ABERFORTH PARTNERS

Compliance with the UK Stewardship Code

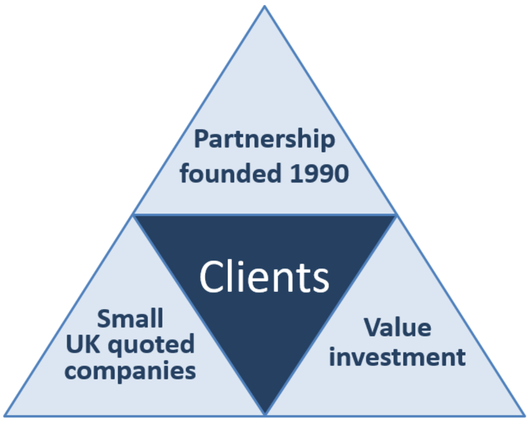
This document describes Aberforth's approach to stewardship and its compliance with the UK Stewardship Code in the reporting period to 31 December 2022. Those looking for more information may contact Sam Ford – the investment partner responsible for co-ordinating stewardship issues – by email at stewardship@aberforth.co.uk or by phone on 0131 220 0733.

Principle 1

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

Context

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



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

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

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

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

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

Clients are at the heart of Aberforth's purpose and culture, but successful stewardship of clients' capital can also be of broader benefit. While small companies have a less significant impact than do their larger peers on the economy, the environment and society, that is not a reason for such issues to be de-emphasised. Aberforth expects investee companies and their boards to consider ESG risks and opportunities in their operational and strategic decision-making.

Except when requested by clients, Aberforth does not exclude investments from portfolios on the basis of ESG considerations alone. There is evidence that investment returns can be enhanced by investment in and engagement with companies that face ESG challenges and are already seeking to address them or can be encouraged to do so.

Activity

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

Outcome

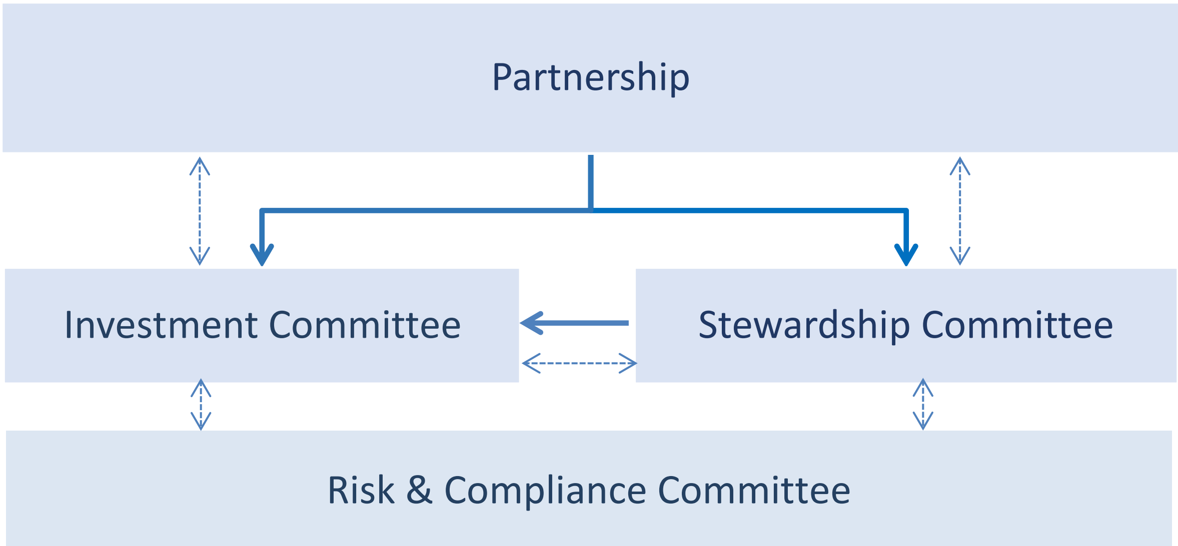
Influenced by the value investment philosophy and a belief that individual directors can have greater effect on the fortunes of a small company, stewardship permeates Aberforth's investment process and culture. This is demonstrated by data provided in the responses to Principles 9, 10, 11 and 12. Aberforth's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

An assessment of Aberforth's effectiveness in serving its clients and beneficiaries may be conducted with reference to the firm's purpose of delivering superior long-term investment returns. The longest standing client – Aberforth Smaller Companies Trust plc – launched on 10 December 1990. From then until 31 December 2022, it had produced a compound annual NAV total return of 11.9%*. This exceeded the 9.6%* return from small UK quoted companies, as measured by the NSCI (XIC). Part of the superior return was attributable to the value investment philosophy, as value stocks outperformed the index as a whole*. Over the same period, the total return of larger UK companies, as measured by the FTSE All-Share Index, was 8.1%*. This size premium therefore supports Aberforth's focus on small UK quoted companies.

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

Principle 2

Signatories' governance, resource and incentives support stewardship.



Activity

The organisational structure and processes that support stewardship within Aberforth are inextricably linked. Stewardship starts with the partnership model itself, which places the client at the centre of Aberforth's business, as described in Principle 1. The commitment to stewardship is demonstrated in the leadership by a partner, Sam Ford, for all stewardship activities. He chairs the Stewardship Committee, on which he is supported by three others including the partner responsible for operations and the Head of Sustainability and Investor Relations (S&IR). The latter role was created in 2022 in response to the need for additional resource linked to investor requests about sustainability and to ensure that the firm is well prepared for evolving ESG regulations. Having the operations partner as a member provides an additional, diverse perspective, independent from the investment function. As described below, day-to-day stewardship decisions are taken by the investment managers. These decisions are made within a framework set by the Stewardship Committee, which reports to the partnership.

Among its peers of investment houses addressing small UK quoted companies, Aberforth has a relatively large team of experienced investment professionals. At 31 December 2022, the team comprised six members, with average industry experience of 20 years. The investment managers have a deep understanding of the sectors and companies they cover. This means that the boards of investee companies, who have a single point of contact at Aberforth, can be more receptive to stewardship engagement. The firm therefore believes that its investment process lends itself well to an integrated approach of stewardship: stewardship decisions are taken by the investment manager responsible for individual investments with input from other members of the investment management team. Further detail on Aberforth's investment philosophy and process can be found HERE. In implementing its stewardship policies, Aberforth's principal investment is in its investment management team, who conduct their own research, analysis and engagement. The firm recruits experienced individuals, whose diversity of knowledge and experience accumulated elsewhere can contribute to the refinement of its processes. Further training and support are provided to investment managers who wish to strengthen their knowledge of stewardship principles and practices.

To support its investment and stewardship activities, Aberforth has invested in and developed bespoke internal IT systems. A series of proprietary data applications, linked to a SQL database (the Aberforth proprietary database), are tailored to the firm's approach and are integral to its investment process.

To complement these systems, Aberforth takes data and analysis from third-party providers. These include relationships with a proxy voting adviser and a supplier of carbon data. The former is long standing and subject to annual effectiveness review. The relationship with the carbon data provider has been useful in corroborating emissions data and has been extended. Experience with third party providers of ESG analysis has remained disappointing to date. The firm has found that the coverage and quality of data relevant to small UK quoted companies remain inconsistent and incomplete.

The structure and ethos of the partnership mean that separate reward structures to incentivise stewardship are not necessary. Aberforth's model is for all its investment managers, and therefore all those with responsibility for enacting stewardship policy, to become partners in the firm. Investment managers are rewarded on the basis of the firm's overall performance, rather than being tied to the investment results of individual sectors or funds. This aligns Aberforth's activities with clients' interests. All operational staff have a specific ESG performance objective as part of their remuneration assessment.

