

ACTIVE VIEWPOINT

MARTIN CURRIE AUSTRALIA



MARTIN CURRIE

Mitigating the risk of modern slavery in Australian companies

AUGUST 2021 FOR INSTITUTIONAL, PROFESSIONAL AND WHOLESALE INVESTORS ONLY



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With the Modern Slavery Act reporting requirements for most Australian companies now in place, the Martin Currie Australia (MCA) investment team delved deeply into the Modern Slavery risk policies of the Australian listed companies, reviewed the actual actions each company is taking to mitigate the risk, and have provided feedback on best practices through ongoing engagement.

“ Modern Slavery remains unacceptably pervasive – including in a developed and lower risk country like Australia. ”

MODERN SLAVERY - AN EXTENSION OF OUR EXISTING ESG FOCUS

The Modern Slavery Act reporting requirements for most Australian companies are now in place. Martin Currie Australia (MCA) have been working closely on the topic of risk mitigation with all companies in our Australian investment universe.

As a firm that invests almost A\$10 billion in Australian corporates (as of 30 June 2021), Martin Currie have long recognised the risks presented by Modern Slavery, and that we have a responsibility to our clients to ensure the companies that we invest in are not engaging in any aspects of Modern Slavery.

As part of our evaluation of companies for investment, we have ongoing engagements with company management and boards on a range of ESG issues, and Modern Slavery has become a particular focus in our discussions over the last few years.

This recognises that the approach companies take to Modern Slavery risk is also a good indication of a company's overarching culture and policies around other Social and Governance issues such as underpayment of workers and substandard working conditions.

Modern Slavery remains unacceptably pervasive – including in a developed and lower risk country like Australia. Australian supply chains weave through the highest risk region in the world, and therefore Australian companies and consumers must be particularly aware of the existence and risk of Modern Slavery.

Seasonal labour use in the agriculture industry, third-party labour hire and the provision of services (e.g. banking-finance) to the adult industry are several domestic examples of high-risk supply chain exposures. These exposures touch the supply chains of several large Australian companies including supermarkets, the banks and the many companies that use third-party labour hire in some form.

Marine services (indentured and forced labour risks), computer & digital equipment sourcing (conflict minerals and child and/or forced labour risks) and medical equipment and supplies sourcing (cotton sourcing and child and/or forced labour risks) are other examples of higher risk in offshore supply chains for Australian companies – and these lists are not intended to be exhaustive.

ACCORDING TO THE WALK FREE FOUNDATION'S GLOBAL SLAVERY INDEX¹

- Over 40 million people were estimated to be in modern slavery.
- The Asia Pacific is one of the highest risk regions.
- Moderate risk countries include some of Australia's top 10 import trading partners.
- Even in a low-risk country like Australia; an estimated 15,000 people are enslaved.
- The highest risk products include consumer electronics, garments, seafood, cocoa and sugarcane.

¹Source: Walk Free Foundation, *Global Slavery Index*.



MCA'S SPECIFIC ACTIONS ON MODERN SLAVERY

The inaugural publication of Australian Modern Slavery Statements under the new Australian *Modern Slavery Act 2018 (Cth)* has provided Australian equity investors like us with an opportunity to derive additional insight on supply chains and supply chain risk management across Australian corporates.

As a firm, we have initiated a focussed project to

- identify risk factors and behaviours that may indicate if a company has a material risk of aspects of Modern Slavery,
- rate each company in terms of that risk,
- create a 'best practice framework' for addressing Modern Slavery risk, and
- engage with company management to push for positive change where policy and action is deficient versus best practice.

ASSESSMENT OF COMPANY RISK FACTORS AND BEHAVIOURS

As part of this project, we personally wrote to the management of the top 190 ASX companies, asking a set of detailed questions to augment their publicly available published Modern Slavery Statements under the legislation.

Our team of fundamental investment analysts have completed company specific Modern Slavery assessments of all stocks that we hold across our portfolios, and for select stocks that responded to our letters from our broader investment universe.

Our assessments were chiefly desktop based using the letter responses and recently published Modern Slavery Statements, but were also supplemented by meetings with management, board members and subject matter experts.

