SMITHSON INVESTMENT TRUST PLC

ESG Integration

Smithson Investment Trust aims to be a long-term, buy-and-hold investor, building a portfolio of high-quality companies that will generate superior, risk-adjusted returns over the long term. As a long-term investor, developing a detailed understanding of the business, its industry, and the variety of risks and opportunities that may influence the performance of the companies we invest in is essential. Assessment of the risks associated with the business's environmental and social performance, as well as the quality of corporate governance, known as "ESG" factors, is a fully integrated component of our pre-investment research; poor ESG performance can generate significant, negative impacts on the financial performance of the company as well as increase its risk profile, particularly over the long term.

Smithson builds an investable universe of, as we define them, "good companies". Good companies are those that can generate a sustainably high return on invested capital over the full business cycle and have the ability to reinvest these returns to generate consistent growth. As long-term investors, fully analysing the sustainability of the company's returns and its growth potential is a central tenet of our research process. Detailed financial analysis of the business is, of course, a large component of this assessment, but fully analysing the variety of risks and opportunities posed by non-financial performance plays an important role. Over-exposure to ESG risks, such as reputational damage, negative consumer sentiment, fines, increased taxes or disruption to a company's supply chain can significantly affect a business's ability to sustain high returns over the long term. Hence, management teams that allocate capital with the sustainability of long-term returns in mind, will typically have better performance from an ESG perspective.

Many of the worst environmentally and socially performing businesses are automatically excluded from the Smithson investable universe, simply due to their unsustainable business models. Industries we find to be unable to sustain a high return on invested capital and are therefore unlikely to invest in, include oil and gas, energy, metals and mining, utilities, and aerospace and defence, among others.

Active ownership, or stewardship (see Fundsmith's 2020 Stewardship Report), is also an important component of our risk management process after we invest in a business. Regularly engaging with investee companies to promote a long-term mindset for capital allocation and appropriate controls over ESG related risk is a powerful tool in protecting the long-term value of our investment. For many companies, improving ESG performance and minimising the negative impacts they may have on the environment/society can be a factor in strengthening their business model and outperforming competition. We use engagement to understand management's perspective, assess their handling of a variety of issues and to raise concerns we may have regarding their approach or outcomes, when appropriate. We also ensure we use our proxy votes to protect and enhance the value of our investments, supporting or opposing the company when necessary. We assess votes and engagements on a case-by-case basis ourselves and don't outsource the decision or use any advisory services. We use both engagement and proxy voting to support decisions that benefit the sustainability of returns and long-term performance of the business.

This approach is used by all of the strategies Fundsmith operates, and is described in more detail in the Responsible Investment Policy, published as part of responsibility as a signatory to the UN Principles of Responsible Investment.

Reviewed - November 2022