

ANNUAL REVIEW 2018

2018

17 Sustainable Development Goals:

- 1. No poverty
- 2. Zero hunger
- 3. Good health and well-being
- 4. Quality education
- 5. Gender equality
- 6. Clean water and sanitation
- 7. Affordable and clean energy
- 8. Decent work and economic growth
- 9. Industry, innovation and infrastructure
- 10. Reduced inequalities
- 11. Sustainable cities and communities
- 12. Responsible consumption and production
- 13. Climate action
- 14. Life below water
- 15. Life on land
- 16. Peace, justice and strong institutions
- 17. Partnerships for the goals



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Executive summary

The Sustainable Future (SF) fund range was launched in February 2001 with the primary aim of delivering strong returns to our clients by investing in sustainable companies. We have a strong track record of doing so across the 'very interesting' times of the last 18 years.

We focus on finding companies that are making our world cleaner, healthier and safer. This means we spend much of our time analysing problems across the globe from climate change, through labour conditions in supply chains to the rise of so-called lifestyle diseases. Day to day, this can lead to a mindset that all these challenges are intractable, so we think it is a good idea to step back periodically and look at just what has been achieved, even in the lifetime of the SF funds.

There has been real progress in many areas and my highlights are:

- Cleaner world: Air quality in cities across the world has improved. In New York, where air quality is cleaner than since monitoring began, and in London, SOx and NOx and particulates are a fraction of their levels in 2000. Even in Beijing, regulation is helping to bring back blue skies *.
- Healthier world: Perhaps the best indicator of progress here is in child mortality – deaths of children under the age of five. In China, there has been a four-fold reduction, and even in the UK with its already low rate this has fallen by 40% **.
- Safer world: It is widely known that road deaths in the UK have halved since 2000; what is less commented on is the improvement in the workplace where accident rates have also halved. Put another way, 400,000 accidents were avoided last year because of improvements in health and safety at work ***.

These are a few examples of powerful improving trends we should celebrate: in general, our world has got much, much better in the last 18 years. Many of these improvements have been achieved with the help of ingenious, efficient businesses whose profits have grown in line with demand for their solutions.

Clearly, there are still major challenges facing our societies – from climate change to inequality, from biodiversity loss to water scarcity – but we should draw strength from the successes of the past to have optimism that we will find solutions to these too. Where these solutions are provided by companies, we will invest in them as

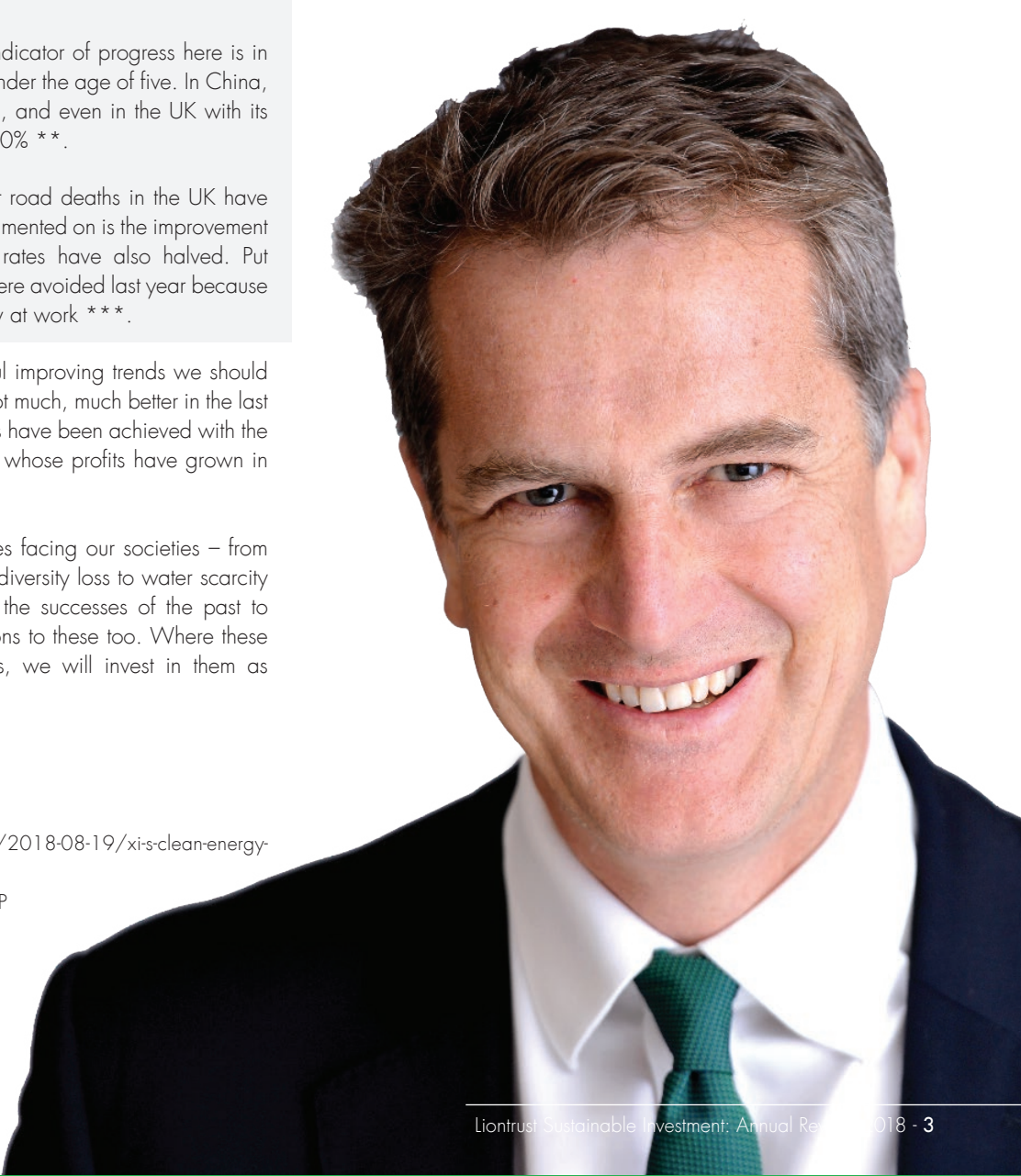
Sources: *bloomberg.com/news/articles/2018-08-19/xi-s-clean-energy-drive-paints-bluest-sky-over-beijing-in-decade
** Gapminder.org, UNIGME and UNWPP
*** hse.gov.uk/statistics

part of our primary aim of striving to deliver strong returns through identifying and backing sustainable businesses.

This report showcases the key themes we invest behind and highlights the positive impact aligned companies have on our world. We also summarise our engagement work – improving the companies we own and promoting sustainable, responsible finance more broadly. Finally, we look beyond 2019 to explain what the future holds for Sustainable Investment.

Peter Michaelis, Head of Sustainable Investment at Liontrust

For more information on Sustainable Investment plus our funds and team, go to www.liontrust.co.uk/sustainable





HOW WE INVEST: OUR SUSTAINABLE VISION

Improving sanitation and access to clean water – Improving financial resilience – Improving industrial waste treatment and recycling – Improving industry

Identifying emerging trends and long-term themes is the cornerstone of our investment process. From the development of personalised medicine to the transition to lower carbon fossil fuels, we are fascinated by the wide-ranging trends that are changing the world and the opportunities they create. Thirty years ago, the IBM PC XT was the pinnacle of technology for example; today, we have the iPhone, which is not only much more powerful but can also fit into your pocket and is half a million times more energy efficient.

We can also point to advances in healthcare that have led to dramatic improvements in life expectancy. For instance, if a man was diagnosed with prostate cancer 30 years ago, he had a less than 50% chance of living more than five years; today the odds are around 90%.

Why is this relevant to investors? Many of these outcomes have been delivered by the power of capitalism and the creativity of businesses generating strong profit growth and investment returns. It is these innovative businesses in which our SF funds have invested for close to two decades, and we feel most investors underestimate the speed, scale and persistency of such trends within our economy.

Therefore, we look at the world through the prism of three mega trends—Better resource efficiency, Improved health and Greater safety and resilience—and 20 underlying themes within these trends.

Well-run companies whose products and operations capitalise on transformative changes can benefit financially. In short, we believe that identifying these powerful themes and investing in the equities and bonds of exposed companies can make for attractive and sustainable investments.

While themes are at the heart of our investment idea generation, there are three further criteria all potential holdings have to satisfy:

- **Broader sustainability of the company:** While a company might have significant exposure to a theme, we also have to check how sustainable the rest of its activities are. We use our Sustainability Matrix to assess a company's overall product mix and operations with respect to sustainability and environmental, social and governance (ESG) performance.
- **Business fundamentals:** Using a set checklist, we assess a company's ability to generate high returns on equity. This includes analysis of the competitive dynamics facing the business and the resilience of its advantages versus competitors. We also meet with management to understand their strategy for the business and how they think about capital allocation.
- **Financial modelling and valuation assessment:** This information is used to construct financial models detailing the revenue, margin and earnings progression the company is likely to deliver over

Past performance is not a guide to future performance, investments can result in total loss of capital. Please refer to the Key Risks section for more information.

the next five years. Applying the relevant valuation multiple to these allows us to derive a price target achievable in the next three years. When this shows significant upside, the investment is recommended as a buy and available to be included in our funds. Every recommendation is presented to and challenged by the Sustainable Investment team at our weekly Friday meetings.

Our team scours the globe for the best investments exhibiting these qualities. We then construct resilient portfolios of these companies with the aim of delivering strong returns while minimising volatility.

