ORCA FUNDS MANAGEMENT

Orca Global Fund ESG Annual Report 2021

Introduction

Welcome to the inaugural Orca Global Fund Environmental, Social and Governance (**ESG**) Annual Report.

The year to September 2021 has been a transformational year for Orca Funds Management (**Orca**), with respect to the documentation of our ESG policies, and our aspirations in aligning our processes with the United Nations Principles for Responsible Investment (**UNPRI**) guiding principles.

As signatories to the UNPRI, we are strongly committed to the UNPRI principles of responsible investment, with these principles guiding the formulation of our ESG approach. This includes how we:

- incorporate ESG issues into investment analysis and decision-making
- engage with companies and act as stewards of investor capital
- participate within the investment community on ESG-related issues
- report, disclose and make available information to stakeholders, and
- continuously monitor and improve our practices.

We are proud to report some strong ESG-related metrics for our portfolio given our exposure to companies with robust ESG credentials. In addition, we are pleased to detail our activism around company engagement and proxy voting on ESG areas of concern. Whilst we believe our portfolio companies are excellent businesses with strong product offerings, we do note there is often scope for improvement. In these instances, we seek to actively engage and advocate for more sustainable operating practices.

ESG overview of the Orca Global Fund portfolio

Portfolio ESG Rating	Carbon Footprint	Company Engagement	Proxy Voting
A+	15%	68%	56%
Investment Grade Based on Orca's proprietary ESG rating model	of the MSCI World Index (tCO2e / $m invested)	% of portfolio companies engaged regarding ESG concerns	Number of meetings voted against management on 1 or more resolutions

Going forward we will continue to target:

- maintenance of a portfolio ESG rating of A and above (A+ achieved for 2021)[1]
- an increase in the level of our company interaction on ESG issues (68 per cent achieved for 2021)
- maintenance of carbon footprint at sub-30% of the benchmark index (15 per cent achieved for 2021)
- voting on 100 per cent of proxies (100 per cent achieved for 2021)

We have prepared this report to allow investors to have a better understanding of the ESG credentials of our portfolio. We are committed to acting as stewards of investment capital, in a sustainable way, and seek continuous improvement of our processes and those of our portfolio companies.

The Orca Global Fund Team.

Signatory of:

PRI Principles for Responsible Investment

1. An overview of Orca's ESG rating scale is provided on page 6 of this report. Details can also be found in Page 3 of our ESG Advocacy Policy.

Key issues in focus: Climate crisis

"I convened this meeting with Prime Minister [Boris] Johnson for a very simple reason. It is a wake-up call to instil a sense of urgency on the dire state of the climate process ahead of COP26."
António Guterres, Secretary-General of the United Nations 20 September 2021[2]

For almost three decades, the United Nations (**UN**) has been uniting world leaders for global climate summits known as COPS, or the "Conference of the Parties".

The subject of these summits is climate change.

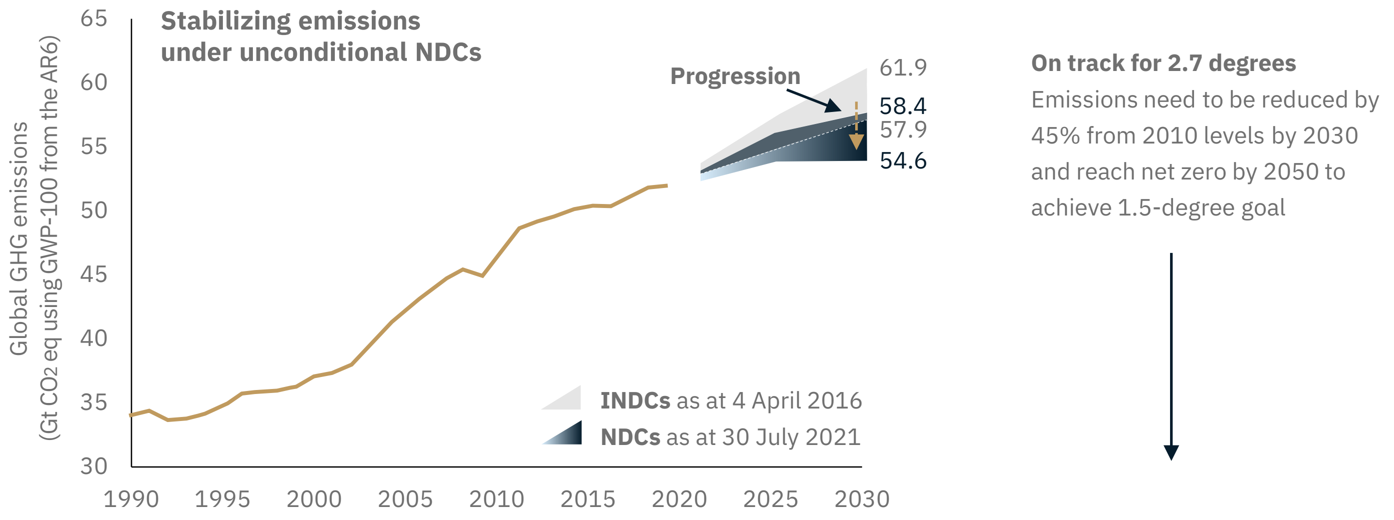
This year the UK will host COP26 in Glasgow on 31 October-12 November 2021. In 2015, COP21 took place in Paris and the outcome was momentous.

