstrated by two main metrics: the way the company has responded over time and the increase in independent shareholder support. Calvert intends to continue its robust approach to engagement and escalation on this topic going forward • As Calvert expands its engagement scope in the future, the method of filing shareholder proposals as a form of escalation can be improved and expanded to other markets • Calvert also intends to evaluate and consider further the feasibility and usefulness of varying its approach to escalation by asset class

SECTION 4

Exercising Rights and Responsibilities

PRINCIPLE 12

Exercising Rights and Responsibilities

Signatories actively exercise their rights and responsibilities

Overview

As noted previously, MSIM investment teams exercise the rights and responsibilities associated with the assets they manage in line with their respective investment strategies in regard to factors such as the type of assets, their risk assessments and investment convictions. At the forefront of this is our collective organisational purpose and Firm Core Value to always Put Our Clients First, and act in their best interests in managing their assets (Principle 1 and Principle 6).

Throughout this report, we have outlined how our investment teams approach stewardship differently in exercising their rights and responsibilities through our Purpose and Governance (Principles 1 – 5), Investment Approach (Principles 6 – 8), and Engagement (Principles 9 – 11) across different investment teams, asset classes and geographies (although as active owners, our approach in exercising our rights and responsibilities does not generally vary by region). We do so by also leveraging support and expertise from our Sustainability governance stakeholders including our Global Sustainability for Investment Management, Sustainability Council, core Sustainability team, Sustainability Oversight & Governance, Sustainability Team Leads and functional experts in Legal, Compliance, Risk, Portfolio Surveillance, etc. Over the past 12 months we have taken additional steps to implement enhanced governance, oversight and processes to ensure that our holistic stewardship approach aligns with evolving client interests and regulatory developments, and that our investment teams have sufficient support as our product platforms and engagement activities expand. At the same time, we uphold our fiduciary duties with our Firm Code of Conduct. All this is taken into consideration in our efforts to minimise greenwashing, stewardship-washing and anti-trust risks, as part of our role within the asset management industry.

For our High-Conviction Equities business, given the nature of the equities asset class, our rights and responsibilities are mainly exercised through one-to-one direct engagement with company management and boards of directors (our preferred engagement approach across investment teams), proxy voting, filing of shareholder resolutions, and, where circumstances are appropriate and situations permit, industry/external collaboration.

With respect to our Fixed Income & Liquidity business, we exercise our rights and responsibilities through good stewardship efforts both at the pre-investment stage and throughout our holding of a security, including through collaborative engagements with stakeholders. We use engagement and escalation (if needed) to inform our investment decisions, which ultimately has an impact on issuers. Please see below for further details regarding our approach to seeking amendments to terms and conditions in contracts and/or indentures.

In our Alternative Investments business, especially for PC&E, given the illiquid nature of the asset class, our rights and responsibilities are exercised based on the nature of each strategy for our underlying portfolio companies (e.g., control versus non-control). As outlined in Principle 9, in control situations, we exercise our rights through our board seats on portfolio companies, which we are invested in to engage and work with portfolio company management teams—steering companies towards best ESG practices and business activities. Conversely in non-control situations, this depends on the nature of our relationship with and the willingness of each portfolio company to engage in ESG-related topics. At times, we may have board observer rights, which provide us with a greater level of transparency; however, this does not enable us to fully engage with companies in the same way as in control situations. Our private equity secondaries and co-investment strategies usually back/invest alongside managers who are regulated entities and have a high standard of governance processes in place. In fact, a component of the manager engagement is to improve governance standards (board frequency, decision transparency, disclosures etc.) for underlying portfolio companies. Much of this is negotiated up front as part of investment documentation. Furthermore, we also supplement our exercise of rights and responsibilities with other engagement methods such as the use of third-party due diligence/service providers to augment our investment teams' activities.

Within Private Real Assets, for MSREI, we generally structure our real estate joint venture ("JV") investments such that our funds will typically possess at least as much control over major property decisions as any of the other joint venture partners. The JVs will also include liquidity provisions intended to enhance portfolio flexibility and governance.

Likewise, our private infrastructure (MSIP) portfolio companies strive to uphold high ethical standards at all times and follow standard codes of business conduct, including anti-corruption and anti-money laundering policies and procedures. Employees and contractors are encouraged to ask questions, voice concerns and report any alleged violations of company policies. Through MSIP's board representation, which typically reflects control equity positions, the board assesses management's policies, practices and performance; it reviews plans and proposals for ESG metrics, policies and the measurement of progress with a focus on continuous long-term improvement. MSIP looks to foster long-term relationships and build trust and good will with all key constituents, including regulators and contractors. MSIP's constituents help shape the team's ESG efforts by sharing valuable feedback on new ideas, best practices and industry trends, where applicable.

In our Custom Solutions Group, rights and responsibilities exercised depend on the type of customised/bespoke investment solutions created for our clients, incorporating their ESG/stewardship priorities and requirements. Where equities or fixed income assets form part of a client's custom solutions portfolio, such rights and responsibilities are exercised via the above methods outlined in relation to the relevant asset classes.

In the same vein, our Parametric business approaches responsible investing by focusing on exercising ownership rights, primarily on proxy voting but also valuing direct engagements with companies. The team reserves specialised portfolio construction techniques primarily for client-directed mandates in separately managed accounts. Parametric's long-term view provides impetus for them to encourage good corporate governance practices that benefit shareholders while continuing to deliver the underlying strategy return.

Similar to our other investment teams, Calvert takes an active shareholder approach in exercising rights and responsibilities. While others may vote in lockstep with management, Calvert's voting record is based on comprehensive guidelines that encourage corporate responsibility, which includes respectful treatment of workers, suppliers, customers and communities; environmental stewardship; product integrity; and high standards of corporate ethics as well as more traditional measures of sound corporate governance.

HIGH-CONVICTION EQUITIES AND GLOBAL LISTED REAL ASSETS

Voting Policy, Monitoring Shares & Voting Rights

Within our Global Stewardship team, our Proxy Review Committee has responsibility for overseeing the implementation of our MSIM Proxy Voting Policy to proxy votes at issuer shareholder meetings across our global portfolios, under one global policy, for which we have a dedicated Proxy Voting section on our website, including our Proxy Voting Records. Please refer to Principle 2 and Principle 5 for further details.

The MSIM Proxy Voting Policy addresses a broad range of issues, and provides general voting parameters on proposals that arise most frequently. We endeavour to integrate governance, sustainability and proxy voting considerations with investment goals, using votes to encourage portfolio companies to enhance long-term shareholder value and to provide a high standard of transparency such that equity markets can value corporate assets appropriately.