Outcome

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

Although existing governance structures are established and working, there are ways in which its processes, particularly regarding environmental and social considerations, can be enhanced. Several improvements have recently been or are currently being implemented.

- The Stewardship Group was formalised to become a Stewardship Committee during the year. Whilst the role of stewardship has always been a vital element of the firm's investment philosophy, this elevated its role in Aberforth's system of governance. This is expected to aid the integration of ESG considerations into the firm's stewardship and the investment philosophy.
- Aberforth enhanced the ESG module that forms part of its proprietary database. This improved the ESG framework for determining the effect of ESG risks and opportunities on investee companies' valuations. As a result of these improvements, Aberforth is now collecting more ESG datapoints in standardised formats, which should offer richer insights as the series build over time.
- The project to link the ESG framework to the recording of engagements within the proprietary database was completed. The main benefit is a more integrated view of a company's ESG credentials, engagement activities and voting record. The results contributed to the examples detailed in Principles 9, 10 and 11.
- Aberforth invested in training and resources to enhance knowledge and expertise in stewardship. In 2022, staff attended industry led training events and seminars related to ESG. One member of the stewardship committee has completed the certificate in ESG investing, issued by the CFA Institute.
- The Head of S&IR initiated a quarterly ESG review session with the investment managers to improve knowledge and understanding on evolving ESG matters.
- The firm began a Diversity, Equity and Inclusion (DE&I) initiative that utilises the Action, Challenge and Transparency (ACT) framework. ACT is a corporate culture standard for investment firms and aims to foster an inclusive, equitable and sustainable investment management industry. This was supported by training provided by Diversity Scotland who delivered a bespoke and interactive training day for all partners and staff.
- The firm progressed its climate related disclosure plans, which are aligned with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). This saw the firm quantify its carbon emissions, supported by environmental consultants.

Principle 3

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

Context

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

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

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

Activity

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

- In buying and selling shares, the firm only ever deals as agent on behalf of its clients and never as principal on its own account.
- The firm's bespoke order management system is designed to deliver fair allocation of aggregated orders between multiple clients. This is subjected to regular compliance monitoring.
- The firm has controls in place to ensure that mandate restrictions directed by clients are known by investment managers and are reflected in systems.
- The firm's policy on gifts and hospitality prohibits the giving or accepting of gifts that may give rise to a conflict of duties owed to clients or the firm and may otherwise only be accepted where the gift or hospitality is modest and infrequent.
- Aberforth encourages long-term savings and investment by partners and employees. Personal dealings in investments are generally permitted, subject to compliance with the personal dealing policy. That policy requires all personal dealing to be approved by a partner and generally prohibits investment in any company that is a constituent of the investment universe.

- Private wealth managers, on behalf of their clients, are significant investors in the collective funds managed by Aberforth. Some of these wealth managers are constituents of the investment universe and the firm can invest its clients' funds in them. On such occasions, the investment decisions are taken transparently in a manner consistent with clients' mandates and Aberforth's purpose and investment philosophy, as described in Principle 1.
- Clients' interests are represented directly with the investment managers through the independent boards of the investment trusts, the independent non-executive directors of the unit trust management company (on behalf of the unit trust) and directly by client representatives on behalf of the segregated charity clients.
- Aberforth's partners are not permitted to take board positions at investee companies or to sit on the boards of two investment trusts that the firm manages.
- A conflict may arise should a director of an investment trust managed by Aberforth be invited to join, or already be a member of, the board of a company in which the firm's clients invest. How this situation is addressed is described in one of the examples below as an outcome.

Outcome

Examples of the management of conflicts in practice are noted below.

Example: client board conflict

Directors of the boards of the two investment trusts managed by Aberforth may be sought as potential board members of other organisations. This risks potential and/or actual conflicts with the stewardship of clients' capital. When this occurs, it is addressed through consultation and consideration by the director in question, the board's chair and Aberforth. In 2022, a director highlighted the risk of a conflict in interest to the investment trust company board and to Aberforth. The director was also on the board of a investee company that was subject to a potential takeover. The situation was thoroughly assessed and it was concluded that there was no direct conflict of interest. It was also determined that any potential indirect conflicts arising could be managed and mitigated through transparent disclosures and the establishment of safeguards regarding the discussion of the company in question. Historically, there have been instances where the conflict has been considered unacceptable. In one example, an investment trust director was invited to become a director of a company where clients of Aberforth had a significant interest. The risk of a conflict could not be mitigated to an acceptable level and so the director withdrew their candidacy.

Example: client engagement

Aberforth takes time to ensure that its corporate philosophy HERE and investment approach HERE are understood when building and maintaining client relationships. During this process, Aberforth seeks to understand clients' stewardship principles and requests. Consistent with this approach, the firm discussed with one client its specific stewardship requirements after the client introduced a 2050 deadline for its investment portfolio to achieve net zero. With a good understanding of these requirements, Aberforth provided additional feedback on how a value investment philosophy could be compatible with these goals. The feedback from the client was supportive and an inaugural environmental report was produced.

Principle 4

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

Activity

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

Aberforth's partners and employees participate in industry forums, both to help identify risks and, if relevant, to influence how the risks are addressed. Such action is undertaken with the aim of improving how financial markets, usually the market in small UK quoted companies, function. During 2022, Aberforth participated in meetings, interactions or forums with the Bank of England, CFA UK, The Investment Association, the Association of Investment Companies (AIC), the Financial Reporting Council, the UNPRI and the Financial Conduct Authority. The objectives of engagement with these forums are: (i) identification of industry issues, such as stewardship regulation and regulatory change; (ii) engagement on stewardship and ESG matters, particularly around application to smaller businesses and in the listed small cap sector; and (iii) economic and market conditions, including regulatory responses.

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

The proliferation of climate change regulation and recommendations from governments and other official bodies may itself be a market-wide risk. Any resulting confusion may complicate and delay the implementation of climate change policies by companies, particularly smaller companies with less resource available. This general risk may be a source of individual investment opportunities in companies that are slow but willing to comply. The regular engagement embodied in Aberforth's stewardship model can help identify such companies and help them on their journey.

Example

The UK government's mini-budget in September caused a sharp decline in gilt prices. In the aftermath, the Bank of England (BoE) determined that the risks to financial stability were such that it embarked on a new programme of liquidity support for the UK's financial markets.

In its November monetary policy report, the BoE shared a gloomier economic outlook, which was affected by the lingering impact of the mini-budget. Their high profile forecasts suggested that the UK was set for the longest recession since records began in the 1920s. In its regular engagement with the BoE's Scotland Agents, Aberforth explored usefulness of these growth forecasts in more detail. The concern was that the BoE's outlook could ultimately undermine the confidence of consumers and businesses in the UK's economy and its financial markets. The BoE acknowledged the point and explained that their scenario was for a prolonged but relatively shallow recession.

Outcome

Aberforth's approach to investment, which is based on fundamental analysis, puts it in a good position to identify and assess systemic and market-wide risks. These risks have been considered through the investment process and have, in some cases, led to adjustments to target valuations of investee companies and changes to holdings.

While acknowledging its small size in the asset management industry, Aberforth will continue to engage with other stakeholders on systemic and market-wide risks where such action seems likely to improve the investment outcomes of its clients or, consistent with Principle Five of the FCA's Principles for Businesses, the functioning of the financial system.

Principle 5

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

Activity

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

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

An additional level of external assurance is provided by the boards of the collective funds managed by Aberforth. The firm presents its stewardship report, together with voting records, to these boards annually. The boards review and challenge the reports, as well as providing an additional check on whether they are fair, balanced and understandable. Summarised updates to stewardship policies and practices are set out in disclosures in the Annual Report and Financial Statements of Aberforth's collective funds. These are approved by the boards and subject to review by external auditors. Aberforth's other clients benefit indirectly from this scrutiny.