Countries in attendance agreed to work together to limit global warming to well below 2.0 degrees and to aim for 1.5 degrees, when compared to pre-industrial levels. From this meeting the Paris Agreement was born. The agreement works on a five-year cycle with each country submitting their Nationally Determined Contributions (**NDCs**) plan for climate action, which details initiatives to reduce the greenhouse gas emissions of their nation.

Under this timeframe, countries should have revised their five-year plans in 2020, however the COVID-19 pandemic resulted in a 12 month delay of the release of such plans. Unfortunately, the individual country commitments laid out in 2015 fall well short of the 1.5-degree goal and revised NDCs received to date by the UN tell a very poor story regarding progress.

Projected range and progression of emissions

1990-2019 (actual) 2020-2030 (estimated based on NDCs)



Source: United Nations, Framework Convention on Climate Change

2. For full speech: https://www.un.org/sg/en/node/259178

The potential tragedy on the horizon

On 17 September 2021, the United Nations Framework Convention on Climate Change issued a report collating revised NDCs commitments released to date, concluding that such commitments could result in global warming by 2.7 degrees by the end of the century – well above the 1.5 degree or less ambition. To reach the 1.5-degree ambition, by the year 2030, CO_2 emissions need to decline by 45 per cent from 2010 levels and gravitate towards net zero around 2050. As illustrated in the chart above from the UN publication, current NDCs would see an increase in CO_2 emissions by 2030, rather than the substantial decrease required.

To provide some additional background on this issue, it has been scientifically determined that global warming above 1.5 degrees would materially increase climate change risks for human and natural systems. The greater the level of global warming, the increased levels of droughts, floods, sea level rises and biodiversity loss. A temperature rise difference as low as 0.5 degrees could have double the adverse impact in some circumstances. Whilst all people will be affected, the most vulnerable will be persons in low and middle-income countries, increasing issues around food security for such populations.[3]

In his 20 September 2021 speech, the UN Secretary-General implored the G20 members to demonstrate leadership on climate change ahead of COP26. These member countries represent 80 per cent of global greenhouse gas emissions with an urgent need for "decisive action now around net zero commitments from all countries and the private sector".[4]

As an Australian-domiciled international fund, we are concerned with Australia's lack of proactivity on setting net zero carbon emission targets to date at a national level. Compared to other nations, Australia's climate targets have been "highly inefficient" noting that Australia's 2030 domestic emissions reduction targets are consistent with warming of 4 degrees, if all other countries followed a similar level of ambition which makes them highly incompatible with the Paris agreement.[5] We hope for some profound step up in commitments on climate action from Australia and other nations in the lead up to COP26. At the time of writing the Australian Prime Minister was reported to be deep in negotiations with the National Party in an effort to lock in a plan to cut carbon emissions.[6]

What can we do about it?

National targets are important, but the implementation of such targets is – to a significant extent – in the hands of individual institutions and the collective efforts of such institutions to set ambitious, yet realistic, carbon reduction targets for their own entities. As fund managers, we can exercise influence on this by being selective in our choice of portfolio companies, favouring those who show sufficient efforts to reduce emissions and become carbon neutral by 2050.