These assessments account for more than 100 companies out of those contacted for reply. This covers 82% of the S&P/ASX 200 index based on market cap, and the majority of our holdings across all of our Australian equity strategies².



As part of this project, we personally wrote to the management of the top 190 ASX companies, asking a set of detailed questions to augment their publicly available published Modern Slavery Statements under the legislation.



²Source: Martin Currie Australia, FactSet; as of 15 August 2021. Holdings are based on representative Martin Currie Australia accounts.

OUR ASSESSMENT FRAMEWORK AND RATING

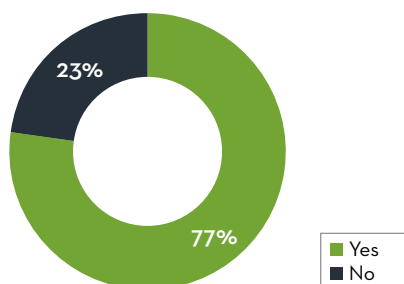
As part of our assessments, we allocated each company with a risk score ranging from 1 (low risk) to 5 (high risk) based on our analyst's identification of risk factors and behaviours that may indicate a material risk that a company is poorly equipped to deal with Modern Slavery risk.

We would note that with this rating, we are not making a judgement on their specific level of exposure to Modern Slavery, rather we are assessing the quality of their risk governance to prevent it in the first place.

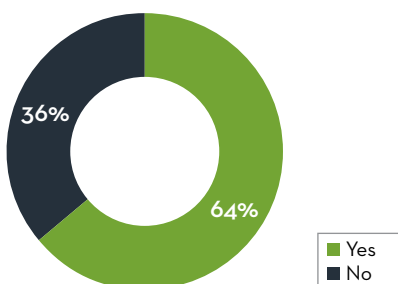
Aggregated results by key questions³

Our rating set out to quantify the results from the following questions:

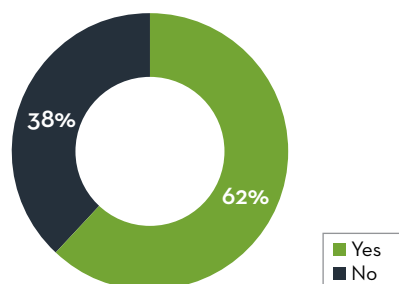
1. Do companies have appropriate policies, processes and structures in place?



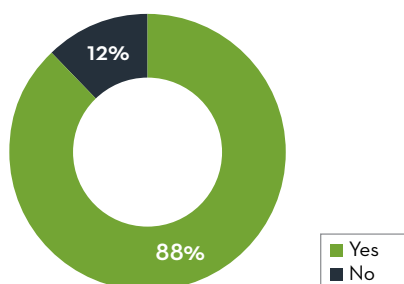
2. Is accountability clear and appropriate?



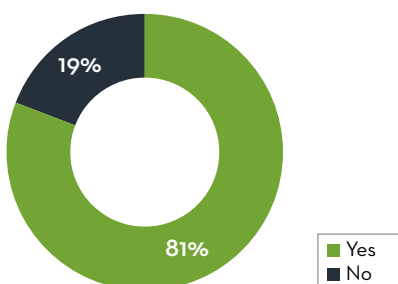
3. Do companies talk openly about material exposures and past incidents – and the limitation of their insights?



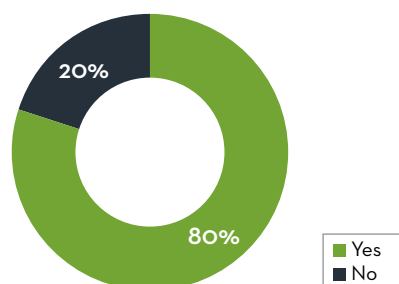
4. Is there evidence of genuine Board oversight?



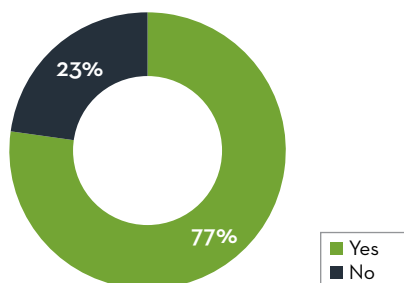
5. Do companies have clear and adequate supplier due diligence processes?



