PRUDENTIAL

Powering change:

unleashing stewardship as an asset owner for a just and inclusive transition

September 2024

Content

1	**Introduction**	**01**
2	**Engagement in Emerging Markets – State of Play**	**03**
	2.1 Engagement requests for corporates in emerging markets	04
	2.2 Collaborative Engagements	05
	2.3 Stewardship codes	05
	2.4 Importance of local circumstances	06
	2.5 Importance of ownership structure	06
	2.6 Representation of emerging markets in Responsible Investment activities	07
	2.6.1 Sovereign Bonds	08
3	**Our approach to engagement**	**09**
	3.1 Corporate engagement	10
	3.1.1 Engagement process	11
	3.2 Proxy voting strategy	13
	3.2.1 Guidance on Climate Mitigation	14
	3.3 Asset manager engagement	15
	3.4 Policy engagement	16

1 Introduction

We are dedicated to Responsible Investment, integrating Environmental, Social and Governance (ESG) factors into our investment decisions in a way appropriate for our markets.

We strongly believe in the importance of engagement

We believe that sustainability and economic well-being go hand in hand. Engagement on active management of ESG risks and opportunities will lead to sustainable business practices, reduce risk and enhance long-term returns.

We emphasise engagement over divestment whenever possible. Our concern is that divestment can widen the already significant financing gap[1] in emerging markets, and according to regulators will not get us to net zero[2].

By supporting a 'just and inclusive transition', we aim to encourage decarbonisation without compromising social and economic development, avoiding the unintended consequences of divestment.

This document is intended to be a technical paper and should be read by audiences with requisite understanding of finance, investment and Environmental, Social and Governance (ESG) knowledge, including (but not limited to) knowledge on Climate Change and Climate Transition.

Prudential plc is an international company incorporated in the United Kingdom. Prudential plc is not affiliated in any manner with Prudential Financial, Inc., a company whose principal place of business is in the United States of America or with the Prudential Assurance Company, a subsidiary of M&G plc, a company incorporated in the United Kingdom.

What does the just and inclusive transition mean to Prudential?

The International Labour Organization defines a just and inclusive transition as 'greening the economy in a way that is as fair and inclusive as possible to everyone concerned, creating decent work opportunities and leaving no one behind'[3].

Prudential's perspective on 'leaving no one behind when we green the economy' is relevant on two levels:

- **Global level:** All countries need to transition, and none should be left behind, especially the most vulnerable ones; and
- **National level:** Within countries, workers' rights and livelihoods should be secured during the transition, such as ensuring jobs for coal workers in coal-dependent regions.

Prudential's Just & Inclusive transition white paper outlines the case for a just and inclusive transition in emerging markets (the first level). This approach is a core part of our sustainability strategy and underpins our climate change initiatives. We aim to place the considerations for emerging markets at the forefront of our Responsible Investment activities.

Emerging markets are incredibly diverse with varying needs. While this paper groups all emerging and developing countries together as 'emerging markets' we recognise the need for further differentiation and ideally a country-specific approach. We feel that differentiation between developed and emerging markets within Responsible Investment frameworks and standards is a good first step.

1 Source: IEA: Clean energy investment in EMDEs needs to grow from USD 770 billion in 2022 to USD 2.2-2.8 trillion by the early 2030s in order to meet growing demand in a sustainable way, to reach energy-related UN Sustainable Development Goals and to get on track for the outcomes targeted in the Paris Agreement. Scaling up Private Finance for Clean Energy in EMDEs (windows.net)
2 MAS Guidelines for Financial Institutions on Transition Planning for a net zero Economy
3 Climate change and financing a just transition I International Labour Organization (ilo.org)

How is the Just & Inclusive Transition approach aligned to the Paris Agreement?

The Paris Agreement aims to 'hold the increase in the global average temperature to well below 2°C above pre-industrial levels' and to pursue efforts 'to limit the temperature increase to 1.5°C above pre-industrial levels'[4].

Achieving this requires 'making financial flows consistent with a pathway to low-greenhouse gas and climate resilient development' (Article 2.i.c). However, an often-overlooked part of Article 2.i.c is that the goal is not just for finance to support net zero and resilience, but to do so 'in the context of sustainable development and efforts to eradicate poverty'.

Additionally, the Paris agreement includes the principle of common but differentiated responsibilities. While all countries have a duty to take climate action, the types of action they take will depend on their differing national circumstances. Prudential's approach on the Just & Inclusive Transition considers these differing national circumstances and allows for some flexibility with regards to emerging markets.