Outcome

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

- The stewardship policy is structured around the UK Stewardship Code 2020. It is reviewed and updated annually for relevant examples, current activity and outcomes.

- The Stewardship Committee, which is tasked with the oversight of policies and their implementation by the investment managers, has evolved from a group to a formal committee and strengthened role of stewardship within the firm's system of governance. Membership of the committee has expanded to include the Head of S&IR, a newly created role that contributes additional expertise on stewardship and ESG matters.

- As set out in Principle 2, Aberforth's ESG framework is now integrated with the engagement module in the proprietary database. These enhancements have aided consistency of investee company evaluations, which influence the assessment of value. An additional benefit is that all engagement activities are recorded and are aligned to the firm's ESG framework methodology and voting practices.
- A further benefit of these IT systems and process improvements is improved reporting. The building of comparable ESG datasets and historical data series assists in providing stewardship activity summaries to clients as well as in preparing for future ESG-related regulation.
- Members of the Stewardship Committee participate in industry forums, hosted by the Investment Association, the Financial Reporting Council, UN PRI and a variety of professional service firms. Such activities are useful in assessing the effectiveness of Aberforth's policies and practices.
- Aberforth commissioned a sustainability consultant to assist in measuring the firm's own environmental impact and strategy for energy transition. Improvements to the firm's voluntary reporting under the Streamlined Energy and Carbon Reporting framework were made. These included the quantification of Scope 3 greenhouse gas emissions in addition to Scope 1 and 2. This will inform the firm's carbon reduction plan and provides a benchmark report for comparability.
- As described in Principle 2, Aberforth began a DE&I initiative in 2022. The initiative aligns to the ACT framework, which upholds a standard of corporate culture for investment companies.

Principle 6

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

Context

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

Aberforth's intended clients are institutional or wholesale entities that seek to give their own clients exposure to small UK quoted companies. Aberforth's assets under management are invested entirely in small UK quoted companies. These are companies with a market capitalisation, at the time of purchase, equal to or lower than that of the largest company in the bottom 10% of the main UK equity market or companies in the Numis Smaller Companies Index (excluding investment companies). At 31 December 2022, the firm managed four funds: three collectives and one segregated fund for a charity. All four funds are managed in a similar way in keeping with the value investment philosophy, though client specific variations allow classification into sub-strategies: **Standard Value**, **Value and Income** and **Standard Value with Client Restrictions**.

- **Standard Value:** Aberforth Smaller Companies Trust plc (ASCoT) has been a client since its inception in 1990. It is an investment trust listed on the London Stock Exchange, with assets of £1,332m* at 31 December 2022. Its underlying investors are overwhelmingly institutional, primarily private wealth managers. Retail investors, including execution-only platforms or non-discretionary stockbrokers but excluding current partners of Aberforth, represent circa 14%* of the fund. Non-UK investors represent circa 15%* of the fund.

- **Standard Value:** Aberforth UK Small Companies Fund (AFund) has been a client since its inception in 1991. It is an authorised unit trust scheme, with assets of £144m* at 31 December 2022. Its underlying investors are overwhelmingly institutional, primarily private wealth managers. Retail investors, including execution-only platforms or non-discretionary stockbrokers but excluding current partners of Aberforth, represent circa 8%* of the fund. Non-UK investors represent circa 1%* of the fund.

- **Value and Income:** Aberforth Split Level Income Trust plc (ASLIT) has been a client since its inception in 2017. It is a split capital investment trust listed on the London Stock Exchange, with assets of £210m* at 31 December 2022. Its underlying investors are overwhelmingly institutional. Retail investors, including execution-only platforms or non-discretionary stockbrokers but excluding current partners of Aberforth, represent circa 14%* of the fund. Non-UK investors represent circa 10%* of the Ordinary Shares. This fund has a limited life, with a planned winding-up date of 30 June 2024.

- **Standard Value with Client Restrictions:** Charity A is a segregated fund managed by Aberforth for one of the UK's largest charities. A client since 2002, assets at 31 December 2022 were £251m*.

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

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

Activity

The three collective funds – ASCoT, ASLIT and AFund – are overseen by boards of directors, who receive detailed quarterly reports and attend board meetings with representatives of Aberforth present. These meetings give the directors the opportunity to scrutinise the firm's chosen approach, its stewardship activities (including a record of significant votes), its stewardship code and investment horizons. Additionally, Aberforth's investment managers meet the funds' largest investors twice a year to explain performance against investment objectives and to set out factors relevant to the investment strategy. Engagement activity with investee companies is addressed, as long as it does not breach confidentiality. During the most recent round of visits in November 2022, the firm conducted 133 meetings with investors, whose combined holdings represented a majority of ASCoT, ASLIT and AFund. This biannual exercise is an opportunity for investors to give feedback and for the investment managers to understand investors' requirements. Appetite for Aberforth's investment offering is formally tested every three years when ASCoT's Annual General Meeting (AGM) contains an ordinary resolution for continuation, with the last occurrence being the March 2020 meeting. Subsequent to this reporting period, ASCoT's shareholders approved a resolution to continue the Company at the AGM in March 2023. Shareholders are kept informed through annual and interim reports, monthly fact sheets and research produced by Kepler Partners.

The charity fund receives quarterly reports and meets representatives of Aberforth regularly throughout the year. Further, an inaugural ESG report shared a bottom-up evaluation of investee companies' specific ESG strategies and disclosures, together with details of related engagement. The report was completed after the period end and further details will be provided in Aberforth's 2023 stewardship policy. The relationship with the charity, including investment policy, is covered by an investment management agreement. The client does not operate an exclusions list. It is, though, concerned about exposure to fossil fuels and has recently committed to a net zero strategy for its wider investment portfolio by 2050 at the latest. In addition to consulting the client before proceeding with a potentially sensitive investment, Aberforth is engaged with the client to support its journey towards a carbon neutral portfolio.

All relevant reports and disclosures made to clients are reviewed by the Stewardship Committee. At least two members of the group attend all fund board meetings to present progress, consider feedback and understand the client position and needs. Aberforth supported all funds in enhancing their approach on stewardship matters in 2022. Consultation with investors is undertaken each year following publication of the funds' annual report and financial statements. The feedback from investors is shared with the boards routinely during board meetings. Additionally, the chair of both investment trust boards writes to the top twenty shareholders offering a meeting and requesting feedback.

Outcome

Aberforth's approach to taking account of the needs of clients and beneficiaries is founded upon regular reporting, contact and dialogue with the clients and underlying investors in the collective funds. This monitoring is undertaken proactively by the investment managers, through twice yearly shareholder visits, and by the board chairs, through annual meetings and feedback. Given the diverse underlying ownership of the collective vehicles, there is inevitably a range of views on investment strategy and stewardship. The boards of the collective vehicles scrutinise Aberforth's stewardship policy and monitor adherence. In the case of the segregated charity fund, regular consultation with its investment committee has led to potential investments not being made. Over the past year Aberforth has followed its stewardship and investment policies for all its investments and clients.

Principle 7

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

Context

Aberforth's investment process encompasses all issues that its investment managers judge to be relevant to a company's valuation. An investee company's journey through the process – from pre-purchase analysis to final exit – is determined by the interplay between Aberforth's valuation of the company and the price attributed to it by the stockmarket. Any environmental, social or governance (ESG) issue could, therefore, be of importance, particularly as the increased profile of ESG has brought greater distortions to stockmarket valuations.

ESG analysis is integrated into Aberforth's investment process alongside all other matters relevant to a company's valuation. Aberforth's approach is rooted in the view that a company's system of governance is crucial to how all risks and opportunities – ESG and otherwise – are identified and managed. If their governance is effective, companies will be well-positioned to manage the increasing number of environmental and social issues.