Our Orca framework emphasises companies who are ambitious around carbon emission reduction across their value chain and not just for their own operations.

The burning of coal, natural gas, and oil for electricity and heat is the largest single source of global greenhouse gas emissions. In late 2020, recognising the dire climate situation we find ourselves in, Orca made the decision to outright exclude all fossil fuel producers from our investment universe, given their significant contributions to global emissions.

This portfolio change, along with progress of our portfolio companies on their carbon emission reduction plans, saw a meaningful reduction in our portfolio emissions over the course of the year as detailed in the next section of this report.

3. For further details refer to: https://www.ipcc.ch/site/assets/uploads/sites/2/2019/06/SR15_Chapter3_Low_Res.pdf

4. For full speech: https://www.un.org/sg/en/node/259178

5. For details see https://climateactiontracker.org/countries/australia/

6. https://www.abc.net.au/news/2021-10-11/llew-obrien-warns-scott-morrison-over-net-zero-2050/100528050

Portfolio carbon emissions

The following tables summarise the Orca Global Fund's listed equities carbon emissions, in contrast to that of the benchmark MSCI world index. The **Carbon Footprint** is a *normalised* measure that expresses the carbon contribution of portfolio companies based on a one-million-dollar USD investment in the Orca Global Fund. The **Weighted Average Carbon Intensity** is a measure of exposure to carbon intensive companies and is useful as a proxy for carbon risk within the portfolio.

Carbon Footprint (metric tonnes CO_2 emissions/US$million invested)

	Sep-2020	Sep-2021	Change
Orca Global Listed Equities	13.4	7.0	-48%
MSCI World	56.3	46.3	-18%
vs Index	*-76%*	*-85%*	

Weighted average carbon intensity (metric tonnes CO_2 emissions/US$milion sales)

	Sep-2020	Sep-2021	Change
Orca Global Listed Equities	35.4	32.3	-9%
MSCI World	138.3	136.4	-1%
vs Index	*-74%*	*-76%*	

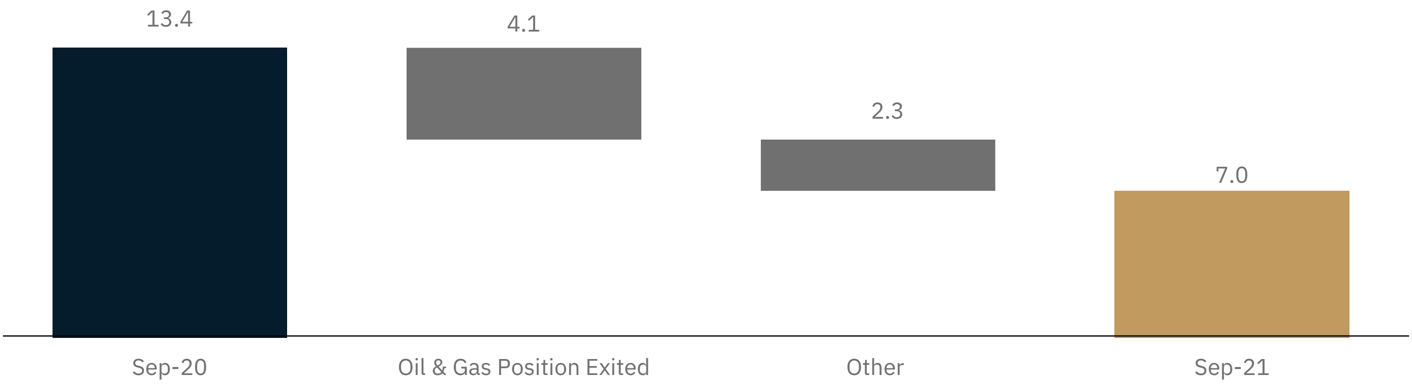
Source: MSCI ESG Research, Orca Funds Management. Includes Scope 1 (Direct) and Scope 2 (Indirect emissions)

Of note is a substantial decline in Carbon Footprint of -48 per cent for the Orca portfolio over the year well ahead of the benchmark index. The fund ended the year at just 15 per cent of the carbon footprint of the benchmark index. The portfolio's carbon intensity also declined over the year by 9 per cent, well ahead of the index.

