Annual report on the integration of environmental, social and corporate governance (ESG) issues

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As a portfolio manager, Hexavest has the duty to act in the best long-term interest of its clients and their beneficiaries. In this fiduciary role and as a signatory of the United Nations PRI, Hexavest commits to report on its activities and progress towards the integration of the Principles for Responsible Investment. The objective of this annual report is to provide an overview of our efforts and progress in the integration of ESG issues in our investment practices.

Approach

Hexavest's approach regarding responsible investment is based on the belief that companies lacking strong governance standards or social and environmental responsibility are taking business risks which may adversely affect them as well as their stock's performance. Because our investment philosophy is strongly geared towards capital protection, the consideration of Environmental, Social and Governance (ESG) factors is consistent with our processes and is a natural fit with our portfolio management activities. We also believe that ESG factors can represent investment opportunities over medium and long-term horizons.

Our approach to responsible investing is based on the following principles, which we adhere to:

Consideration of ESG factors is in line with the fiduciary duty of asset managers.

Responsible investing contributes to sound risk management.

Shareholder engagement can lead to better management of risks by target companies.

Disclosure and corporate transparency are key to assessing their ESG risks.

Sound management of ESG factors can create long-term value.

Responsible investment promotes more sustainable and prosperous economic and social development.

Coverage

Our general approach in terms of integrating responsible investment principles is applied to all of the firm's assets under management. Some of our assets, however, are treated differently to meet the specific needs of certain investors:

1. Our voting policy, which is strongly focused on ESG issues, is not applied to certain clients who have chosen to exercise their own voting rights or who adhere to a policy other than that of Hexavest (six of our clients).

2. The assets of certain portfolios use a combination of our standard integration strategy (see section "Integration in the investment process") and of a screening strategy, according to criteria established in their investment policy. Portfolios using this combination of ESG strategies account for 18% of the firm's total assets.

   - <u>Separately managed portfolios with exclusions</u>: Hexavest manages multiple mandates in segregated accounts on behalf of investors who wish to exclude controversial sectors such as tobacco, gambling, controversial weapons production and nuclear energy.

- Climate Focus Fund (formerly the Global Fossil Fuel-Free Fund): Since February 2016, Hexavest has been managing a portfolio aimed at investors who wish to reduce their exposure to climate change risks using an exclusion strategy. This portfolio invests in the MSCI All-Country World Index (ACWI) universe, from which are excluded all companies owning proven or probable oil, gas or coal reserves, as well as those using coal as a source of energy.

Resources

Because responsible investment practices involve a large number of activities and evolve very quickly, they require several resources and expertise to ensure proper implementation. As Hexavest cannot sustain a complete team dedicated to responsible investment due to its size, our approach is to entrust certain responsibilities to internal experts and to supplement the efforts of our professionals with external partners who have developed in-depth expertise in the domain.

Internal Resources

Board of directors: The members of Hexavest's Board of Directors are responsible for approving the Responsible Investment Policy.

Head of Responsible Investment: The resource in this role is responsible for overseeing the implementation of the Responsible Investment Policy, coordinating the PRI accountability process, and liaising with external resources.

Management team: The analysts and portfolio managers are responsible for considering ESG issues as part of their fundamental and quantitative analysis. They must cover, when relevant, risk factors and investment opportunities in their fundamental research, and they are required to maintain a percentage on the ESG variable in the quantitative model they use to help their decisions. The integration into the portfolio construction process is overseen by the firm's investment committee and supervised by either one of the C0-Chief Investment Officers.

Risk Committee: As part of its market risk monitoring, the Risk Committee is responsible for analyzing ESG risks and presenting the results of its analysis to the Management team.

Quantitative Research Team: This team is responsible for optimizing the integration of ESG variables into the quantitative tools used by the Management team. It also assesses the relevance and the quality of the methodology specific to the ESG variables used in the systems.

Middle office and Compliance: The members of these teams are responsible for integrating the specific ESG constraints of the relevant accounts into the firm's systems in order to ensure that the portfolios comply with the restrictions set out in the investment policies. Middle Office analysts are also responsible for optimizing portfolios with significant restrictions in order to respect the active strategy implemented by the management team.