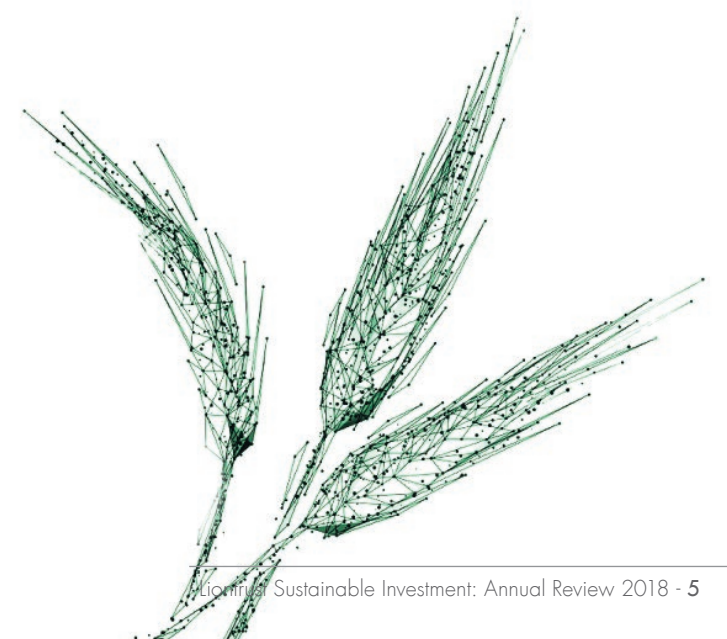
Sustainability is an increasingly important theme for today's consumers, with companies expected to adopt more socially responsible behaviour, and investors, with a growing proportion keen for their financial assets to have a positive impact on the wider world.

We feel most investors underestimate the speed, scale and persistency of such trends within our economy.

As ever, with popularity comes proliferation, and we continue to see more and more asset managers launching funds for this market and promoting their ESG credentials. We can point to a track record of more than 18 years of sustainable investing, and we have a 13-strong team investing in equities and bonds.

Among our key differentiators is the fact that all the sustainable elements are integrated within a single team. We do not have separate fund management and ESG divisions, for example; instead, every team member is responsible for all aspects of financial and ESG relating to an investment decision. Because of this approach, our team engages with companies across a broad range of issues relating to stages in our process, including screening criteria, sustainable investment themes and company-specific ESG issues.

We also have a five-strong external Advisory Committee to provide another layer of expertise in key areas of social and environmental impact. The members of the Advisory Committee are featured on page 30.



Performance of our funds

	Peer Groups	Quartile Rankings to 31.12.18				
		1 Year	3 Years	5 Years	7 Years	10 Years
Liontrust Sustainable Future UK Growth	IA UK All Companies	①	①	①	①	①
Liontrust Sustainable Future Global Growth	IA Global Equities	①	①	①	①	②
Liontrust Sustainable Future Managed	IA Mixed 40% - 85% Equities	①	①	①	①	①
Liontrust Sustainable Future European Growth	IA Europe ex UK	③	③	③	②	③
Liontrust Sustainable Future Corporate Bond	IA Sterling Corporate Bond	③	①	②	②	②
Liontrust UK Ethical	IA UK All Companies	①	①	①	①	①
Liontrust Monthly Income Bond	IA Sterling Corporate Bond	④	①	②	①	-
Liontrust Sustainable Future Cautious Managed	IA Mixed 40% - 85% Equities	①	①	-	-	-
Liontrust Sustainable Future Defensive Managed	IA Mixed 20% - 60% Equities	①	①	-	-	-
Liontrust Sustainable Future Absolute Growth	IA Flexible Investments	①	①	①	①	①
Liontrust GF SF Pan-European Growth Fund*^	FE Offshore regulated peer group	④	④	④	②	③

Source: Financial Express, as at 31.12.18, total return (net of fees, income/interest reinvested), primary share class, in GBP. Quartiles correct as at 03.03.19.
 * In Euros. ^The Luxcellence – Liontrust SF Pan-European Equity Fund, which had launched on 14 March 2001, merged into the Liontrust GF Sustainable Future Pan-European Growth Fund, which launched on 19 October 2018. Primary share class, total return (net of fees, interest/income reinvested). Discrete data is not available for five full 12 month periods for Sustainable Future Cautious Managed Fund and Sustainable Future Defensive Managed Fund due to the launch date of the portfolio.

Discrete performance (%)

	12 months ending				
	Dec-18	Dec-17	Dec-16	Dec-15	Dec-14
Liontrust Sustainable Future UK Growth	-6.7	20.7	8.0	9.8	1.9
MSCI UK	-8.8	11.7	19.2	-2.2	0.5
IA UK All Companies	-11.2	14.0	10.8	4.9	0.6
Liontrust Sustainable Future Global Growth	1.3	18.8	17.3	6.5	7.7
MSCI World	-3.0	11.8	28.2	4.9	11.5
IA Global	-5.7	14.0	23.3	2.8	7.1
Liontrust Sustainable Future Managed	-0.5	16.1	11.8	6.1	6.0
IA Mixed Investment 40-85% Shares	-6.1	10.0	12.9	2.7	4.9
Liontrust Sustainable Future European Growth	-14.8	19.8	16.0	12.4	-2.6
MSCI Europe ex UK	-9.9	15.8	18.6	5.1	-0.7
IA Europe Excluding UK	-12.2	17.3	16.4	9.3	-0.9
Liontrust Sustainable Future Corporate Bond	-3.6	7.2	10.5	0.5	9.8
iBoxx Sterling Corporate	-2.2	5.0	11.8	0.6	12.3
IA Sterling Corporate Bond	-2.2	5.1	9.1	-0.3	9.8
Liontrust UK Ethical	-7.3	22.5	4.5	10.6	2.0
MSCI UK	-8.8	11.7	19.2	-2.2	0.5
IA UK All Companies	-11.2	14.0	10.8	4.9	0.6
Liontrust Monthly Income Bond	-3.0	8.9	9.4	1.4	7.4
iBoxx Sterling Corporates 5-15 years	-1.7	5.7	10.8	1.2	12.6
IA Sterling Corporate Bond	-2.2	5.1	9.1	-0.3	9.8
Liontrust Sustainable Future Cautious Managed	-2.2	13.4	9.7	4.9	-
IA Mixed Investment 40-85% Shares	-6.1	10.0	12.9	2.7	-
Liontrust Sustainable Future Defensive Managed	-2.2	11.9	9.3	3.7	-
IA Mixed Investment 20-60% Shares	-5.1	7.2	10.3	1.2	-
Liontrust Sustainable Future Absolute Growth	1.1	18.1	15.0	5.4	6.1
IA Flexible Investment	-6.7	11.2	13.8	2.0	4.9
Liontrust GF SF Pan-European Growth Fund*^	-17.0	13.6	-4.5	17.0	4.9
MSCI Europe	-10.6	10.2	2.6	8.2	6.8

Last year was difficult for investors in just about every asset class, with equities and bonds both suffering losses, a very rare occurrence. We always compare the performance of our funds to conventional sectors and where applicable to relevant mainstream indices. The funds had a strong 2018 on these measures, as seven

out of 11 were first quartile versus the average performance in their respective IA sectors. All our Global Equity, UK and Managed funds delivered first-quartile performance. The SF Global Growth Fund, for example, delivered a return of 1.3%, versus -3.0% from the MSCI World Index and -5.7% from the IA's Global sector.

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Longer term, our funds across asset classes generally outperformed their IA sector average over three, five, seven and 10 years to the end of 2018. Over three years, for example, nine out of 11 were first quartile in their respective sectors.

The funds are designed to outperform over the longer term. Our

Sustainability and corporate bonds

Sustainability has also helped to deliver strong long-term returns along with lower volatility from our fixed income funds. Screens have successfully protected the funds from companies that have suffered significant underperformance and/or volatility: in 2018 alone, our screens ensured the portfolios were not exposed to one of the biggest underperforming issuers in our benchmark, namely General Electric. For us, this company continues to be undermined by its focus on producing equipment for fossil fuel electricity power stations.

In addition, by avoiding companies dependent on nuclear energy, the funds have not been exposed to the volatility in bonds issued by EDF and RWE, which have been impacted by uncertainty over decommissioning costs.

Beyond what to avoid, our investment process is designed to identify high-quality companies. By way of an example, we use positive screening within the banking sector to invest in companies with lower-risk business models: this includes retail-focused banks that concentrate on mortgage lending and/or lending to small and medium-sized enterprises (SMEs) such as Nationwide and Close Brothers. We also look to invest in “best in class” names. With

flagship fund, SF Managed, has delivered 144.0% over the last 10 years, compared to a 101.3% average from its peer group. We feel this represents significant outperformance for a multi-asset portfolio.

Similarly, the SF Absolute Growth fund has returned 182.4% over the past 10 years, compared to a 106.7% average from its sector.*

insurers, for example, we focus on companies that take a strong stance on embedding ESG into their investment portfolios as well as having strong credentials in the management of insurance operations.

Finally, we look to invest in sectors and companies that demonstrate a positive impact. This has led us to housing associations and stocks specialising in renewable energy such as Greater Gabbard.

In terms of outlook, we expect corporate bonds to outperform government debt during 2019 and, within this, believe the following sectors will outperform:

- Insurance (attractive valuations, robust solvency, strong ESG, important to society).
- Banks (with a focus on high-quality, retail-focused names with strong capital).
- Telecoms (strong cashflow generation, diversified business models).

In addition, we expect UK government yields to rise during 2019. This is based on a post-Brexit bounce in business investment, increased consumer confidence and strong wage growth and, in light of this view, we remain significantly underweight interest rate risk across all of our bond funds.

Ratings

The following table shows external ratings for our funds from across a range of third parties.