Evolution of carbon footprint

The following chart illustrates the evolution of the carbon footprint of the Orca Global Fund over the last year.

Carbon Footprint (Sep-20 to Sep-21)



Around October 2020, Orca made the decision to outright exclude all fossil fuel producers from our investment universe, given their significant contributions to global emissions. This decision resulted in the exit of an oil and gas position (<1% portfolio position) which had a material impact on the carbon footprint of our portfolio (contributing 30% of the 48% reduction in carbon footprint). In addition, progress on reducing emissions by portfolio companies also had a material impact on overall carbon footprint reduction.

We envisage this to be the driver of further reduction in carbon footprint of the portfolio in the future.

Orca proprietary ESG rating system

Overall portfolio ESG rating

Portfolio ESG Rating

A+

Investment Grade
Based on Orca's proprietary ESG rating model

The Orca Global Fund achieved a portfolio rating of A+[7] for ESG, based on our proprietary ESG rating model. This implies that, overall, the portfolio companies are generally highly investable from an ESG perspective and skewed to a lower (mild) level of controversies.

As detailed in our ESG Policy, Orca have developed and implemented a proprietary process for scoring businesses on ESG risks and opportunities. Prior to investment, each prospective investment will have a full ESG analysis completed by the team, with an overall ESG score assigned. This score is based on the team's opinion of the company's performance against each of the three pillars of the ESG framework – Environmental, Social and Governance – and in aggregate (typically an average of each pillar).

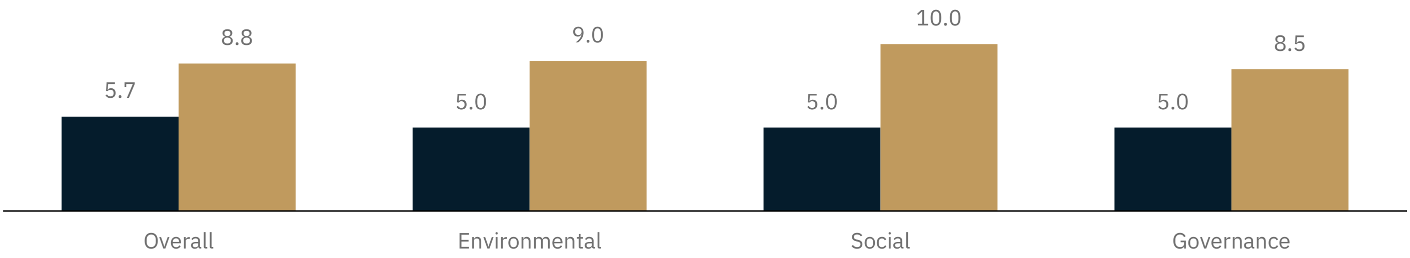
To derive an overall portfolio score, individual company scores are collated and averaged based on portfolio weightings. This score is then translated into a rating per the conversion table below. We use ratings (similar to those used by debt rating agencies) as we believe they provide a more effective indicator of the ESG investability of a stock.

Orca ESG rating system

	Orca score	Orca rating	
Investment Grade	10	AAA	Leader Proactive in managing ESG risks and opportunities
	9	AAA	
	8	AA	Investable – some areas of concern Mild to moderate controversies, varied quality/ambition in ESG policy
	7	A+	
	6	A	
	5	BBB	
Non-Investable	4	BB	Non-investable Mixed track record with some exposure to significant controversies ↓ High exposure and failure to manage ESG risks
	3	B	
	2	CCC	
	1	CC	
	0	C	

The above table illustrates how an ESG score assigned to an individual company translates into an investment rating. Orca will not invest in any company that is rated a BB or lower (sub-investment grade) for any of the three E, S or G pillars – as it is deemed non-investable.

Minimum and maximum assigned company scores by pillar



7. This rating excludes cash and non-liquid legacy investments to which we do not assign an ESG rating.

Company scoring examples

While the overall average ESG rating of our portfolio is highly investable (A+), the underlying environmental, social and governance pillar contributions reflect a broad range of scoring (as per the minimum and maximum scores above). To help provide insight into the Orca ESG rating process, we have provided the following specific company examples (with names redacted) to illustrate their rationale.