The aim of this paper is twofold:

1. **Highlight challenges and opportunities:** We focus on the transition in our most important markets, particularly emerging markets.
2. **Explain our engagement approach:** We detail how engagement is a key tool to achieve Responsible Investment and net zero in emerging markets, which we consider crucial to the global transition to net zero.

Prudential's approach to engagement includes three areas:

- **Corporate engagement, including proxy voting;**
- **Asset manager engagement; and**
- **Policy engagement**

Our approach has been assessed against market standards and is in line with applicable taxonomies on the date of publication. The paper and our approach will continue to evolve in line with evolving and transitioning taxonomies, regulation, and market standards and practices.

Creating more growth opportunities in our markets

Prudential is uniquely positioned as both a global and a local asset owner, influencing our engagement approach and collaboration with asset managers. Our role as a local asset owner in many emerging markets in Asia and Africa means we invest a significant portion of our assets in the countries where we operate. In addition, regulatory requirements for local investments necessitate a more selective approach to investment opportunities.

By matching local insurance liabilities with local currency assets, we often become significant buyers of securities traded on local markets, frequently issued by government or state-controlled entities. We believe that this investment positively contributes to local society and to the development of local securities markets. This should lower the overall cost of investment funding in emerging markets, channel individual savings to long-term investments, create more opportunities for economic growth, higher employment and incomes, and, in line with our engagement strategy, support a just transition.

4 Source: The Paris Agreement

2 Engagement in emerging markets – state of play

Emerging markets are crucial for the global energy transition. Although these markets have historically contributed less to cumulative greenhouse gas emissions, most future emissions are projected to come from emerging markets as they continue to develop economically.

Decarbonising the real economy involves decarbonising thousands of companies, both public and private. In the industry, engagement is seen as an effective tool for investors to assist investee companies in this transition. Impactful engagement by asset owners and managers means actively and knowledgeably interacting with investee companies in a constructive way to encourage them to adopt more sustainable business models and reduce their climate risk.

At Prudential, we believe that differences between the markets in which we operate, such as their stage of economic development, are important considerations for how to conduct engagement.

Emerging Markets Transition Investment (EMTI) project

Prudential initiated and led a sub-track within the net zero Asset Owner Alliance (NZAOA) on 'Financing the Transition in Emerging Markets', which includes the EMTI project as a key component. The project's purpose was to identify practical, near-term solutions to accelerate investment towards the net-zero transition of emerging markets. The project was supported by the NZAOA, the World Economic Forum and the EU-ASEAN Business Council.

As part of the EMTI project, we helped develop best practice recommendations on engagement within emerging and developing economies (link). These recommendations set out the following guiding principles for responsible and effective engagement in emerging markets:

1. **Establish a local approach**: Appreciate the complexity and variation of challenges;
2. **Integrate the 'common but differentiated responsibilities' principle** (Paris Agreement): Tailor asks to locally specific social factors and aspects of a just transition;
3. **Prepare for ongoing engagement:** Maintain sustained dialogue to build trust;
4. **Commit to knowledge sharing:** Foster collaboration between global and local investors; and
5. **Be flexible with the engagement ask**: Consider the practicalities around ambitious target setting

2.1 Engagement requests for corporates in emerging markets

Engagement on ESG issues in emerging markets

Many companies in emerging markets are less familiar with engagement on ESG issues. Additionally, companies are at different stages on their transition, so a 'one size fits all' approach is not feasible. A long- term approach is therefore needed, as companies need time to determine how to respond to the engagement.

Starting with sustainability disclosure

Company data is crucial to determine how companies are addressing ESG issues. Initiatives by the International Sustainability Standards Board, and the European Union's Corporate Sustainability Reporting Directive and Corporate Sustainability Due Diligence Directive aim to address this challenge. However, we expect the lack of data to remain a challenge for the near term, especially for emerging markets. Therefore, asking for sustainability disclosure data is usually a good starting point for deeper engagement on credible climate strategies and targets. Disclosure on carbon emissions provides a reasonable foundation for climate engagement, leading to discussions on target setting and transition plans[5]. However, some requests on disclosure can be overwhelming for companies in emerging markets, such as those for CDP[6]. ISSB reporting alignment, and TCFD recommendations.

Bridging the gap

As a company operating in numerous emerging markets, we believe we can bridge the gap between expectations from developed markets and feasibility in emerging markets, and share our experiences with disclosure and transition plans.

