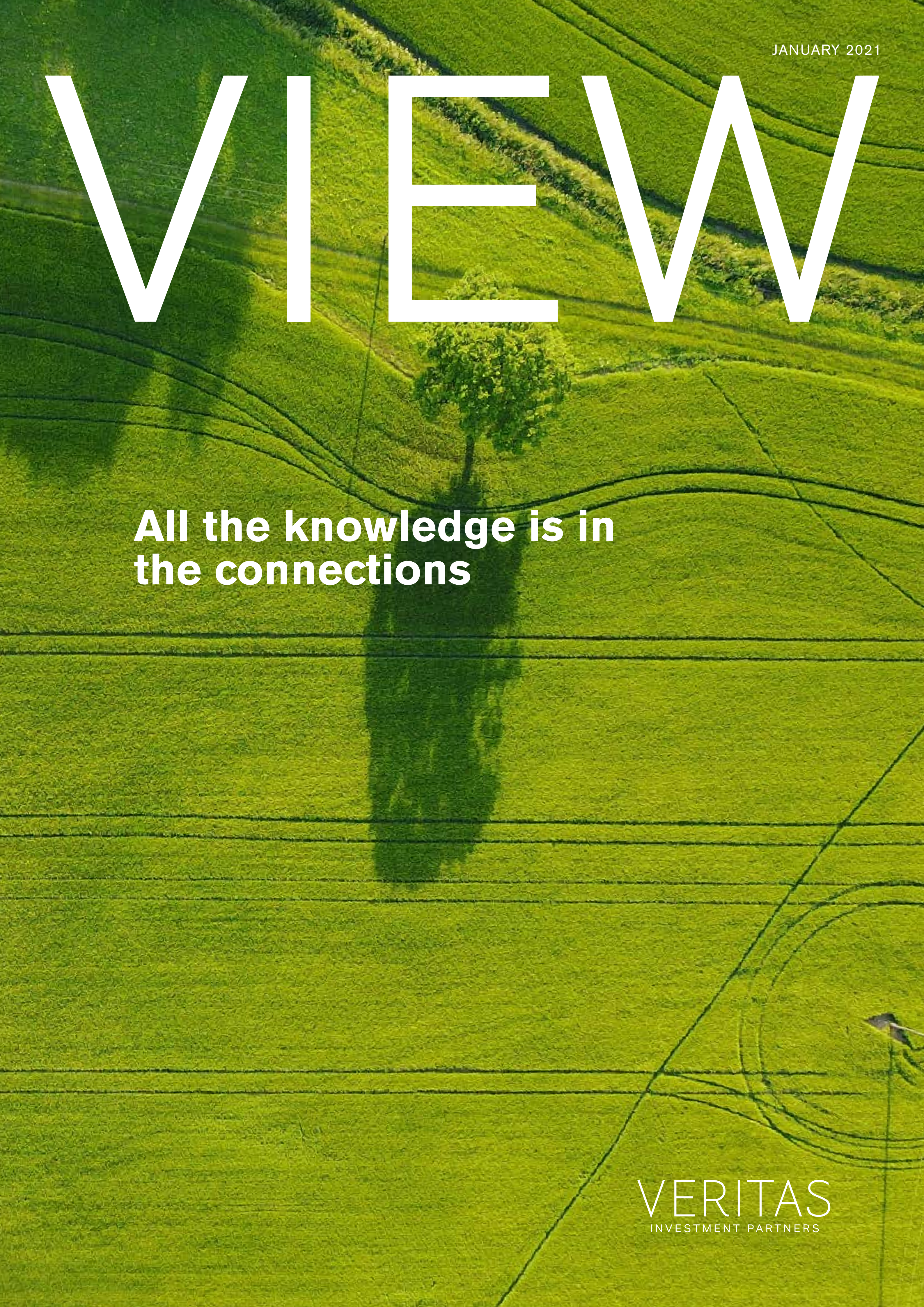
JANUARY 2021

VIEW



All the knowledge is in the connections

VERITAS
INVESTMENT PARTNERS

ARE WE NEARLY THERE YET?

Anyone waking up to an Xbox console under the Christmas tree this year is now the proud owner of the world's most powerful computer from the year 2000[1]. The last 20 years have seen huge developments in technology and computing power, which when applied to science are having extraordinary results. A project to sequence the human genome by 2000 cost billions of dollars; today, a full sequence costs as little as $200[2].