Investment and commercial bank

One of the worst-ranked companies in our portfolio from an environmental perspective, this bank is a large financer of clients across the fossil fuel cycle.

What we like

Despite its current loan book exposure, the company is taking steps to accelerate clients on a path to net-zero emissions, including the creation of a center of excellence that provide clients with sustainability-focused financing and advisory solutions to help with their transition. The company plans to finance and facilitate more than $2.5 trillion over 10 years, including $1 trillion in green activities, and to advance long-term solutions that address climate change.

Areas for engagement

Beyond environmental issues, we have some corporate governance concerns for this business, including lack of separation between CEO and Chairman roles on the board and a lack of sufficient independent representation on the board. We have questioned the business directly on these practices and voted against management on resolutions covering these topics in the latest AGM.

How we differ from the external view

A key agency we subscribe to rates this bank highly, relative to its peers, on efforts to finance environmental impact with no acknowledgement of their concurrent position as current major financers of businesses across the fossil fuel cycle.

Offshore wind producer

One of best-ranked companies in the portfolio from an environmental perspective this company is an industry leader in offshore wind farm installation and operation.

What we like

We rate companies highly that actively play a role in displacing high emission technologies with sustainable cleaner alternatives. The offshore wind power market has enormous potential to displace high emitting coal powered energy suppliers. This company pioneered the industry, with the first offshore wind farms and leading market share. They will play an important role in driving further improvement in the environmental impact of power generation.

Areas for improvement

The company has committed to sustainable end of life planning for turbines, which are not easy to dispose of or recycle. The company still has some pollution emitting operations and is a large user of raw materials such as steel.

How we differ from the external view

This company is generally seen as one of the ESG leaders globally, and we agree with this view. We have travelled to meet with executives on ESG issues and have followed the stock through its energy transition. Despite its leading position, we do see further improvements to come.

Carbonated drinks and snack foods manufacturer

One of the worst-ranking companies in the portfolio from a social perspective, we estimate that a significant portion of the company's current earnings are from sale of unhealthy snack foods.

What we like

This company is an enormous part of the global food supply chain, selling over a billion consumable items daily. While the legacy product footprint relates to higher calorie, lower nutrition products, the company has launched a series of healthier alternatives including plant-based products, nuts, grains, and zero sugar drinks. The company has major business lines with healthier foods, but consumer preferences skew towards unhealthy. The company has also been proactive in promoting sustainable agricultural practices, particularly through emerging markets.

Areas for engagement

The company sets quite obtuse nutritional goals, such as saturated fat per hundred calories. There is a lack of a clear measure of food health and strong targets. We believe they should be ambitious in setting strong and clear targets to improve product nutrition and should be communicating this to the market.

How we differ from the external view

A key agency we subscribe to rates this business highly on 'opportunities in nutrition' relative to peers and while pursuit of such opportunities is a positive, this scoring does not adequately reflect the high portion of food with a low nutrition ranking currently sold by the business.

Genetic sequencing specialist

One of best-ranked companies in the portfolio from a social perspective, this company is the leader in genetic sequencing devices.

What we like

This company is leading a push to dramatically improve human life expectancy and quality of life through fighting the impact of cancer. By developing new liquid biopsy technologies, this company could substantially improve diagnosis for cancers, improve the effectiveness of treatments and improve outcomes for cancer patients.

Areas for improvement

There have been concerns raised about the market power of this company, and the potential for genetic medicine to unfavorably impact society through genetic discrimination. Their technology is still yet to be proven effective for general population screening.

How we differ from the external view

We do not discount the company's social impact due to ethical questions over genetic medicine, believing the potential benefits may significantly outweigh costs. As such, we view their potential social impact at a premium, comparative to many other listed companies.

Tool manufacturer

One of the worst-ranking companies in the portfolio from a governance perspective, this manufacturer did not have a female board member until early 2021, with the board largely made up of entrenched interests and limited independent oversight.

What we like

The company are industry leaders in reducing the environmental impact of tools, replacing petrol powered mowers and diesel generator powered corded tools with energy-efficient cordless tools. The company has taken market share and grown profits through displacing legacy technologies, and shareholders have shared in this growth through strong returns.