Client Servicing: The firm representatives have a responsibility to understand ESG issues and to communicate client needs and expectations to the internal and external resources involved. They are also responsible for disclosing the Responsible Investment Policy and the firm’s ESG efforts to clients and consultants.

External Resources

Hexavest uses four main external providers as part of its responsible investment and ESG integration practices.

- Sustainalytics: Research and ESG scores
- AEquo: Shareholder engagement
- MSCI: Investment universe (screening) for the Climate Focus Fund
- Groupe Investissement Responsable: Proxy voting agent

Shareholder Engagement

Proxy Voting

Hexavest has incorporated ESG issues in the guidelines of its Proxy Voting Policy. Our main basis of analysis when exercising our voting rights is the maximization of returns for our clients, which requires sound risk management. As such, we require that companies submit to the regulations in force in the countries and jurisdictions where they do business, that their conduct be socially responsible and that they submit to high standards of governance and ethics. By actively exercising our voting rights, we hope to improve the quality of governance, environmental and social practices of the companies in which we invest, which contributes to a better management of risks for specific securities.

Our Proxy Voting Policy has been developed in collaboration with the Bâtirente National Union Retirement Committee, based on the *Extrafinancial Risk Management Guidelines*. These guidelines are themselves based on the principles of responsible investment of the United Nations and applied to all portfolios managed by our firm (with the exception of portfolios of clients who have decided to exercise their own voting rights). Hexavest's Proxy Voting Policy is public and available on the firm's website.

2017 Statistics

During the year 2017, Hexavest exercised its voting rights in the assemblies of 694 companies and voted on 7 976 resolutions. In 54% of cases, Hexavest voted in opposition to the Board’s recommendations a large majority of the advisory resolutions on compensation were rejected (262 out of 356). In the majority of cases, it was the inclusion of option grant plans in the executive compensation program that accounted for our negative vote. Indeed, we believe that this type of plan is not aligned with shareholder interests. Lastly, Hexavest has supported 79% of shareholder proposals over the past year.

The table below compares our Proxy Voting Policy with the SRI policy of one of the world's largest providers of proxy voting solutions.

Comparison of the Hexavest Proxy Voting Policy
% of votes in 2017

	SRI Reference Policy for Institutional Investors	Hexavest Policy
% of votes in opposition with companies' management	4%	54%
% of votes in opposition to compensation proposals	12%	74%
% of votes in favor of shareholder proposals on factor E (environment)	81%	100%
% of votes in favor of shareholder proposals on S and G factors (social and governance)	96%	77%

Engagement with companies

Given our top-down approach, our portfolios include a large number of public companies. Our managers and analysts meet with management, but this is not a mandatory step before investing, and company visits are relatively infrequent. As a result, our managers and analysts have few opportunities to encourage companies to improve their practices. In order to overcome this constraint, Hexavest has entrusted a mandate to a firm specializing in shareholder engagement: AEquo, whose mission is to lead shareholder engagement with listed companies – on behalf of managers and asset holders – on ESG issues. AEquo's experts carry out engagement activities on behalf of Hexavest, primarily with North American companies, according to a predetermined plan of action or occasional opportunities. Every quarter, AEquo reports on the status of the various dialogues in a report that is provided to our team of managers and analysts.

In 2017, AEquo has had communications with 16 companies to discuss different ESG issues, as summarized in the table below:

COMPANY	INDUSTRY	COUNTRY	ESG ISSUES		
			Environment	Social	Governance
BMW	Automobile	Germany	•		
Dollar Tree	Retail	United States		•	
Dollar General		United States		•	
Eldorado Gold	Mining	Canada		•	
Goldcorp		Canada		•	•
Nevsun		Canada		•	
Yamana Gold		Canada		•	•
CIBC	Financials	Canada	•	•	
Scotiabank		Canada	•	•	•
American Electric Power	Utilities and pipelines	United States	•		
DTE Energy		United States	•		
Duke Energy		United States	•		
Embridge		Canada	•	•	
Public Service Enterpr. Gr.		United States	•		
Southern Company		United States	•		
TransCanada		Canada	•	•	

Please note that details on the discussions with these companies may be provided upon request.