6. Do companies have clear and adequate ongoing supplier risk review processes?



7. Do companies outline areas for future focus/improvement?



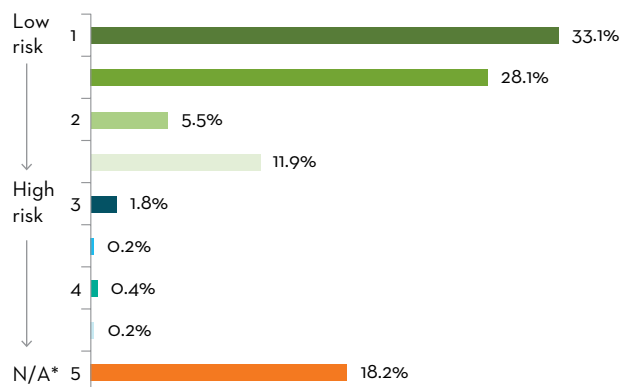
³Source: Martin Currie Australia; as of 15 August 2021. Based on MCA analyst assessment of company responses received.

GENERALLY STRONG GOVERNANCE RESPONSE FROM AUSTRALIAN CORPORATES

The letter responses and the published Modern Slavery Statements have varied widely in both quality and content across companies, however, in general, the responses and our assessment show us that most large Australian companies have to some extent policies and procedures to deal with the risk of Modern Slavery.

On average, S&P/ASX 200 companies rated 2.1 out of 5 in terms of their Modern Slavery risk.

S&P/ASX 200 Modern Slavery risk rating distribution (%)⁴



*These stocks have either not responded or fall outside of the Australian Modern Slavery Act 2018 (Cth) requirements to produce a Modern Slavery Statement.

BEST AND WORST IN FIELD

Stocks with our best score of 1, which we consider having the lowest risk and/or best policies, procedures and levels of disclosure include⁴:

- AGL Energy
- Ansell
- ANZ Banking Group
- APA Group
- ASX
- BHP Group
- Brambles
- Coles Group
- Domain Holdings
- Endeavour Group
- Fortescue Metals Group
- Goodman Group
- Iress
- Newcrest Mining
- NextDC
- Scentre Group
- SCA Property Group
- Stockland
- Transurban Group
- Telstra Corporation
- Westpac Banking Corporation
- Wesfarmers
- Worley Limited
- Woolworths Group
- Woodside Petroleum

On the flip side, excluding those stocks where we have not received a response or been able to complete full a review, only ~3% of the S&P/ASX 200 index market cap has been assessed to fall below our nominal 'passing score' of 3⁵.

The poor-scoring stocks include:

- Altium
- AfterPay
- Chorus
- Corporate Travel Management
- Healius
- Omni Bridegeway (*held*)
- Sims Metal Group
- Spark Infrastructure Group (*held*)
- Spark New Zealand (*held*)
- Washington H Soul Pattinson
- Unibail-Rodamco-Westfield

These stocks largely merit a poor score because we deem them to not have appropriate policies and disclosures in place to mitigate Modern Slavery risk. In particular, ownership and accountability for Modern Slavery risk was also not always clear. While many people need to play a part in Modern Slavery risk management, we believe that day to day accountability must be specific and clear as otherwise accountability becomes too easily blurred. There was also some evidence of companies, who believe that they have a low exposure to Modern Slavery risks, undertaking minimal work in comparison to other companies.

The information provided should not be considered a recommendation to purchase or sell any particular security. It should not be assumed that any of the security transactions discussed here were, or will prove to be, profitable.

⁴Source: Martin Currie Australia, FactSet; as of 15 August 2021. Data shown for the S&P/ASX 200 index.

⁵Source: Martin Currie Australia, FactSet; as of 31 July 2021. Data shown for the S&P/ASX 200 index. Holdings are based on representative Martin Currie Australia accounts.

SHARING MCA'S BEST PRACTICE

Combining our analysis of responses with existing research from our extensive company engagements, we have compiled a Modern Slavery risk 'best practice framework' that have shared with all Australian companies in our investment universe, along with a summary of our findings. With those stocks that we hold in Martin Currie Australia portfolios that rate poorly, we will be pushing hard on these companies for improvement.

