

Hyperion Asset Management - Task Force on Climate-related Financial Disclosures – 2022 Report

Mark Arnold, Chief Investment Officer

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Overview

Hyperion Asset Management Limited (**Hyperion**) has been a signatory to the United Nations supported Principles for Responsible Investment (**PRI**) since February 2009 and has been an official supporter of the Task Force on Climate-Related Financial Disclosures (**TCFD**) since November 2019. This TCFD report (**Report**) relates to the period from 1 July 2021 to 30 June 2022 and it provides our response to the TCFD recommendations. We will aim to increase our disclosure each year as we update this Report. Our transparency reflects the commitment we have towards climate-related disclosure. Where appropriate, Hyperion also encourages portfolio companies to implement the TCFD recommendations.

Sustainability has always been central to Hyperion's business and investment philosophy. Due to our long-term investment horizon, it is imperative that we evaluate the sustainability of our portfolio companies and how they impact all stakeholders. These stakeholders include the wider community, and we conduct an assessment of the company's future likely long-term impact on the overall natural environment, including its carbon footprint.

Hyperion considers the impact on the natural environment for both:

- 1) its own business operations; and
- 2) the business operations of the companies it holds in its portfolios.

Governance

Material climate-related and environmental, social and governance (**ESG**) concerns or opportunities are discussed and addressed by Hyperion's Board, as required. Additionally, new initiatives and strategies are considered and policies are approved. Hyperion's Executive Committee (**EC**) meets monthly and as part of these meetings discusses any company-specific climate-related issues or opportunities. Furthermore, all members of the team can raise any concerns regarding climate or ESG risk for specific companies with the members of the EC. ESG risks are documented as part of the investment process within the Research Template, which is completed for every stock that Hyperion is researching. The Research Template is a standardised research report that is completed by the research analysts and is reviewed by the Investment Committee and Research Committee on a regular basis.

The Board has tasked Hyperion's Chief Investment Officer (**CIO**) and Deputy CIO with the responsibility of climate-related oversight and integration within our investment process. Hyperion considers that ESG and climate-related risk may affect the long-term risk and return profile of a stock, therefore ESG integration is standardised with set processes which analysts must follow when conducting ESG analysis. Due to this, Hyperion's investment team is the first point of contact as they conduct company and industry specific research. If a material risk is identified, it will be immediately raised with the CIO and Deputy CIO, who will evaluate it and take any required action.

Hyperion's Voting, Sanctions, Expert Network, Stewardship, Climate Change and ESG policies are publicly available on our website.

Strategy

Hyperion's ESG Policy outlines how we manage our responsibilities relating to ESG and climate-related issues.

We believe that strong ESG and climate change strategies are important to sustainability. Since we have a long-term investment philosophy, sustainable business practices, particularly as they relate to the environment, are critical. We also aim to protect our clients from potential risks associated with poor ESG and climate change management. As such, sustainability, climate change, and ESG are components of our philosophy. We believe our portfolios contain low ESG and climate risks due to our long-term focus and the substantial qualitative and quantitative research completed on all our holdings. As an example of risks we have identified relating to climate change, see Table 1 below.

Table 1: Climate Change Risks

Type	Climate-Related Risks	Potential Financial Impacts
Transition Risk	Policy and Legal Risk	
	This relates to the potential risk that businesses face from governments responding to climate change by implementing regulations such as increasing pricing of greenhouse gas emissions, capping supply and use of resources, and increased emissions reporting obligations.	<ul style="list-style-type: none"> • Lower returns on capital. • Increased costs/and or reduced demand for products or services. • Increased business expenses relating to things such as higher levels of disclosure and introduction of or increases in tariffs. • Asset write-offs as they become illegal to use.
Transition Risk	Technology Risk	
	The rise of more energy efficient and lower emissions technology that replaces existing technology.	<ul style="list-style-type: none"> • Increased investment. • Costs to transition to lower emission technology. • Increased Research and Development costs.
Transition Risk	Market Risk	
	This relates to how consumers' behaviour could change. This could be through consumers possibly not buying products or using services of companies that are not addressing climate-related issues as well as climate-friendly products becoming substitutions for existing non-climate-friendly products. Additionally, the risk that raw materials and natural resources (e.g. water, energy, land) costs will increase.	<ul style="list-style-type: none"> • Reduced demand leading to loss of revenue. • Increases in production costs. • Re-pricing of assets.