Technology and sequencing have also played a crucial role in the development of the Covid-19 vaccines, contributing to the accelerated speed of development which sets the vaccines apart from their predecessors. In 1921, the first dose of the BCG vaccine against tuberculosis was given to a human 13 years after work started to develop it[3]. It would take a further three years for mass production to begin. Almost 100 years later, and the Covid-19 vaccines have sped through the design process to mass roll-out in under a year. Once the genetic information of the virus had been sequenced and published, Pfizer/BioNTech had manufactured its first candidate vaccine after 42 days and injected it into a patient after only 63 days[4].

Are we nearly there yet?

With vaccines bringing hope that lockdowns may soon be a thing of the past, attention is turning to the year ahead as we all wonder: what comes next? Sadly, we cannot wave goodbye to the legacy of 2020 just yet as many unresolved issues remain high on investors' agendas, such as the increased levels of unemployment, which have led to record levels of government debt. The Fed, ECB, BoJ and BoE own financial assets that now equal 54.3% of their countries' combined GDP. In 2018, that figure was 10%[5]. But rather than dwelling on the negatives and trying to predict the range of macroeconomic outcomes that may (or may not) be around the corner, we are looking ahead to the positive trends that will outlive the pandemic.

The "tech-celeration" across every sector shows no sign of abating. This was of course up and running long before the pandemic and we have discussed before how it reached breakneck speed over the last year. For example, in the six weeks to 24 April, there was a 70% increase in the number of UK companies opening websites compared with the preceding six weeks[6].

The need for investment will continue in the months and years ahead. As **Microsoft** CEO Satya Nadella said: "*the next decade of economic performance for every business will be defined by the speed of their digital transformation*"[7]. Those that do not keep up may quickly find themselves left behind, by both changing consumer behaviour (across developed nations, of those that tried online shopping for the first time during the pandemic, around 75% said they plan to continue shopping online[8]) and the pace of development in the underlying technology itself. "Huang's Law" describes how silicon chips that power artificial intelligence more than double in performance every two years[9]. The specific speed is being hotly debated by computer scientists but one thing they all agree on is that it is increasing rapidly. The potential implications are far reaching and are as difficult for us to imagine as it would have been for a scientist in 1921 to imagine the Xbox. Companies which help others make sense of this new world will be well-placed. In its latest results, consultancy firm **Accenture** reported that it is no longer just Chief Technology Officers that are spending on IT driving strong growth in its digital, cloud and cyber-security businesses.

The rapid development of vaccines has shown the compounding benefit of investing over the long term: without the technological advances over the past decades, chances are we would still be waiting for a vaccine. We have long made the case that the same is true for companies. Those that have made innovation part of 'business as usual' will be best placed in times of difficulty. **Roche** has been one of the top spenders on research and development in the healthcare sector since 2005 and as non-urgent medical care took a

1. https://news.xbox.com/en-us/2020/0 16/xbox-series-x-tech/.
2. The Economist Espresso via Email, 23 December 2020
3. https://www.ncbi.nlm.nih.gov/pmc/articles/PMC3749764/
4. https://thedailyguardian.com/how-covid-19-vaccine-could-develop-so-quickly/
5. JP Morgan "2020 in Numbers – When History is not a Guide"
6. https://www.theguardian.com/technology/2020/may/25/pizzas-in-the-post-shopify-challenges-amazon-for-slice-of-lockdown-trade.
7. https://news.microsoft.com/en-in/culture-of-innovation-key-economic-recovery-and-resilience-rajiv-sodhi/
8. https://www.wsj.com/articles/huangs-law-is-the-new-moores-law-and-explains-why-nvidia-wants-arm-11600488001
9. https://www.wsj.com/articles/huangs-law-is-the-new-moores-law-and-explains-why-nvidia-wants-arm-11600488001

backseat during 2020, the company was able to offset a reduction in standard diagnostics tests with testing products for Covid-19 that did not exist in January this year[10]. In an industry that really has been turned on its head by the pandemic, freight forwarder **Kuehne + Nagel**'s investment in IT infrastructure has enabled it to gain market share and increase its lead over competitors.

All the knowledge is in the connections[11]

The tremendous advances in technology only tell one side of the vaccine story. None of the developments would have been possible without brilliant scientists and willing volunteers proving that, in successful projects, the human connections are often as important as the technological ones. This recognition is another trend that has been pushed into the limelight during the past year. Many businesses recognise that, in addition to the investments they have made in technology, it is their people that are giving them a competitive edge.