In doing so, our Global Stewardship team has developed a proprietary system that tracks and monitors our MSIM shares and voting rights, including a ballot reconciliation module (rather than just relying on our proxy service providers). We perform a ballot reconciliation for every meeting to ensure share positions eligible to participate in the event are voted—and any discrepancies, if any, are investigated and resolved prior to the cut-off date. The proprietary system also handles work-flow around proxy voting, and to document views of various parties at MSIM and voting rationale for the final decisions. We are notified of upcoming voting events by ISS through electronic feeds. Our proprietary system performs an automated reconciliation comparing our shareholding data with the ballots received and highlights exceptions for review. All exceptions are investigated and resolved by MSIM, which may entail communication with intermediaries and vendors to resolve or document explanations for discrepancies. MSIM's Proxy Voting related controls are part of SOC examination, and in the past seven years there were no exceptions found. As noted under Principle 5, MSIM maintains voting records of individual agenda items at company meetings in a searchable database on its website on a rolling 12-month basis. These Proxy Voting Records are published periodically on our website.

ISS serves as MSIM's voting agent, but all vote decisions are made by MSIM, informed in part by research from ISS and from Glass Lewis. MSIM is responsible for ensuring that voting instructions for the client account are communicated to the proxy advisor. Our proxy advisors assist us in monitoring the voting rights we have in relation to shares we hold by aggregating proxies and notifying us of all upcoming shareholder meetings and the relevant voting rights we have in relation thereto.

The Global Stewardship team maintains a control process to ensure eligible holdings are voted at shareholder meetings. The Proxy Review Committee makes the proxy voting decisions for certain types of votes in accordance with the Firm's Proxy Voting Policies and Procedures together with input from our equities investment teams. The Proxy Review Committee meets on a periodic basis or as needed. The Corporate Governance Committee is available to the Proxy Review Committee for guidance in ensuring votes are in accordance with the firm's Proxy Voting Policies and Procedures.

Our MSIM equities and global listed real assets teams vote proxies in a prudent and diligent manner and in the best interest of clients, including beneficiaries of and participants in a client's benefit plan(s), for which the sub-advisor manages assets, consistent with our Core Value to Put Clients First and our overarching investment objective of maximising long-term investment returns (Principle 1 and Principle 6). We consider voting to be an important stewardship and investment responsibility that impacts shareholder value and portfolio managers have in-depth knowledge of the companies and markets in which they invest.

Individual Circumstances and Client Preferences

As noted under Principle 3, there are occasions where different portfolio teams may view an issue differently and, in those cases, we may split our votes to accommodate those different views. Some clients may also wish to retain voting rights for their shares or accounts. Any client with a separately managed account that has delegated proxy-voting authority to MSIM is permitted to request, at any time, how they would like a certain meeting or ballot item voted. We do not currently facilitate clients directly voting in a pooled vehicle because of the practical difficulties in proportioning a ballot, and because we are mindful of potential legal and regulatory hurdles that may restrict or prevent client directed voting in pooled fund structures.

Retention and Oversight of Proxy Advisory Firms

As mentioned above and in Principle 7 and Principle 8, MSIM retains the services of ISS and Glass Lewis as independent advisors that specialise in providing a variety of fiduciary-level proxy-related services to institutional investment managers, plan sponsors, custodians, consultants, and other institutional investors. The services provided include in-depth research, global issuer analysis, record retention, ballot processing and voting recommendations.

Notwithstanding the retainment of ISS and Glass Lewis, services provided by both are only used in an advisory and administrative capacity; we do not rely on either firm to implement a custom stewardship policy. As a result, their voting recommendations are not used to determine our final vote decisions. We only rely on them for proxy vote execution, reporting record-keeping, and where appropriate, to provide company-level reports that summarise key data elements within an issuer's proxy statement or on specific thematic/market topics. It is important to note that between 1 July 2021 and 30 June 2022, MSIM voted differently from our primary proxy advisor, ISS, 5% of the time across all ballot items, which further reinforces our direct stewardship/proxy voting philosophy.

MSIM performs ongoing monitoring and due diligence reviews on retained proxy advisors on an annual basis; periodic reviews are conducted onsite by members of the Global Stewardship and Proxy teams and MSIM Compliance (please see Principle 8 for more details).

Securities Lending

MSIM Funds or any other investment vehicle sponsored, managed or advised by an MSIM affiliate may participate in a securities lending programme through a third-party provider. The voting rights for shares that are out on loan are transferred to the borrower and, therefore, the lender (e.g., an MSIM Fund or another investment vehicle sponsored, managed or advised by an MSIM affiliate) is not entitled to vote the lent shares at the company meeting. In general, MSIM will not recall shares for the purpose of voting. However, in cases in which MSIM believes the matters being put to vote are critical for the investment thesis or client interests, we reserve the right to recall the shares on loan on a best-efforts basis. In order to effectively monitor whether recalling shares may be necessary, ISS provides electronic feeds, which enrich Provosys with meeting details, including ballot-level holdings. The team performs ballot reconciliation for each meeting to ensure appropriate ballots are received and shares out on loan are identified by GST through this review. We generally do not encounter scenarios where all holdings associated to a meeting are out on loan—the scenarios would be limited to a few portfolios, and even then, the entire holding may not be out on loan.

EQUITY VOTING STATISTICS, SELECT TOPICS AND CASE STUDIES (1 JULY 2021 – 30 JUNE 2022)

Between 1 July 2021 and 30 June 2022, MSIM voted on more than 98% of the ballots on which it is eligible to vote. The residual <2% of votes not voted were generally due to various issues that can arise when voting proxies of companies are located in certain overseas jurisdictions, where local processes can often restrict or prevent the ability to vote such proxies, or entail significant costs.

These problems include, but are not limited to: (i) proxy statements and ballots being written in a language other than English; (ii) untimely and/or inadequate notice of shareholder meetings; (iii) restrictions on the ability of holders outside the issuer's jurisdiction of organisation to exercise votes; (iv) requirements to vote proxies in person; (v) the imposition of restrictions on the sale of the securities for a period of time in proximity to the shareholder meeting; and (vi) requirements to provide local agents with power of attorney to facilitate our voting instructions. As a result, we vote clients' non-U.S. proxies on a best-efforts basis only, after weighing the costs and benefits of voting such proxies.

MSIM provides rationales for votes where we vote against key issues like director and executive remuneration, and rationales for shareholder sponsored resolutions. We disclose vote rationales to clients upon request in aggregate, in our annual public reporting. For a full disclosure of how we voted in any meeting, please visit our website for full voting records, which are updated on a rolling monthly basis. We also disclose our proxy votes globally through annual N-PX requirements with the U.S. SEC for all Mutual Funds under the U.S. Investment Advisers Act of 1940.

The following examples illustrate how the engagement and proxy voting processes work together in the exercise of our stewardship duties. These cover some of the most common proposals we review each year.