Areas for engagement

We welcomed the appointment of the company's first female board director in April 2021, but recognise the company still has significant room for improvement. We believe the business should be encouraged to continue the process of improving governance and strive to be viewed as an ESG leader, which has the potential to drive up the company valuation. We believe best governance practice would be to remove entrenched directors and replace with qualified, independent, diverse voices.

How we differ from the external view

The company is not currently on the radar of the major ESG rating providers we subscribe to.

Computer software and cloud services provider

One of the best-ranking companies in the portfolio from a governance perspective, this company is an industry leader across technology and software, with a strong governance framework in place to preserve management accountability and support shareholder value creation.

What we like

There are 10 of 11 board members who are independent (including the Chair) with very strong current or recent executive experience across technology, consumer, financial services, and healthcare sectors. Ethnicity and gender diversity is also strong with board, including five female members. To ensure high levels of performance and independence, the company seeks to maintain an average tenure of <10 years for independent directors. Widely held, single class share structure is also cleaner and more transparent than some peers.

Areas for engagement

The company has previously been subject to anti-trust investigations and sanctions but has faced less scrutiny than peers in recent years. As a technology provider that is now more integrated in daily lives for work and entertainment, decision making structures and policies need to ensure business integrity and responsible business practices are preserved, including around areas such as potential M&A.

How we differ from the external view

The company is viewed as an ESG leader by external rating providers which is in line with our view. Executive compensation is an area flagged as exceeding broader technology peers, but we generally view this as acceptable given the transformation led and high levels of performance achieved by the current executive team.

Proxy voting

Proxy Voting

56%

Number of meetings voted against management on 1 or more resolutions

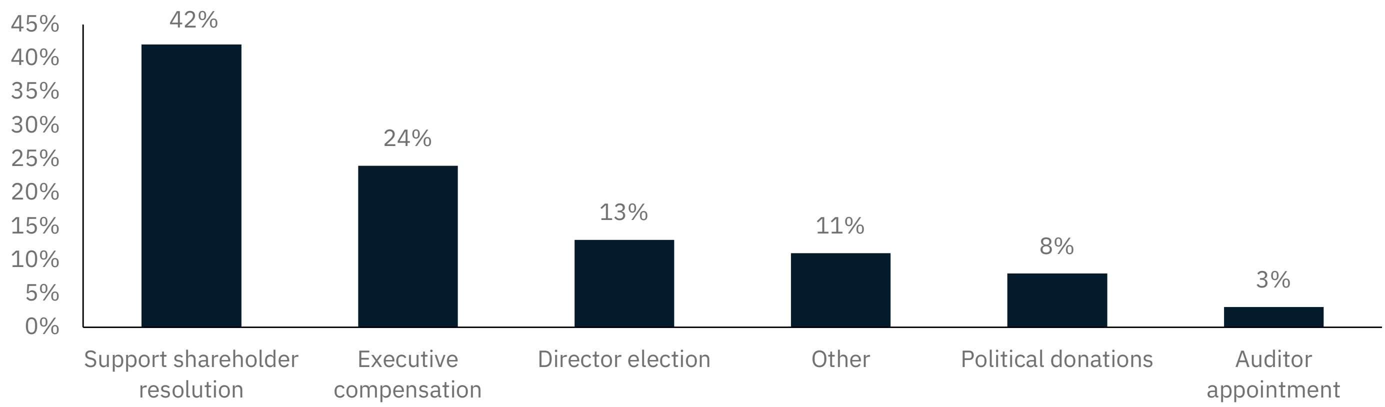
For the Orca team, proxy voting is an important lever for shareholder activism.

Over the year to September 2021, Orca Global Fund voted in 100 per cent of proxies and against management on one or more resolutions at a general meeting 56 per cent of the time.

We find that some of our ESG concerns around a business are often shared by other shareholders. Where this is the case and where we view a shareholder proposal in an AGM is fairly posed i.e. not overly onerous or requesting reports/initiatives a company has already addressed, we make an effort to support such proposals.

As per the chart below, supporting shareholder proposals is the key reason why we have voted against management recommendations in proxies this year.

