RUFFER

Responsible Investment Report

Q1 2021

Contents

Responsible investment at Ruffer	5
Overview of the quarter	6
Stewardship activities	8
Engagement in focus	10
Shifting gears: the transition to electric vehicles	12
About Ruffer	19

Responsible investment at Ruffer

AT RUFFER, WE ARE COMMITTED TO BEING GOOD STEWARDS OF OUR CLIENTS' ASSETS.

To do that, and to generate good investment performance, we have always needed to analyse environmental, social and governance (ESG) issues. They represent both sources of value and investment risks. Fully incorporating these considerations into our investment approach forms an essential part of our responsibility to our clients.

Whether it's climate change or indigenous rights, executive pay or workforce safety, we believe our considered approach helps us make better investment decisions.

To the advantage of our clients' portfolios.
For the benefit of the companies we invest in.
And to the good of the environment and society.

HOW WE DO IT

INTEGRATION

ESG risks and opportunities are considered throughout our investment process

ENGAGEMENT

Directly engaging with companies is a key part of our investment process

VOTING

Equity investing comes with rights and responsibilities

We take this seriously

Ruffer are 'climate neutral'. We are signatories and supporters of

Overview of the quarter

2021 IS A LANDMARK YEAR FOR TACKLING CLIMATE CHANGE. FIVE YEARS ON FROM THE PARIS AGREEMENT, THE 2020 UN EMISSIONS GAP REPORT SHOWED EFFORTS ARE SOME WAY OFF MEETING THE TARGET OF LIMITING THE GLOBAL TEMPERATURE RISE TO 1.5°C.[1]

The 26th United Nations Climate Change Conference (COP26) will take place in Glasgow this November, with the United States the most noteworthy nation due to attend the summit. Just hours after being sworn into the Oval Office, President Joe Biden returned the US to the Paris climate accord. President Biden's ambition is to "rally the rest of the world to meet the threat of climate change". Countries will need to significantly ratchet up their climate policies if we are to stave off the worst effects of global warming, and greater US support could prove vital. We look forward to seeing updated plans of action and the galvanisation of international efforts.

The race to net-zero is also accelerating at the national level. In the UK, the Chancellor of the Exchequer, Rishi Sunak, announced the Bank of England's mandate would change to reflect the UK's commitment to combating climate change.[2] Under the new mandate, the bank's actions and balance sheet expansion will be consistent with the transition to a net-zero economy.

In February, the UK government declared its ambition to become a leading centre of green finance. Based on this decision, and our recent experience of implementing European sustainable finance disclosure regulations, we arranged a meeting with the Financial Conduct Authority (FCA), to discuss the evolution of sustainable finance regulations in the UK. We offered our views on practical

1 UNEP
2 gov.uk

"Countries will need to significantly ratchet up their climate policies if we are to stave off the worst effects of global warming."

implementation and lessons to be learnt: encouraging UK equivalent regulations to both protect consumers, whilst also enabling the investment industry to play an important role in decarbonising the real economy.

Elsewhere, our engagement efforts continue apace and we are pleased to see progress being made by a number of companies in which our clients are invested. Barclays will soon face a shareholder resolution calling for it to align its financing with the Paris agreement,[3] and Royal Dutch Shell strengthened its 2050 net-zero plan.[4] General Motors (GM), the American vehicle manufacturer, announced plans to sell only zero-emission vehicles by 2035 and aims to be carbon neutral by 2040. In accelerating the transition to lower emission vehicles, President Biden issued an executive order to convert the 645,000 strong federal fleet to electric vehicles and install 500,000 EV charging stations.[5] Alex Barnett, Research Director, explores the transition to electric vehicles later in this report.

We submitted our response to the revised UK Stewardship Code in March, and as part of our commitment to addressing climate change issues, we will publish our first Task Force on Climate-related Financial Disclosures (TCFD) report this summer.