	Rayner Spencer Mills SRI Rated	Morningstar Sustainability Rating	Morningstar Rating	3D Investing Rating	Defaqto Diamond Rating	FE Crown Rating
SF Managed			5 ★			
SF Defensive Managed			5 ★			
SF European Growth			3 ★		-	
SF UK Growth			4 ★		-	
SF Absolute Growth			5 ★			
SF Cautious Managed			5 ★			
SF Corporate Bond			4 ★		-	
SF Global Growth			3 ★		-	
UK Ethical	-		4 ★		-	
Monthly Income Bond	-		3 ★	-	-	

Past performance is not a guide to future performance, investments can result in total loss of capital. Please refer to the Key Risks section for more information. *Source for all data: Financial Express, to 31.12.18, primary share class, total return (net of fees, income and interest reinvested).

Meet the team

Name	Role	Academic background	Industry / Team tenure
Peter Michaelis	Head of Investment	• MA in Physics from Oxford University • MSc in Energy & Environmental Engineering from Sussex University • PhD in Environmental Economics from the University of Surrey	19 years / 18 years
Simon Clements	Investment Manager	• BSc in Economics from the University of Newcastle, Australia • Graduate Diploma in Applied Finance & Investment from Securities Institute of Australia • CFA Charterholder	23 years / 10 years
Neil Brown	Investment Manager	• BA in Economics from Manchester University • MSc in Development Economics from SOAS London	16 years / 10 years
Mike Appleby	Investment Manager – Energy & Utilities	• BSc (Hons) in Biological Sciences from the University of Edinburgh • MSc in Environmental Management from Imperial College London	19 years / 15 years
Harriet Parker	Investment Manager – Telecommunications	• BSc in Economics & Management from the University of Bristol	14 years / 14 years
Laurie Don	Investment Manager – Healthcare	• BSc (Hons) in Computer Science from Durham University • CFA Charterholder	11 years / 4 years
Martyn Jones	Investment Analyst – Consumer Staples & Consumer Discretionary	• MA in Management from The University of Glasgow • CFA Charterholder	7 years / 5 years
Chris Foster	Investment Analyst – Financials	• MA in Economics and Mathematics from the University of Edinburgh • CFA Charterholder	6 years / 4 years
Stuart Steven	Head of Fixed Income	• BA in Accountancy from Stirling University • MSc in Investment Analysis	25 years / 9 years
Kenny Watson	Investment Manager – Fixed Income	• BA in Accounting and Economics from the University of Strathclyde • Chartered Accountant	22 years / 5 years
Aitken Ross	Investment Manager – Fixed Income	• BSc in Accountancy and Finance from Dundee University • MA in International Financial Analysis from Newcastle University • CFA Charterholder	9 years / 6 years
Jack Willis	Assistant Investment Manager – Fixed Income	• BSc in Mathematics with Finance from the University of Leeds • MSc in Finance and Investment from the University of Leeds • CFA Charterholder	4 years / 2 years
Hannah Jones	Investment Analyst	• Studying for the IMC in 2019	4 years / 2 years

Active in the sustainable world



Neil Brown is the immediate past Chair of the Integration Working Group, a member of the Listed Equity Advisory Committee and co-chair of the SDG in Active Ownership Working Group of the UN Principles for Responsible Investment (PRI).



Aitken Ross was formerly a participant on the World Business Council for Sustainable Development Young Leaders programme and is now a regular contributor to this course specialising in the role of finance in sustainable development.



Harriet Parker is a member of the PRI’s Tax Taskforce and Tax Advisory Committee, and also leads and manages the engagement and screening activities of the Sustainable Investment team and liaises on this with clients.



Our themes

Better resource efficiency

- Improving the efficiency of energy use
- Improving the management of water
- Increasing electricity generation from renewable sources
- Improving industrial and agricultural processes
- Increasing waste treatment and recycling
- Making transportation more efficient

Improved health

- Providing affordable healthcare
- Connecting people
- Delivering healthier foods
- Building better cities
- Providing education
- Enabling innovation in healthcare
- Enabling healthier lifestyles

Greater safety and resilience

- Increasing financial resilience
- Saving for the future
- Insuring a sustainable economy
- Leading ESG management
- Improving auto safety
- Enhancing digital security
- Better monitoring of supply chains and quality control

20 areas of predictable and resilient growth

Within our three mega trends of Better resource efficiency, Improved health, and Greater safety and resilience, we invest in 20 themes covering everything from eating more healthily to improving the quality of our global supply chains.

Identifying these trends and themes have been key to performance over the last decade and we revisit them annually to make sure they continue to drive returns.

Following our latest review in the summer of 2018, we reduced the number of themes from 22 to 20 by removing four and adding two new ones. The following new themes both fall within the financials space, split out from our Increasing financial resilience theme (which remains one of our 20) because they have become so prominent:

- **Saving for the future:** As people live longer and governments and corporations retreat from providing long-term cover and pensions, individuals will need to take control of their own finances over the long term. Savings rates will have to increase and companies providing suitable products will enjoy strong growth.
- **Insuring a sustainable economy:** This recognises that insurance, when done well, allows risk to be spread across a community. This lessens the impact of any single event, providing greater peace of mind and encouraging greater risk taking and innovation. Economic development and insurance penetration are strongly correlated; a function, we believe, of the positive social impact of insurance services.

The four themes removed all show how our thinking evolves in line with changing conditions.

Improving the fuel efficiency of cars has long been a key tenet of sustainable investing but we are now keen not to distinguish cars from other forms of transportation, especially with the advent of autonomous vehicle fleets. As a result, the theme has been subsumed into Making transport more efficient, as is another now-defunct theme: Reducing pollution from cars and industry.

We have also removed the Accelerating the transition to lower carbon fuels theme: we had previously identified low carbon fossil fuels as an area of growth but following the Paris Accord and the success of solar and wind generation, this is no longer true.

Finally, we have removed Making food production sustainable as we feel it is sufficiently covered by our broader Improving industrial and agricultural processes theme.

Other changes that influenced our thinking last year included:

- The continued fall in the cost of renewable energy. We have seen over \$300bn invested in renewables over the last four years, with onshore wind halving in cost since 2014 and photovoltaics falling even faster.*
- The advent of truly competitive electric vehicles, with growing penetration of new car sales.
- The Paris Accord on Climate Change and the need to decarbonise quicker than previously thought: the ambition is to limit warming to 1.5C, implying a timeframe of less than two decades to cease using fossil fuels.
- Revelations around the true impact of diesel combustion (VW and Dieselgate) on urban air pollution.
- The fall in the cost of gene sequencing to below \$1,000.
- The ongoing rise of social media networks and the emergence of negative impacts on society.
- The Blue Planet Effect, which has driven home the harm caused by the way we use and dispose of plastics.

We found opportunities in a range of themes last year, some new and others where our work has kept us ahead of rapid change within areas we have tracked for many years. Our work in 2018 focused on key themes including Increasing financial resilience, Improving industrial processes, Better monitoring of supply chains, and Enabling innovation in healthcare. We present a few case studies of these below.

Overall, we have concluded that the majority of our themes still have strong prospects for growth and we believe the updated list will continue to help drive performance over the coming years. And because it is too early to judge the outcome of investments made with a three, five and even a 10-year investment horizon so soon, we also look back to thematic work and stock picks from five and 10 years ago to assess our performance and what we can learn from it.

*Source: BNEF CleanEnergy Investment, July 2018

2018 case studies



Better monitoring of supply chains and quality control: Testing, inspection and certification

The Testing, inspection and certification (TIC) industry is vital for sustainable development, ensuring the safety of our products both for the users and the people making them. The TIC industry helps to reduce the risk of product defects, health and safety accidents and poor quality products.

With more complex supply chains, product innovation, stringent regulations and ever-increasing consumer demands around sustainability, this sector enjoys a long-term structural growth rate that should continue to rise ahead of global GDP.

We have identified Intertek as a positively exposed company benefiting from structural growth in increasing safety standards, outsourcing, regulations and sustainability. It also has the sustainability profile, business fundamentals and valuation that we need to invest with confidence.



Improving industrial processes: Building information modelling (BIM)

A key aspect of the drive to sustainability is improving the efficiency of processes. Over the course of the average large construction project, there are an estimated 2,000 to 3,000 design errors. This inefficiency can create a range of wastes, not least financial, and we believe companies can create value by driving them out.

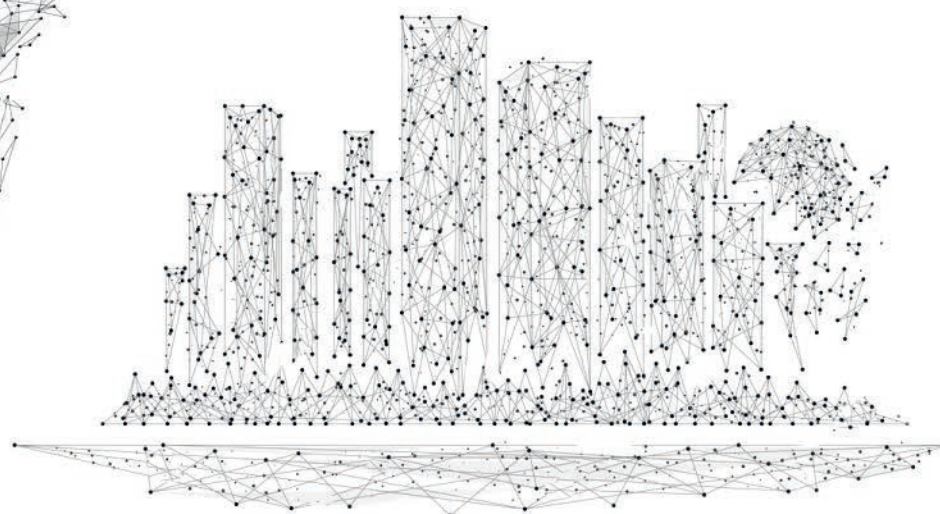
One area of exciting growth is Building information modelling (BIM), which creates project management systems for the construction industry. BIM is the process of managing information over the life of a project, providing a centralised digital platform for all the individuals involved from initial design to final build.