Shareholders in the U.S. and certain other markets submit proposals encouraging changes in company disclosure and practices related to particular sustainability issues. MSIM investment teams, with support from the Global Stewardship team, consider how to vote on such proposals on a case-by-case basis by determining the relevance of the issues identified in the proposal and their likely impacts on shareholder value. We also take into account a company's current disclosures and our understanding of its management of material ESG issues in comparison to peers.

We seek to balance concerns about reputational and other risks that lie behind a proposal against costs of implementation while considering appropriate shareholder and management prerogatives. We may abstain from voting on proposals that do not have a readily determinable impact on shareholder value and we may oppose proposals that intrude excessively on management prerogatives and/or board discretion.

Between 1 July 2021 and 30 June 2022, MSIM supported 49% of shareholder proposals and abstained on 0.3% of shareholder proposals. On the environmental side, notwithstanding thematic updates below, we generally voted on an increased number of proposals seeking to promote sustainable-packaging efforts by reducing the use of plastic packaging and were supportive. With respect to political lobbying and spending, we observed

Overall Voting Statistics (1 July 2021 – 30 June 2022)

Total Number of Meetings Voted	8,982
Total proposals	92,612
(of which are Shareholder Proposals)	875
Number of markets voted	73
% of meetings with at least 1 vote against management	49%
% votes against management	12%
% with management	88%

Shareholder Proposals by Region

REGION	NUMBER OF SHAREHOLDER PROPOSALS	NUMBER OF VOTES SUPPORTING SHAREHOLDER PROPOSALS*	% OF VOTES SUPPORTING SHAREHOLDER PROPOSALS
Asia	67	13	19%
EMEA	130	21	16%
North America	631	379	60%
South America	0	0	0%
Rest of World	47	12	26%
Total	**875**	**425**	**49%**

*Includes cases where we have abstained from voting

i) Corporate Governance/Executive Compensation

REGION	NUMBER OF PROPOSALS	NUMBER OF VOTES AGAINST EXECUTIVE REMUNERATION*	% OF VOTES AGAINST
Asia	2	0	0%
EMEA	1,670	543	33%
North America	2,355	518	22%
South America	1	0	0%
Rest of World	244	66	27%
Total	**4,272**	**1,127**	**26%**

*Includes cases where we have abstained from voting

CASE STUDY 12.1: SAY-ON-PAY

Scenario

The long-term investment horizon of one of our equity investment teams encourages a close eye on incentive schemes that appear too short term in their outlook. They are also alert to schemes that award high pay for ordinary or even poor performance - in their opinion simple time served is not a good enough reason for large rewards.

Voting Outcome

At the annual general meeting of a European multinational software company owned in their global portfolios, the team voted against the company's remuneration plan due to the inclusion of non-IFRS earnings, the short vesting period, and an insufficient degree of performance-based targets. While the company had moved away from rewards being cash settled to shares, the team were not convinced this was sufficient to warrant a "for" vote, given aspects of the plan could detract from long-term shareholder value.

CASE STUDY 12.2: SAY-ON-PAY

Scenario

One of our multi-asset teams met with a British professional services business prior to their annual general meeting, as part of the team's ongoing monitoring of their portfolio's corporate governance. The team had significant concerns with continued poor remuneration policy implementation. Notably, they were concerned that the Remuneration Committee intervened and exercised positive discretion to adjust metrics in order to make them more achievable. The team expressed satisfaction at the board's Remuneration Committee refreshment, but were concerned that the former Chair remained a member. The team believed that as the company moves toward a new remuneration policy, they should exercise a break with the past and relieve the director of their remuneration committee duties. The team pointed out significant shareholder discontent with the director in question at the last annual meeting.

The company agreed in hindsight that exercising positive discretion was egregious and signalled poor governance and accepted that the former Chair of the Remuneration Committee was the focus of a lot of shareholder ire.

The team notified the company it would vote against the Pay Report and for the Pay Policy in light of adjustments made as well as voting against the former Chair of the Remuneration Committee.

Voting Outcome

In the last annual general meeting, the management Pay Report received only 28.69% of votes cast while the Pay Policy received 90.01%. Notably, in the days after the team's engagement with the company, the director in question opted not to stand for re-election.

ii) Other Topics Aligned With MSIM's Engagement Priorities

CATEGORY	NUMBER OF PROPOSALS	NUMBER OF VOTES SUPPORTING SHAREHOLDER PROPOSALS (VOTES AGAINST MANAGEMENT)	% OF VOTES IN SUPPORT FOR SHAREHOLDER PROPOSALS
Climate Action	87	54	62%
Board and Employee Diversity	48	39	81%
Human Rights	28	20	71%
Political Lobbying and Spending	57	36	63%
Environmental – Other	59	23	39%
Social – Other	41	8	20%

an increased number of proposals asking companies to assess the congruency between their stated values and their political lobbying activities. We are supportive of proposals requesting increased disclosure of political contributions resulting in improved transparency; however, we have not supported proposals if the company has sufficient transparency in its lobbying-related disclosure.

SELECT TOPICS

MSIM has a long history of focusing on corporate governance. We believe that good corporate governance is a signal of quality management and that well-managed companies will produce long-term returns for our clients. Executive compensation is an important indicator of good board oversight and we consider advisory votes on remuneration on a case-by-case basis. Considerations include a review of the relationship between executive remuneration and performance based on operating trends and total shareholder return over multiple performance periods. In addition, we review remuneration structures and potential poor pay practices, including relative magnitude of pay, discretionary bonus awards, poorly defined target metrics, tax gross-ups, change-in-control features and internal pay equity. As long-term investors, we support remuneration policies that align with long-term shareholder value.

Between 1 July 2021 and 30 June 2022, MSIM took into consideration the uncertainty created by COVID-19 and the exercise of discretion by compensation committees. We supported 74% of say-on-pay proposals and voted against 26% of proposals. MSIM voted against say-on-pay proposals primarily due to excessive compensation relative to company performance, upfront and mega grants, and poor pay practices.

a) Climate- and Environment-Related Proposals

MSIM recognises that climate change poses risks to the global economy. When voting on environmental and social

CASE STUDY 12.3: BOARD DIVERSITY

Scenario	One of our Equity teams also met with a large-cap IT consultancy and services company prior to its annual general meeting to discuss the board's work toward rebuilding gender diversity, which is currently at 17%, down from 33% two years ago. This indicates a deterioration in board diversity rather than the improvement the team had hoped to see.
Voting Outcome	As a result of this, the investment team voted against the Nomination Committee members at the latest annual general meeting, and each nomination received at least 75% support of votes cast. Undeterred, the team will re-consider our approach and plan to re-engage the company in 2022 to ensure improvement in board diversity at the company.

proposals we take action by considering a company's disclosures compared to peers, which is why we tend to support more climate resolutions at U.S.-based companies, given they can lag behind their global peers on climate reporting and transitioning to a low-carbon economy.