Aberforth's contention is that the perception of ESG deficiencies can create valuation opportunities, as the stockmarket often under-estimates the ability of small companies to take effective remedial action. Aberforth further contends that valuation discounts related to ESG issues can be challenged through a programme of active engagement to encourage the issues to be addressed. Aberforth is well positioned in this regard: engagement has always been a fully integrated component of the investment process. It is achievable because of the firm's commitment to a high level of dedicated and experienced investment management resource.

Philosophy, policies and practices

The Managers' approach to Stewardship and ESG is available on the Aberforth website in the "About Aberforth" section. The policy framework is set out in the following documents, which are managed by the Stewardship Committee.

- *About Aberforth*: the background and founding principles of the firm, its core strategic philosophy and nature of the business.
- *Investment Philosophy*: the investment manager's approach to investing as adopted for Aberforth's clients.
- *Stewardship Policy*: Aberforth's approach to the stewardship of its clients' capital.
- *ESG Framework*: the methodology underpinning Aberforth's integration of ESG into the assessment of company value.
- *Engagement and Voting Framework*: how Aberforth engages and votes, along with what is expected of investee companies.

- *Examples of Engagement and Voting*: examples of how the Engagement and Voting framework is put into action, included as part of this response.
- *Governance and Corporate Responsibility*: Aberforth Partners LLP's approach to Stewardship, which is reported annually.

Activity

Integration of stewardship and investment is straightforward, facilitated by Aberforth's ownership structure, client engagement and portfolio management approach. As described under Principle 2, all investment managers are normally also partners of the firm. This ensures that the importance placed by the firm on issues such as ESG flows directly into company analysis, engagement and the management of clients' portfolios.

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

Moreover, engagement with clients is also undertaken by the investment managers. This assists in the effective implementation of clients' objectives, time horizons and instructions into the investment process. This degree of integration is possible because of Aberforth's small size, the experience of its investment managers and its relatively flat hierarchy.

In 2022, enhancements were made to the ESG module that forms part of the firm's proprietary database. This followed regular evaluation of third-party service provider offerings. On each occasion, the review concluded that a bespoke internal system would provide more complete and comparable data on small UK quoted companies. The ESG module that forms the basis of this system makes use of an enhanced methodology to assess the ESG attributes of investee companies.

Risk and opportunities are considered in the context of 12 environmental, social and governance sub factors that are detailed in the table below.

Factors	Environmental	Social	Governance
Subfactors	Climate change	Employee culture	Board composition and succession
	Pressure on natural resources	Health and safety	Effectiveness
	Pollution and waste	External stakeholders	Remuneration and alignment
		Product liability and consumer protection	Capital allocation
			Ethics

The analysis is updated annually for all investee companies, which allows insights to be formed on companies' strategies related to ESG risks and opportunities. Two years of data and resulting analysis have so far been recorded. This was supported by an ESG survey conducted across Aberforth's investee companies during 2021, which was supplemented by direct engagement with investee companies in 2022. The findings are influential in directing engagement priorities, particularly when stockmarket valuations are thought to be affected.

The engagement module that forms part of Aberforth's database was also upgraded in 2022. It was enhanced to record all engagements taking place through e-mail and ad hoc phone calls. Any course of active engagement is now also logged against an objective set at the outset. This objective is ascribed to the relevant ESG subfactor any collaboration with other shareholders is recorded. Completed engagements capture the extent to which the original objective was met.

Integration of stewardship into the investment process, including the risk component of the ESG framework, is subject to an annual review by the Stewardship Committee, whose role is set out more fully under Principle 2. The first annual review occurred in the fourth quarter of 2022.

The ESG and stewardship initiatives outlined above were helped by the appointment last year of the Head of S&IR to support sustainability matters.

Outcome

Aberforth has a long record of frequent and in-depth engagement with investee company boards, which, together with its voting commitment, demonstrates the importance of stewardship to the investment process.

Given the frequency of engagement, stewardship considerations affect the overwhelming majority of investment decisions, from new purchases to exit decisions. These investment decisions are always taken in the interests of long-term value for clients and investors, though, as described above, benefits to the economy, environment and society are also considered. The examples below pertain to engagement on environmental and social issues with existing holdings in 2022. Engagement examples where governance issues are the major focus are featured in the responses to Principles 9, 10 and 11.

Example: EnQuest [Environmental, Social, Governance – monitoring]

EnQuest, an operator of mature oil and gas fields in the UK North Sea, was the subject of several engagements in 2022 covering environmental, social and governance issues.

- We continued our engagement on policies and targets related to emissions reduction. A 15% reduction in absolute Scope 1 and 2 emissions was achieved in 2021 through a cut to flaring and the usage of diesel on platforms. As a result of falling production and 'green' operational improvements, emissions have fallen by c.43% since 2018. This is close to the UK Government's 50% reduction target by 2030, outlined in the North Sea Transition Deal. We have encouraged EnQuest to go further by providing detail on the reduction in carbon emissions that have been shown on operated assets relative to incumbent operators. The engagement continues.
- A second stream of engagement related to the interests of external stakeholders. Refinancing risks resurfaced amid signs that creditors were reining back support for fossil fuel companies. Risks were compounded by creditors' angst on possible scope changes to the UK government's energy profit levy, which targeted recouping super-normal profits among oil and gas production companies. We engaged on the looming refinancing and learned that creditors were also expected to consider the group's plans for carbon capture in depleted oil fields and the associated capabilities in decommissioning. The group's debt facilities were subsequently refinanced successfully later in the year.
- A final stream of engagement concerned governance. High oil prices meant good progress was made on debt reduction in 2021 and 2022. Considering high interest costs and risks to the fiscal regime overseeing North Sea operations, we have engaged to advocate for further debt paydown before commencing dividend payments. This has been acknowledged by the company whose capital allocation priorities are centred on debt paydown.

Example: Energean [Social, Governance – decision to purchase, monitoring]

The company is a producer of natural gas with its major asset located offshore in Israel. Ahead of production commencing, our engagement sought to understand why there was no Israeli representation on the main board. This reflected concerns that the major external stakeholder was the Israeli government and that the nascency of the country's gas industry meant the board would benefit from an Israeli national with experience in domestic governance. The company acknowledged the benefits such an appointment might bring, though have yet to make changes to the composition of its board.

Example: Reach [Social - monitoring]

Our engagement priority in 2022 focused on liabilities related to other external stakeholders, specifically the pension scheme. We engaged to understand why the company had not been able to agree funding schedules linked to 2019 triennial valuation for the group's pension schemes. Following a programme of significant deficit recovery payments, the company is on track to close the funding deficit by 2027. If these payments are increased yet further, we believe they risk compromising the health of the business, which would have negative connotations for wider stakeholders. Whilst negotiations progressed through the year, intervention by the UK Pensions Regulator was required. At the end of the year, one of the group's six pension schemes has yet to achieve a funding resolution. Our engagement on this topic will continue into 2023.

Example: Centamin [Environmental – monitoring]

As a gold miner in the Egyptian desert, the company's high carbon emissions are predominantly related to a reliance on diesel generators for power. We engaged with the company to understand how solar power could be used to improve environmental credentials and lower operating costs. Late in the year, the company successfully commissioned its 36MW solar farm and 7.5MW battery-energy storage system, spread over 85 hectares. This is expected to reduce diesel consumption by up to 70,000 litres per day or 22m litres per annum and promises a payback on investment of roughly three years. However, as the solar plant only represents c.25% of Centamin's annual power needs, a further project is under way to connect the mine to Egyptian grid power via a 24km power line. With Egyptian grid power generated from natural gas, hydro, solar and wind, Centamin's diesel consumption and emissions will significantly reduce over time, which should be evident in disclosures over the coming years.