Turning back to **Accenture**, a big part of its strength lies in its people and the company puts a great deal of effort into attracting and retaining its employees. The firm has been recognised on Fortune's 100 "Best Companies to Work For" list for eleven consecutive years[12]. US retailer Tractor Supply has made significant investments in its data platforms so it can tailor products to match customers' needs but on a recent call, the CEO spent more time discussing the importance of culture and the benefits gained from looking after staff well during the past year. Meanwhile, manufacturer of connectors and sensors **Amphenol** has some of the best technology in its industry but again, its CEO knows that it's the employees that are the real asset: "*most companies run themselves by a system... we run ourselves by a culture*"[13].

This focus on people extends far beyond the boundaries of individual companies as attention turns to the impact companies have on all their stakeholders, not just shareholders. This principle is a central factor in our stewardship work which we discuss in the accompanying report. In a similar vein, governments are starting to question the value of GDP as a measure of success, given its focus is purely financial. Scotland, Iceland and New Zealand have signed up to the Wellbeing Economy Governments partnership which targets ecological and human well-being as well as economic growth and they are already in discussion about budgeting and tourism through this new framework[14].

In the middle of difficulty lies opportunity[15]

As with the vaccines, some companies are using the connections between technology, data and people to solve some of society's biggest problems. "*It may not seem so at first, but all of this data can be valuable for us*." These are the words of the Vice President of Applied Advanced Analytics at dialysis company **Fresenius Medical Care**. In addition to traditional healthcare data, such as that from more than 1.9 million dialysis patients and 1.7 billion laboratory tests, the company is using weather forecasts, demographic data and traffic data[16] to improve treatment for people with kidney disease (by ensuring dialysis appointments do not clash with important baseball games, or an incoming blizzard).

This is just one example of the vast changes taking place across the healthcare sector. The combination of innovative technology, data and people is coming into its own and leading to positive change, both in the delivery of care and in making better clinical decisions.

Continued overleaf.

10. https://www.roche.com/investors/updates/inv-update-2020-07-23.htm
11. David Rumelhart, American psychologist and computer scientist
12. https://www.accenture.com/bg-en/company-recognition-great-employer
13. https://podcasts.apple.com/gb/podcast/the-interface/id1474539157?i=1000449631569
14. https://www.ted.com/talks/mike_o_sullivan_the_end_of_globalization_and_the_beginning_of_something_new/transcript
15. Albert Einstein
16. https://www.freseniusmedicalcare.com/en/healthcare-professionals/renal-it/therapy-data-management-system-tdms/

The pandemic starkly highlighted the cracks in healthcare systems and the impact of social factors on health outcomes. Technology and data are key to addressing this and to shifting the entire healthcare sector from a *reactive* one, where people are treated when they are sick, to a *proactive* one that focuses on trying to keep people well. Insurance provider **UnitedHealth** is a leader in this field: its Level2 digital therapeutic programme, which supports type-2 diabetics by combining medical technology and virtual coaching, saw 50% of patients achieve a reduction in medicine use.

It is not just the healthcare sector where technology and data are improving lives. Information services company **Experian** is using its industry-leading data depository and analytics tools to improve financial inclusion and economic opportunities for all. In education, online learning can be a useful substitute for face-to-face learning (as recent lockdowns have proved) and can provide education for those who may otherwise be unable to access it. **Alphabet**'s Google Classroom currently has 100 million users around the world[17] and **Microsoft**'s LinkedIn Learning education platform is connecting people to provide retraining opportunities for those affected by the unemployment crisis[18].

But it is worth remembering that the relationship between technology, data and people is not always plain sailing. We have previously highlighted the risks that some jobs and sectors face from automation and these have not gone away. Similarly, big questions remain about the use of data and privacy and these are unlikely to be settled any time soon. Such risks remind us of the importance of our valuation discipline and not getting carried away with the opportunities.

On to the next…

The world still faces many problems beyond the pandemic that would benefit from the combination of technology, data, and people. The race against climate change is a case in point: the COP26 talks later this year will require the best of diplomacy if they are to stand a chance of making any progress. At the same time, we need innovation in technology to reduce carbon emissions. This logic could be applied to other issues that will soon require global attention, such as antibiotic resistance and the need to feed a rapidly growing global population. These are areas where we continue to look for investment ideas, but we do not want to compromise our quality of business and track record requirements or diverge from our valuation discipline.