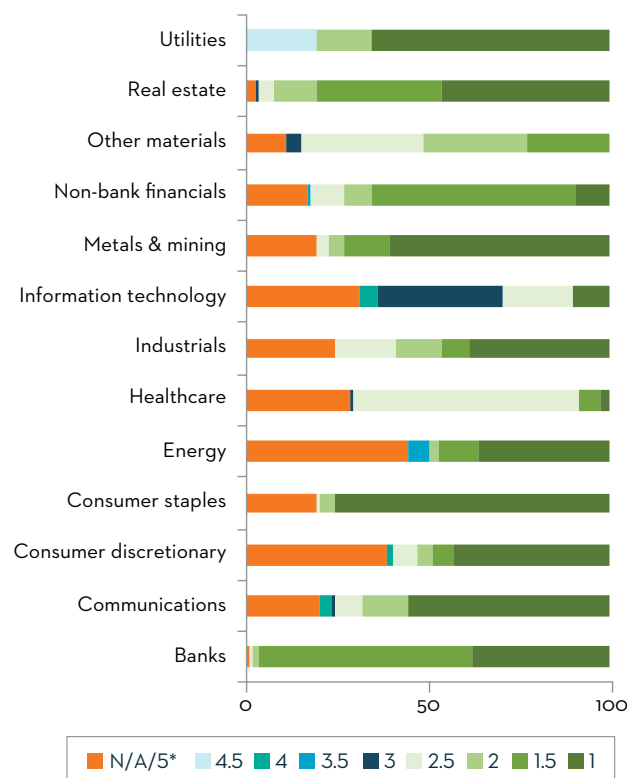
NONRESPONSE OR NON-COMPLIANCE SECTOR THEMES

In addition to companies that have not replied to our requests for information, some companies do fall outside of the Australian Modern Slavery Act 2018 (Cth) requirements to produce a Modern Slavery Statement due to their size or location (e.g. NZ-dual listed). We have rated both the non-responders and the non-compliers with the highest risk score of 5 in the rating scale described above.

Concerningly, several sectors highly represented in the 18% of the S&P/ASX 200 market cap are also considered to have high exposure to Modern Slavery risk. These include information technology, healthcare, consumer discretionary and non-bank financials which do have high-risk supply chain exposures. On the other side, banks and REITs have on average the best risk ratings and best response rates.

We would note that while most of these companies captured by exemptions or have not replied to our letters do not currently reside in any Martin Currie Australia portfolio, we also plan to engage with them to discuss the importance of best practice in Modern Slavery despite any legal obligation to comply with the Australian Act.

Modern Slavery risk rating: by sector⁶



*These stocks have either not responded or fall outside of the Australian Modern Slavery Act 2018 (Cth) requirements to produce a Modern Slavery Statement.

Concerningly, several sectors highly represented in the 18% of the S&P/ASX 200 market cap that we have rated with the highest risk score of 5 are also considered to have high exposure to Modern Slavery risk.



⁶Source: Martin Currie Australia, FactSet; as of 15 August 2021. Data shown for the S&P/ASX 200 index.

RISK MANAGEMENT POLICIES AND PROCESSES ARE REALLY STILL IN THEIR DEVELOPMENT STAGES

While most companies are meeting their minimum obligations of a Modern Slavery Statement under the Act, and have a Modern Slavery policy of some level of quality, generally we have found that companies have honestly described their Modern Slavery risk management approaches as relatively new and developing.

Importantly, many have already taken steps to improve their supply chain visibility, due diligence and risk management in response to the new legislation and increased community focus, while others have outlined their genuine goals in this area.

For example, **Stockland** outlined to us their future priorities for Modern Slavery risk assessments that include⁷:

- an annual assessment of 100 per cent of Category A and Category B suppliers.
- all suppliers required to formally acknowledge 'What Stockland Expects of its Suppliers' policy as part of the supplier on-boarding process.
- the establishment of modern slavery-related key performance indicators (KPIs) for key management personnel and other employees.
- all employees to complete modern slavery awareness training.
- the identification of trends across their supplier base to develop collaborative improvement opportunities.
- working with industry experts, civil society (including the UNGC) and peers to develop a robust, collective strategy towards remediating modern slavery risks within the supply chain.