Example: Helical [Environmental – decision to purchase, monitoring]

In the wake of the pandemic, there was widespread concern about the effects of working from home on office valuations. The share prices of property investment companies specialising in offices suffered. Through engagement with Helical, it became clear that its approach to the London office market could offset these demand concerns. The company's strategy focuses on the provision of sustainable and high quality office space that is designed to meet high environmental ratings, while providing wellbeing benefits to those using the buildings. So far, the evidence is that this emphasis on sustainability is being rewarded with higher rents in the form of a "green premium", which has yet to be reflected in the stockmarket's valuation of the company. With the logic for Helical's approach established, engagement is now turning to how the board can best access capital to take advantage of the opportunity.

Example: Vesuvius [Environmental – monitoring]

Vesuvius is a fascinating test case for how an industrial manufacturer can manage both the challenges and opportunities of climate change. The company's board has responded thoughtfully to regulation, notably including a carbon cost within the overall cost of capital used to assess investments. In 2022, engagement started to emphasise the competitive advantage that might accrue to a manufacturer able to help its steel manufacturing customers reduce their emissions. We encouraged management to consider quantifying what might be thought of as "Scope 4" benefits. Disclosure of such information should help highlight Vesuvius's strengths and, as others respond, could contribute to an overall reduction in emissions.

Example: Speedy Hire [Environmental - monitoring]

As a provider of tools and equipment to the construction, infrastructure and industrial markets, most of Speedy Hire's carbon emissions are related to fuel consumption by its fleet. Our engagement has focused on emissions reduction targets and confirmed that management recognise climate change as one of its biggest challenges. Decarbonisation efforts are planned through the use of alternative sustainable fuels and low carbon technologies. For larger fleets, diesel has already been replaced with hydrotreated vegetable oil, which is made from renewable materials such as fat, waste vegetables and other oils, and generates up to 90% less greenhouse gases.

We are encouraged that management are incentivised on climate performance metrics, which are built into variable remuneration. In time, it is possible that the company's sustainability credentials generate incremental demand for the fleet. Customers seeking to achieve their own sustainability goals would benefit from a fleet hire with lower emissions.

Example: Robert Walters [Social – monitoring]

Specialist recruitment consultancy Robert Walters operates in a highly competitive sector, relying on the retention of talented individuals possessing the necessary skills to grow the business. We engaged to understand how retention would be affected by the backdrop of a tight labour market and soaring salaries. The company characterised the environment as a "war for talent", but we were reassured by the company's culturally entrenched approach to remuneration. It is underpinned by a policy of linking bonuses to the profitability of discrete operating units, which has resulted in above average retention of higher performing employees. Engagement revealed other elements of the strategy to improve staff retention, including investments in career opportunity resources and training in management skills. The engagement stream also reassured us that there is a comprehensive approach to succession planning in place across all levels in the group.

Principle 8

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

Context

Aberforth has few third-party service providers in the area of stewardship and has instead chosen to conduct most of these activities internally and directly. The firm has a long-standing relationship with a proxy voting adviser and has also contracted with a provider of carbon data since 2020 following a review of various environmental data vendors.

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

Activity

Relationships with external data provider relationships are subject to formal annual review but in practice are assessed continually throughout the year based on the timeliness and quality of their individual reports.

To date, the proxy voting service has been satisfactory. Further information on Aberforth's voting policy can be found HERE.

The contract with the carbon data provider has been renewed for 2023. The report is informative and has been particularly useful for understanding the broad carbon characteristics of the portfolio versus the benchmark.

Other third-party providers of ESG information and data are kept under periodic review and may prove useful in the future to improve the firm's sustainability analysis and disclosures.

Outcome

While Aberforth employs the services of a proxy voting adviser, investment managers are under no obligation to follow its recommendations and on many occasions take a different view. The response to Principle 12 shows examples where this was the case in 2022. It is also the case that interaction with companies on issues raised by the proxy adviser can lead to a change in the investment manager's original voting decision.

As in previous years, the review of external ESG data providers has contributed to Aberforth's view that the measurement and evaluation of relevant factors cannot reliably be outsourced to a third-party. This is because of the lack of consistent methodology and inadequate coverage of the small UK quoted companies amongst the data providers. As a result, Aberforth enhanced its proprietary database by updating its ESG module, which makes use of a revised methodology for the evaluation of ESG risks and opportunities. Population of the ESG module is informed by engagement with companies and by investee companies' annual reports and sustainability reports. Assurance on the quality of emissions data is provided through a comparison with externally sourced carbon data.

Principles 9, 10 and 11

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

Signatories, where necessary, participate in collaborative engagement.

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

Context

Aberforth's policy on engagement can be found on its website in the Stewardship & ESG section. Responses to Principles 9, 10 and 11 have been combined to avoid repetition and to reflect the related nature of the three components.

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

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

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

Activity

Aberforth's clients in aggregate often hold significant stakes in investee companies. The investment managers tend, therefore, to have good access to executive and non-executive directors. The preference is for face-to-face meetings, particularly when addressing sensitive topics. Meetings at the firm's Edinburgh office makes it easier for several members of the investment management team to participate. In practice, much of Aberforth's engagement is conducted through video calls, conventional phone calls and e-mail. Logging of this sort of *ad hoc* engagement was improved in 2022 through enhancements to the engagement module of Aberforth's proprietary database.

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

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

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

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

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

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

Outcome

Meetings with board members of investee companies are an important element of Aberforth's investment process. Each year, there are several meetings with each holding. Over the course of 2022, Aberforth conducted 398 executive level meetings and 137 non-executive meetings with companies. These numbers compare with 380 and 116 respectively during 2021. There were several factors that contributed to a busier year of engagement.

- It was a year of significant macro-economic events. The war in Ukraine precipitated a round of engagement to confirm the direct and indirect exposure of investee companies. At the portfolio level, the overall exposure was limited. Any material exposure has since been exited or disposed of by the affected investee companies.
- Later in the year, the Chancellor's mini budget brought systemic pressure on the gilt market. This had material implications for large pension schemes through their exposure to Liability Driven Investment strategies. Aberforth engaged with investee companies with large defined benefit pension schemes. Several of those schemes were affected but all were able to meet required collateral calls without the need for support from the sponsor company.

- It was another busy year for M&A activity as overseas acquirers took advantage of the depressed pound and attractive valuations among small UK quoted companies. Aberforth regularly asks that chairs consult about incoming M&A interest well before announcement of a formal takeover offer. If this does not happen, there is a risk that Aberforth's valuation aspirations are not met, in which case the firm would not support the offer. Additionally, timely consultation can enable Aberforth to support a board in rejecting an opportunistic and under-valued approach.
- As described in Principle 7, Aberforth enhanced the ESG module that forms part of its proprietary database in 2022. This exercise prompted several specific engagements, some of which are detailed in the response to Principle 7.

The examples below show the breadth of engagement issues covered in 2022. All engagement streams were conducted with the common purpose of value enhancement, which can also manifest itself through the protection of value that Aberforth ascribes to its investee companies. Engagements more focused on environmental and social issues are shared in the response to Principle 7.

Example: Senior

In recent years, our engagement with this aerospace engineer has focused on portfolio composition. Efforts to develop the profitable fluid conveyance business have been overshadowed by the commoditisation of the structures business, which machines parts for aircraft. We supported a disposal process for structures, though it had to be postponed after the onset of the pandemic. In 2022, the discussion moved on to the topic of when the process should recommence. Supply chain woes meant that production rates of civil aircraft remained in the early stages of recovery. It therefore made sense not to rush a disposal but to wait for more supportive end markets.

A second topic of engagement relates to remuneration. Specifically, we challenged the board to set stretching hurdles for financial metrics that corroborate the board's view on the value of the company. This followed the rejection of a possible offer from private equity in 2021. Both streams of engagement continue.