3 Bloomberg
4 Royal Dutch Shell
5 White House briefing, Jan 2021

Stewardship activities in brief

COMPANY	SUMMARY
COUNTRYSIDE	A wide-ranging discussion covering stakeholder management through the pandemic, the scaling up of modular housing to reduce greenhouse emissions, as well as the company's capital allocation strategy and remuneration policy.
EQUINOR	A Climate Action 100+ call to review progress made since the joint statement made in 2019, and to discuss forward-looking topics such as capital allocation and remuneration.
KOITO	A discussion covering the company's relationship with its largest shareholder, director independence and board structure and how it has responded to its MSCI ESG rating.
LAND SECURITIES	A discussion on the details of the key environmental, social and governance (ESG) objectives that will replace the current key performance indicators in the annual bonus distribution, as well as changes to the long-term incentive plan to incorporate ESG targets.
NIPPON TELEVISION	A discussion on the company's decision to not pay dividends to foreign shareholders over the 20% ownership threshold, significant shareholder influence and board attendance.
RAKUTEN	A discussion on our support for a three committee board structure and more visibility around remuneration performance targets, the company's financial protection practices and how these are reflected in its ESG rating and data security.

TBS	A discussion on the company's use of a poison pill, as well as the company's significant cross-shareholdings.
TS TECH	A discussion focused on the company's greenhouse gas emissions reduction targets, board structure and its new employee share ownership scheme.
UK FINANCIAL CONDUCT AUTHORITY	A meeting about the development of sustainable finance regulations in the UK. We gave feedback and offered opinion on recent European regulatory change, before discussing the important role asset managers can play in decarbonising the real economy.

Further detail can be found in our Stewardship Activities report, available at ruffer.co.uk/2021-Q1-stewardship

ENGAGEMENT IN FOCUS

COUNTRYSIDE
Places People Love

COUNTRYSIDE PROPERTIES is a leading UK housebuilder.

Meeting with David Howell (Chair of the Board) and Amanda Burton (Chair of the Remuneration Committee).

Issues: Environmental, social and governance – climate change, stakeholder management, board composition and remuneration

WE DISCUSSED HOW THE COMPANY HAD APPROACHED THE CHALLENGES PRESENTED BY THE COVID-19 PANDEMIC OVER THE PAST YEAR.

We were encouraged the company continued supporting its employees during this period, ensuring motivation has remained strong within all business divisions. We spoke about the recent gender pay gap report and pushed the company on why the gap has not meaningfully narrowed. The new CEO, Iain McPherson, is striving to improve diversity at the leadership level and we will continue to monitor the company's progress.

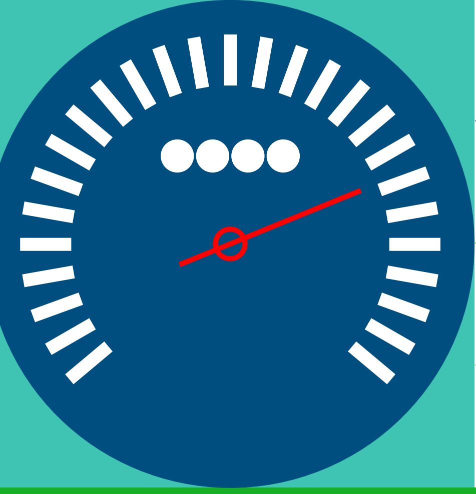
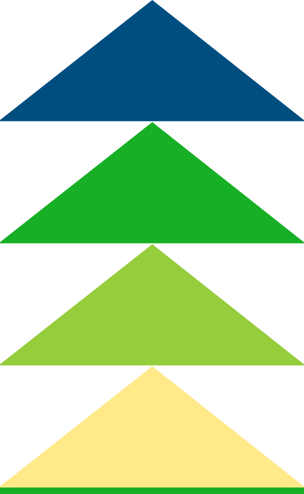
On the topic of climate change, we spoke about the scaling up of modular housing production which significantly reduces greenhouse gas emissions. Given the scale of the reduction needed across the industry, and the increasingly clear government policy on de-carbonisation, the company confirmed it is focusing on achieving emissions reductions.

We also discussed the company's capital allocation strategy. Decisions in this area are critical and will ultimately determine its long-term financial performance. We shared our view that the company would benefit from a non-executive director with a proven track record in capital allocation. Given the changing strategy of the business, significant changes need to be made to the remuneration policy to ensure management is incentivised to deliver on the revised strategy and, importantly, to align their interests with shareholders.

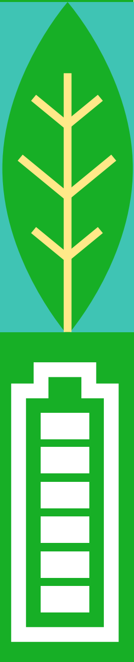
We shared our thoughts around this, including a total shareholder return measure, a meaningful shareholding requirement and ensuring post-cessation and vesting requirements are in line with the guidance from the Investment Association. We attach significant importance to the company's strategy, board composition and executive remuneration as we deem addressing these to be essential for the long-term success of Countryside and all stakeholders.