BIM splits into two key end markets: architecture, engineering and construction (AEC), and manufacturing. Super-normal growth and, for us, the real opportunity to adopt technology to improve efficiency lies in the AEC space.

Growth rates for BIM in manufacturing are expected to be around 7% to 8% a year over the medium term, whereas in construction this expands to 20%. With such low penetration of technology, estimates suggest the addressable market of 4.3 million users could expand five-fold in the near future.

A key part of our investment process is identifying where the wider market is underestimating structural change and, while these drivers have been in place for years, the evolution of technology is now resulting in a step change in adoption.

We see Autodesk as the clear leader in BIM, with the company boasting five leading products and accounting for more than half the market.



Increasing financial resilience: Digital payments

Increasing financial resilience remains a key theme across our SF portfolios and we believe the shift from cash to digital payments can provide positive impacts on society. Our assessment of the net benefit to society centres on transparency and the role of digital payments in both closing the tax gap and reducing those aspects of anonymous cash payments that support criminality.

The major opportunities we see are in the transactions themselves as networks such as Visa, a long-term holding in our portfolios, provide the central role in any transaction, connecting merchants seeking payment with the bank that issued the card. Visa takes a minuscule part of the trillions of transactions it helps to process and we believe the complex nature of this system gives such companies considerable barriers to entry.

This is the ultimate scale industry: cost per transaction falls steeply as they grow, enabling companies to be more competitive and create a classic economic moat. This scale argument also applies to the merchant acquirers space, where we hold businesses including Worldpay and PayPal.

PayPal makes transacting online easier and safer for both consumers and businesses. The value we see from this business should come from the long runway of growth from exposure to this theme amplified by the excellent position PayPal has created for itself.



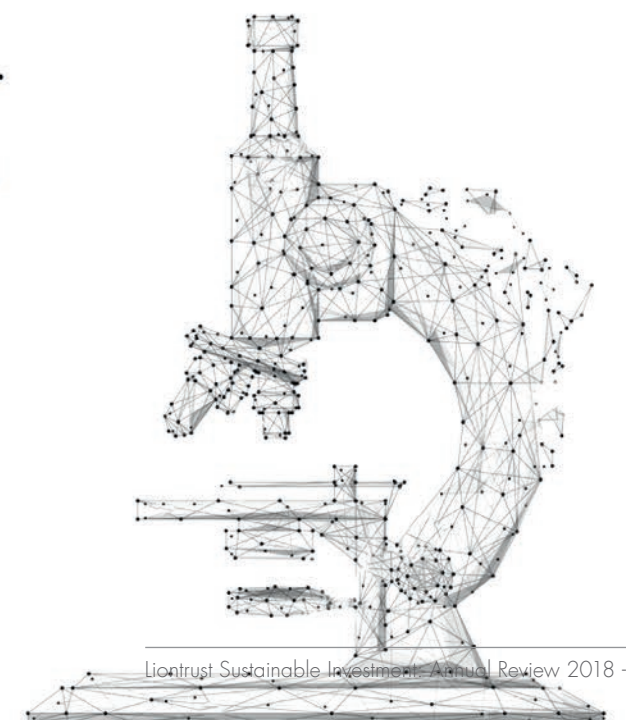
Enabling innovation within healthcare: Rare diseases

Within healthcare, we are looking for cures for or management of a genuine unmet medical need. Haemophilia is one such disease, where an individual is unable to produce naturally the proteins necessary to clot their blood. There are currently no pre-emptive measures to prevent the disease and life expectancy falls by around 10 years on average.

We believe there is a big opportunity for companies that help individuals, governments and/or healthcare systems pre-empt, reduce or manage the personal and financial costs of this disease. Within this context, we see a number of revolutionary steps in treatment.

First, Roche's Hemlibra drug provides an efficacious, easy to administer and cost-effective alternative to the current standard of care. The company continues to show progress with both its recent launches and pipeline. Thematically, Ocrevus in MS and Hemlibra have both seen good uptake since launch, demonstrating that true innovation will quickly get adopted by patients and healthcare payers. The company has the highest number of Breakthrough Therapy designations in the industry.

Second, gene therapy potentially provides a future of a once and done therapies for the disease. We know it is caused by only one gene, therefore gene therapy is theoretically an ideal solution if it can be implemented safely and cost effectively.



Themes: looking back

2009

10 years

Better monitoring of supply chains:

Sustainable apparel

In 2009, we assessed the fashion industry's global supply chains and the working conditions within them. We concluded conditions were unacceptable in a significant number of supply chains, that change was coming, and there were opportunities available to companies that could drive improvements. We focused on the need for decent work and wages throughout the chain.

Over the years, we have invested in a range of companies we felt could create financial value through delivering a positive social impact in supply chains, including Inditex, the owner of the Zara brand, whose proximity sourcing model we believed allowed for a more sustainable form of manufacturing.

Ultimately, after many years of analysis, we have concluded that retailers have been unable to show sufficient improvements in the supply chain and the image of 'Fast Fashion' has become irrevocably damaged as a result. The theme exposed more risks than opportunities for the large retailers and we exited the last of them, Inditex, in 2018.

The theme now focuses on companies that assess these chains on behalf of retailers and we added Intertek to the funds shortly after. Our engagement on this critical issue continues.

2013

Five years

Delivering healthier foods:

Nutrition

Our work on Global Obesity and Nutrition in 2013 identified that "Global Obesity is a major issue that will change the competitive landscape for a range of companies from retailers of packaged foods all the way down to ingredient providers".

Health is a central theme of sustainable development as people need to be fit and healthy enough to reap the benefits of an improving world. This is a theme we have returned to repeatedly, adapting and enhancing our understanding of the prevention side of the equation, primarily via improving our diets and taking more exercise.

We identified in 2015 that consumption of calorie-dense food and lower levels of physical activity had led to a global obesity epidemic. We noted that 36% of US adults were obese and the number of obese adults in Britain was forecast to double by 2030. Steadily increasing press attention was also evident, indicating consumer demands would continue to shift.

It was clear to us that financial value would be created by those companies having a positive social impact through diet and we concluded that "sustainable producers of high growth, high value Natural, Reformulated and Nutraceutical products will experience volume, price and mix growth ahead of peers".

Delivering healthier foods has been a key theme across the SF Funds for many years with Kerry Group in particular standing out. Kerry enables what it calls the 'five Rs': reduce, remove, replace, reinvent and reposition. It works to reduce calories, remove artificial chemicals and replace them with natural alternatives. We also like Kerry because it is managed for the long term and consistently invests in research and development to maintain leadership in the food technology space.

Highlighting the value in such businesses, another of our holdings in this area, the French natural chemicals business Naturex, was acquired at a 42% premium by flavour and fragrance company Givaudan in March 2018.

2015

Three years

Improving industrial processes:

Collaborative Robots (Cobots)

Our work on Cobots in 2015 identified Keyence and this Japanese company remains a core position across the SF Global and Managed Funds. It supplies the sensors and machine vision technology that are critical to collaboration robots, an area where we continue to see considerable growth opportunities.

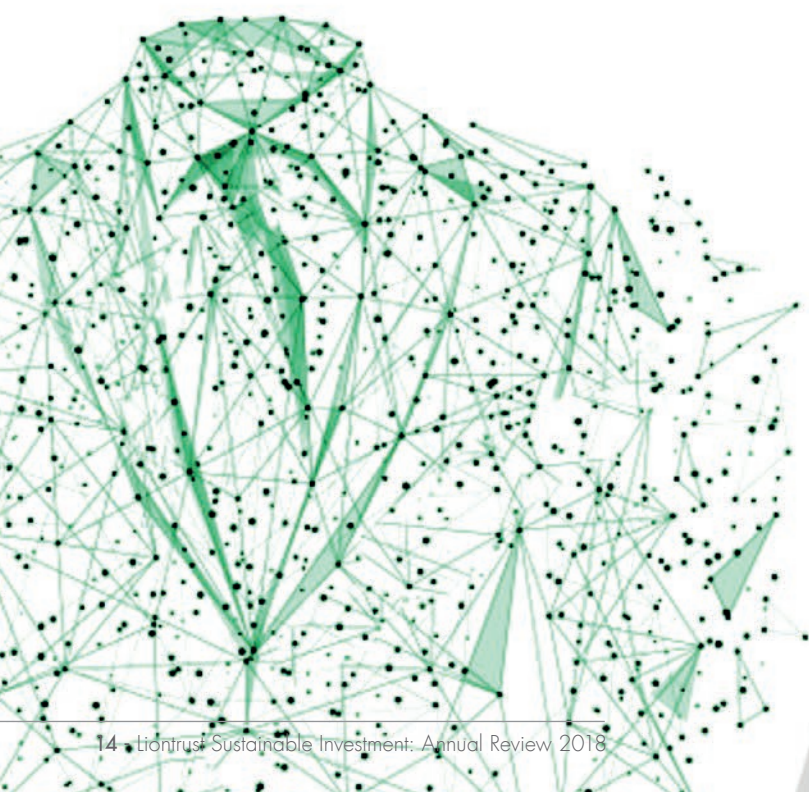
Cobots are designed to work alongside humans rather than replace them and tend to be much cheaper than fully automated factory lines. While robots are effective at repetitive actions, they tend to struggle with more complex and delicate tasks: it takes a robot 20 minutes to fold a towel for example. Bringing Cobots into the production line can free up people for work that requires ingenuity and manual dexterity rather than precision and stamina.

While there is structural growth potential in more traditional automation, the real inflection point – and supernormal growth – is evident in the Cobot market. According to Deloitte, only 9,000 of 300,000 robots produced last year were Cobots but this market is expected to grow close to 50% a year up to 2025, compared to 12% for industrial models.