Example: FirstGroup

FirstGroup is a transport company and has been a longstanding holding of Aberforth's clients. The investment has been challenging but the outlook is much improved following the disposal of its US school bus assets in 2021. The resulting group is simplified and, although disposal proceeds were returned through a tender offer, the balance sheet is stronger. In 2022, our engagement focused on the corporate value of the business. This was necessary after a takeover approach from a US private equity firm. Ultimately, the board agreed with our view that the valuation was inadequate and the approach was rejected. We remain confident that FirstGroup's strategy of maximising returns from the UK operations and returning excess capital through progressive dividends and buybacks should generate a more favourable outcome for long term owners.

Example: TI Fluid Systems

While supply chain problems were the main influence on TI Fluid System's share price in 2022, two longer term engagement streams continued through the year. The first concerns governance and is a legacy of the company's previous ownership by Bain private equity, which retains a 37% stake and has two representatives on the board. Our engagement has focused on executive remuneration, which is high for a listed UK business but not unreasonable for an American PE owned company. As always, it is important to take into account competition for talent – particularly from private equity – but there have been encouraging changes under the new chair.

The second engagement stream is on the environmental front. As a supplier to the automotive industry, the company is involved in the transition to battery electric vehicles. Our enquiries were initially aimed at the continued relevance of its products – steel and nylon tubes. Satisfied that there is a good demand opportunity, we have turned our attention to the profit profile of the transition, as profitable programmes run down and as the profitability of new programmes for electric vehicles takes time to ramp up.

Example: Videndum

The company owns a portfolio of profitable businesses serving photographers, independent content creators and broadcasters. The main thrust of engagement over several years has been capital allocation. Consistently strong cash flow has given the board the ability to acquire other businesses, with efforts in recent years focused on relatively high tech assets within the Creative Solutions division. We have been interested in the risk that accompanies the growth opportunities for this division and have supported the board in considering opportunities to realise value. Concurrently, we have engaged on remuneration, with the board seeking flexibility amid retention concerns, particularly for employees and management within Creative Solutions. Engagement on both capital allocation and remuneration continues.

Example: RPS

RPS has been a long-standing investment for clients of Aberforth. The initial investment was made in 2009 in the aftermath of the financial crisis. The subsequent recovery was handicapped by the collapse in the oil price between 2014 and 2016, which decimated profits in the energy division. This precipitated the appointment of a new chair, Ken Lever, whom we knew from his previous executive and non executive roles. A period of investment followed, during which our regular engagement with the board reassured us that the investment case was on track. So, through engagement with chair about a series of opportunistic takeover bids in 2019 and 2021 at valuations below relevant industry transaction multiples, we supported RPS's continued independence and allowed the board to cite Aberforth in their rejection letters.

We kept an open channel with the board through the pandemic period and supported a placing in September 2020 to restore strength in the balance sheet. In early 2022, we became insiders after being consulted by the chair about a third M&A approach. Aberforth clients' significant 17% stake supported the Board's position and eventually a sixth bid of 206p was secured with the help of an irrevocable undertaking. The terms of the irrevocable included flexibility in the eventuality of a counter-offer, which we believed to be likely. A counter-offer came and in September 2022, we agreed to an irrevocable at 222p with a 10% collar. Our engagement and clients' significant stake in the equity were instrumental in delivering a good outcome for shareholders. RPS's board deserves credit for their exemplary engagement and consultation under the chair.

Example: Morgan Advanced Materials

Aberforth's clients have been long-standing shareholders in this manufacturer of carbon and ceramic products. Our most recent course of engagement began in the wake of the pandemic after the dividend was rebased. Strong operational progress through the challenging economic backdrop positioned the company to maintain its dividend record and a reset policy felt like a missed opportunity. Ultimately, the board acknowledged our points, but the dividend policy stood.

In 2022, we continued the engagement through the broader lens of capital allocation. We wanted to understand the board's ambitions towards inorganic growth and resolving the pension deficit. The company has not undertaken any significant M&A for a prolonged period. We therefore sought reassurances that the executive team had the required skills and experience to deploy capital in a way that would enhance value for shareholders. While the company has yet to undertake any M&A transactions, pension deficit has been de-risked through a buy-in and a cash injection by the company.

Example: Eurocell

Eurocell is a manufacturer, distributer, and recycler of PVC profile for the UK's window, door and building industries. Following an IPO in 2015, a record of strong sales growth has not been matched by profits. While the business is well placed to succeed within its industry, a sharper focus on execution of a refreshed business plan was required. With most of the non-executive directors due to leave as they approached nine years of service, we engaged extensively about the appointment of a new chair and the need for succession planning more broadly. We became insiders on the final shortlist after consultation with the senior independent director. The board's preferred candidate was an individual with whom we have worked successfully with before. We therefore supported the appointment.

Example: TT Electronics

Split into three divisions, TT Electronics manufactures and assembles electrical components for use in broad industrial markets. In more recent years, a course of self-help including disposals and acquisitions has placed the Power & Connectivity division at the core of the strategy to unlock faster growth and achieve a 10% operating margin. However, since the pandemic, the stronger trading performances have been in the Sensors and Global Manufacturing Solutions divisions.

In our engagement with the company, we have sought to understand the synergies between the three divisions. This exercise has made clear that the Sensors division has limited overlap with the rest of the business. This has not affected its performance and it has the highest margin profile and sales growth rate in the group. Consequently, our engagement in 2022 moved on to exploring the value that a sale of the Sensors division might unlock for shareholders. The engagement continues.

Collective engagement

Working with other shareholders can be an important option in Aberforth's approach to stewardship with its investee companies. In 2022, there were 25 examples of collective engagement involving dialogue with other institutional investors related to 19 investee companies. Topics of engagement were capital allocation priorities, alternative options for companies subject to a proposed takeover, board succession, remuneration, and broader strategic issues. Some of these engagements are sensitive in nature and disclosure at this time would be counterproductive to the objectives.

Example: XPS Pensions

Aberforth was consulted on the process to appoint a new chair in what was a cycle of routine succession planning. Having followed due process and completed a search, the board's preferred candidate was an existing non-executive director, who was also and the finance director of another investee company, the recruitment consultant Robert Walters. Whilst it is common for executives to broaden their experience with a single non-executive role, it is most unusual that this extends to the role of chair.

Although we had no concerns about the ability of the individual, we expressed concern about time commitments: executive board roles require an individual's full effort and attention.

In light of the circumstances, we engaged with another large shareholder. This shareholder communicated a similar view to the board after their own consultation. XPS was satisfied that the new chair has the capacity to take on a chair role as his executive responsibilities are supported by a deep management team in his finance department. Finally, we engaged directly with the new chair to express our concerns. The engagement continues.

Example: Jupiter Fund Management

During the year, Aberforth was approached by another shareholder who was concerned about the effectiveness of the board. This followed a period of significant redemptions from Jupiter's funds and a large acquisition. We had already begun to engage about these issues after the unexpected departure of the CEO. As part of this, we suggested improving the breadth of experience on the board, which we felt could benefit from industrial and operational experience. This view was informed by historical investments in financial services companies where such skills have been additive. No changes to the composition of the board have been made yet. Engagement with the chair, and with the other shareholder, continues.

Example: Go-Ahead

Go-Ahead, an operator of bus and rail assets, announced conditional takeover approaches in June from two parties. Shortly thereafter, the board announced a recommended takeover from a consortium at a value of 1450p in cash and a special dividend of 50p per share. Our assessment was that the valuation fell considerably short of fair value, a path to which could have been realised through the revamped strategy that had been announced only months before. Further, we were frustrated that the board did not consult, and instead presented the acquisition as a *fait accompli*.

