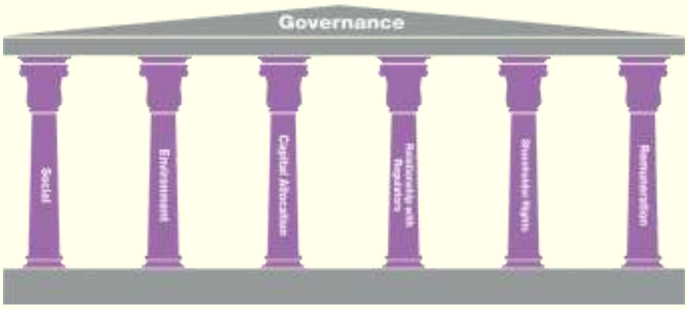
Corporate Governance: Autumn 2014 review

What do we mean by corporate governance? Governance refers to the people behind the companies and the values, time horizons, relationships and attitudes which are integral to the decisions they make. These decisions influence not just environmental and social performance but capital allocation, remuneration structures, relationships with external stakeholders and attitudes towards minority shareholders. Each of these 'pillars' should not be considered in isolation or without understanding the relevant governance structures.

Management are critical. There are obviously many internal and external factors that feed into the growth and success of a company, but over a five to ten year time horizon, the decisions that management make will be very influential. Assessing management is not simple and we have many conversations about how we analyse and measure executive quality. Within our ten question research framework, we specifically ask about the calibre of the management team and in question eight, we ask ourselves about management attitudes to capital allocation. Ultimately, actions speak louder than words. We like to maintain an open dialogue with your holdings in order to gain a better understanding of the business and to facilitate investigation should we have cause to question decisions at any point in the future.



Amazon always gets in touch following their AGM to ensure we have no concerns. We don't, but their call does offer the opportunity to discuss any issues raised at the AGM and follow-up on previous conversations. On this occasion we touched on a number of broad matters including governance structure, the flow of information between executives and non-executives, tax policy and warehouse working conditions. The company acknowledges the need to manage these issues and specifically in relation to the recent tax issue, improve government relations.

Remuneration has been the topic for recent debate with both Burberry and Tesla. We abstained on the remuneration policy and supported the associated report at the 2014 Burberry AGM. This report containing details of CEO Christopher Bailey's one-off award of shares last year (worth nearly £15 million) was voted down with 53% voting against. Whilst we are generally opposed to the one-off awards, we did not want to vote against Bailey's first remuneration report; we would like to maintain the productive working relationship we have worked hard to achieve. The repercussions of the (non-binding) no vote, one of the biggest-ever protests staged by shareholders against boardroom pay, will need to be addressed by the board. We will continue our dialogue with the company on this matter and hope to address our concerns regarding the level of flexibility and discretion written into the company's new remuneration policy.

At Tesla's AGM, we abstained on remuneration as the company includes a re-pricing provision within its long-term incentive plan. This policy has never been used and is unlikely to be used in the future given the share price relative to the exercise price of outstanding options. Nonetheless, re-pricing is a very poor pay practice and we could not support the policy. We have subsequently met with the company and the remuneration committee is aware of our objection to the option re-pricing clause and whilst they couldn't say more at this stage, there is the possibility of removing it in the future.

In the Spring Review, it was eBay in the spotlight with regards to their remuneration policies. Since then we have had lengthy discussions with management about the PayPal business. Activist investor, Carl Icahn has been very vocal about the benefits of a PayPal spin-off, but management were in the 'better together' camp. We took a call with Mr Icahn and whilst we agreed with many of his points; we have been concerned about the management of PayPal and disappointed by the core business, we chose to direct our concerns to management rather than the press. We have been in frequent contact with eBay throughout the summer and following the departure of PayPal's CEO, David Marcus, we had a particularly frank discussion. In essence, our initial concerns have grown. In order to retain meaningful share of this market, we believe innovation and the desire to disrupt should be inherent in the business culture and this appears to be lacking. PayPal remains interesting but we feel there are too many questions around the future growth of eBay itself and after almost ten years as a shareholder, we have advised the company of our decision to sell.

