Engagement Policy

Environmental and Social Sustainability – Based Negative Screening Criteria

Date: 15th June 2024

BOV
Bank of Valletta

Version Control Data			
Version Number	**Changes**	**Date**	**Approved By**
1.0	**First Version**	**15th June 2024**	**ESG Committee, Risk Committee**

Overview

The amended Shareholders Rights Directive (the "SRD II") aims to promote effective stewardship and long-term shareholder engagement by imposing transparency obligations on institutional investors and asset managers (including entities providing discretionary portfolio management services).

In this regard, as an entity providing discretionary portfolio management services, the Bank, which is considered as an asset manager for all intents and purposes throughout this Policy, has formalised this Engagement Policy in light of the requirements outlined in SRD II in order to generally summarise its engagement activities when it carries out investments in investee companies on behalf of investors. As a result, this document comprises the Bank's Engagement Policy in line with the requirements of SRD II as well as the relevant rules issued by the MFSA.

Background

Shareholders Rights Directive

The regulatory requirement for the Bank to have an Engagement Policy in place emanates from Directive 2007/36/EC, referred to as the Shareholder Rights Directive ("SRD"). In 2017, this was amended by Directive 2017/828/EC ("SRD II"), which included provisions regarding the encouragement of long-term shareholder engagement. This amendment was subsequently transposed into Maltese law by the Malta Financial Services Authority (MFSA) in its Investment Services Rules for Investment Services Providers in June 2019, following industry consultation and subsequent feedback[1]. For the purposes of this Engagement Policy, reference shall be made to SRD II given its wholesale transposition locally.

Aim of SRD II Amendment

The stated aim of SRD II is to strengthen the position of shareholders and to promote a long-term approach to financial and non-financial performance by listed companies as well as tackle underinvestment in activities such as R&D. Thus, SRD II aims to mitigate capital markets' tendency to focus on short-term gains at the expense of holistic medium and long-term performance. It is argued that increased transparency of investment strategies and engagement policies of institutional investors[2] and asset managers[3] can help achieve these aims:

> *"Effective and sustainable shareholder engagement is one of the cornerstones of the corporate governance [...] that can help improve the financial and non-financial performance of companies,* ***including as regards environmental, social and governance factors****, in particular as referred to in the* ***Principles for Responsible Investment, supported by the United Nations****."*

Of note is the explicit relationship between an engagement policy and ESG factors – with the Principles of Responsible Investment (PRI) serving as the conceptual framework connecting the two. Indeed, an engagement policy is viewed as an integral component of sustainable investing, such that the Regulation (EU) 2019/2088 (i.e. the Sustainable Finance Disclosure Regulation or "SFDR") requires that financial market participants summarise their respective engagement policies as part of their sustainability disclosures.

SRDII and Engagement Policy Obligation: Article 3g

SRD II article 3g imposes the obligation on Asset Managers to publicly disclose (on their respective websites), free-of-charge, how shareholder engagement is integrated within their investment strategies. They are expected to describe how investee companies are monitored "on relevant matters" which SRD II states includes:

- Strategy
- Financial performance and risk
- Non-financial performance and risk
- Capital structure
- Social and environmental impact
- Corporate governance

In accordance with SRD II, an engagement policy also ought to specify:

- How the Bank integrates shareholder engagement in its investment strategy.

[1] Feedback Statement to the Consultation Document on Investment Services Rules for Investment Services Providers regarding Encouragement of Long-Term Shareholder Engagement, June 2019.

[2] 2017/828/EC Article 2 (e) defines an institutional investor as an undertaking carrying out activities of life assurance and reinsurance covering life-insurance obligations and institutions for occupational retirement provision.

[3] 2017/828/EC Article 2 (f) defines an asset manager as an investment firm that provides portfolio management services, an AIFM or an authorised investment company (i.e. UCITS).

- How dialogue with investee companies is conducted.
- How voting rights and other rights attached to shares are exercised.
- How they cooperate with other shareholders.
- How they communicate with stakeholders of investee companies.
- How actual and potential conflicts of interest are managed.

Furthermore, Asset Managers are required to furnish, on an annual basis, a general description of past voting behaviour, explaining the most significant votes, how such votes were cast in company general meetings and disclose any use of proxy advisors. Pursuant to the discretion afforded to it under article 3g of SRD II, the Bank may, however, exclude (for the purposes of this annual disclosure obligation) any vote/s which it deems to be insignificant due to the subject matter of the vote/s in question and/or the size of its holding in the relevant investee company, as long as any definition is applied consistently[4].

In determining the relevant materiality threshold for disclosure based on the size of its holdings, the Bank (having considered the extent of its holdings in both local and foreign portfolios) considers 5 per cent (5%) or more of the shares or voting rights in an investee company to constitute a disclosable holding for the purposes of this public disclosure obligation.

Finally, SRD II imposes an obligation to provide a “clear and reasoned” explanation why any entity may choose not to comply with one or more of the requirements.

Principles of Responsible Investment

The Principle for Responsible Investment (PRI) is the “world’s leading proponent of responsible investment” [5]. The PRI acts in the long-term interests of its signatories, the markets and economies within which they operate as well as the environment and broader society. It is an independent entity that is supported by (but not a part of) the United Nations. PRI encourages responsible investment and does not operate for its own profit.