In response, we outlined our opposition to the takeover through engagement with the chair and senior independent director. We also contacted several major shareholders to share our thoughts and ultimate opposition to the proposal on the basis of its existing terms. Despite these efforts, we failed to garner enough support to vote the transaction down. At the court meeting to approve the transaction, 78.6% of shareholders voted in favour, compared with the 75% approval threshold required. The takeover proceeded and it was of small consolation that the consortium raised the offer price through a 50p increase to the special dividend.

Principle 12

Signatories actively exercise their rights and responsibilities.

Context

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

- The investment managers engage with the boards of investee companies in order to understand strategy and governance and, if necessary, to effect change. The ability to engage is improved by Aberforth's willingness to take meaningful stakes in investee companies on behalf of its clients. On most occasions, issues of board structure, dividend policy, remuneration and share issuance permissions will have been discussed, and potentially changed, before these issues are put to shareholders for approval at a General Meeting.
- Voting is a fundamental right for shareholders and is an important means by which Aberforth exercises stewardship on behalf of its clients. The firm's policy is to vote on every resolution put to shareholders at a General Meeting. Aberforth voted on all items at all general meetings over the past year, in line with its policy. Because of the depth and frequency of engagement with the boards of investee companies, Aberforth will have had the opportunity to influence important issues before they are put to shareholders at a general meeting. This results in fewer votes against the board or abstentions than might otherwise be expected.
- The third method is to sell a holding – a basic concept but one that sets listed equities apart from some other asset classes. When an investee company encounters operational difficulties, Aberforth typically engages to understand if a change of strategy or of personnel on the board might plausibly contribute towards an improvement in the company's prospects. If that does not appear forthcoming, Aberforth will typically exercise its right to sell the holding.

Aberforth manages four client funds, as described under Principle 6. Three of the funds follow the firm's voting policy, with the firm exercising the voting rights. The segregated charity account retains its own voting rights and, while it receives voting advice from Aberforth, may choose to override Aberforth's policy. Aberforth's three collective funds do not engage in stock lending. The segregated charity fund may do so.

Research from Aberforth's proxy adviser, ISS, is considered, but the firm does not automatically follow ISS's recommendations. Aberforth takes a pragmatic, rather than a prescriptive one-size-fits-all approach, which has proven beneficial over time. This acknowledges the heterogeneous nature of the universe of small UK quoted companies and the proportionately greater governance burden on the typical small company.

Further information on Aberforth's engagement and voting framework can be found HERE.

Activity

Votes were cast on all resolutions in respect of all shares held under Aberforth's voting control. No voting decisions were taken by another entity on behalf of these shares. Shareholdings and voting rights are monitored through in-house fund accounting systems and ISS, which are reconciled with custodians' records.

	For	Against	Abstain
Aberforth Partners	1,511	3	15
ISS Voting Guidance	1,492	31	6
Aberforth Partners	98.8%	0.2%	1.0%
ISS Voting Guidance	97.6%	2.0%	0.4%

The above table summarises Aberforth's voting statistics during 2022 and compares them with ISS voting guidance. Of the 1,529 resolutions voted, Aberforth was for 1,511, against 3 and abstained on 15. Consistent with the explanation above, Aberforth's lower proportion of votes against or abstentions compared to ISS' guidance reflects the regular dialogue with investee companies. This often results in Aberforth being consulted on major issues and being able to influence them before they are put to a vote. In 2022, Aberforth voted at 105 meetings, 86 of which were general and 19 special, for 88 portfolio companies.

Outcome

Votes AGAINST or ABSTAIN are purposeful and planned. Aberforth views voting against as an important tool when engagement is unable to facilitate change, while abstain votes can be a useful signal in on-going engagements. Intentions to vote either against or abstain are usually communicated to the boards ahead of time. Notable examples of votes against and abstentions are provided below.

Example: McBride

ABSTAINED on the re-election of Igor Kuzniar, a non-executive director representative of Teleios Capital Partners

Our withheld vote reflected concerns that shareholders who become board members may have an agenda that, under specific circumstances, could prove detrimental to our clients' interests. This action was consistent with a withheld instruction in previous years. The decision was taken despite reassuring engagement with the chair, who understands the board's responsibilities to all shareholders. We were therefore reassured that appropriate processes are in place to manage the risks, which are also mitigated by the clear majority of non-executives on the board being independent.

The32esolutiion was passed with 99.8% of votes FOR

Example: SIG

ABSTAINED on the re-election of two shareholder representative non-executive directors

Private equity company Clayton Dubilier & Rice (CDR) became a c.28% shareholder in SIG following the equity issue in 2020. The accompanying shareholder agreement granted two board seats to CDR, which were up for re-election. Though Aberforth's clients' interests are aligned with CDR's in the present recovery phase, this may not always be the case and CDR's board positions could prove detrimental to clients' interests in certain circumstances. Our decision to withhold our vote against the reappointment of CDR's directors followed reassuring engagement with the chair who is alive to the risks and ensured a majority of non-executives on the board are independent.

The33esolutionns passed 99.4% and 83.4% of votes FOR

Example: Card Factory

ABSTAINED on the re-election of Nathan Lane, a non-executive director

The appointment of Nathan Lane as a non-executive director in 2020 followed discussions between the board and Teleios Capital Partners, c.20% shareholders in the company. Whilst the individual was not a nominated director of Teleios, the board's judgement is that he was not independent. We are cognisant of the risks that, under certain circumstances, this director could bring influence that is not in our clients' best interests. Meanwhile, our engagement with the chair has demonstrated that the board has considered these risks carefully, hence the non-independent designation. However, the board also believes the individual brings relevant skills and experience that have already proved valuable to the company.

The resolution passed with 100% of votes FOR

Example: TI Fluid Systems

ABSTAINED on the remuneration policy

The high variable element of the remuneration package has been a concern and engagement topic for several years. With the recent appointments of a new chair and CEO, change to remuneration has been forthcoming. Notably, the combined upside multiplier of the long- and short-term variable awards has been reduced from seven times to six times. This encouraged a change in Aberforth's vote from against in previous years to abstention.

The resolution passed with 98.2% of votes FOR

ABSTAINED on the re-election of two shareholder representative non-executive directors

Votes were also withheld on the re-election of two non-independent non-executive directors. These are representatives of Bain, the private equity firm that owned the company before IPO and that retains a 37% stake. The risks of such a stake to other shareholders were highlighted in 2020, when, at the last minute, Bain withdrew their support for a dividend to be paid by the company in respect of 2019. Abstention, rather than a vote against, was appropriate in view of the circumstances of the second quarter of 2020, when uncertainty about the pandemic was at its most intense.

The resolutions passed with 80.4% and 100% of votes FOR

Whilst voting FOR a resolution does not usually merit explanation, there are circumstances in which such votes are significant. The examples below demonstrate the importance of combining voting decisions with proactive engagement.

Example: Senior

Voted FOR the approval of the remuneration report

Following the board's rejection of a possible offer for the company in 2021, we engaged with the chair and the head of the remuneration committee. Our contention was that the board should ensure incentive hurdles were compatible with the board's view of the value of the company. Upon release of the annual report, we were concerned that this was not the case. The board outlined that it was concerned at the potential loss of important senior managers within Senior's business units. Although engagement on this topic continues, pragmatism was exercised and Aberforth voted in favour of the remuneration report.

The resolution passed with 91.1% of votes FOR.

Example: Hyve

Voted FOR the approval of the remuneration report

In 2021, Aberforth was consulted on a plan to introduce a value creation plan (VCP) at Hyve, an events company. Such plans are controversial in the wake of historical uncapped pay outs that involve the issuance of new shares to management teams. In this case, the board felt the plan was required to retain and motivate the senior management team. Through our engagement, we were able to increase the hurdle annual rate of the return above which the share price must increase before a capped pay out would occur. As a result we voted FOR the remuneration policy, which passed with 75% of votes supporting the proposal.