Whilst we value the engagements with the non-executive directors so far, we have not received acknowledgement our concerns will be addressed. Consequently, we decided to abstain on our votes in relation to the re-election of all non-executive directors.

We will continue to engage ahead of the upcoming remuneration consultation, and we look forward to continuing our discussions.

Shifting gears:
the transition to electric vehicles



Road transport contributes almost an eighth of global greenhouse gas emissions.[1] We have known about the damage caused by our cars and lorries for many years, and that cleaner transport is essential to reduce emissions and limit the damage to our environment. Yet, the rate of adoption of electric vehicles (EVs) has been disappointing over the last two decades. So why is the transition to EVs taking so long?

A SLOW START

The sluggish transition to EVs is in stark contrast to other energy transitions, like solar and wind power, whose adoption has regularly surpassed expectations.

The challenges with EV adoption are manifold. There are technological constraints: batteries are expensive and lack high enough energy density; automaker constraints: long planning periods and resistance to change; and consumer issues: high price points, lack of model choice, autonomy concerns.

OVERCOMING CHALLENGES

These challenges have not vanished, nor will they overnight, but rates of adoption are picking up. Battery costs continue to fall rapidly as the technology matures and the battery manufacturing industry scales up. Innovations including higher density high nickel content batteries, battery pack form factors and improved software for battery management have all contributed to longer range. Hesitancy of the incumbent automakers has been overcome by the rise of disruptors and capital markets penalising the incumbents with low valuations, which has forced them to

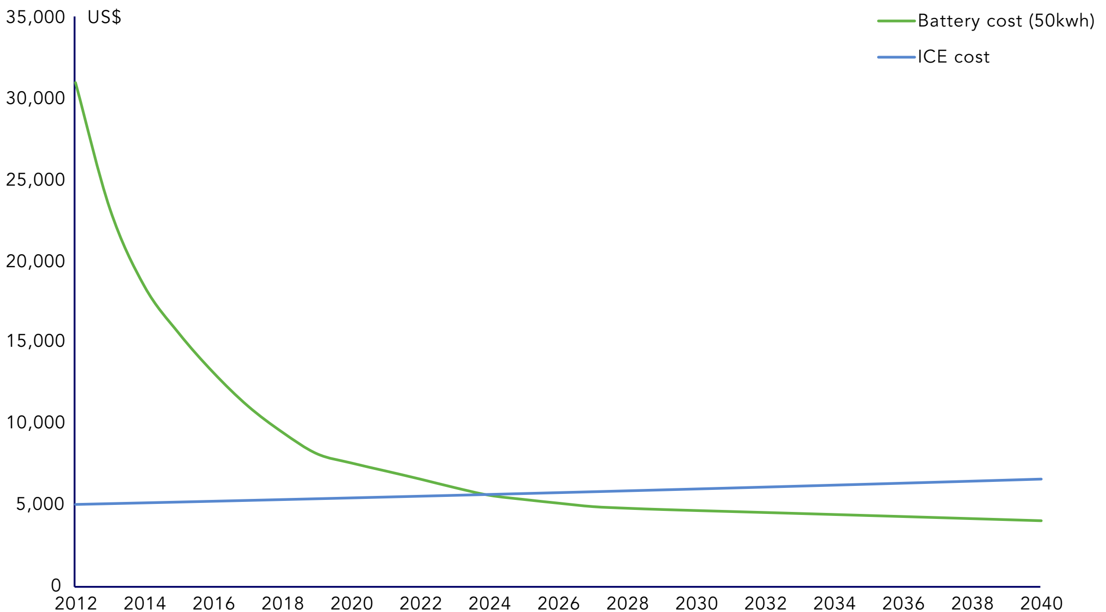
1 Climate Watch

re-evaluate their EV strategies. Numerous automakers have come full circle: from dragging their heels on EVs to the complete phase-out of internal combustion engine (ICE) powered models. Lastly, consumer acceptance of EVs remains an issue, but falling prices and an ever-expanding range of models has increased consumer appetite.