Between 1 July 2021 and 30 June 2022, MSIM supported 56% of climate-related proposals overall. We voted on an increased number of proposals seeking GHG emission-reduction targets, and were supportive of proposals requesting companies to set greenhouse gas ("GHG") emissions reduction targets where we felt they were lagging peers or that GHG emissions were a material risk.

With respect to the remaining 44% that were not supported, this came down to several factors. In 2022, financial institutions received proposals seeking to limit or end financing of new fossil fuel supplies. As outlined above, while we take various factors into consideration, we seek to balance concerns on reputational and other risks that lie behind a proposal against costs of implementation while considering appropriate shareholder and management prerogatives. We may abstain from voting on proposals that do not have a readily determinable financial impact on shareholder value and we may oppose proposals that intrude excessively on management prerogatives and/or board discretion. We generally vote against proposals requesting reports or actions that we believe are duplicative, related to matters not material to the business, or that would impose unnecessary or excessive costs.

CASE STUDY 12.4: CLIMATE ACTION

Scenario	In 2021, Calvert, in cooperation with As You Sow (a nonprofit leader in shareholder advocacy) and another stakeholder, filed a shareholder resolution with a North American energy infrastructure company asking its board of directors to evaluate and issue a report describing if, and how, the company's lobbying activities align with the Paris Agreement's goal to limit temperature rise to 1.5oC. Calvert also requested information on the company's plans to mitigate risks presented by any misalignment with the Paris Agreement.
Proposal Outcome	At the company's May 2021 annual meeting, the shareholder proposal received 37.5% support. Following that annual meeting, the company engaged in ongoing dialogue with Calvert and other stakeholders. In December 2021, the company committed to continue an open and productive dialogue with Calvert, in partnership with As You Sow and the second stakeholder, toward a common goal to improve and promote transparent disclosure regarding the company's lobbying practices. The company committed to issuing a report assessing the alignment of direct and indirect lobbying activities with the Paris Agreement, including actions taken, or proposed to be taken, in any areas of misalignment with the goals of the Paris Agreement, and committed to a timeline for that report's production. It also committed to issuing a similar report on an annual basis through at least 2024. Calvert, in collaboration with its two other stakeholders and the company has committed to an ongoing dialogue around other areas of interest, including timelines and interim goals related to the company's goal to reduce Scope 3 emissions, either on an agreed upon regular basis or as appropriate. In addition to climate lobbying, the company has also agreed to continue Calvert's discussions around the announced Net Zero goals and targets, especially as it relates to Scope 3 disclosure associated with its natural gas utility business.

CASE STUDY 12.5: DECARBONISATION

Scenario	In another example, one of our equity teams is conducting an ongoing carbon transition engagement programme, aiming to understand the climate profiles of the companies they own, and encouraging progress. This could involve seeking better transparency and accountability, challenging well-meant targets that lack credible pathways or, for those already on the right track in terms of disclosure, targets and actions, engagements are used to track performance and encourage continued leadership. The team also uses voting to reinforce their support of the companies in their portfolios taking positive actions in relation to climate change. A multinational technology conglomerate owned by the team received 17 shareholder resolutions for its 2022 AGM. Two of these proposals were climate related: one requesting the company report on climate lobbying and another requesting the company produce a report on the physical risks of climate change.
Voting Outcome	The company advocated a vote against the proposal requesting a report on climate lobbying, arguing that its comprehensive lobbying disclosures provide shareholders with all necessary information to understand the scope of the company's lobbying activities. However, while the company publicly supports the Paris Agreement, and discloses a list of its memberships of trade associations and policy-focused nonprofits, it does not disclose sufficient information as to how it ensures lobbying proposals (both directly and indirectly via these groups) align with the Paris Agreement's aims. Particularly concerning are industry and policy groups that represent businesses but present obstacles that impede global emissions reductions. A review of the company's disclosed memberships reveals inconsistencies with the company's actions on, and commitments to, the Paris Agreement. The team therefore chose to vote in favour of the proposal. The company also recommended a vote against the second climate-related proposal, which requested that it publish a regular assessment on its resilience to the physical risks of climate change, including the measures the company is taking to mitigate these risks. The company argued that given the existing environmental and climate change reporting it already produces, such an assessment would not be a good use of company resources. However, while the company discloses the physical risks it has identified, it does not provide much disclosure in terms of its adaptive planning in relation to these risks. The team chose to vote in favour of this proposal, believing that more granular detail would be beneficial to shareholders.

b) Gender Pay Gap Proposals

Several U.S.-based companies in consumer discretionary and information technology sectors have recently received shareholder proposals requesting that they report on the gender pay gap across their global employee base. We are supportive of these proposals for two main reasons. First, because all targeted companies already provide gender pay gap data for their U.K. operations, making the prospect of rolling this reporting out globally less burdensome. Second, because we believe pay gap data provides a helpful lens alongside pay equity data. Most companies that received these proposals already disclose pay equity data, which illustrates pay disparities between men and women in similar roles. Pay gap data shows the unadjusted difference between what women in an organisation are paid as compared to men. This raw number can be helpful in illuminating a company's "leadership gap" or the extent to which women are disproportionately in lower-paying positions than men.

Between 1 July 2021 and 30 June 2022, MSIM supported 86% of proposals on gender pay gap disclosure. We are committed to supporting fair pay, promotion and development opportunities. The proposals were analysed on a case-by-case basis and we supported proposals where we observed the company's disclosures did not provide adequate transparency. We did not support proposals where, as a result of our analysis, we concluded the company has sufficiently addressed the requirement.

With respect to the remaining 14% of proposals that were not supported, MSIM votes on proposals related to gender pay gap on a case-by-case basis taking into consideration the company's policies and disclosure related to diversity and inclusion, compensation policies, controversy or regulatory actions related to gender pay gap, and whether the company's reporting is lagging peers. We may oppose proposals that would impose excessive costs or if the company has sufficiently addressed requirements of the proposal.

CASE STUDY 12.6: GENDER PAY DISPARITIES

Scenario	Over recent months, one of our equity investments teams has been encouraging greater gender pay gap ("GPG") disclosure among their holdings through both their engagement and voting activities, given that it serves as a useful indicator of a company's diversity and culture. Today, a U.S.-based technology conglomerate that the team owns reports the representation gap of various groups at different seniority levels within the firm. They also report 0% "same pay for same work" gap. However, this does not address the gender pay disparity issue or the under-promotion of women to senior, better-paid jobs.
Voting Outcome	At the company's annual general meeting, the team voted in favour of a shareholder proposal asking the company to report on their median unadjusted pay gaps across race and gender. While the shareholder proposal failed, the company has agreed to publish median racial and gender pay gaps after 40% of shareholders voted in favour of the proposal. Apart from helping the team meet the EU SFDR requirements, which requires this level of disclosure, the single unadjusted pay gap measure encapsulates the economic loss by the under-represented groups in one number, which is a useful indicator. It also enables the team to compare and measure the progress of the company's diversity and inclusion initiatives. This measure is supported by the UN, ILO and the U.S. government. MSIM is also supportive of additional disclosure on this issue.