Another significant vote followed in 2022. After the onset of the Ukraine war in 2022, Hyve moved quickly to exit its Russian operations. This crystallised a significant loss of earnings. In response, we were consulted on a lower hurdle rate for the VCP. Our support for this arrangement was evidenced in vote FOR the approval of the remuneration report.

The resolution passed with 91.6% of votes in favour.

Example: Company A

Voted FOR the re-election of the chair

Our engagement with the chair highlighted dysfunctional board relationships and differing views on strategy. After a period of challenging engagement, we met with the senior independent director to transmit our loss of confidence in the chair. This involved asking for confirmation that the chair announced plans to step down at the AGM. To improve the chance of the objective being achieved, pragmatically we signalled our readiness to vote in favour of the individual’s notional re-appointment. Prior to the AGM, the chair signalled their departure and accordingly we voted FOR their re-election.

Example: Topps Tiles

Voted FOR all resolutions at the AGM

Amid a broader review of the company’s capital allocation priorities, Aberforth engaged with the executives and chair to elevate the profile of the ordinary dividend and highlight the importance of capital allocation discipline. During 2022, the company revealed an updated capital allocation policy, which acknowledged the importance of progressive dividends. This was reflected in resilient financial results, where the full year dividend was raised 16% year on year to 3.6p.

The resolutions all passed.

Example: De La Rue

Voted FOR Kevin Loosemore, the chair, to continue serving as a director of the company

A general meeting was convened at which the company put to shareholders whether the chair, Kevin Loosemore, should remain in post. This move was in anticipation of the likely requisition of an EGM by another shareholder who sought to remove the chair. It was our judgement that the chair deserved more time owing to macro-economic headwinds hampering a recovery in the group's currency printing division. We remain actively engaged with De La Rue's board.

The resolution passed with 82.9% of votes FOR.

Votes different from proxy adviser recommendation

During 2022 there were 43 resolutions on which Aberforth voted differently from ISS's recommendations. Examples are set out below.

Example: National World

Voted FOR the re-election of David Montgomery, executive chair – proxy advisor recommended ABSTAIN

Aberforth agrees that in most situations, governance is enhanced by the separation of the roles of chair and the CEO. However, there are circumstances where we are prepared to support the appointment of an executive chair. These exceptions typically involve companies undertaking heavy restructuring plan, where there is reliance on the performance record of specific individuals. This was the case for National World, which is embarking on a strategy of consolidation among legacy printing assets under its executive chair, David Montgomery. Despite the reservations of the proxy advisor, Aberforth voted FOR the re-appointment of David Montgomery.

The resolution passed with 100% of votes FOR.

Example: Card Factory

Voted FOR the approval of the remuneration report – proxy adviser recommended AGAINST

In light of the company's receipt of Covid-19 government support, the proxy adviser raised a general concern over payment of bonuses and appropriateness of the metrics. Nevertheless, Aberforth's clients voted in favour of the remuneration report. The justification for the payment was that it was made against the background of excellent financial performance, significantly exceeding the stretch target. Notably, the remuneration committee exercised downward discretion by disregarding the benefit of government support in assessing whether the targets had been achieved. Therefore, a vote in favour was warranted.

The resolution passed with 83.3% of votes FOR

Example: Castings

Voted FOR the remuneration policy – proxy adviser was AGAINST

The proxy adviser's recommendation was due to a discretionary bonus of £32,000 paid in addition to the £21,000 earned in line with the remuneration policy. Our decision to vote in favour was motivated by the unusual culture of the company, which has contributed to its strong and persistent record of profitability in a competitive industry. One notable aspect of the culture is that remuneration is much lower than the average for companies of its size. The CEO's basic salary last year was £298,000 and there was no long-term incentive available until the introduction of a nil cost option scheme in 2020. We are particularly conscious of the risk of losing executives to competitors and so were comfortable with the discretion exercised by the remuneration committee.

The 37esolutionn passed with 85.0% of votes FOR

Example: CMC Markets

Voted FOR the re-election of the nominations committee – proxy adviser was AGAINST

The proxy adviser recommended a vote against the re-election of the Chair of the Nomination Committee, on the basis that less than 33% of the board currently consists of women. As a result, the composition of the board falls short of the recommendation to the Hampton Alexander Review. We were satisfied that the board's policy considered diversity in its broader sense and that this should result in increased female representation on the board over time. Steps have already been taken to address this as evidenced by women representing 50% of the independent non-executive directors.

The resolution passed with 93.7% of votes FOR.

Example: International Personal Finance

Voted FOR the approval of the remuneration report - proxy adviser was AGAINST

The proxy adviser recommended a vote against the approval of the remuneration report on the basis that the departing CFO was treated as a good leaver. This entitled the individual to receive an annual bonus and retain existing LTIP awards. Aberforth was satisfied with the company's detailed response, which referenced legal entitlements under the terms of his service agreement.

The resolution passed with 77.8% of votes FOR

Example: S&U

Voted FOR all resolutions – proxy advisor was AGAINST the remuneration report, remuneration policy and certain directors.

The proxy advisor recommended a vote against the approval of the remuneration report and policy, and against the re-election of the executive chair and all non-executive directors. Regarding votes related to board composition, the issues were the lack of gender diversity, the structure of sub-committees and the chair's executive responsibilities. We were satisfied that the board considered diversity in its broadest sense and that the board's experience is relevant given the nature of the business.

Moving to the remuneration report, the proxy advisor's view was that the disclosures of LTIP and bonus performance targets were insufficient. Our engagement with the company concluded that this stance was acceptable given the commercial sensitivity of divisional PBT targets. Furthermore, total compensation figures for executives are in line with peers' and are backed up by significant personal shareholdings in the company.

The resolutions passed with c.93% of votes FOR.

Example: Hostelworld

Voted FOR the remuneration policy – proxy adviser was AGAINST

The proxy adviser raised concern over the introduction of Hostelworld's 2022 Restricted Share Award, which proposed to reduce vesting hurdles for the previously awarded LTIP and to remove post-cessation shareholding requirements. Our engagement with the chair concluded that concern over management retention was justified. Ensuring the executive management is adequately incentivised was important in the context of the company's turnaround plans, which had been challenged by the pandemic. Consequently, pragmatism was exercised.

The resolution passed with 80.2% of votes FOR

Example: Capital

Voted FOR the remuneration report – proxy adviser was AGAINST

The proxy adviser raised a concern over plans to award an annual bonus equivalent to 150% of the maximum opportunity. In doing so, the board exercised a discretionary clause in the policy, recognising the strong operational progress made by the company, which saw stretching financial targets comfortably exceeded. Indeed, Capital has grown its mine site drilling fleet and associated profits significantly since changes to the remuneration policy were made previously in 2018. We concluded that the strong operational performance was compatible with the board's view on remuneration.

Voted FOR the re-election of Jamie Boyton, executive chair – proxy adviser was ABSTAIN

Aberforth agrees that in most situations, governance is enhanced by the separation of the roles of chair and the CEO. However, there are circumstances where we are prepared to support the appointment of executive chairs. In the case of Capital, our clients' longstanding interest in the company has meant we have had frequent exposure to Jamie Boyton. This process has given us confidence in his abilities and relevant experience, which is backed up by a strong performance record for shareholders. We are also assured by the executive chair's significant personal holding in the company.

A step towards best practice occurred later in October when a CEO was appointed with Jamie Boyton continuing in his role as executive chair.

The resolutions passed with votes FOR of 81.6% and 97.4% respectively.

Aberforth Partners LLP
14 Melville Street
Edinburgh
EH3 7NS

April 2023