Around 70% of the world's manufacturing is done by small and medium-sized businesses and with the majority of this yet to be automated, Cobots look set to play a vital role in the future.

Key drivers in this growing penetration have been the falling price of robots overall alongside rising labour costs, plus the importance of efficiency in areas such as consumer electronics and logistics. Estimates suggest the cost of a Cobot has fallen from \$150,000 in 2010 to \$24,000 today and this is expected to keep dropping.

Cobots are clearly less likely to cause direct displacement of jobs than fully automated lines and data from a Gartner study suggest the former could create 2.3m jobs by 2020 while only replacing 1.8m.



Impact measurement

Like many sustainable investors, we are working on ways to measure and disclose the environmental and social performance of our investments. This extra-financial investment performance has been called 'impact' and has grown as people want to understand the positive contribution their money has on the development of a more sustainable economy.

The desire is to report environmental and social performance quantitatively, in a similar manner to investment returns. Unfortunately, however, the process of aggregating the individual performance of a fund's holdings is not so straightforward.

First, there is no globally accepted standard of measurement or disclosure to enable consistent and comparable impact measurement. There are also a number of methodological and practical challenges associated with measuring impact, raising questions such as what do we measure and is the data from our investments reliable and consistent.

Impact investing and impact measurement – what's the difference?

Another challenge is the language we use to describe extra-financial environmental and social performance.

Impact investing: The strict classical definition

The strict classical definition of impact investments are those made with the intention to generate positive, measurable (and typically pre-determined) social and environmental impact alongside a financial return. Key to this is that the investment is additional, this is to say that the positive environmental or social impacts would not have happened without investing in this project or business.

Impact investments can be made in emerging and developed markets, across asset classes, and target a range of returns from below market to market rate, depending on investors' strategic goals.

Impact measurement: A broader definition

A broader definition of impact is now in use in an investment context, which is looser and simply tries to measure extra-financial (environmental and social) impacts. This includes funds looking to invest in companies having a positive environmental or social impact where the exact metrics to measure these impacts have not been pre-determined. The 'additionality' of these investments is harder to prove as companies in these funds can be publicly listed or freely traded. Proving the additionality (that these positive outcomes would not have happened without this investment) is far less clear than under the classical definition.

To add to the confusion, impact is also a term used in relation to a distinct subset of sustainable investing, and viewed as part of the 'engagement' approach we have illustrated below.



The impact here is the positive changes made to how a company is managed, specifically in its environmental or social performance arising from engagement.

Our SF Funds use the broader definition as they have some but not all of the pre-requisites for the stricter definition of impact investing. The funds were launched with the intention of investing in companies that make our development more sustainable (with positive impacts on the environment and society) but the exact measurement of these environmental and social impacts were not predetermined and continues to evolve.

We do engage with companies to improve how they are managed as well as finding ways for them to disclose the impacts, both good and bad, that their business has.

We believe the terminology used to describe environmental and social performance is not actually that important, call it impact or not. What is important is how we communicate it, and how it guides our investment process.

Our funds positively contribute to sustainable development and we do want to quantify this contribution and communicate this to our clients and stakeholders.

How we intend to measure our fund impacts

With this aim in mind, we have been reviewing a number of impact measurement methodologies to find the most accurate and comprehensible solution. The intention is to report on a range of impacts at the fund level and our criteria for selecting an impact measurement methodology is as follows:

- (i) Suitable for equity and fixed income funds (covering our whole range).
- (ii) Consistency and comparability.
- (iii) Alignment with our sustainability themes.

Recently, the Cambridge Institute of Sustainable Leadership (CISL) launched its Impact Assessment Framework, designed for investors in all asset classes. CISL's framework was developed by a group of asset managers and asset owners seeking an "objective, comparable, consistent and reproducible" methodology for measuring the non-financial impact of investment.

This framework measures quantitative investment outcomes on six Sustainable Development Goal (SDG) linked themes (three social and three environmental: Basic needs, Well-being, Decent work, Resource security, Healthy ecosystems and Climate stability). These metrics map well with our process themes and, although simple at present, have the opportunity to develop into an ideal metric that would indicate a fund's compliance with the SDGs.

We are currently testing the framework on a sub-set of our funds to understand its strengths and limitations. We intend to publish the output of this in 2019 and, if appropriate, will use this methodology to report on all our funds. This will be in addition to the work we are already doing with companies to get better information and disclose on their impacts.

Other impact measurements

In addition to trialling The Cambridge Impact Framework, we will continue to disclose information on environmental and social impacts such as:

- Independent analysis on carbon and how the SF Funds compare to the markets in which they are invested, in terms of carbon emitted and investments in solution providers as well as information on exposure to fossil fuels (which is zero). This is in line with our commitment to do so in 2012.
- The investment ideas in our equity portfolios are driven by finding companies exposed to our 20 themes. We will continue to engage with companies to disclose the impacts of these positive themes and share these as we progress.
- We will continue to disclose how we are engaging with companies and where we are affecting positive change in how companies are managed (see pages 24-28).

Measuring impact is a challenging and evolving area but we are committed to developing this and to meeting the increasing demand from clients who want to know what impact their investments are having on the real world.

Climate change: how we think about it and how this influences our investments

How we generate and consume energy is undergoing huge change, which is affecting many different parts of our economy. The science is telling us to act ever faster to reduce greenhouse gas emissions. We think the transition from high to low-carbon energy sources and how we can use energy more efficiently to reduce emissions presents a huge structural shift that has a major impact on our investment decisions.

First, companies helping us to reduce emissions will experience significant structural growth and those that can meet this structural demand for products and services and produce them in a profitable way can potentially provide interesting investments.

The energy transition will reduce emissions in power and heat generation, industry, transport and in heating and cooling buildings. Many of our themes play directly into this transition and we have meaningful exposure to companies set to benefit from delivering lower emissions through:

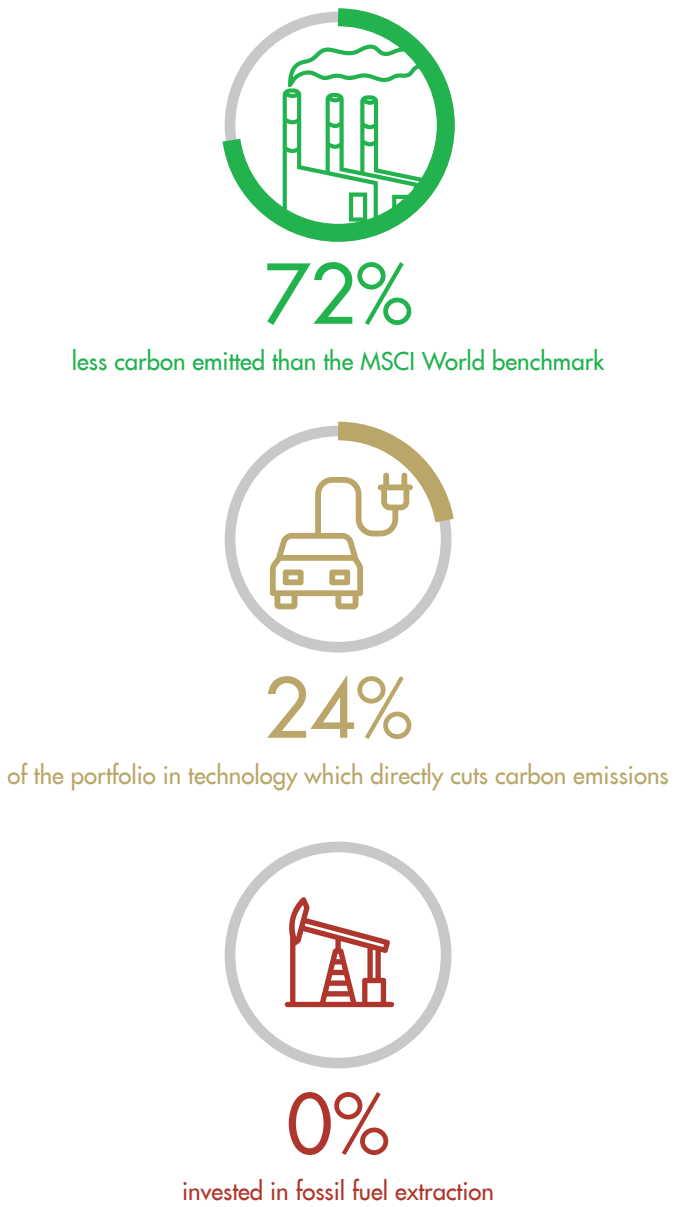
- Increasing electricity generation from renewable energy sources.
- Improving the efficiency of energy use.
- Making transport more efficient.
- Improving industrial and agricultural processes.
- Increasing waste treatment and recycling.

Second, we want to ensure the companies we own understand the magnitude of the energy transition and we encourage them through engagement to manage their businesses in a proactive way to protect them from inevitable tightening regulations.

There are some industries, no matter how proactively managed, on the wrong side of this transition and these will experience secular decline in demand for their carbon-intensive products or services. We choose to avoid areas such as fossil fuel extraction and production, internal combustion engine car manufacturers, airlines and energy

intensive businesses that are not positioning themselves for a lower carbon world.

We disclose the aggregated carbon emissions for our single strategy funds, which we started doing in 2012. This work is carried out independently and shows that, on average, our SF Funds emit 72% less carbon dioxide than the markets in which they are invested, have 24% exposure to companies whose products help to reduce emissions and hold 0% in companies exposed to the extraction and production of fossil fuels such as coal miners and oil and natural gas exploration and production (Source for all figures: MSCI Carbon Analytics Report, Liontrust, as at 31.12.18).



There are important positive attributes to these characteristics. In the event of a tax on carbon, companies that can pass this cost on to their customers will not suffer a negative impact on their margins (and profitability). Companies that are not able to pass these carbon costs through to their clients will have to bear this cost themselves.