ADOPTION ACCELERATION

In 2015, 0.3% of vehicles sold globally were electric and 0.3% plug-in hybrids. In 2020, those figures had risen to 2.0% and 0.7% respectively.[2] Consensus estimates are that EVs and plug-in hybrids will account for 10% of global auto sales by 2025, with a higher proportion in China and the European Union. By 2030, the proportion is expected to be almost 30%. Experience tells us we should take these forecasts with a pinch of salt, but there is cause for optimism. The conjunction of technological improvements, falling battery costs, motivated automakers, and increasingly assertive regulators makes these targets eminently achievable.

THE COST OF EV BATTERIES IS EXPECTED TO BREAKEVEN WITH INTERNAL COMBUSTION ENGINES IN 2024



Source: CLSA

2 Bernstein, CLSA, Deutsche Bank and BNEF

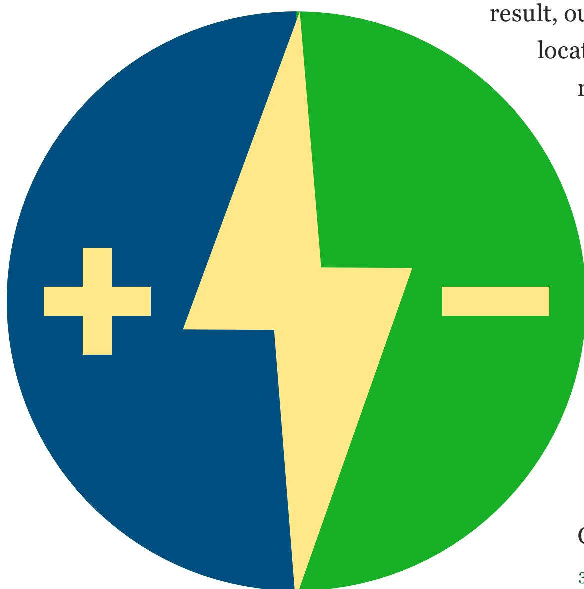
Regulation is a key driver of EV adoption, with national and local regulators seemingly competing with each other to implement a phase-out of ICE cars. Norway is leading the pack, with a planned phase-out by 2025,[3] while the UK has brought forward its target date for an ICE phase-out to 2030 and only zero carbon emission passenger vehicles to be sold from 2035.[4]

Increasing regulatory support, and an inflection in demand has resulted in excitement around the electric vehicle value chain, and much higher valuations for many of the companies involved. This has made finding attractively priced businesses in the sector increasingly difficult, but not impossible.

RUFFER'S EXPOSURE TO ELECTRIC VEHICLES

Ruffer has invested in a broad spectrum of businesses involved in the EV transition: upstream lithium producers, battery manufacturing equipment makers, battery component makers, final battery assemblers, EV semiconductor manufacturers, and automakers. The industry challenge has never been finding growth, but finding businesses with barriers to entry which would allow them to thrive, despite the influx of capital.

While the chemical composition of vehicle batteries is evolving rapidly, and new technologies including solid state batteries are emerging, the use of lithium is a constant for the foreseeable future. While there is no global shortage of lithium resources, low cost and environmentally sustainable deposits are rare. As a result, our holding in Livent, which has quality assets located in Argentina, forms the bedrock of our EV materials exposure.



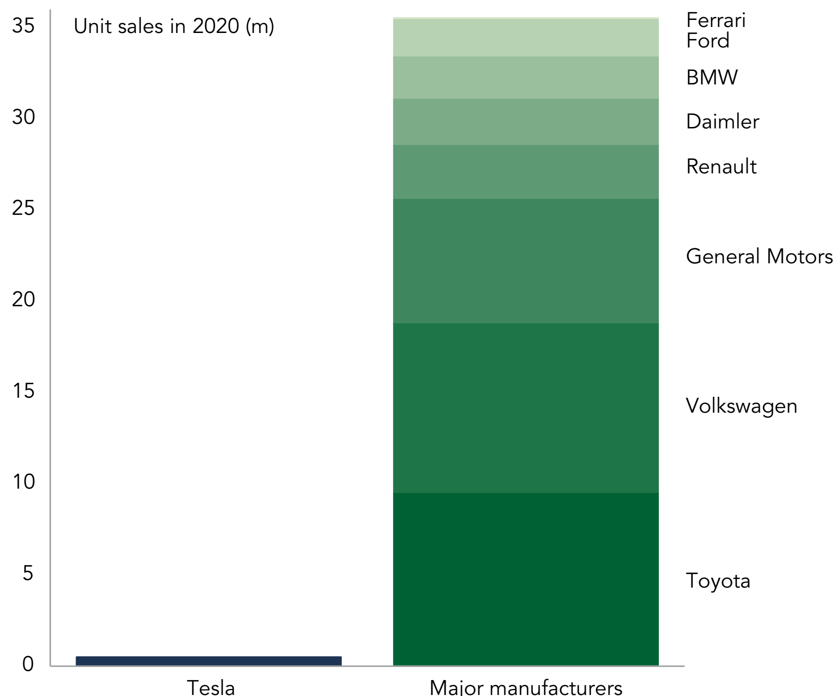
OUT WITH THE OLD?