As we look to the year ahead for our own business, again we are focusing on the opportunities. The team has done a brilliant job, maintaining our culture of curiosity, openness and collaboration in these challenging times. We are particularly grateful to our superb support and administrative colleagues who allow us to remain focused on your investments. We are incredibly excited to be moving to our new office at Riverside House and to rekindle face-to-face connections with you and with each other. But whether we are working remotely or all together, one trend that will never change at Veritas is our focus on delivering returns ahead of inflation for our clients.

17. https://www.bloomberg.com/news/articles/2020-04-09/google-widens-lead-in-education-market-as-students-rush-online
18. https://www.linkedin.com/learning/

STEWARDSHIP REPORT 2020

We are delighted to share our latest annual stewardship report with you. We hope that the engagement and voting examples below will bring our stewardship activities to life and show our four stewardship principles in action.

Engaging with companies has long been an integral part of our investment process and has continued despite the restrictions imposed as a result of the pandemic. In fact, we would argue that during these turbulent times, building long-term and constructive partnerships with our investee companies has become even more important. During 2020, we had over 100 meetings with companies. The majority of these were with companies in which we invest but some were part of our broader investment research.

For more information on our stewardship processes, please read our Engagement and Voting policies which are available on our website, alongside our statement of compliance to the UK Stewardship code and our latest Assessment Report from the Principles of Responsible Investing (PRI).

COMPANY ENGAGEMENT
Principle 1 *– An aversion to box ticking: our focused investment approach enables us to fully understand the material risks to each business.*

Much of our engagement work this year has focused on encouraging broader and clearer disclosure, particularly on environmental and social factors. Despite all the attention given to climate-related issues, many companies, particularly those based in the US, are still not publishing transparent data. Recent analysis by Bloomberg found that over 100 of America's largest public companies on the S&P 500 did not disclose adequate environmental data this year[19].

However, we fully acknowledge that navigating this territory is tricky. There are many ESG reporting frameworks and standards and without armies of reporting staff, no company can possibly respond to them all. We therefore encourage our investee companies to focus on identifying and managing the most material sustainability risks they face. This means that companies can concentrate on what is relevant to them, rather than on issues that may not have as much impact on the long-term durability of their business.

For example, this year we began a dialogue with healthcare technology company Cerner about the most appropriate metrics for the company to disclose. For a healthcare technology company, the most material sustainability risks include energy management, consumer privacy, data security, and employee engagement, diversity and inclusion. We believe this will provide a solid framework, not only for disclosure, but for **Cerner**'s on-going work on establishing long-term objective targets.

Taking a case-by-case approach also informed our conversation with **Microsoft**. As a very large technology company, Microsoft's environmental impact could be significant. But with the launch of its ambitious climate targets earlier in the year[20], we chose to focus on issues that could represent a material risk to the company but are less widely reported: its approach to data security and privacy, and its policies on employee rights throughout its supply chain. During the call we were reassured on all issues and were reminded that when it comes to protecting customer data, Microsoft has an advantage over some of its "big tech" peers: because customers pay for its products, it does not need to rely on monetising customer data to the same extent as other tech companies do.

Continued overleaf.

19. https://www.bloomberg.com/graphics/2020-company-emissions-pledges/?srnd=premium-europe

20. Microsoft has pledged to be carbon negative by 2030, and by 2050 to remove from the environment all the carbon the company has emitted either directly or by electrical consumption since it was founded in 1975 https://blogs.microsoft.com/blog/2020/01/16/microsoft-will-be-carbon-negative-by-2030/

***Principle 2** - A focus on all stakeholders: we recognise that businesses exist within society and therefore have a duty to all stakeholders, not just shareholders.*

We have long believed that companies do not have to choose between doing good and doing well and this has been demonstrated by many companies, including Unilever, over the past decade.

During the last year, we have been actively encouraging companies to include non-financial/ sustainability goals in their remuneration packages to ensure management is as committed to delivering these targets as typical financial ones. This, of course, fits well with our preference for management teams with appropriate long-term incentives, recognising that financial and non-financial performance are closely linked, and it is an issue in which regulators are increasingly interested. For example, in France, it is already a requirement for companies to include environmental and social factors in remuneration schemes. Several companies in our portfolios[21] already include non-financial goals in remuneration packages, in some cases at both executive level and throughout the business.

When we have raised the issue with companies, several have asked for our input on metrics to include, including **Align Technology** and **Hasbro**.