Type	Climate-Related Risks	Potential Financial Impacts
Transition Risk	Reputation Risk	
	Destruction of company or industry reputation due to not meeting consumers' expectations on climate change issues.	<ul style="list-style-type: none"> • Reduced demand leading to loss of revenue. • Reduction in capital availability. • Increased public relations and marketing expenses to repair reputational damage.
Physical Risks	Acute	
	This includes natural disasters such as floods, cyclones and fires.	<ul style="list-style-type: none"> • Reduced revenue from decreased production. • Increased insurance premiums. • Increased capital costs due to replacement of damaged assets. • Staff unable to travel to work.
Physical Risks	Chronic	
	These risks relate to events such as rising sea levels and temperatures.	<ul style="list-style-type: none"> • Increased electricity costs. • Increased capital costs due to replacing damaged assets. • Asset write-offs and impairments.

Hyperion's portfolios are constructed using a 'bottom-up' methodology. Our fundamental research is highly structured and all key qualitative information and insights are captured in a proprietary research document. A key output of this document is a company's 'Business Quality Score' (**BQS**) which incorporates both a specific ESG score as well as broader business sustainability scoring. These two factors represent approximately 30% of a company's overall BQS, which feeds directly into portfolio weightings.

Hyperion does not incorporate positive screening into our investment process, however we implement negative screening in the form of exclusions. The following exclusions apply to all Hyperion portfolios and are the subject of regular review:

- Controversial weapons and nuclear weapons - Hyperion does not invest in companies which are involved in the development, production, transferring or stockpiling of biological and chemical weapons, nuclear weapons, depleted uranium ammunition/armour, anti-personnel mines or cluster munitions/sub-munitions and their key components;
- Tobacco, tobacco-based products and nicotine alternatives - Hyperion does not invest in companies which are involved in the production of tobacco or the manufacture of nicotine alternatives and/or tobacco-based products; and
- Client specific exclusions - negative exclusions are agreed on a case-by-case basis with mandate clients, which may include additional exclusions to those noted above.

If Hyperion identifies that an investment does not meet its exclusion criteria, we have 90 days to review the investment. After this period, if we decide that there is not a justifiable reason for maintaining the investment, divestment is required as soon as practicable given the circumstances.

Finally, we eliminate companies included in the UNSC, US (OAC), and Australian Autonomous Sanctions lists, in addition to any other applicable overseas sanctions regime.

ESG factors are considered at the individual company level through detailed fundamental company research, which has formal oversight from three investment team members (including two portfolio managers) at all times. Our long-term investment framework is based on comprehensive fundamental research with a focus on the sustainability of a company's value proposition. Both quantitative metrics and qualitative characteristics relating to ESG are an imperative component of understanding a company.

ESG integration is standardised with set processes which analysts must follow when conducting ESG analysis. However, the research may vary in both scope and method based on individual company factors or the industry a company operates within. It is the responsibility and duty of the investment team member researching a company to apply sound judgement when assessing and evaluating ESG risks. We leverage ESG research from our broker panel and maintain subscriptions for carbon data and carbon risk assessment.

Climate-related opportunities

Hyperion has from time to time identified climate-related opportunities and specific companies that could benefit from the transition to sustainable energy and transportation. In addition, the companies we hold in our portfolios are generally less sensitive to economic growth rates compared with many listed businesses. Therefore, we believe the companies in our portfolios will be able to handle a low growth, climate disrupted world much better than many listed companies. In a relative sense, our portfolio companies will be less impacted than many listed companies if governments decide in the future to more aggressively tax CO2 emissions.

We expect the rate of growth in the global economy to decline over the coming decade and beyond due to several structural headwinds. One of the most challenging of these is the constraints on our natural resources and the environmental impact of using fossil fuels as our main source of energy. Structural disruption due to renewable energy is likely to be far-reaching, initially impacting resource, utility, transport, and infrastructure sectors. Further, the finite nature of our natural resources makes unbridled consumerism unsustainable. We have structured our portfolios to reflect this and enable our investors to prosper from this disruption through a group of companies that are implementing strong ESG values and/or actively moving the world to a cleaner future.

An example of this is the disruption to the automotive industry as internal combustion engine vehicles are phased out due to government regulation and consumer preference to lower carbon emissions. Another example is the structural change occurring in the energy industry as fossil fuel production is reduced/retired and more renewable energy is implemented.