Collaborative Initiatives

By signing the Principles for Responsible Investment, Hexavest is committed to working with other investors to improve its effectiveness in implementing the Principles. By collaborating on various investor initiatives, we help align our investment activities with the broader interests of the company.

Thus, Hexavest frequently links its potential for influence with that of other participants in the financial sector. The table below shows the seven initiatives to which Hexavest participated in 2017:

Initiative	Details
Investor statement on financial risks related to climate change	The declaration invited Canadian public companies to disclose more information on their exposure to climate change risks and the measures they take to manage them. Hexavest participated in the Finance Montréal working group that initiated this statement.
Investor statement to banks financing the Dakota Access Pipeline	Hexavest co-signed a letter initiated by Boston Common Asset Management to the 17 international banks of the financial syndicate that finances the Energy Transfer Partners pipeline project. The letter asked the banks to support the Standing Rock Sioux Tribe's petition to change the route of the pipeline to avoid the risk of oil spills in their water resources. The aim was to encourage the banks concerned to protect their reputation and avoid the risks of litigation and legal liabilities.
Investor statement on the 4th anniversary of the Rana Plaza tragedy	This statement was part of an initiative of Interfaith Center on Corporate Responsibility (ICCR) and was addressed to the different parties involved in the Bangladesh Security Agreement to mark the 4th anniversary of the collapse of the Rana Plaza textile factory. The statement, which was co-signed by Hexavest, called for the renewal of the agreement and noted the need for continued efforts to build a textile sector that protects the lives of its workers and respects their dignity.
Letter from global investors to G20 governments on climate change	The letter, signed by 390 investors representing more than US $ 22 trillion in assets, was intended to reiterate previous support for the Paris Agreement. It also urged all G20 governments to put in place policy measures to contain the increase in global average temperature.
Letter to the Canadian government to create a task force on sustainable finance	A letter was sent to the Canadian federal government asking it to adopt a financing strategy focused on a clean growth. This letter was signed by a group of investors, including Hexavest.
“Banking on a low carbon future” letter	Initiated by Azzad Asset Management, this letter asked 62 banks to disclose climate risk information in accordance with the recommendations of the Taskforce on Climate-related Financial Disclosure (TCFD).
Letter on the refugee crisis in Myanmar	Azzad Asset Management has initiated this letter, inviting major oil companies operating in Myanmar to sensitize the local government to adopt the Annan Commission's recommendations and to explore the possibility of adopting a policy of not dealing with governments complicit in genocide.

Integration in the portfolio construction process

ESG Philosophy

We believe that the companies lacking strong governance standards or social and environmental responsibility are taking business risks that can have an adverse effect on company and stock performance. Our investment team is mindful of the potential risks associated with ESG issues, which are therefore considered from a risk assessment standpoint. We also believe that certain investment opportunities may arise from ESG factors.

ESG Factors in Portfolio Construction

Hexavest favors an active and top-down investment approach to build a highly diversified equity portfolio in order to minimize stock-specific risks. As such, our global portfolios contain more than 300 stocks. Our efforts are focused on top-down decisions, such as the selection of regions, countries, currencies, sectors and industries. Stock selection represents a smaller proportion of our decision-making process. We actively manage several decision-making levels, mainly using fundamental analysis and with an investment horizon that varies between 12 and 18 months. Our fundamental analysis is based on three vectors: the macroeconomic environment, market valuation and investor sentiment.

Integration of ESG factors in the selection of countries, sectors and industries
ESG factors are considered, where appropriate, under the first vector, i.e. the macroeconomic environment. For example, if a sector is likely to be negatively impacted by the likelihood of new regulation focused on protecting the privacy of individuals, or if a country benefits from improved corporate governance standards, the portfolio manager will take these factors into account in his research and analysis, which may have a positive or negative impact on his decision.

Integration in stock selection
Managers use quantitative tools to support them in the portfolio construction process, including a stock selection model. This model ranks companies according to the main families of variables. Sustainalytics' overall ESG score represents one of these families of variables. Thus, companies' ESG performance impacts their rank among their peers and can ultimately influence their presence in the portfolio. The image below, taken from our quantitative model, illustrates an example of rankings based on the software industry in the United States. Each family of variables positions companies at a percentile rank; the last column represents the overall percentile rank of each security.