The very low carbon emissions coming from the businesses held in the SF Funds compared to the market mean these portfolios are more resilient to tightening carbon regulations, will have more resilient margins and should therefore outperform the market as emissions regulations tighten.

Alignment of the SF Funds with the UN's Sustainable Development Goals

Our clients have asked us to show how the companies in which we invest are aligned with the United Nations' Sustainable Development Goals (SDGs). The SDGs are an internationally recognised set of goals to aim for by 2030, which will help the world develop in a more sustainable way. They replaced the United Nations' Millennium Goals and have captured many progressive investors' interest as a more comprehensive way of

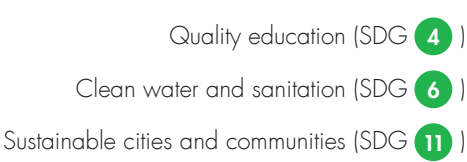
thinking about and reporting on sustainable investing. We have enhanced the work we did in our 2017 Annual Review showing how our investment themes are aligned with the SDGs by analysing where each theme is directly linked to Key Performance Indicators in the SDG text. Each of our themes is limited to one main SDG, although, in reality, there are overlaps and most companies are exposed to more than one goal.

Our investment theme	Sustainable Development Goal
Better monitoring of supply chains and quality control	12 Responsible consumption and production
Building better cities	11 Sustainable cities and communities
Connecting people	9 Industry, innovation and infrastructure
Delivering healthier foods	3 Good health and well-being
Enabling healthier lifestyles	3 Good health and well-being
Enabling innovation in healthcare	3 Good health and well-being
Enhancing digital security	9 Industry, innovation and infrastructure
Improving auto safety	3 Good health and well-being
Improving industrial and agricultural processes	9 Industry, innovation and infrastructure
	2 Zero hunger
Improving the management of water	6 Clean water and sanitation
Improving the efficiency of energy use	7 Affordable and clean energy
Increasing electricity generation from renewable sources	7 Affordable and clean energy
Increasing financial resilience	8 Decent work and economic growth
Saving for the future	8 Decent work and economic growth
Insuring a sustainable economy	8 Decent work and economic growth
Increasing waste treatment and recycling	12 Responsible consumption and production
Leading ESG management	20 Multiple SDGs, dependent on company operations
Making transportation more efficient	11 Sustainable cities and communities
Providing affordable healthcare globally	3 Good health and well-being
Providing education	4 Quality education

The SDGs where our funds have largest exposure are:

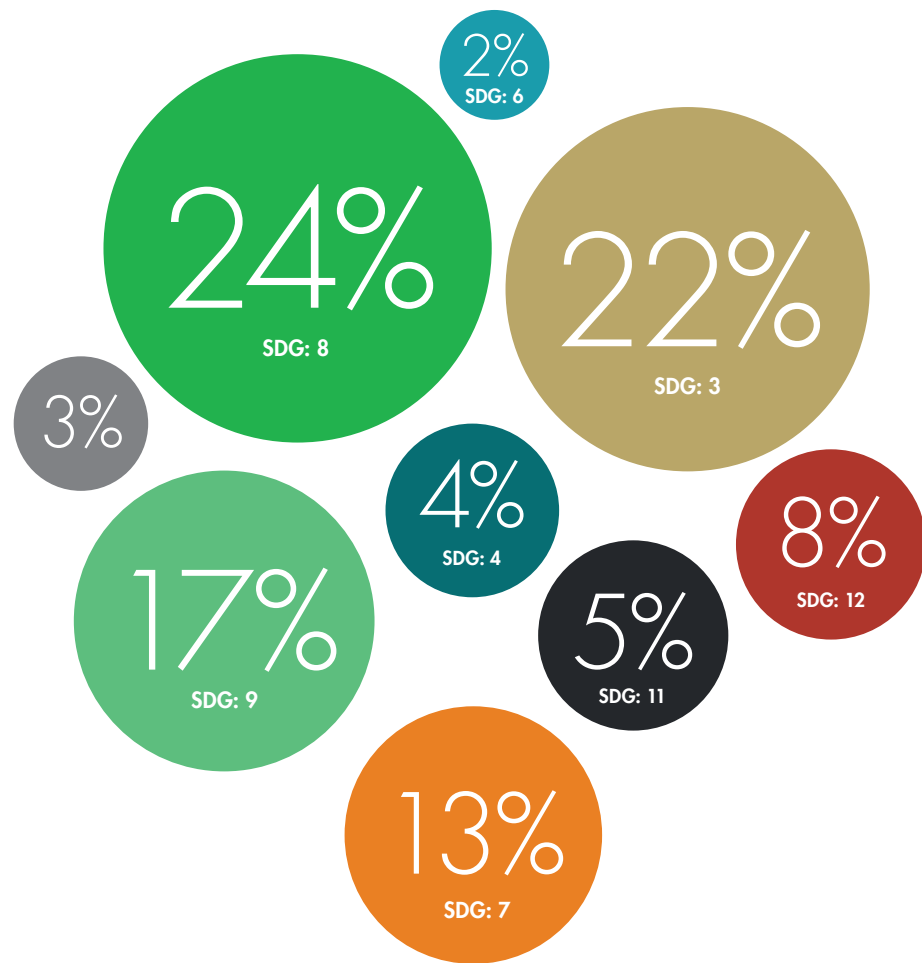


We also have exposure to:



Sustainable Future Funds' exposure to primary SDGs

- SDG: 3
Good health and wellbeing
- SDG: 4
Quality education
- SDG: 6
Clean water and sanitation
- SDG: 7
Affordable and clean energy
- SDG: 8
Decent work and economic growth
- SDG: 9
Industry, innovation and infrastructure
- SDG: 11
Sustainable cities and communities
- SDG: 12
Responsible growth and consumption
- Multiple SDGs, company dependent on their operations



Source: Liontrust as at 31.12.18

How our themes are aligned to the SDGs where we have most exposure

Good health and well-being (SDG #3)

We have five investment themes aligned with this SDG to ensure healthy lives and promote wellbeing for all at all ages.

Improving auto safety: We have identified companies whose products improve the safety of travel and reduce road traffic accidents, principally through active safety, which involves collision avoidance, active braking and semi-autonomous driving. We concentrate on the specialist companies making the kit to improve safety (or reduce emissions) rather than the car manufacturers we believe are challenged to meet tightening regulations to improve safety as well as reducing emissions.

Delivering healthier foods: There is a trend in the food industry of consumers changing their preferences and demanding healthier options. We have identified companies that provide reformulation services to change the recipe of foods to make them healthier (less fat, sugar and salt) while maintaining the taste. These companies are a beneficiary of this demand for healthier food as their customers (many of which are the big incumbent food producers) respond to changing consumer preferences and use their reformulation

services. This improved diet has positive health impacts. For example, it can help to reduce non-communicable diseases such as obesity and cardio-vascular disease. This contributes to the Key Performance Indicator 3.4 of the SDGs, which is to reduce by one third premature mortality from non-communicable diseases through prevention and treatment.

Enabling healthier lifestyles: Companies that promote healthier lifestyles, principally through increasing activity, taking exercise and sport help meet the same Key Performance Indicator 3.4 of this SDG.

Providing affordable healthcare globally: Companies that help to deliver affordable, positive patient outcomes in managing disease also help to achieve this goal.

Enabling innovation in healthcare: Companies whose products or services promote innovation within healthcare are helping to achieve this goal. They do this by coming up with new, more effective ways to treat diseases (creating a significant step change in the mechanism used to treat a given disease), by providing essential equipment or services for biotechnology research (such as specialist measuring equipment, genetic sequencing equipment or high quality consumables for research) or developing software to help make treatments more effective.



Affordable and clean energy (SDG #7)

We have three main themes aligned with achieving this SDG to ensure access to affordable, reliable, sustainable and modern energy for all.

Increasing electricity generation from renewable sources: Substituting coal-intensive fossil fuel electricity generation with renewable power sources reduces carbon emissions as well as providing a cost effective means in some off-grid situations to connect people to cheaper, more reliable power sources.

Improving the efficiency of energy use: We see many ways of making energy cheaper by reducing wasted energy while also reducing emissions through more efficient use. This cuts across many areas of the economy and includes building insulation, efficient lighting, energy-efficient climate control, travel and industrial processes. Companies that provide services or equipment, particularly in upgrading the power grid network to be able to deal with changing production and consumption patterns of electricity, are an important requirement to achieve affordable clean energy.

Decent work and economic growth (SDG #8)

We have three themes aligned with this development goal to promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all.

Increasing financial resilience: We believe a resilient financial services sector is necessary for economic well-being through utility-like provision of banking, lending and effective ways of appropriately saving for the future, as well as mitigating risks through insurance. This does not mean that any company in the financial sector is automatically investable, but we do see positive ways that these companies contribute to society when appropriately and proactively managed. This is aligned with the SDG Key Performance Indicator 8.3 to encourage growth of business through access to financial services.

Insuring a sustainable economy: We believe insurance can spread the risk faced by an individual or corporation and makes a beneficial contribution to society.

Saving for the future: We believe there is a real need for people to be able to get good advice and choose appropriate investments to ensure they have saved up for their retirement. Failing to invest for the future and relying on state-funded pension schemes will result in a significant drop in quality of life as government finances come under increasing pressure, exacerbated by demographic shifts towards a higher proportion of people past working age. Again, not every company involved in financial services is exposed to this theme, but we look for what we consider the best-managed businesses catering for people's needs.

Industry, innovation and infrastructure (SDG #9)

We have three themes aligned with this SDG to build resilient infrastructure, promote inclusive and sustainable industrialisation and foster innovation.