CASE STUDY 12.7: BOARD DIVERSITY

Scenario	As part of their regular engagement with company management on board diversity, one of our equity teams uses their Diversity, Equity & Inclusion checklist as a tool to push for better data, greater transparency, aligned incentives and credible pathways for change. A U.S. communication services company they own has reached the minimum goal of 30% women articulated by the 30% Club. Yet while the holding is not lagging U.S. peers in terms of board diversity the team felt that there was still room for improvement, given that the board's diversity is not yet reflective of the company's customer base (27% are women and 18% are underrepresented minorities, versus the demographic makeup of the U.S. at 51% women and 32% under-represented minorities).
Voting Outcome	The investment team supported the shareholder proposal asking the company to report annually on its policies and practices to help ensure the company's elected board of directors attains racial and gender representation that is better aligned with the demographics of its customers. The team intends to engage further with the company on this topic as necessary.

CASE STUDY 12.8: DIVERSITY AND INCLUSION AUDIT

Scenario	Regarding diversity and inclusion policies, the protests against systemic racism in the U.S. have garnered international media attention, prompting the topic to become a major focus of stakeholders. One of our equity investment teams believes that for a U.S. Communication Services company they own, a racial equity audit would help mitigate reputational, regulatory, legal and human capital risk, particularly in light of discrimination allegations that the company has faced.
Voting Outcome	The investment team voted in favour of the shareholder proposal, urging the board of directors to commission a third-party, independent racial equity audit analysing the company's impacts on Black, Indigenous and People of Colour communities. The team believes that having a third party conduct this assessment would be particularly beneficial and instil confidence in the impartiality of results.

c) Diversity & Inclusion Proposals

MSIM believes that diverse and inclusive workplaces lead to more productive and innovative work environments and that the boardroom plays a powerful role in laying the foundation for more diverse and inclusive workplaces. We generally support proposals asking companies to disclose more information on the diversity breakdowns of their workforces or on their policies and programmes for improving diversity and inclusion.

Between 1 July 2021 and 30 June 2022, MSIM supported 81% proposals to increase board and employee diversity. This year there has been an increase in proposals requesting companies to oversee Civil Rights, Diversity and Inclusion, and Racial Equity and to report on the effectiveness of their Diversity, Equity and Inclusion efforts. MSIM has reviewed these on a case-by-case basis and has been broadly supportive of these proposals.

With respect to the remaining 19% of proposals that were not supported, MSIM generally supports proposals that if implemented would enhance useful disclosure on employee and board diversity. We support shareholder proposals urging board and employee diversity with respect to gender, race or other factors where we believe the board has failed to take these factors into account.

We may oppose proposals where the expected cost of giving due consideration to the proxy does not justify the potential benefits or if the company has sufficiently addressed requirements of the proposal.

d) Human Rights Proposals

We also support proposals requesting companies to provide disclosure on how they approach human rights risks in their own operations or on their human rights due diligence processes in their supply chains. We believe that human rights violations not only present legal and reputational risks for companies, but they also detract from the value and sustainability of the global economy.

Between 1 July 2021 and 30 June 2022, MSIM supported 71% of proposals to improve human rights disclosure and risk management. MSIM seeks to enhance useful disclosure and improvements on material issues related to human rights risks, labour practices and supply-chain management including the elimination of forced labour and child labour. We review these proposals on a case-by-case basis and have been generally supportive. We have not supported proposals where we believe the company has taken adequate steps to address this concern or the proposal is prescriptive.

CASE STUDY 12.9: FORCED LABOUR

Scenario	A sporting apparel manufacturer owned by one of our Equity teams was named as one of the well-known global brands that allegedly used forced Uyghur labour in its supply chain. Following this, a shareholder proposal was tabled, requesting that the company release a report on its human rights impact of its cotton-sourcing practices.
Voting Outcome	The investment team voted in favour of the shareholder proposal, against management and ISS recommendations. ISS voted against the shareholder proposal as they felt it provided sufficient disclosure related to its human rights policies and sustainable sourcing practices, and it is not lagging its peers in terms of human rights disclosure. The team chose to support the proposal as they believed it was important to apply pressure on a subject that posed a large supply-chain risk and where information was scarce. The team engaged further on the subject with the company, who stated their commitment to not sourcing from Xinjiang and outlined the actions they had taken with their suppliers regarding sourcing. The company shared that they were actively working on tools to verify suppliers' claims on sourcing, adding two senior positions within the firm. This is evidence that the shareholder resolution on the social risks of cotton sourcing—despite not passing—has led to positive changes. The team strongly encouraged the company to look into working with a sustainable cotton charity that offers traceability and a company providing a new technology helping verify the origin of raw materials.

ACTIVE FIXED INCOME – APPROACH TO SEEKING AMENDMENTS IN TERMS AND CONDITIONS, CONTRACTS AND OTHER LEGAL DOCUMENTATION

As highlighted earlier in this section, the Fixed Income team exercises rights and responsibilities through good- stewardship efforts both at the pre-investment stage and throughout our holding of a security. Whilst as bondholders, the team does not regularly vote on governance issues, they frequently use engagement to inform their investment decisions, which ultimately has an impact on issuers.

Prior to investment, Credit Analysts conduct due diligence across a wide range of factors, including on material ESG issues, and may request to engage with an issuer to obtain additional insights. The team draws upon a variety of data sources for ESG-related information pre-investment, including both third-party and proprietary analysis. Engagement is also used as an opportunity to provide granular feedback to issuers on the structure of their deals. The Fixed Income approach in seeking amendments to terms and conditions, contracts, and other legal documentation depends on the issue in question, type of security held, investment strategy and their fiduciary duty to act in clients' best interests. Credit Analysts are trained to review bonds and loans documentation including covenants. The team is planning to conduct additional in-house training, especially for junior members of the team. Furthermore, there is additional training available from rating agencies to law firms and associations, such as the European Leveraged Finance Association (Principle 10), of which MSIM is a member. Our in-house legal expertise also provides support for in-depth analysis where needed, especially in ESG-related areas when evaluating terms for any potential transaction.