Investigating the EV supply chain has resulted in some promising investment opportunities for Ruffer. The most undervalued and direct exposure currently comes through the traditional original equipement manufacturer (OEM) automakers. The industry was caught flat-footed by technological change, and equity markets have punished incumbent OEMs over concerns their businesses are being

3 ICCT
4 gov.uk

disrupted and their profit pools dissipating. This has led to a stark polarisation of interest and valuation between new entrants such as Tesla, and traditional OEMs.

GLOBAL VEHICLE DELIVERIES IN 2020



Source: Ruffer, Factset

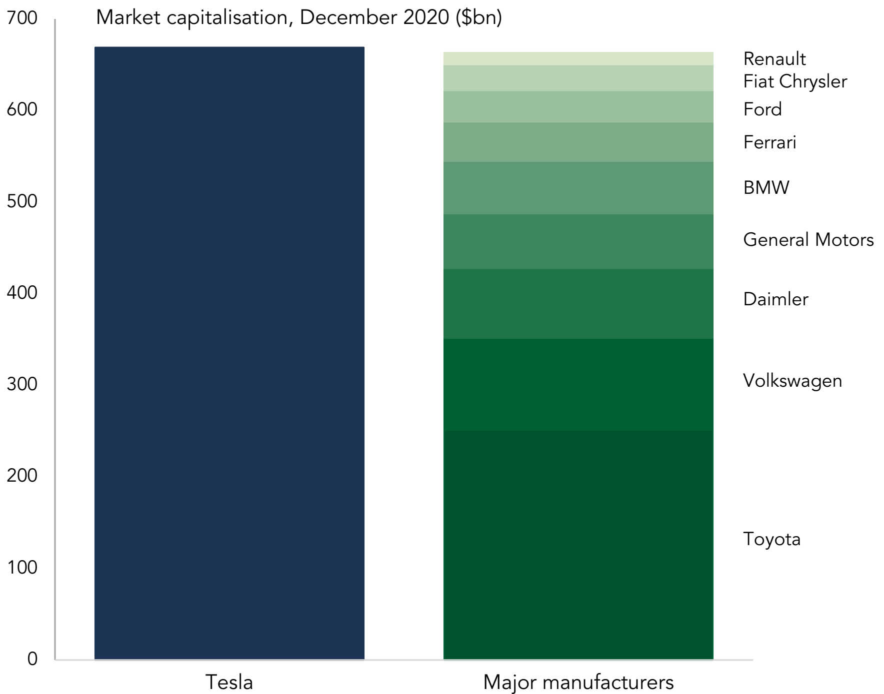
The scale of EV investment taking place within businesses such as Volkswagen (VW) and General Motors (GM) is remarkable, with VW planning to become the global market leader in e-mobility by 2025 and launch 70 different EV models by 2030.

AUTOMAKERS: TODAY'S HORSE-DRAWN CARTS?

At Ruffer, we see considerable value and investment upside in traditional automakers, who come with an entrenched market share, a loyal customer base and deep pockets for significant EV-related investment and development.

Despite significant disruption to supply chains and production processes during the pandemic, these traditional manufacturers were able to rapidly grow EV shipments in 2020, with VW selling

VALUATION



Source: Ruffer, Factset

more EVs than Tesla in the fourth quarter of 2020 in Europe. Crucially, they have been able to do this while maintaining profitability. This supports our view EVs will not be the death knell of the automakers and the investment community have been too pessimistic on their outlook, which in turn creates scope for a re-rating.