Brambles have identified several improvement initiatives including supplier policy review, enhanced due diligence on lumber suppliers & third-party labour hire, supplier acknowledgement forms, self-assessments and certifications, and supplier training academies.⁸

At **Australia and New Zealand Banking Group**, they have identified three areas to focus on across their operations and supply chain in FY20 including building awareness of modern slavery through training and education, policy and process improvements; and enhancing supplier due diligence.⁹

The recent changes being made by companies highlights that supply chain risk has historically been underappreciated and/or overlooked. The changing nature of risk and community expectations means this is no longer acceptable and we commend those companies who have acted to better understand their supply chain risks in response to the new legislation.

Transurban seek and receive feedback from both internal and external sources including employees, suppliers, investors, industry groups, external specialist consultants and NGOs. Transurban will also undertake external collaboration to further develop and refine the overall approach.¹⁰

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⁷Source: Stockland, FY20 Modern Slavery Statement; available from <https://www.stockland.com.au/-/media/corporate/pdf/about-stockland/sustainability/modern-slavery-statement-FY20.ashx?la=en>

⁸Source: Brambles, FY20 Modern Slavery Statement; available from https://www.brambles.com/Content/cms/Corporate_Governance/Brambles_2020_Modern_Slavery_Statement.pdf

⁹Source: ANZ, FY20 Modern Slavery Statement; available from <https://www.anz.com.au/content/dam/anzcomau/documents/pdf/aboutus/modern-slavery-statement.pdf>

¹⁰Source: Transurban, FY20 Modern Slavery Statement; available from <https://www.transurban.com/content/dam/investor-centre/06/FY20-Modern-Slavery-Statement.pdf>

LARGER, GLOBAL COMPANIES MORE ADVANCED

Larger companies, or those that have had requirements to report in foreign jurisdictions already, were generally more mature in their approach, and were more likely to be able to show evidence of having applied dedicated resourcing to the issue, even if only in recent times.

However, risk mapping has often relied heavily on third-party geographic and industry flags. This offers useful insight but also comes with obvious limitations.

With a dual listed structure, **BHP Group** has already given its fifth annual statement based on the UK Modern Slavery Act. BHP also implements standards that must be met by suppliers, has an Ethical Supply Chain and Transparency guide, and provided stakeholders with the externally managed Ethics Point tool, which is available in different languages and allows anonymous complaints to be made on a range of issues including Modern Slavery.¹¹

Commonwealth Bank of Australia assesses 'all potential institutional bank loans, as well as large business loans for ESG risk based on country of operations and covering more than 500 industry sectors', highlighting that its 'ESG assessment criteria includes a specific assessment of Modern Slavery and labour standards risks', and that, 'additional due diligence is required for transactions with a medium or high ESG risk profile'.¹²

DUE DILIGENCE BEYOND THE FIRST TIER

A key challenge is that Modern Slavery is often hidden deep within supply chains, beyond the direct or Tier-1 suppliers. This makes it a shared responsibility across the whole chain and thus industry collaborations are critical to addressing risks and improving standards.

Wesfarmers has a detailed policy on Ethical Sourcing and Modern Slavery and has already undertaken work mapping Tier-1 (direct) suppliers and where possible Tier-2 and 3 suppliers. The policy sets the minimum standards expected for all divisions within the Firm. Before any division (such as Kmart) can accept a new supplier, they must assess the risk profile against specific divisional criteria via a questionnaire or audit.¹³

Worley has operations both within and outside Australia. All customers are screened for a responsible business assessment, and suppliers must comply with a code of conduct.¹⁴

Dexus's Modern Slavery Working Group has developed a staged approach to managing Modern Slavery in its supply chain. The focus for FY20, the first reporting year under the Act, has been on Tier 1 suppliers, which are those suppliers with whom Dexus has a direct contractual agreement. In future years, Dexus will expand its focus to Tier 2 suppliers (i.e., entities who are suppliers to Tier 1 suppliers) and beyond. Future focus areas will also include Dexus's joint venture partners and customers who occupy Dexus' property portfolio.¹⁵