The following are examples of different approaches based on different types of income securities:

Green/Labelled Sustainable Bonds – Split of Proceeds Allocations

In the context of green and other labelled sustainable bonds, for example, the team pays particular attention to the split of proceeds allocations between refinancing and financing of new assets, and they advise issuers during their roadshows to maintain a balance between the two, avoiding excessive lookback periods that can compromise the credibility of a green financing programme. For example, the team recently assessed a green bond from a waste processing company, where all of the proceeds had been allocated towards refinancing, with a five-year look-back period. Given this is beyond the three-year best-practice mark, and the company did not aim to publish a separate impact report, the team engaged to request further information on the actual positive impact of the bond, and to recommend the adoption of a forward-looking approach, with a more balanced split of the eligible green projects between re- and new financing.

In some cases, the Fixed Income team will organise a one-to-one call with management, including relevant sustainability directors, to share views and to provide constructive advice on their labelled bond frameworks. The team has also voted on consent solicitations related to the conversion of a company's outstanding debt into green debt. This is becoming an increasingly common practice amongst real estate companies that can leverage large portfolios of certified green buildings to this end. For example, the team assessed a European real estate company's green financing framework at the start of 2022, given the company intended to conduct such green conversion exercise. The eligibility criteria the company was applying for their green buildings category were rigorous, aligned with market best practices in terms of the minimum levels of certifications, or the energy efficiency characteristics. As a result, the team voted in favour of the conversion.

Sustainability-Linked Bonds – Specific Target and Potential Coupon Step-Ups; Call Dates/Prices

In the case of sustainability-linked bonds associated with specific targets and potential coupon step-ups, the team engages with issuers ahead of the transaction through one-to-one meetings or group roadshow calls to provide our views on the appropriateness of the trigger event date and the size of the step-up, and request changes if necessary to increase the level of ambition and accountability, if required. For example, there has been a surge in the number of high-yield bond issuers using the sustainability-linked format, often setting call dates very close to the trigger date of the coupon step-up. In those cases, the team has asked the issuer to ensure the penalty would be reflected in the call price, to avoid creating an incentive to call the bond.

In a recent example, the Fixed Income team engaged with a food and beverage retail company earlier this year, ahead of their inaugural Sustainability-Linked Bond. The company had included three KPIs within their framework, focusing on packaging, food waste and emissions; however, the bond issuance was linked to only two of those, ignoring the emissions reduction target. The team flagged to the company that they would like to see this KPI included within its Sustainability-Linked transactions. They also recommended that the company should include Scope 3 emissions in the target, given that Scope 1 and

2—currently covered by the framework—only represent 3% of the company's total emissions. The team also noted that for the shorter bond tranche, the trigger date for the sustainability penalty would result in the coupon step-up being paid to investors for one year only, which the team saw as non-material. All of these elements weighed negatively on the team's internal evaluation of the bond.

The Fixed Income team has also engaged with multiple high-yield issuers of callable Sustainability-Linked Bonds, to recommend that whenever the step-up trigger date is close to the call date, the penalty should be reflected in the call price as well, to avoid creating an incentive to call the bond.

In addition to this, the Fixed Income Sustainable Investing team has started to collaborate with ELFA's ESG Committee on the development of specific guidelines for leveraged borrowers, expected to be finalised in the course of 2022, which should help address these concerns.

High-Yield – Prospectus Review; Bond Structure/Covenants

In relation to high-yield issuance more broadly, investors tend to receive a prospectus a few days in advance. Each prospectus is reviewed by the Fixed Income research team. Using a combination of in-house expertise (several team members have either investment banking or loan experience) and Xtract Research (legal research available via paid subscription), the team determines whether covenants and/or structure are too aggressive. In cases where the team thinks the documentation is too aggressive, they provide written feedback directly to the syndicate desks involved in marketing the bond deal. If there is significant pushback from the investor base, either the documentation is tightened up or the pricing of the deal makes up for the looseness of the documentation. Loose documentation does not preclude the Fixed Income team from participating in a deal if they believe they are being appropriately compensated on the issuance level. Equally, the team has also chosen to withdraw our interest in deals as a result of loose documentation where no changes were made despite our feedback.

Securitised Products – Loan Collection and Modification Policies, Conditions

In securitised products, the Fixed Income team assesses loan originators and servicers' collection and loan modification policies that are described in the documentation, and the conditions imposed on borrowers. Avoiding predatory lending and promoting responsible lending and servicing practices remains a priority for the team. Over the past year, the Fixed Income team continued to engage with securitisation issuers in the U.S., offering equity-sharing mortgage proposals, whereby if the price of a borrower's home goes up, the investor receives a percentage of the increase. In the event of a home price appreciation, the effective mortgage rate for the homeowner could become very high, triggering aggressive lending issues and potential regulator involvement.

While new variations of "shared appreciation" mortgages have emerged over the past year, the investment team has continued to systematically convey our disapproval of this type of practice to issuers either on calls or in face-to-face meetings, and the team will continue to choose not to invest in these types of products unless remedial action is taken. By doing so, the team aims to influence issuers to alter the terms of their contract to ensure fair lending practices.

APPENDICES

Policy Glossary

Business Continuity Management Programme	The Firm's Resilience organisation maintains global programs for Business Continuity Management (BCM), Disaster Recovery (DR) and Third Party Resilience that facilitate activities designed to protect Morgan Stanley during a business-continuity incident. A business-continuity event is an interruption with potential impact on normal business activity of the Firm's people, operations, technology, suppliers and/or facilities.
Firm Code of Conduct	Our Code of Conduct reflects our continued commitment to act in accordance with our core values and in full alignment with the letter and spirit of applicable laws, regulations and our policies. Our values are as follows, and inform everything we do: Put Clients First, Lead with Exceptional Ideas, Do the Right Thing, Commit to Diversity and Inclusion, and Give Back.
Global Confidential and Material Non-Public Information Policy	The Global Confidential and Material Non-Public Information Policy addresses handling confidential information in a manner that protects Morgan Stanley's reputation for integrity, promotes relationships with our clients, safeguards Firm assets and helps ensure compliance with the complex regulations governing the financial services and banking industry.
Global Conflicts of Interest Policy ("Global Conflicts Policy") and related procedures	The Global Conflicts of Interest Policy addresses business conduct and practices at Morgan Stanley that give rise to an actual or potential conflict of interest. For example, Conflicts can occur when there is a divergence of interests between Morgan Stanley and a client, or among clients. Conflicts can also occur when there is a divergence of interests between an employee on the one hand and the Firm or a client on the other. This Policy sets forth guidance on the identification of Conflicts, and the Firm's conflicts governance framework. Firmwide procedures identify those activities for which each business unit is required to enter either a notification filing, review or conflict clearance request into the Firm's Conflict Management System. These Procedures are designed to allow the Firm to, amongst other things: (i) record details of activities conducted across the Firm that may be relevant to addressing potential conflicts of interest; (ii) resolve expeditiously transactional conflicts that may arise and select the transactional opportunities that present the best apparent long-term franchise building opportunities for the Firm; and (iii) include the appropriate parties across the Firm when evaluating potential conflict issues. Under the Policy, MSIM has established procedures intended to identify and mitigate conflicts of interest related to business activities on a worldwide basis. A conflict management officer for each business unit and/or region acts as a focal point to identify and address potential conflicts of interest in their business area. When appropriate, there is an escalation process to senior management within the business unit, and ultimately, if necessary, to firm management or the firm's franchise committees, for potentially significant conflicts that cannot be resolved by the conflict management officers or that otherwise require senior management review.
Global Employee Trading and Outside Business Activities Policy	The Global Employee Trading, Investing and Outside Business Activities Policy sets forth general rules that employees must follow with respect to personal trading and investing, including transactions in Morgan Stanley securities, and specific rules for particular types of transactions and accounts.