The Puma Ocean Racing boat competing in the Volvo Ocean Race in 2012.

Away from the AGMs, we have had several interesting meetings with the management teams of the companies in your portfolio. Kering has an interesting stable of luxury brands with notable success in nurturing their international expansion. It has been a niggling concern for the LTGG team that this luxury portfolio sits uncomfortably alongside the sports and leisure division which includes their 2007 acquisition, Puma. Management have been less successful in the execution of the Puma strategy but they are firm in their belief that it still has a place within the group structure and remain optimistic about its future. Puma's new CEO, Bjorn Gulden, is focusing on four core categories and a few new exciting areas such as sailing which he believes, along with the €70 million brand re-launch, will rejuvenate the business and make 12% operating margins achievable. Furthermore, CEO Monsieur Pinault maintains that the sportswear division brings balance to the group. We still have our doubts, being number three in the sportswear market is tough; we will engage more vociferously and hold them to their 12% operating margin target.

In a recent call with Whole Foods Market, the management team acknowledged that the recent share price weakness had a lot to do with the increased competition from mainstream supermarkets which are making more of a concerted effort in the organic/healthy eating area. The increased competition does put additional pressure on WFM. However, the big picture remains attractive and the category should have good growth potential as consumers place more emphasis on provenance and healthy eating. In addition to competition, which we believe is manageable, it is the market's emphasis on quarterly guidance which has exaggerated the movement in the share price. We do acknowledge that the company will need to redouble their efforts to remain differentiated from its competitors. Indeed store growth will need to be managed carefully and the location of new openings will likely be key to returns; if the new areas are just less appealing then WFM may not enjoy the same returns profile of its current mature store base. We will be visiting the company's headquarters later in the year and will continue our dialogue with management on these matters. But, perhaps more importantly we will reiterate our advice to end quarterly guidance at a suitable time.

Corporate governance is at the core of our investment decisions. Our task involves understanding the culture of a business as being long-term, multi-generational and nuanced; our approach tries to be practical, logical and holistic. We hope this comes through in our reporting; should you wish for further information on our corporate governance policies and procedures, please visit our website or speak to your client contact.

Voting Activity

Votes Cast in Favour		Votes Cast Against		Votes Abstained/Withheld	
Companies	5	Companies	1	Companies	2
Resolutions	56	Resolutions	3	Resolutions	4

Company engagement remains a key component of our investment process

In this quarter, after a busy proxy voting season, the Corporate Governance Team has focused on more qualitative research

The investors have met several management teams over the period and a number of these meetings are detailed earlier in this report

Firmwide Company Engagement

Please refer to Corporate Governance Autumn 2014 Review for comments on engagement

Votes Cast in Favour

Companies	Voting Rationale
Burberry, Ctrip.com ADR, HDFC, Inditex, Stratasys	We voted in favour of routine proposals at the aforementioned meeting(s).

Votes Cast Against

Company	Meeting Details	Resolution(s)	Voting Rationale
Stratasys	Annual 10/07/14	5A-5C	We opposed the request to approve stock option awards to three non-executive directors given the Long-term Incentive Plan permits repricing. We do no believe this is in shareholders' best interests.

Votes Abstained

Company	Meeting Details	Resolution(s)	Voting Rationale
Burberry	AGM 11/07/14	2	We abstained on the resolution to approve the Remuneration Policy because it allows a significant flexibility with regards future one-off awards. The company has used these in the past.
Stratasys	Annual 10/07/14	2-4	We abstained on the request to approve cash bonuses to three executives given the lack of disclosure on performance objectives and their discretionary nature. We will engage with the company to ascertain greater insight into their calculation.

Votes Withheld

We did not withhold on any resolutions during the period.