***Principle 3** – A culture of partnership with management teams: we recognise and value progress in pursuit of long-term sustainability.*

With any interaction, our goal is always to work with companies and to encourage improvement over the long term. This starts with the introductory letter we send to companies when we first become shareholders and extends throughout our relationship with them, from how we vote to how we engage with management. We recognise that companies are on a journey and that it can take time for our engagement work to yield results.

In January, **Experian** asked for our views on its non-financial reporting. Some of Experian's ESG characteristics are excellent: improving social inclusion by enabling access to finance (important pillars of the UN Sustainable Development Goals) is at the heart of its business. However, while the company has long been aware of the environmental challenges it faces, reporting of these issues and the setting of clear targets was falling short of best practice. Because of our long-term relationship with the company, we were able to have an open and honest discussion explaining which parts of the company's disclosure we liked, where we thought there was room for expansion and, importantly, why the management and disclosure of these issues is integral to the long-term success of the business. In September, the company told us it had taken on board investor recommendations and has introduced a new goal to reach net zero emissions by 2030, and is reporting carbon emissions in line with TCFD recommendations[22]. While there are still improvements to be made, we are delighted with this progress.

***Principle 4** – We are prepared to vote with our feet: if we identify a risk to a business's long-term viability, we will sell.*

Of course, building relationships is all well and good, but our fundamental aim remains to deliver real returns for our clients. Should any of these meetings lead us to believe that the investment case for a company has changed, such that our clients' capital is at risk, then we would vote with our feet and sell the shares. During this year, none of our engagements led us to take such action.

21. These include Avery Dennison, Fresenius Medical Care, Microsoft, Novartis and Unilever

22. TCFD stands for Taskforce for Climate-related Financial Disclosures https://www.fsb-tcfd.org/

VOTING ACTIVITIES

We continue to believe shareholder voting is an important way of communicating with companies.

In line with our principle of focusing on materiality, each voting decision is taken on a case-by-case basis by our investment managers, based on independent judgement, analysis, and the outcome of engagements with companies. As we aim to only invest in well-run companies which have strong management teams and governance structures, we typically expect to vote with the board recommendations. Further, we consider ourselves active, rather than activist, shareholders and hope there will never be a time when we need to report multiple examples of voting against companies. That said, there have been cases this year when we felt it necessary to vote against certain proposals.

When we do vote against proposals, we always write to the company to explain our decision and hopefully start a dialogue.

Issue case study – auditor tenure

Once again, several of our abstentions have centred on the issue of auditor tenure. We take our responsibility for auditor appointment seriously, especially given several recent high-profile failures, most notably the recent issues with Wirecard in Germany. Best practice in Europe is to re-tender after 10 years and change auditor firm every 20 years. However, in the US indefinite tenure is common and we have been speaking to some of our US companies to understand

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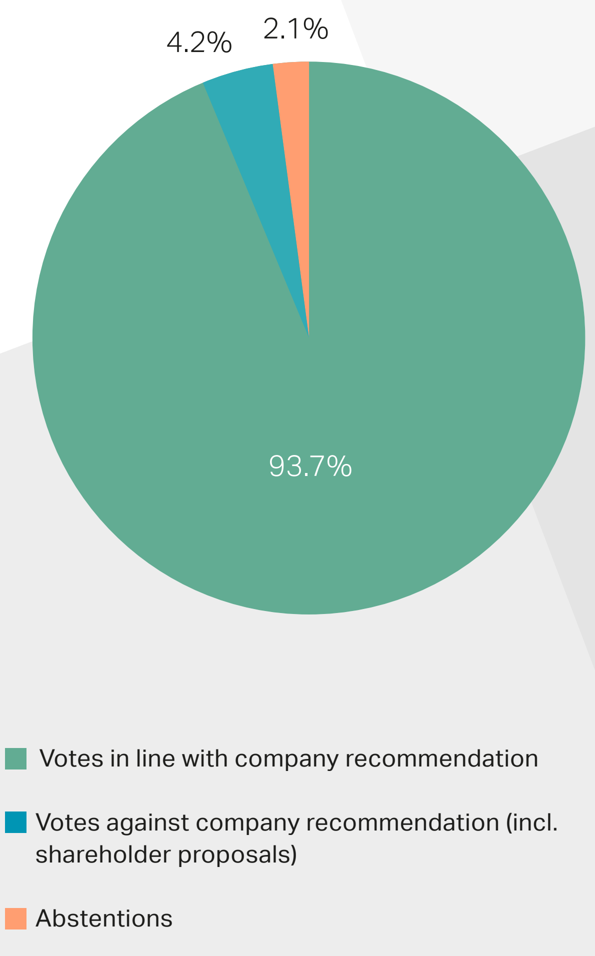
Overall voting record



Votes against companies & abstentions by theme

Fig 1.