Global Gifts, Entertainment & Charitable Giving Policy	The Global Gifts, Entertainment and Charitable Giving Policy sets forth guidance and limitations with respect to the provision or receipt of gifts and entertainment, as well as the provision of charitable contributions, in connection with business relationships as a Morgan Stanley employee. This Policy addresses gifts, business entertainment (including payment for travel, lodging and meals), charitable contributions, and assumption or forgiveness of debt or any other item of value.
Global Incentive Compensation Discretion ("GICD") Policy	The Global Incentive Compensation Discretion Policy sets forth the terms under which an employee of Morgan Stanley, its subsidiaries and affiliates may be eligible to receive a discretionary incentive compensation award, establishes standards with respect to the process for determining the discretionary incentive compensation to be awarded to an employee and provides guidance for the escalation of a possible clawback of previously awarded incentive compensation.
Global Investment Management Risk Management Policy	Effective risk management is vital to the success of Morgan Stanley and Morgan Stanley Investment Management. Accordingly, the Global IM Risk Management Policy establishes a framework to integrate the diverse roles of the Risk Management functions into a holistic structure and facilitates the incorporation of risk assessment in decision-making processes. This Policy helps members of senior management understand and monitor all significant risk categories on a consistent, proactive basis and defines the roles, responsibilities, guidelines and other elements that formalize the governance framework that is central to risk management and embodies the Firm's risk management culture.
Global Side-by-Side Management Policy and Procedures	When an advisor manages multiple portfolios (side-by-side management) with different structures (e.g., registered funds and unregistered funds) and/or fee structures (e.g., performance-based fees versus flat management fees) certain perceived or actual conflicts may arise. To address these types of conflicts, we have adopted policies and procedures, including the Global Side-By-Side Management Policy and Procedures, pursuant to which allocation decisions may not be influenced by fee arrangements and investment opportunities will be allocated in a manner that we believe to be consistent with obligations as an investment advisor. To further manage these types of conflicts, we have formed a Side-by-Side Management Subcommittee to ensure that side-by-side management guidelines are met.
Global Third Party Risk Management Policy	The Global Third Party Risk Management Policy sets forth the standards and requirements for Morgan Stanley's Third Party Risk Management Program. The Firm manages overall third-party risk within risk tolerance levels established and updated periodically by the Firm. The Program implemented through the Policy is designed to support effective identification, assessment, management and mitigation of risks associated with third-party relationships. The Program requires that outsourcing and sourcing decisions incorporate a risk-based assessment of the associated risks that may impact the Firm.
Global Third Party Selection and Engagement Policy	The Global Third Party Selection and Engagement Policy establishes a framework for Morgan Stanley's sourcing activities from external, unaffiliated third parties for which the Firm's sourcing team is engaged. This Policy is designed to help ensure that the sourcing of goods and services by Morgan Stanley is done in a fair, competitive, independent and objective manner and with appropriate due diligence. Additionally, sourcing decisions must be made in accordance with all applicable laws, regulatory requirements and sound business practices.

Investment Management Public Markets Enhanced Vendor Management Programme Procedures	These procedures describe the Investment Management Public Markets Enhanced Vendor Management Program. The goal of the Enhanced Program is to ensure that service providers that support the Public Markets business are monitored and payments made to the vendors are reviewed by designated personnel.
Investment Private Enhanced Vendor Management Programme Procedures	These procedures describe the Investment Management Private Enhanced Vendor Management Program. The goal of the Enhanced Program is to ensure that service providers that support the Private Markets business are monitored and their payments are reviewed by designated personnel.
Morgan Stanley Diversity and Inclusion Report	The Morgan Stanley Diversity and Inclusion Report can be found in this link here.
Morgan Stanley Environmental and Social Risk Policy	Morgan Stanley's Environmental and Social Policy Statement reflects the firm's global commitment to our stakeholders, communities and the environment to identify and address environmental and social risks. To help us deliver long-term value for our clients and shareholders, we employ comprehensive risk management policies that include environmental and social risk, as laid out in this policy.
Morgan Stanley Europe SE – SFDR disclosures	The SFDR disclosures for Morgan Stanley Europe SE can be found in this link here.
Morgan Stanley Modern Slavery & Human Trafficking Statement	The Morgan Stanley Modern Slavery & Human Trafficking Statement is published in accordance with Section 54 of the United Kingdom's Modern Slavery Act 2015 and Section 16 of Australia's Modern Slavery Act 2018. It outlines the steps taken by Morgan Stanley to address the risk of modern slavery in our own operations or in any of our supply chains, as well as our future plans in that regard. This Statement applies to the global operations and supply chain of Morgan Stanley and our consolidated subsidiaries.
Morgan Stanley SGR S.p.A. Disclosures under Regulation (EU) 2019/2088	The Disclosures under Regulation (EU) 2019/2088 for Morgan Stanley SGR S.p.A. can be found in this link here.
Morgan Stanley Supplier Code of Conduct	We expect our suppliers, and our suppliers' suppliers, to adhere to these key values and apply them to how they do business with Morgan Stanley and in general.
Morgan Stanley U.K. Gender Pay Gap Report	The Morgan Stanley U.K. Gender Pay Gap Report can be found in this link here
Morgan Stanley U.K. Regulated Entities Supplement to the Global Third Party Risk Management Policy	The Morgan Stanley U.K. Regulated Entities Supplement (the "Policy Supplement") to the Global Third Party Risk Management Policy establishes requirements specific to U.K. Regulated Entities. The Policy Supplement is designed to enable U.K. Regulated Entities to manage risks within the Morgan Stanley International Group's Third Party Risk Appetite in compliance with SYSC of the FCA Handbook, the Outsourcing section of the PRA Rulebook, the EBA Guidelines on Outsourcing and other relevant regulations.
MSIM's Counterparty Risk Policy	The Morgan Stanley Investment Management Counterparty Risk Policy sets forth the broad principles that serve as the foundation for managing globally, in a consistent and integrated manner, counterparty risk for all IM businesses. The objective of the Policy is to avoid or mitigate risk of loss arising from the default or inability of a counterparty to meet its financial obligations.