Engaging on net zero targets

Many investors, including Prudential, engage with investee companies on setting net zero targets. When doing so it is important to incorporate the 'common but differentiated responsibilities' principle from the Paris Agreement. This principle states that countries that have historically higher greenhouse gas emissions have more responsibility to act on climate change.

Therefore, net zero targets with different timelines are allowed within the Paris agreement.

While we can ask certain companies (for example, those already on a relatively accelerated path) to be more ambitious than their respective governments, as investors we must understand the limitations and sensitivities of doing this.

Challenges with net zero

One practical challenge is that net zero targets set for dates later than 2050 are not always recognised as net zero targets. For example, current net zero target assessment screens by third-party data providers focus on 'best practice', scoring companies only if they have a net zero 2050 target. Companies aligning with a beyond 2050 net zero target of their home country will not be scored well despite their transitioning efforts.

Ambition level of net zero targets

One example of assessing net zero targets of countries which considers different starting points is the net zero Atlas[7] of FTSE Russell. This Atlas estimates the Implied Temperature Rise of countries based on its net zero target and Nationally Determined Contributions. It focuses on emissions per capita and assign percentage shares of the global annual carbon budget to specific countries.

By focusing on emissions per capita and estimating cumulative emissions over time, countries with high emissions per capita are expected to set more ambitious targets. This approach also factors in key macro-economic factors such as population and socio-development.

For example, using this method, FTSE Russell assessed that the implied temperature rise of India's net zero target by 2070 is lower than that of Netherlands' 2050 net zero target. This is because India's starting point on emissions per capita is much lower, thus taking up a smaller share of the global annual carbon budget. This justifies allowing India more time to reach net zero.

5 Source: Jan 2023 EMTI (eu-asean.eu)
6 In full: CDP: Carbon Disclosure Project, ISSB: International Sustainability Standards Board, TCFD: Task Force on Climate-Related Financial Disclosures
7 Source: net zero Atlas

2.2 Collaborative engagements

The importance of collaborative engagements

Collaborative engagements are widely recognised as effective in influencing companies. One opportunity we see is to consult local investors more frequently about global initiatives. Local asset managers are often underrepresented in powerful global collaborative investor engagements, usually because they are not being asked to participate.

Launching global engagements without consulting local investors can be counterproductive for a couple of reasons.

1. **Long-term perspective:** Local investors and fund managers are more likely to take a long-term view of their investments compared to foreign investors and have a better understanding of the local context.
2. **Local significance:** Including local investors in collaborative engagements is a clear signal to the corporate that this topic is also high on the local agenda.

2.3 Stewardship roles

One way to increase local investors' engagement is through stewardship codes. These codes encourage local asset managers to engage with companies and promote good governance and sustainability practices. Investors can ask local regulators or industry bodies to implement or strengthen stewardship codes.

Additionally, we recommend that regulators and industry bodies explore differentiated stewardship codes (or implementation guidelines) for developed versus emerging markets. Each market is unique, and a tiered system could make engagement more meaningful and accessible.

The Malaysian Code for Institutional Investors (MCII)

In 2022, the Institutional Investors Council published the MCII. This code emphasises that 'the collective voice of institutional investors is an important lever in promoting good corporate governance and sustainability practices by investee companies'.

The code is based on an 'apply or explain principle' and includes principles on engagement, monitoring, voting, sustainability issues and disclosure. It also includes expectations, such as requiring investee companies to have at least 30 per cent women representation on their boards, aligning with the Malaysian Code for Corporate Governance.

Prudential's asset management business, Eastspring (Malaysia) publishes an annual statement on their progress in aligning with the stewardship principles set out in the MCII.

2.4 Importance of local circumstances

Local circumstances are crucial to understand the challenges companies face. In addition to sectoral approaches on decarbonisation, we believe a country-specific view is also critically important. Countries can have unique characteristics which need to be considered when assessing the transition potential of companies.

For example, cement producers in Japan are generally more carbon-intensive than their peers in other countries. This is because Japan has a high risk of earthquakes. The government has enacted regulations requiring cement producers to use a higher portion of clinker (burning crushed limestone and other additives under extreme heat) and a higher cement mix in the concrete. This reduces fatalities related to earthquakes but makes Japanese cement producers more carbon intensive.

Data challenges can also be very local. For instance, in Vietnam and Indonesia, data and metric standardisation is still in its early stages (if data is available at all). This adds to the challenge of reaching a common agreement and understanding of what is required for transition.