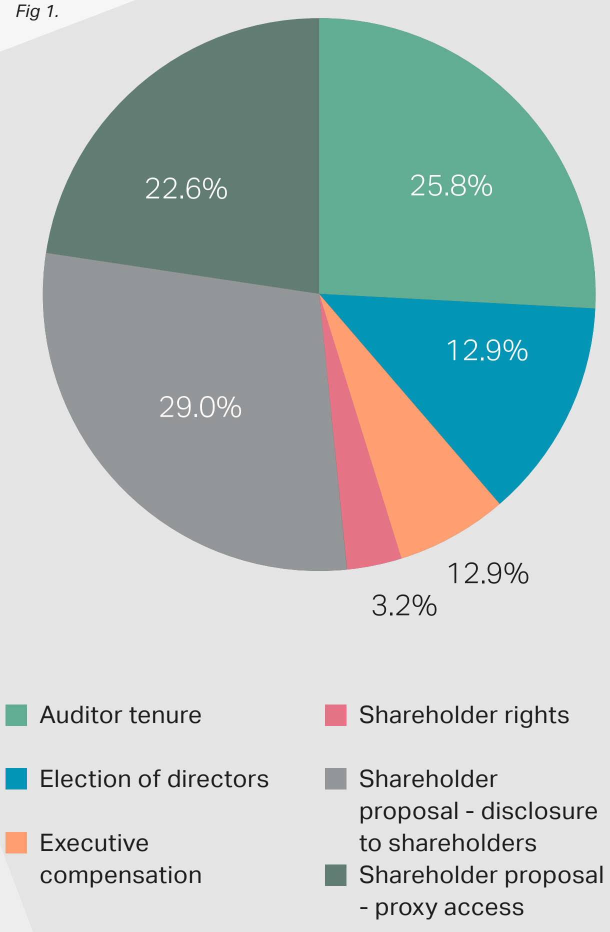


Fig 1. Veritas Investment Partners (UK) Limited

their reluctance to change audit firm and to ensure that, as far as possible, other safeguards are in place.

One such company is **ADP (Automatic Data Processing)**. While overall ADP's governance arrangements are strong, long auditor tenure was one of the topics we raised in our introductory letter when we first became shareholders in March. We were pleased that this letter not only led to a call with the Investor Relations team and the Assistant Corporate Secretary but was also discussed by the Audit Committee. The Committee ultimately decided not to put the audit out to tender, but the Chair offered us a call to explain the decision. She ran through the checks and balances they use to ensure the quality of the audit work remains high, such as carrying out an annual appraisal of the audit firm using a detailed scorecard and obtaining independent audit quality oversight by the PCAOB (The Public Company Accounting Oversight Board).

We had a similar meeting with the Chair of the Audit Committee at **Avery Dennison** and discussed the issue with management at several other companies. While in each case, they provided some reassurance that the Audit Committees are very aware of the issues and have appropriate mitigating controls in place, we still disagree on principle with the reappointment of long-tenured auditors and so chose to abstain on these votes.

Issue case study – shareholder proposals on proxy access

When it comes to shareholder proposals, we take the same approach as we do to company proposals: decisions are taken on a case-by-case basis particularly as voting for shareholder proposals often means voting against company management. Shareholder proposals we supported this year at the AGM's of **Amphenol** and **LabCorp** amongst others requested a change in the share ownership threshold needed to call a special meeting. This is another area in which there is a stark difference between practices in Europe and in the US. In Europe, usually only a 5% holding is required to call a special meeting whereas in the US shareholders often cannot call special meetings at all or the ownership threshold is high (usually 25% or more). For some of the largest companies, this means needing to hold billions of dollars-worth of shares to be able to call a meeting. The rights in Europe generally do not result in multiple extra meetings and as the proposals were calling for the threshold to be dropped to 10-15% (still a higher threshold than in Europe), we chose to support measures that potentially give shareholders greater rights.

Written by **Philippa Bliss** and **Catriona Hoare**
on behalf of the Investment Team

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