Hexavest Securities Analysis Model - Ranking of US Software Industry Firms

As of December 31, 2017

Name	Growth	Effectiveness	Debt	Size	Value	Momentum	Quality of the consensus	Volatility	ESG	Percentile rank
ALPHABET C	62.57%	87.52%	98.22%	93.27%	38.22%	27.13%	29.70%	28.12%	93.27%	**94.85%**
ALPHABET A	79.01%	86.34%	98.22%	98.61%	11.88%	28.12%	94.65%	24.36%	93.27%	**92.08%**
FACEBOOK CORP	78.22%	97.03%	99.21%	96.63%	6.34%	9.50%	63.76%	59.21%	49.50%	**87.72%**
AKAMAI TECHNOLOGIES	55.84%	71.29%	83.76%	9.11%	26.34%	95.64%	96.24%	98.02%	81.98%	**81.98%**
EBAY INC	6.34%	98.42%	68.51%	61.78%	41.98%	17.03%	98.81%	55.25%	93.47%	**78.81%**
VERISIGN INC	21.19%	98.22%	73.66%	1.39%	6.53%	7.72%	58.02%	36.24%	29.11%	**17.82%**

Note: The rankings in the top and bottom two deciles are highlighted (in green and red).

Monitoring

Every month, a risk report is presented to the Investment Committee as part of a formal meeting. The elements of greatest concern are then discussed among the members of the team. These discussions may lead to subsequent analysis by certain regional teams and, occasionally, to decisions to adjust certain portfolio positions.

Developments and objectives

Developments in 2017

As a UN PRI signatory, Hexavest is committed to incorporating ESG issues into its analysis and decision-making. Through our Responsible Investment Policy, we are also committed to continuing to evolve our ESG approach. Here are the developments that were made by our firm in 2017:

Reduction of the carbon footprint of the Climate Focus Fund (formerly the Global Fossil Fuel-Free Fund)

The investment universe of this strategy was reduced when the investment policy was amended in March 2018 to exclude companies that process coal. This change allows us to offer a portfolio that not only reduces long-term risks by eliminating companies that hold fossil fuel reserves, but also manages the shorter-term risk associated with carbon emissions.

Expansion of shareholder engagement coverage in the United States

Until 2016, the dialogues with the companies we held in the portfolio focused on Canadian companies. We have mandated our shareholder engagement service provider to expand coverage across North America. Seven US companies with various ESG issues were added to our annual action plan list and contacted in 2017.

Systematization of the integration of ESG scores into our portfolio construction process

Various tests were conducted by our quantitative analysts and portfolio managers to improve ESG integration methodology in the portfolio construction process. The objective was to optimize the consideration of ESG risks and opportunities without compromising the integrity of the firm's management style. The chosen process uses the quantitative decision support tools used by the portfolio managers. The securities' ESG rating has been incorporated into the models and a significant weight has been allocated to all regions, making the consideration systematic.

Integration of ESG risks into monthly risk reports

Since this year, the Hexavest Risk Committee has included a section on ESG risks in each monthly risk report presented to the management team.

Adoption of a responsible investment policy

On December 7, 2017, Hexavest's Board of Directors adopted a Responsible Investment Policy to define and regulate the practices of the firm for this purpose. The policy is public and can be consulted on the firm's website.

2018 Objectives

Four objectives have been set for the coming year to continue to improve our responsible investing practices:

- Obtain the tools and data needed to measure and analyze the carbon footprint of our portfolios.
- Communicate our responsible investment practices more transparently.
- Formalize a training plan for our resources with responsibilities related to our responsible investing practices.
- Increase the number of companies held in our portfolios with which we carry out shareholder engagement.

Contact Information

www.hexavest.com

1250 René Lévesque Blvd. West
Suite 4200
Montreal, Quebec
Canada H3B 4W8

Jo-Annie Pinto, CIM®

Vice President and Head of Responsible Investment
T: 514-390-1188
jpinto@hexavest.com