Risk management

Hyperion identifies, assesses and manages climate-related risks through its investment analysis and portfolio construction process, as outlined in the Strategy section above.

We believe activities detrimental to the environment are not sustainable in the long term and will lead to increased costs and/or lower returns on capital. There will be certain industries where the environmental impacts of a company's activities are so great that the company is considered non-investable.

Our view is that poor governance and activities that have a detrimental impact on society or the environment will result in such companies being unattractive investments as the company's overall sustainable competitive advantage will be impacted. Our conclusions can result in stocks either being

excluded from consideration for Hyperion portfolios or, in less extreme circumstances, being held at low weights.

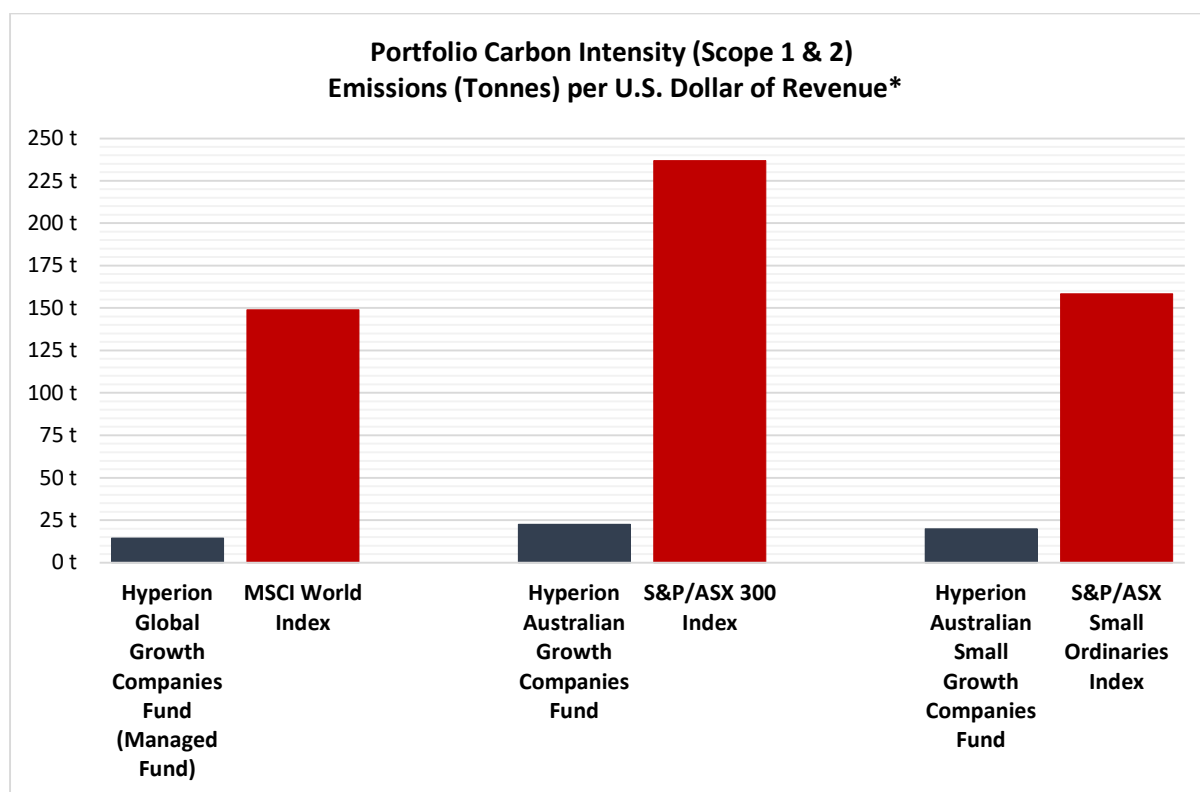
Engagement

Another method of risk management used by Hyperion is engaging with our portfolio companies and raising questions or concerns related to ESG and climate-related matters. Additionally, when deemed necessary, we will encourage our portfolio companies to implement better climate-related reporting and to lower their carbon footprint. This has resulted in increased climate-related reporting and carbon reduction plans from portfolio companies.

In relation to proxy voting, we believe our role as proxy voters for our clients is important. We take time reviewing third-party research, completing our own research, and where necessary, we will talk with company management to express our thoughts and/or concerns.