MSIM's Proxy Voting Policy and Procedures ("MSIM Proxy Voting Policy")	Our MSIM Proxy Voting Policy addresses a broad range of issues, and provides general voting parameters on proposals that arise most frequently. We endeavour to integrate governance and proxy voting policy with investment goals, using the vote to encourage portfolio companies to enhance long-term shareholder value and to provide a high standard of transparency such that equity markets can value corporate assets appropriately. The MSIM Proxy Review Committee ("Committee") has responsibility for overseeing the implementation of the MSIM Proxy Voting Policies and Procedures.
Remuneration Policy of MSIM Fund Management (Ireland) Limited	The Remuneration Policy of MSIM Fund Management (Ireland) Limited can be found in this link here.
Sustainable Investing Policy	MSIM's Sustainable Investing Policy outlines our approach to stewardship and sustainable investing. Our sustainable investment beliefs, strategy and culture are collectively guided by the key principles laid out in the policy here.

APPENDICES

Mapping to U.K. Stewardship Code Principles

PRINCIPLE	PAGE	ADDITIONAL KEY DETAILS REFERENCED IN OTHER PRINCIPLES	STARTING PAGE
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.	3	• Purpose guiding our stewardship approach [Principles 7 & 9]	71, 99
		• How MSIM's core values are embedded in the stewardship function and engagement priorities [Principles 2, 5, 6, 7, & 9]	15, 55, 60, 71, 99
		• Approach to Stewardship and Sustainable Investing across asset classes [Principles 7 & 9]	71, 99
		• Approach to clients' interests and stewardship needs [Principle 6]	60
		• Details of EV integration with MSIM [Principles 7 & 10]	71, 131
		• Updates on our active engagement, voting and escalation activities [Principles 9, 11 & 12]	99, 139, 147
		• Our implementation of enhanced ESG governance procedures [Principles 2, 3, 4 & 5]	15, 30, 35, 55
		• Long-standing client relationships [Principle 6]	60
Principle 2: Signatories' governance, resources and incentives support stewardship	15	• Our use of proxy advisors [Principle 8]	94
		• Details of sustainability expertise per investment team [Principle 1]	3
		• Investment team specific examples of sustainability coverage and expertise [Principle 7]	71
		• Activities of the Proxy Review Committee inc. conflict management [Principle 3]	30
		• Our management of sustainability risks [Principle 4]	35
		• Details of our enhanced sustainability oversight and governance process in relation to Promoting Well-Functioning Markets and Review and Assurance [Principles 4 & 5]	35, 55
		• Progress on internal assurance of stewardship [Principles 5, 6, 7, & 10]	55, 60, 71, 131
		• Details of engagement and collaboration efforts to further our commitment to DEI [Principle 10]	131
		• How each investment team incorporates third-party ESG data into their investment process [Principle 7]	71
		• How we monitor our service providers, activities and progress [Principle 8]	94
		• Further information on use of service providers [Principles 7 & 8]	71, 94
		• Details of ESG Amendments to regulatory-related policies [Principle 3]	30
		• Increasing collaboration with external stakeholders [Principle 10]	131
		• Evolving our data & technology capabilities [Principle 8]	94

PRINCIPLE	PAGE	ADDITIONAL KEY DETAILS REFERENCED IN OTHER PRINCIPLES	STARTING PAGE
Principle 3: Signatories manage conflicts of interest to put the best interests of clients and beneficiaries first.	30	–	30
Principle 4: Signatories identify and respond to market-wide and systemic risks to promote a well-functioning financial system.	35	• Details of policy, process governance and resource uplifts to minimise greenwashing and stewardship-washing risks [Principle 2]	15
		• Details of enhancement to our sustainability oversight and governance process [Principle 2]	15
		• Details on active participation in industry bodies and forums and collaboration examples [Principle 10]	131
		• Availability, consistency and comparability of ESG data [Principle 8]	94
		• Details of collaboration and key industry initiatives [Principle 10]	131
		• Details on IAD's review of MSIM's ESG/Sustainability governance and control frameworks, investment activities and commitments [Principles 2 and 5]	15, 55
Principle 5: Signatories review their policies, assure their processes and assess the effectiveness of their activities.	55	• Details of MSIM's Proxy Voting Policy and Procedures [Principle 2]	15
		• Sustainability Organisational Structure [Principle 2]	15
		• Reference to ESG Compliance Test [Principle 2]	15
		• Sustainability Governance and Oversight [Principles 2, 3 & 4]	15, 30, 35
		• Product/Investment Objectives and External Industry Commitments [Principles 2, 4, 6, 7, 9 & 10]	15, 35, 60, 71, 99, 131
		• Details on ESG Data Provider Due Diligence process [Principle 8]	94
		• Holistic Reporting Solutions for MSIM and EV, and Catering to Respective Client Bases [Principle 8]	94
Principle 6: Signatories take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.	60	• Details of data collection and ESG data technology build-out to support our clients' needs [Principle 2]	15
		• MSIM's Portfolio Surveillance team [Principle 2]	15
		• MSIM's thematic engagement priorities [Principle 9]	99
Principle 7: Signatories systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.	71	• MSIM's thematic engagement priorities [Principle 9]	99
		• MSIM's incorporation of client needs and requirements [Principle 6]	60

PRINCIPLE	PAGE	ADDITIONAL KEY DETAILS REFERENCED IN OTHER PRINCIPLES	STARTING PAGE
Principle 8: Signatories monitor and hold to account managers and/or service providers.	94	• Information on vote splitting due to client preference or differing investment team convictions [Principle 3]	30
		• MSIM's Proxy Policy updates [Principles 2 & 5]	15, 55
Principle 9: Signatories engage with issuers to maintain or enhance the value of assets.	99	• Details of our collaborative engagement activities with MSIM [Principle 10]	131
		• International Equity team's escalation approach and case studies [Principle 11]	139
		• Details of Fixed Income's collaborative engagement efforts [Principle 10]	131
Principle 10: Signatories, where necessary, participate in collaborative engagement to influence issuers.	131	–	131
Principle 11: Signatories, where necessary, escalate stewardship activities to influence issuers.	139	–	139
Principle 12: Signatories actively exercise their rights and responsibilities.	147	• Details of MSIM's Proxy Voting Policy, Voting Records and Proxy Review Committee [Principle 2 & 5]	15, 55
		• Details of MSIM's ongoing monitoring and due diligence of proxy advisors [Principle 8]	94

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