Improving industrial and agricultural processes: We like companies providing products or services that help to make industrial processes more resource efficient, as well as safer for workers and users. These improved industrial processes help to reduce the negative impacts on people and the environment and are making a positive contribution. We see investment opportunities in software and systems that help to implement life-cycle design (including the disposal of products) and help to manage supply chains as well as opportunities in automation of factory processes to remove repetitive or dangerous mechanical tasks as they all help to modernise industry and meet this SDG.

Enhancing digital security: As more and more of our lives and critical services are carried out online, we need to protect the data from theft. Digital security helps to make this growing area of the economy secure.

Connecting people: We believe access to easy communication tools and information, increasing amounts of which are online, is a positive requisite of a more sustainable economy.

Sustainable cities and communities (SDG #11)

We have two themes aligned with achieving this SDG to make cities and human settlements resilient and sustainable.

Making transport more efficient: Urban transport systems are improved by reducing congestion as well as transport emissions (which make the local air quality toxic) as the mode of transport shifts from self-driven cars to public transport systems such as trains, tubes and buses.

Building better cities: Shelter is a basic human requirement and companies that build quality affordable homes or key infrastructure needed in cities are helping to provide this.

How companies manage their business is also important in meeting the SDGs

Companies we hold contribute positively to SDGs mainly through the products and services they provide. The way companies manage their operations and how they treat and pay their staff, however, has an obvious impact on the quality of the work (SDG #8) they provide and is relevant to all the stocks we own.

Which ESG challenges are most material varies depending on the industry in question. For example, this can include quality of work (through working conditions, fair pay and working conditions in supply chains) as well as equality and diversity in the workforce and on the Board of Directors. Our engagement to promote proactive management of ESG issues, and the SDGs to which they are aligned, can help to achieve the SDGs, and we intend to explore and report on this further.

ENGAGEMENT

Our approach to engagement and voting

Engagement is integral to how we ensure we invest in high-quality companies. Engaging on key ESG issues gives us greater insight, helps us to identify leading companies and is used as a lever to encourage better business practices.

Our team has been engaging in this way for more than 18 years, and we have found this approach challenges and encourages companies to proactively manage the wider aspects of their business, which, in turn, protects their longer-term prospects.

Engagement is a resource-intensive process and our team conducts sustainability research alongside traditional financial and business fundamental analysis. This approach enables us to better target engagement on material issues and integrate this into our financial assessment of a company, maximising the information advantage that engagement can bring to analysis.

In 2018, we had 214 face-to-face meetings with companies. We raised 226 key ESG issues with companies over the year, either in direct meetings or through other forms of correspondence such as letters and emails.

ESG issues	2018	2017	2016
Environmental impacts	18	24	28
Human Rights & Supply Chain	2	n/a	n/a
Employees	11	7	9
Customers	13	8	17
Cyber Security	6	4	3
Product Safety	8	8	9
Corporate tax	7	7	15
Anti-bribery & corruption	7	n/a	n/a
ESG integration and disclosure	56	22	14
Other environmental or social issue	12	14	24
Governance:			12
- Remuneration	21	23	
- Gender Diversity	31	30	
- Auditors	13	32	
- Other Governance	21	8	
Total	226	191	131

Engagement
on key ESG
issues

Engagement highlights

- We engaged with a large UK consumer company on timber sourcing, encouraging it to adopt industry best practice on wood sourcing and move to 100% Forest Stewardship Council (FSC) certification. We met with the company several times and also with a leading non-governmental organisation (NGO) with expertise in the area. The company has indicated it will move to source wood from the FSC and that it is a priority.
- We have continued to engage on corporate governance with our Japanese holdings and note that several continue to show improvements on board independence and gender diversity. All four companies we held over the year now have a minimum of two independent board members and two have female representation.
- We engaged extensively with one of our holdings after an incident where extreme rainfall forced its Bauxite processing plant in Alunorta, Brazil to release waste water into the river – which is clearly in breach of its operating licence. Our engagement continued throughout the year, focusing on operational knock-on effects, and this work included contacting NGOs in Brazil to get a more balanced idea of the local view around what happened. We also spoke to experts familiar with this operation to get context about the complex situation on the ground. Looking forward, we want to explore further how this company can do more to improve its relationship with the local community and regulator and facilitate the faith needed to resume full production. We also discussed this at our Advisory Committee in December.
- We began engaging with 12 insurance companies held across our equity and fixed income portfolios. This is designed to help us to review their responsible investment policies and practices, seek clarification on how each company currently considers ESG factors in their investment decision processes, and to understand any exclusionary criteria (negative screening) used. This engagement has kick-started our initiative on Encouraging the transition to sustainable investment.
- We wrote to 41 companies held across our funds where we had withheld support for proposals at their Annual General Meetings (AGM) in 2018. We wrote to each company, providing our voting rationale along with a copy of our voting policy. There were three broad areas where we withheld support:
 - There was a lack of gender diversity
 - We disapproved of a company's remuneration report or policy
 - We felt there was an issue relating to the auditor.

In many cases, we also took the opportunity to request that some report more information on their impact and the SDGs.

- Over the year, we tightened our thresholds for revenues derived from a number of unsustainable or unethical activities. Companies are now only able to generate 5% of revenues from activities such as tobacco, gambling, weapon systems and nuclear power as opposed to the previous threshold of 10% and we engaged with a number of holdings over the year to seek additional clarification on the level of involvement in such areas.

2018 Priority Engagement Initiatives

Priority Initiative	Our approach	Targets	Outcomes and highlights	Conclusion	
Impact and Sustainable Development Goals	We have been making efforts to demonstrate what broad impacts our funds have on society. We have been quantifying the main impacts (good and bad) from the companies in which we invest. We will engage with companies to disclose their main impacts so we can report more fully to clients. This is an evolving field and we are keen to build on the work we have already done in this area.	<ul style="list-style-type: none"> Collaborate with other investors to look at best practice on corporate disclosure on impact and SDGs. Look at new ways to report to clients on the impact of our funds. Engage with holdings on improving disclosure of impact metrics and what SDG targets the company is aiming to contribute towards. 	<ul style="list-style-type: none"> Co-chaired Collaborative Engagement Group on SDGs with the PRI. A report will be published in 2019. Initiated a trial using the Cambridge Institute for Sustainable Leadership (CISL) model for reporting on impact for two of our funds. 	Successful in some areas, will continue to prioritise this initiative in 2019.	SUCCESS
Encouraging sustainable use of plastics	In addition to investing in companies that provide solutions to plastic pollution we will continue to encourage companies to reduce the amount of single use plastics and packaging they introduce to the environment.	<ul style="list-style-type: none"> Understand the path companies need to be on to make their plastic use more sustainable. Understand the associated financial risks and opportunities. Drive companies to adopt and disclose against targets in line with sustainable outcomes. 	<ul style="list-style-type: none"> Contacted consumer products companies held in the funds to find out more about their strategies to reduce plastic pollution. Held discussions with a further three companies in the funds regarding their product development and innovation that directly tackles plastic pollution. Discussed the issue with our Advisory Committee to gather ideas for furthering our impact on this initiative. 	Somewhat successful, but more work needs to be done and we will continue to prioritise this initiative in 2019.	PARTLY SUCCESSFUL
Anti-Bribery and corruption	Corruption is bad for people and ultimately bad for business. We want to better understand how companies can reduce the chances of being complicit in corruption and encourage them to manage potential conflicts to the best of their ability as ideas for how best to do this continue to evolve.	<ul style="list-style-type: none"> Assess portfolios for companies with weak policies or systems on bribery and corruption and engage with them to improve in this area. Collaborate with an NGO on an initiative related to financial services bribery and corruption. 	<ul style="list-style-type: none"> Screened companies in the portfolios and wrote to those where we felt policies and programmes on anti-bribery and corruption could be strengthened. Met with an NGO and discussed ideas for a collaborative project. 	We have not done what we set out to do here, but made some progress towards the end of last year and will continue to prioritise this initiative in 2019.	PARTLY SUCCESSFUL NOT MET
Responsibility in apparel supply chains	Low-cost apparel often comes at a high price to workers in global supply chains. We are encouraging companies to build long-term, symbiotic relationships with suppliers to ensure the safety and human rights of workers in global supply chains.	<ul style="list-style-type: none"> Maintain relationships with NGOs and keep up to date with initiatives in the sector. Engage with companies directly on issues of concern. 	<ul style="list-style-type: none"> Continued our collaborative work stream through discussions with other investors and NGOs focused on transparency and advocacy. These discussions have contributed to a joint work stream with investors and an NGO, which will drive direct engagement next year. Did not engage directly with companies on this issue. 	We do not have a large exposure to apparel in the funds. We will continue efforts on this issue, but will be rolling it into another priority initiative relating to workers well-being more generally.	PARTLY SUCCESSFUL
Promoting gender diversity	We believe companies that are more gender diverse are better able to prosper over the long term so we are engaging to encourage greater gender diversity, looking at gender balance at a board level and senior positions, and looking at efforts to reduce any gender pay gaps.	<ul style="list-style-type: none"> Use our voting policy to withhold support for management where gender diversity is poor and could be strengthened. Strengthen our voting policy to more easily withhold support on companies outside the UK. Engage with all companies where we have withheld support on this issue. 	<ul style="list-style-type: none"> Withheld support for the adoption of the annual report and accounts of 31 companies held across the funds where there was a lack of gender diversity on the board. From next year, we will instead be withholding support for the Chair of the Nominations Committee for companies that have fewer than 30% women on the board. Wrote to all companies where we withheld support to request a meeting to discuss diversity policies, programmes, pay gaps and corrective action plans and began to engage directly with these companies. We also asked about recruitment and nominating procedures for board and senior management. 	Successful in all areas and from next year, we will be stepping up efforts on this issue, but with a wider diversity lens, which will also include ethnicity.	SUCCESS
Encouraging corporate tax responsibility	Tax is not just a cost to be minimised and aggressive tax minimisation is a concern for investors as it can be a risk to earnings and can damage reputation. We are engaging with companies to better understand tax risks and to encourage better disclosure of tax policies and strategies.	<ul style="list-style-type: none"> Engage with companies with high tax risks stemming from either a lack of policy, disclosure or high 'tax gaps'. Continue to collaborate with other investors to find and learn from best practice by discussing tax policies, systems and reporting with leaders on this issue. 	<ul style="list-style-type: none"> Raised the issue of corporate tax with seven companies held across the funds. Collaborated with other PRI signatories on two companies in the funds, one of which we hosted. 	Successful engagement on this issue. From 2019, engagement on tax will be included in our routine assessment and dialogue with companies where needed.	SUCCESS
Ensuring privacy and data security	Companies' data security and management have come under intense scrutiny following cyber security breaches in recent years. We are engaging with companies to better understand how they manage and mitigate these risks and to ensure they adhere to European General Data Protection Regulation (GDPR).	<ul style="list-style-type: none"> Engage with investee companies both directly and collaboratively through the PRI Cyber security project. 	<ul style="list-style-type: none"> Engaged with six companies held in the funds. Participated in several PRI Cyber Security engagement group education and engagement calls. Co-led collaborative engagement for two of these companies. 	Successful engagement on the issue. From 2019 engagement on cyber security will take the form of routine assessment and dialogue with companies where necessary and we will continue to collaborate with other investors through the PRI.	SUCCESS
Value creation in the healthcare system	We are engaging with companies to request more information that can help us determine whether their products truly deliver value to patients and to wider healthcare systems.	<ul style="list-style-type: none"> Meet with investee companies and raise this issue and request information. 	<ul style="list-style-type: none"> Discussed this issue with all investee healthcare companies we met with, alongside some additional businesses not held in the funds. Discussed with our Advisory Committee about how to take this initiative further as well as how it relates to the Impact/SDG initiative. 	Successful engagement and some good dialogue that informed our investment decisions. Engagement on this issue will still be conducted, but will be part of our Impact and SDGs initiative.	SUCCESS