Metrics and targets

Hyperion aims for our portfolios to have a weighted average carbon intensity of at least 75% lower than their respective benchmarks. As of 30 June 2022, the Hyperion Global Growth Companies Fund (Managed Fund)¹, the Hyperion Australian Growth Companies Fund, and the Hyperion Small Growth Companies Fund all had weighted average carbon intensity levels significantly lower than the relevant benchmark (see graph below).



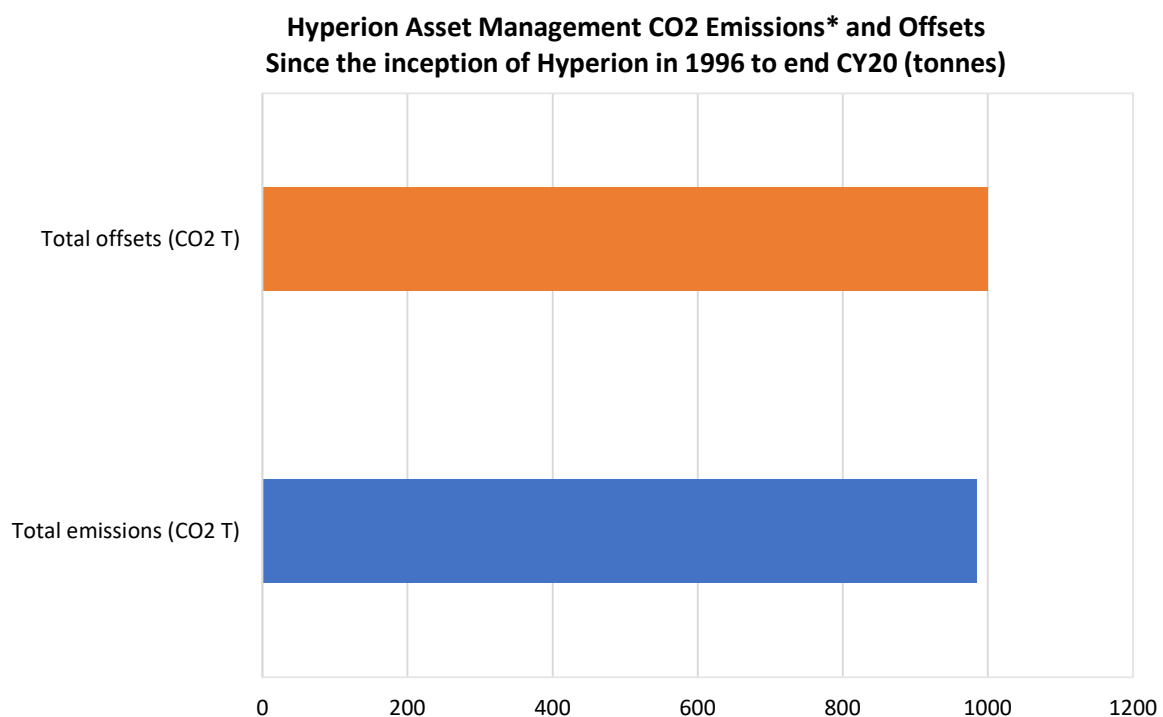
*as at 30 June 2022

Source: Sustainalytics (FactSet), Hyperion Asset Management

¹ The fund changed its name from Hyperion Global Growth Companies Fund on 5 February 2021 in order to facilitate quotation of the fund on the ASX. Under ticker ASX: HYGG, the Fund was made available on the ASX in March 2021.

Firm activities

In support of the global reduction of carbon emissions, Hyperion has offset its historical carbon emissions since its inception in 1996 through the purchase of carbon credits. Hyperion partnered with leading project developer and global climate solutions provider South Pole to support climate action projects both in Australia and abroad, including the EcoAustralia Biodiverse Tree Planting project, which aims to plant one million trees across Australia. Hyperion received the 2021 Climate Neutral label from South Pole. At the time of drafting this report, Hyperion is in the process of being certified as a carbon neutral company for the 2022 financial year and will update its [website](#) accordingly once finalised.



**Emissions refer to those by Hyperion Asset Management Limited as a company and do not include the emissions from the companies in our portfolios.*

Source: South Pole

Hyperion's carbon emission reduction measures that have been implemented to date include: providing the optionality for staff to work from home, which assists with the reduction of emissions from commuting to the office; encouraging all lights and computers to be turned off at night or when not in use; predominantly using digital file copies in order to reduce printing requirements and only using recycled paper when printing; and a reduction in travel. We endeavour to further reduce our carbon footprint over the coming years.