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¹¹Source: BHP; Ethical Supply Chain and Transparency report; available from https://www.bhp.com/-/media/documents/suppliers/200217_ethical-supply-chain-and-transparency-guide.pdf?la=en

¹²Source: CBA; 2019 Annual report; available from <https://www.commbank.com.au/content/dam/commbank/about-us/shareholders/pdfs/annual-reports/CBA-2019-Annual-Report.pdf> and CDP statement, available from <https://www.commbank.com.au/content/dam/commbank-assets/about-us/docs/CBA-2020-CDP.pdf>

¹³Source: Wesfarmers (Kmart Group); Human rights and ethical sourcing website; available from <https://www.wesfarmers.com.au/sustainability/our-businesses/kmart-group/human-rights-and-ethical-sourcing>

¹⁴Source: Worley, Operating Responsibly website; available from <https://www.worley.com/sustainability/operating-responsibly>

¹⁵Source: Dexus, FY2020 Modern Slavery Statement; available from <https://modernslaveryregister.gov.au/statements/file/8ab2645c-9609-42c6-9e10-54055bf7dbob/>

CLEAR ACCOUNTABILITY, OPENNESS AND BOARD RESPONSIBILITY

Even for companies that have policies and processes in place, ownership and accountability for Modern Slavery was not always clear. While many people need to play a part in Modern Slavery risk management, both day to day accountability and board level responsibility must also be specific and clear as otherwise accountability becomes too easily blurred.

For example, accountability for IAG's Modern Slavery Program clearly resides with IAG's Chief Operating Officer. Daily responsibility for assessing and managing Modern Slavery risks sits with the Executive Manager Procurement. In addition, IAG have a cross-functional Modern Slavery Working Group, comprising participants from various functions across IAG including People, Performance and Reputation, Safer Communities, Supply Chain and New Zealand teams. The membership of this Working Group will be expanded in the next reporting period as they look to build collaboration and communication across IAG.¹⁶

Leading examples have also placed supply chain risk under their internal control and audit framework, ensuring there are controls in place that are subject to independent testing.

AGL Energy's Group Audit function provides independent and objective assurance to AGL on the effectiveness of governance, risk management and internal controls, including those relevant to AGL's modern slavery risks.¹⁷

LEADERS UNDERSTAND THAT IT NEEDS TO COME FROM THE TOP

Our assessments have found that detailed policies and processes alone, especially if they are reliant on third-party certification, are not enough. Culture and behaviours are critical and need to flow through all levels of the organisation, in particular the board and executive team given the organisational influence these roles entail.

A strong example of behaviour from the top was how in 2018, the Chief Executive Officer of Wesfarmers travelled to Bangladesh and India to personally visit factories supplying garments to Kmart and Target and was part of supplier due diligence meetings with his in-house team.¹⁸



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¹⁶Source: IAG, FY2020 Modern Slavery Statement; available from <https://www.iag.com.au/sites/default/files/Documents/Suppliers/IAG-FY20-Modern-Slavery-Statement.pdf>

¹⁷Source: AGL Energy, FY2020 Modern Slavery Statement; available from <https://www.agl.com.au/-/media/aglmedia/documents/about-agl/sustainability/agl-modern-slavery-statement-fy2020.pdf?la=en&hash=20C4354423FB7C312639BFCCC9ADA82D>

¹⁸Source: Wesfarmers; 2019 Annual Report; available from <https://www.wesfarmers.com.au/docs/default-source/asx-announcements/2019-annual-report.pdf?sfvrsn=0>

NEXT STEPS

Our project to influence Modern Slavery practices across all our Australian holdings is ongoing and will remain a key topic for future engagements with companies in our investment universe and portfolios.

We would like to see all Australian companies that we invest in take our best practice framework on board, and we also will be using our extensive company engagement program with boards and management to provide guidance and to push for positive change.

Engaging with companies is a perpetual effort and we will continue to dynamically revisit our risk assessments, and monitor disclosure and opportunities around supply chain management.

Ultimately, our aim is to invest in companies that help to improve lives, and hence ongoing engagement with companies to ensure they are working towards best practice in reducing Modern Slavery risk in their supply chains is very important in this regard.



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