2.5 Importance of ownership structure

Ownership structures can differ significantly between developed and emerging markets. Emerging markets often have an outsized exposure to family-and state-owned enterprises, many of which can be carbon-intensive (e.g. utility companies).

To successfully engage with these companies, it is essential to bring together investors, global networks, NGOs, regulators, and other stakeholders to drive change. Local banks should play a key role because they provide most financing in emerging markets and already have a close relationship with these companies. Additionally, direct engagement with policymakers can be effective in driving change at state-owned companies[8].

8 Source: Jan 2023 EMTI (eu-asean.eu)

2.6 Representation of emerging markets in Responsible Investment activities

In its Just & Inclusive transition white paper, Prudential highlights that current ESG investment frameworks can lead to less capital being allocated to emerging markets. Although this is often an unintentional consequence of how these frameworks are structured, the impact is concerning. For example, the IMF states that while EMDE Asia makes up about 10% of global assets for non-ESG funds, these assets make up only 2% for ESG funds[9].

Raising awareness of unintentional consequences

Asset owners can raise awareness of these unintentional consequences when engaging with their asset managers:

- **ESG ratings:** ESG ratings of sovereigns and companies are backwards looking and systematically lower for firms in emerging markets[10]. This leads to capital outflow from emerging markets in favour of developed markets if an ESG ratings overlay is applied on a global investment strategy. The same often occurs when a global portfolio is decarbonised, as emerging markets tend to be more carbon intensive. Additionally, research[11] shows that better ESG scores only translate into better sovereign credit ratings for high-income countries. Middle- and low-income countries do not benefit from better energy transition policies.
- **Global decarbonisation pathways:** Companies and countries are judged on their alignment to global decarbonisation pathways, which often only differentiates between sectors but not between countries or the state of economic development. These science-based standards are based on technological feasibility and therefore typically favour countries with more technological and financial resources.
- **Decarbonisation targets:** Many investors have set decarbonisation targets for their investment portfolios. Investing actively in the transition of carbon-intensive companies will increase the carbon footprint of an investor's portfolio, even if that investment is used to finance the energy transition.

Ensuring emerging markets are not unintentionally underweighted or excluded due to ESG considerations should also benefit the risk/return characteristics of the portfolio.

9 International Monetary Fund (IMF), 2024, Unlocking Climate Finance in Asia-Pacific: Transitioning to a Sustainable Future

10 IMF, 2022, Global Financial Stability Report, Chapter 2: Scaling up Private Climate Finance in EMDE

11 Gratcheva, Ekaterina, Bryan O'Reilly Gurhy, Andrius Skarnulis, Fiona Elizabeth Stewart, and Dieter Wang. 2022. 'Credit Worthy: ESG Factors and Sovereign Credit Ratings.' Report, World Bank, Washington, DC.

2.6.1 Sovereign bonds

As an insurance company, we invest significantly in local sovereign bonds. Sovereign bonds are increasingly becoming a focal point in the climate change debate, both from risk management and decarbonisation perspectives.

For calculating the carbon footprint of a sovereign bond, PCAF[12] and other standards primarily focus on a country's production emissions, following the Paris agreement: 'Production emissions are emissions attributable to emissions produced domestically and include domestic consumption and exports'[13].

While consumption emissions (demand-side emissions accounting for consumption patterns and trade effects) are included in frameworks, data availability restricts the integration of this metric in practice.

Production emissions are generally higher for emerging markets, while consumption emissions are generally higher for developed markets[14]. This, combined with the lack of available consumption emissions data, might lead to an unintended consequence of investments being channeled away from emerging markets.

Prudential believes a holistic approach towards sovereign emissions is needed, one that takes imports and consumption emissions into account. We believe the ASCOR[15] project is a good starting point as it provides useful guidance for engaging with sovereigns on their responsibility to act on climate change.

12 In full: Partnership for Carbon Accounting Financials
13 Source: Partnership for Carbon Accounting Financials (PCAF): The Global GHG Accounting and Reporting Standard for the Financial Industry, Part A: Financed Emissions
14 Source: Territorial and consumption-based CO_2 emissions
15 In full: Assessing Sovereign Climate-Related Opportunities and Risks

3 Our approach to engagement

Prudential advocates for localised approaches and frameworks to ensure a Just and Inclusive Transition. While global standards and frameworks are an important driver of progress for that transition, input for our engagement strategy comes from various sources, such as CA100+, IIGCC, AIGCC[16], and NZAOA. These sources help to standardise our engagement requests.