It aims to understand the investment implications of ESG factors and support an international network of signatories to incorporate these factors into investment and ownership decisions. As of writing, the Bank is not a signatory to the PRI.

The PRI has six principles for responsible investment that signatories onboard:

1. Incorporate ESG issues into investment analysis and decision-making processes.
2. Be active owners and incorporate ESG issues into ownership policies and practices.
3. Seek appropriate disclosure on ESG issues by investee companies.
4. Promote acceptance and implementation of PRI within the industry.
5. Cooperate to enhance the effectiveness of PRI implementation.
6. Report activities and progress towards implementing the principles.

Monitoring and Engaging with Investee Companies

The Bank oversees the companies in which it invests to make sure they create long-term value for its investors and stakeholders and act in the interest of shareholders. This supervision involves regular monitoring of various indicators and metrics that not only include economic and/or financial aspects, but also environmental, social and corporate governance elements.

Furthermore, the Bank considers that maintaining a relationship with the companies in which it invests on behalf of its clients, which guarantees that its customers’ interests will be safeguarded, is a very important part of its investment process, essential in the search for the creation of long-term value for its clients’ portfolios.

Use is made of investment research conducted by the Investment Strategy and Research Unit (ISRU) and approved by the Bank’s Research Analysis Committee in monitoring the strategy, financial and non-financial performance, risk, capital structure of securities issued on the local market.

Use is also made of third-party research provided by reputable research houses with respect to international investments in monitoring the strategy, financial and non-financial performance, risk, capital structure of international investments. On the basis of the above, an assertion as to whether the performance of the investee company is satisfactory or subpar is made.

Engagement with investee companies may take place if the latter’s longer-term strategy, financial or nonfinancial performance, capital structure, social and environmental impact or corporate governance is judged as subpar. In the case of concerns surrounding any of these,

[4] 2017/828/EC preamble paragraph 18.

[5] https://www.unpri.org/about-us/what-are-the-principles-for-responsible-investment (accessed 28th November 2023).

such concerns would be addressed with the investee company in a collaborative effort involving the Bank's senior analysts and portfolio managers.

Following engagement with an investee company, and if a company is deemed not to have a viable long-term business strategy or financially sustainable capital structure and/or is unlikely to have such a strategy or capital structure in the future, the Bank in its capacity as asset manager may abstain from further investing in the company or divest of existing clients' holdings.

Exercise of Voting Rights and Other Rights Attached to Shares of Investee Companies

Voting rights and other rights attached to shares will be exercised with a view to promote the long-term financial and non-financial performance of the investee company as well as seeking proper disclosure on ESG issues and/or ESG performance when needed. ESG matters are considered in relation to Principal Adverse Impacts as specified in Annex I of Regulation (EU) 2022/1288 (i.e. the Regulatory Technical Standards supplementing SFDR).

Voting rights with respect to international securities market are only exercised where BOV's holdings, in its capacity as asset manager defined above, exceeds 5%. With regards to investments in the Maltese securities market, as a systematically important financial institution within the Maltese economy, the standard practice is to appoint the Chairman of the company as the proxy in exercising voting rights irrespective of the percentage holdings. Nevertheless, BOV reserves the right to vote directly.

A full voting record, and historical record, can be found on the Bank's website.

Cooperation with Other Shareholders and Communication with Relevant Stakeholders of the Investee Companies

Aiming to create long-term value for the portfolio it manages, the Bank considers that it is very important to act for the improvement of the quality of corporate governance of the companies in which it invests on behalf of its clients; always ensuring that it acts in their best interests. Cooperation with other shareholders of the investee companies and/or communication with stakeholders (such as the Malta Financial Services Authority and the Malta Stock Exchange, for example) is an important part of exerting influence, when necessary, although the feasibility of this form of action is considered on a case-by-case basis.

The Bank also strives to enhance proper corporate governance practices by working with other institutions and joining working groups.

Managing conflicts of interest arising from engagement with investee companies and issuers

As a regulated entity, the Bank is subject to the rules relating to conflicts of interest which require it to identify, prevent, manage or disclose conflicts of interest as well as to establish appropriate criteria for determining the types of conflicts of interest whose existence may damage the interests of its clients. As a result, the Bank maintains a Conflicts of Interest Policy which sets out how it manages actual and potential conflicts of interest arising from or affecting its business activities.

Any conflicts of interest are clearly disclosed during Research and Analysis Committee meetings and minutes accordingly, any conflict of interest is mitigated in line with the Bank's conflict of interest policy.

Furthermore, the Bank implements a number of policies that are designed to limit actual and potential conflict of interest, placing portfolio managers' fiduciary duty above Bank interests. To this end, the Group Regulatory Compliance Policy, Conflicts of Interest Policy, the Code of Ethics Policy, the Code of Conduct Policy and the Market Abuse Policy, work to minimise conflict of interest. For example, a "Chinese Walls" policy (which emanates from Conflicts of Interest Policy and Group Regulatory Compliance Policy) ensures that portfolio managers only have access to any information regarding the Bank's business dealings with an investee company on a need-to-know basis.

Policy review and Annual disclosure

The Policy will be reviewed annually and amended as necessary. The Bank will publish, on an annual basis and free of charge on its website, the application of this Engagement Policy, which will include, inter alia, a general description of its performance in relation to its voting rights, an explanation of the most important votes and specify if any voting advisers were used.