Engagement: looking to 2019

We prioritise a number of proactive engagement initiatives in collaboration with our Advisory Committee at the beginning of each year. We assess how our holdings are positioned on these issues and where appropriate, define target lists of companies for engagement.

For 2019, we have reduced the number of priority initiatives to target our efforts more effectively with the aim of having greater impact and success. As well as continuing our efforts to increase corporate disclosure on ESG impacts, mitigation efforts and performance, we have the following priority initiatives:

- **Impact and SDGs:** We continue to prioritise our efforts to quantify the main impacts (good and bad) from the companies in which we invest. We will engage with companies to disclose their main impacts so we can report on these. This is an evolving field and we are keen to build on the work we have already done in this area.
- **Sustainable use of plastics:** We are looking for companies providing solutions to plastic pollution as potential investments as well encouraging companies to reduce the amount of single use plastics they introduce to the environment.
- **Anti-Bribery and corruption:** Corruption is bad for people and ultimately bad for business. We want to better understand how companies can reduce the chances of being complicit in corruption and encourage them to manage potential conflicts to the best of their ability as ideas for how best to do this continue to evolve.
- **Increased corporate diversity:** We believe companies that are more diverse are better able to prosper over the long term so we are engaging to encourage greater diversity, looking at gender balance at a board level and senior positions, and looking at efforts to reduce any gender pay gaps.

- **Worker well-being:** How companies manage human capital of their direct operations, as well as workers further down supply chains, can affect their long-term success. We will engage to encourage companies to offer decent work and pay living wages and to ensure they mitigate risks, protect workers' rights and maximise the opportunities to support employees. We will also encourage companies to use their influence to drive forward best practice further down their supply chains.
- **Encouraging the transition to sustainable investment:** Individuals are having to take responsibility for their long-term finances and adequate savings and pension provision is critical. We have long viewed companies that provide this service as beneficiaries of our Saving for the future theme. To date, the majority of saving has been into non-sustainable funds but as demand for sustainable investment grows, companies should do all they can to promote it. We will focus on determining which are leading the way and which need to do more. This also applies to insurers offering life and health cover while investing premiums in companies that cause ill health, such as tobacco stocks.

2019 investment outlook

The political and economic crystal ball is not very clear at present and while the mists are especially thick in the UK, Europe and the US are far from clear on the way ahead.

We are now a decade on from the financial crisis and special measures, in the form of low interest rates and other stimulus, are still in place across much of the world. In the US, which has done the most to normalise its central bank rates, there is concern that rate hikes have turned the screw too tightly, dampening growth too soon. You can add to this the continued high debt levels of governments, which limit their ability to spend.

Over the last 18 years, the aim of the SF funds has remained constant – to deliver strong returns by investing in sustainable companies

Nevertheless, while the broad economic direction is hard to predict (our best estimate is for dampened growth this year, followed by a pick up to trend growth in 2020), we are confident the growth identified by our themes will endure, making the companies exposed to these more likely to deliver their financial goals.

Our 20 themes capture the increasing share of the global economy devoted to making our societies cleaner, healthier and safer. Companies exposed to these themes experience strong growth, which tends to be under-appreciated by the market, while also delivering positive outcomes to society and the environment.

All our themes matter but over the next year we are especially excited for the prospects in:

- **Increasing renewable energy:** As the costs of wind and solar fall so does the carbon intensity of electricity generation. Cheaper electricity will then enable revolutions in other industries such as vehicle electrification.

- **Improving industrial and agricultural processes:** Better software and data enable step changes in construction (BIM systems), supply chain management and the efficiency of getting high-quality food onto our plates with lower environmental impacts and improved animal welfare.

- **Enabling innovation within healthcare:** New treatments for cancer and rarer diseases will be developed through immunotherapies and gene therapies combined with cheap DNA sequencing to diagnose conditions earlier.

- **Increasing financial resilience:** A decade on from the financial crisis, it remains critical to strengthen stability and trust in financial interactions. We focus on digital payments and online apps to reduce fraud and allow individuals and corporations greater visibility of and ability to plan their finances.

Companies in these areas will, we believe, see real change in their markets as the development of new approaches and technologies alters the competitive landscape. The aim of the SF funds is to be invested in those companies that will thrive in this new environment.

Over the last 18 years, the aim of the SF funds has remained constant – to deliver strong returns by investing in sustainable companies – and we are extremely proud of our track record in doing so. The team itself and the investment process have evolved and improved over the years as we develop better techniques to identify successful companies and adapt to the changing world.

As we look forward to continuing this work to meet the challenges ahead in 2019, I would like to thank all our clients for their support over nearly two decades of sustainable investment.

Past performance is not a guide to future performance, investments can result in total loss of capital. Please refer to the Key Risks section for more information.

External Advisory Committee



Jonathon Porritt is Founder Director of Forum for the Future, the UK's leading sustainable development charity. His book, "The World We Made", seeks to inspire people about the prospects of a sustainable world in 2050. He is also Chancellor of Keele University and President of The Conservation Volunteers and former Chair of the UK Sustainable Development Commission.



Sophia Tickell is Co-founder and Director of Meteos, a non-profit company, which runs senior dialogues, focused on finance, health and the environment. She is the author of "Banking on Trust", "Vital Connections: Science, Society and Sustaining Health", the EnergyFutures report, and the PharmaFutures (www.pharmafutures.org) series. Sophia was previously Chair of the Board at SustainAbility Ltd and led Oxfam's policy work on the private sector.



Tony Greenham is Director of Economy, Enterprise and Manufacturing at the RSA (Royal Society of Arts, Manufactures and Commerce), where he leads a programme of policy research into the future of work, social impacts of technology, green industrial strategy and economic democracy. He is a former corporate stockbroker and has written extensively on financial sector reform including the undergraduate economics textbook 'Where Does Money Come From?'



Tim Jackson is Professor of Sustainable Development at the University of Surrey and Director of the Centre for the Understanding of Sustainable Prosperity (CUSP). From 2004 to 2011, he was Economics Commissioner on the UK Sustainable Development Commission, where his work culminated in the publication of the controversial bestseller "Prosperity without Growth" – economics for a finite planet.



Valborg Lie is founding director of Borg Consulting, which advises investors on the development and implementation of Responsible Investment (RI) policies and practices, including stewardship activities and ESG integration. She previously worked at principal level of the Norwegian Sovereign Wealth Fund (SWF) as head of RI. During autumn 2017, she coordinated a landmark research project commissioned by the Norwegian Ministry of Finance, assessing global best practices in RI.

Liontrust is a signatory of:



The United Nations Principles for Responsible Investment (UN PRI) is a global initiative for international investors to implement the six principles. The objectives are to understand the implications of sustainability for investors and support signatories to incorporate these principles into their investment decision making and ownership practices. As a PRI Signatory, Liontrust Investment Partners LLP commits to completing the PRI Reporting Framework on an annual basis. For more information about UN PRI and the six principles, please visit unpri.org

Key risks

Past performance is not a guide to future performance. Do remember that the value of an investment and the income generated from them can fall as well as rise and is not guaranteed, therefore, you may not get back the amount originally invested and potentially risk total loss of capital. Some of the Funds managed by the Sustainable Future Equities team involve foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. Investment in Funds managed by the Sustainable Future Fixed Income team involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. The value of fixed income securities will fall if the issuer is unable to repay its debt or has its credit rating reduced. Generally, the higher the perceived credit risk of the issuer, the higher the rate of interest. The Monthly Income Bond Fund has a Distribution Yield which is higher than the Underlying Yield because the fund distributes coupon income and the fund's expenses are charged to capital. This has the effect of increasing dividends while constraining the fund's capital appreciation. The Distribution Yield and the Underlying Yield is the same for the SF Corporate Bond Fund.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

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