

FY23 ESG Update for the Merlon Capital Partners Board

Merlon prefers an integrated, issues based ESG approach. We delve deep into ESG issues that most affect our portfolio and reflect this research in our valuations and conviction scores, just as we do for investment issues. As active owners, we share our learnings with portfolio companies as part of our engagement programme, with the goal to influence better investment returns and societal outcomes. We hold ourselves as a business to the same standards we ask of our portfolio companies.

Recurring ESG issues discussed with portfolio company Boards in FY23

- Capital allocation (appeared in 23 letters)
- Board issues such as succession planning, skills mix, “over boarded” Directors (10 letters)
- Energy transition including net zero analysis, sustainability, climate opportunity (8 letters)
- Remuneration (3 letters)
- Problem gambling (1 letter, and 1 additional letter in August 24)

Engagement

In early 2022, we formalised our introduction letter to Boards. In FY24 it continues to evolve with deeper investment integration.

Engagement	FY23	FY22
Introduction letters	16	8
Meetings arising from introduction letter	9	1
Written replies to introduction letter	10	4
AGM & other letters (e.g. M&A, inquiry submissions, franking)	7	10
AGM issues meetings	12	6
Result meetings	37	27
Other meetings with Directors	1	6
Other meetings with management teams or IR	11	38

We believe voting is a special and legally protected form of engagement, as such we voted on 100% of resolutions in FY23 and FY22. Where we have concerns relating to a particular resolution, we engage with the company Board, this has resulted in resolutions being withdrawn.

How we voted in FY23	FOR	AGAINST	ABSTAIN
Board resolutions	99%	1%	NIL
Shareholder resolutions	18%	82%	NIL

Common issues raised in AGM engagements:

- Long-term incentive lacks alignment to shareholder experience (discussed in 2 engagements)
- Short-term incentive hurdles were not stretching for executives (2 engagements)
- Nominated Director lacked the experience to fill skills shortages previously identified by the Board (2 engagements)
- Appropriateness of the Board’s response to the prior year’s first strike against the Remuneration report (2 engagements)
- Board’s use of discretion in executive remuneration (1 engagement)

Portfolio & partnership snapshot

- In FY23 the MCP Board has one female Director, but no Indigenous, or culturally diverse Directors. Three of five Directors have been on the Board for more than 10 years. This broadly aligns with boutique, privately owned funds management peers.
- Employees were retained using the principles outlined in the Merlon ESG Policy
- We began an initial investigation of our Scope 1& 2 emissions and believe they will be low due to the size and nature of our business. However, this analysis has not yet been completed.

Carbon intensity risk as at 30 June	2023		2022	
	Fund	Benchmark	Fund	Benchmark
Australian Share Income Fund	373	169	445	233
Concentrated Australian Share Fund	424	169	451	233

Source: MSCI ESG Manager

Non-investment ESG activities:

- 2022 UN PRI reporting commenced (completed August 2023)

Climate case study: *Energy system stability: risks, opportunities and the decarbonised future*

- In October 2022 Ben Goodwin analysed the current state of the Australian grid and the global energy supply chain it is supported by, as well as the opportunities and risks on the path to decarbonisation
- This research led to us taking profits in ALD, VEA, WDS, STO, NHC, and WHC

Ben’s full paper is available [here](#).

Priorities for FY24:

- Continued integration of ESG and investment issues in introduction letters to Boards
- Continued meaningful engagement with portfolio companies
- Investigating Task Force on Climate-Related Financial Disclosures (TCFD) compliance for Merlon's own reporting (governance, strategy & risk management), as well as investigating aligning Merlon with the Paris Agreement