Rationale for voting against management recommendation



The second key area of focus in proxy voting has been executive compensation – with our team deeming several management remuneration structures to be inadequate. Reasons behind our objections are varied but generally include a lack of breath in performance metrics i.e. focussing on just one or two metrics, upon which discretionary bonuses are determined and/or the use of poorly constructed incentives. One example of this is rewarding Earnings Per Share (**EPS**) growth solely, which may increase management appetite for potentially poor acquisitions and leverage to meet such hurdles.

We look more favourably at longer-term metrics such as organic growth.

This year was an unusual year for many organisations given the impact of COVID, with many short-term earnings hurdles not met, given the decline in earnings related to the pandemic. Despite this, several boards of our portfolio companies recommended the award of short-term incentives given their executives 'handling of the COVID crisis'.

For one of our holdings, we voted against such a proposal given the company had reduced its workforce in the 1000's during the COVID outbreak.

When considering executive compensation structures, we score favourably in our ESG-rating model those companies who include sustainability metrics in the determination of executive incentives. However, despite our preference for the inclusion of these metrics, we do note that these metrics remain in their infancy and some do not include a clear and tangible link between sustainability targets and organisational materiality. For example, one of our portfolio holdings defines several metrics for sustainability targets and yet chooses only a couple of these, without apparent rationale, for the purposes of setting executive compensation hurdles.

Sustainability targets and their impact on executive compensation are a source of ongoing discussion with our portfolio companies.

The Orca Global Fund team

Ted Alexander

Portfolio Manager & Head of Investments

Ted is Head of Investments at Orca Funds Management and Portfolio Manager for the Orca Asia Fund and the Orca Global Fund.

Prior to this Ted worked at Magellan Financial Group where he was Portfolio Manager and Head of Healthcare, as well as being a voting member of the Investment Committee and the Macro Committee.

Ted also previously worked as a Portfolio Manager at Neptune Investment Management, where he was Head of Alternative Investments, Head of Technology and Telecoms and ran several strategies including European Long/Short Equities, Global Long/Short Equities, UK Equities, International Bonds, and UK Corporate Bonds. He initially commenced his career at the Reserve Bank of Australia.

Ted holds a Master of Philosophy in Economics from Oxford University, where he was a Rhodes Scholar, and has a Bachelor of Economics with First Class Honours from the University of Tasmania.

Kunal Valia

Assistant Portfolio Manager

Kunal is Assistant Portfolio Manager for the Orca Global Fund and Senior Analyst for the Orca Asia Fund.

Prior to his current position, Kunal worked as a healthcare analyst at Magellan Financial Group for three years where he analysed large global pharmaceutical and health service companies and carried out research to support investments.

As a qualified Doctor of Medicine, Kunal has formerly practised across different hospitals in Australia for six years, before deciding to eventually leverage his medical experience and follow his passion for investments.

Kunal holds a Master of Applied Finance from Macquarie University and has a Bachelor of Medicine and Surgery from the Maharashtra University of Health Sciences. He is also a CFA Charterholder.

Jumana Nahhas

Assistant Portfolio Manager

Jumana is Assistant Portfolio Manager for the Orca Global Flagship Fund.

She has more than 12 years of dedicated equities research experience spanning the European markets as well as select markets across the Asia Pacific.

Prior to joining the Orc Funds team, Jumana lived in London for eight years where she was an investment analyst at Lansdowne Partners, working on the Lansdowne European Equity Fund (long/short strategy) and a senior analyst at CFRA Investment Research, publishing reports on companies that underperformed markets. Jumana also spent time in the equities research division at Credit Suisse, where she covered the Australian Insurance sector.

Jumana holds a Bachelor of Science and Bachelor of Commerce with First Class Honours from the University of Sydney.

Important information

This document has been prepared and issued by Orca Funds Management Pty Limited (**Investment Manager**) (ACN 619 080 045, CAR No. 1255264), as investment manager for the Orca Global Fund (**Fund**) (ARSN 158 717 072). The Trust Company (**RE Services**) Limited (ABN 45 003 278 831, AFSL 235150) is the Responsible Entity of the Fund. For further information on the Fund please refer to the PDS and Target Market Determination which is available a orcafunds.com.au.

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