VW and GM also have interesting ventures in future mobility: from advanced battery materials to autonomous driving, which suggest they are not the lumbering dinosaurs some would portray them to be. These strategic investments and subsidiaries have great potential: Honda, for example, have announced plans to use GM's Ultium batteries for their next generation of EVs, whilst Microsoft have also teamed up with GM to accelerate Super Cruise, the recently number one rated self-driving technology.[5]

5 Consumer Reports

AT THE WHEEL: ENGAGING WITH AUTOMAKERS

Beyond investing in these businesses for exposure to electric vehicles, we also view meaningful engagement with them on their ESG efforts as indispensable. For VW in particular, we have actively engaged with management on their governance practices and stressed how crucial their EV transition is to the business and to financial markets. From our conversations with company management, it is encouraging to hear the VW Group is not only pursuing an EV focused future, but is already making progress to reduce carbon emissions from the production process as part of its plan to become a 'net-zero' company and meeting the Paris Climate Agreement goals.

Electric vehicles finally coming of age is a watershed moment for the climate and the auto industry. While the excitement has driven pockets of market exuberance, we continue to see interesting opportunities in the theme and expect that to remain the case in the decade to come as the EV wave gains further momentum.

ARE ELECTRIC VEHICLES REALLY BETTER FOR THE ENVIRONMENT?

Three factors raise cause for concern

1. 'Dirty' electricity is used to power 'clean' vehicles.
2. Manufacturing batteries, and the EVs themselves, is more damaging to the environment.
3. EVs weigh more. This increases the energy needed to power them and the tyre particulates they generate.

These are all valid concerns. Driving a heavy (luxury) EV model powered by electricity generated by a coal power plant has little or no environmental benefit. However, life cycle emissions of an EV are estimated to be 65% lower than an ICE in the US and a similar level in the UK . Importantly, as electricity generation becomes cleaner over time and EV production matures, the benefits will increase as they have done over the last decade.

ALEX BARNETT

Research Director

About Ruffer

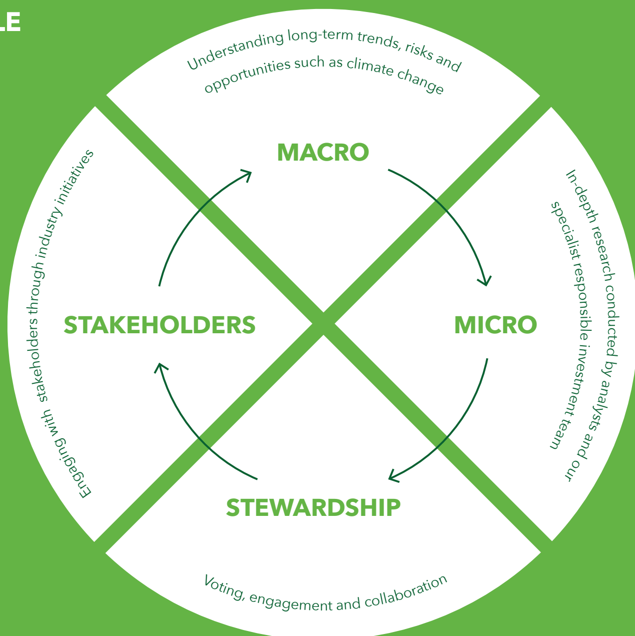
OUR AIM IS TO DELIVER GOOD POSITIVE RETURNS – WHATEVER HAPPENS IN FINANCIAL MARKETS.

To invest well, we need to take on risk. With risk comes great responsibility. Our preoccupation is with not losing money, rather than charging headlong for growth. It's by putting safety first that we have made good money for our clients. Through boom and bust. For over 25 years. If we keep doing our job well, we will protect our clients' capital – and increase its real value substantially.

We believe that investing responsibly will lead to better long-term outcomes for our clients.

Our decision to invest in companies is based on both fundamental and ESG analysis. As part of the investment process, our responsible investment team partner closely with the analysts in our research team to identify and evaluate the impacts a company's operations could have on the environment and society. Likewise, the risks associated with weak corporate governance practices are evaluated. To fulfil our duty to act as responsible stewards of our clients' assets, we use our judgement to determine when to engage and how to vote at shareholder meetings to best protect the economic interests of our clients, while remaining cognisant of the impact on all stakeholders. Engagement with the companies we invest in not only gives us an opportunity to deepen our understanding of the business, but it is also an effective tool to achieve meaningful change.

OUR RESPONSIBLE INVESTMENT FRAMEWORK



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