When global standards may not be fully applicable to emerging markets, we amend the application of them to suit the markets in which we operate. For example, our engagement requests related to climate change align with guidance from the NZAOA and refer to the net zero Benchmark of CA100+. We have then integrated the 'common but differentiated responsibilities' principle of the Paris Agreement into our requests to allow flexibility for emerging market operators.

In practice this means that the decarbonisation pathway is considered fair when the stage of economic development of the country is taken into account. The fair share concept of decarbonisation is difficult to quantify, but principles are set out by Climate Action Tracker, the ASCOR project and the Climate Equity Reference Project.

Taking a market-specific approach

In the Just & Inclusive transition white paper, Prudential argues that a one-size-fits-all approach to sustainability, particularly the energy transition, is not fair. It does not account for the considerations of emerging markets, which are often unique to each country.

Prudential is implementing market-specific responsible investment approaches, which will complement our Group Responsible Investment Policy on the website. The objective is to have a more impactful approach to responsible investment in the markets in which we operate. We aim to maximise our position as a local asset owner, especially since we often have our wholly-owned asset manager operating in the same markets.

In practice, this means focusing on the most material sustainability topics for a particular market. For example, in Malaysia, the key sustainability topics are climate change (e.g. the coal transition), biodiversity and human rights (e.g. labour rights). Malaysia also has new regulations on sustainability for financial institutions and corporates. This provides an opportunity to engage with both corporates and policymakers/regulators. All these factors shape our market-specific engagement approach in Malaysia.

16 In full: CA100+: Climate Action 100+, IIGCC: The Institutional Investors Group on Climate Change, AIGCC: Asia Investor Group on Climate Change

3.1 Corporate engagement

Targets and policy

Prudential is an asset owner and has a wholly-owned asset manager. Asset management activities are performed by our asset management arm Eastspring Investments ('Eastspring')[17] and other external asset managers. These asset managers are responsible for corporate engagement as they invest on behalf of Prudential.

Prudential, as an asset owner, has defined targets and policies on engagement, which will be implemented by our asset managers. We believe that collaboration amongst investors is an effective way to address ESG issues and maximise investor influence. Therefore, Eastspring actively participates in carefully selected collaborative engagements.

The following table summarises Prudential's activities on corporate engagement.

<table>
<tr><td>Corporate Engagement Target</td><td>Climate Change</td><td>We engage with companies responsible for 65 per cent of the absolute emissions (measured by scope 1 and 2) in our investment portfolio.</td></tr>
<tr><td rowspan="8">Bilateral Corporate Engagement Initiatives</td><td>Biodiversity – palm oil</td><td>We engage with the entire palm oil supply chain, including producers, buyers and other relevant stakeholders. All actors in the supply chain have a responsibility to encourage sustainable palm oil production.</td></tr>
<tr><td>Biodiversity – timber</td><td>We engage with companies that have been identified as producing timber, depending on, or using commodities that contribute to deforestation. Engagement asks include credible deforestation policies and commitments to responsible timber /paper sourcing with an explicit reference to biodiversity.</td></tr>
<tr><td>Climate change, scope 3 emissions</td><td>We engage with the top 20 investee companies with the highest scope 3 emissions in the investment portfolio.</td></tr>
<tr><td>UN Global Compact</td><td>We engage with companies identified by an external party as violators of the United Nations Global Compact.</td></tr>
<tr><td>Financial materiality</td><td>We engage on financially material ESG risks identified through the ESG integration process.</td></tr>
<tr><td>Engagement with ESG 'laggards'</td><td>We engage with companies identified as laggards on ESG. We rely on third party and internal ESG and market research, including ESG controversy tracking, to determine companies that may be engaging in practices affecting a company's license to operate. Engagement seeks to monitor and clarify mitigating actions taken by the company.</td></tr>
<tr><td>Local engagement</td><td>We engage on relevant local ESG considerations, including adherence to regulatory implementation. While asset managers have the discretion to identify material ESG issues, we set minimum expectations for engagement on specific topics (as set out in this paper). Additionally, we ask asset managers to comply and prioritise local regulations, such as the Climate Change and Principle-based Taxonomy launched by Bank Negara, the central bank for Malaysia.</td></tr>
</table>

17 For more information, see Eastspring Group Responsible Investment Policy on the website and Responsible Investment Report 2023

Collaborative Investor Engagements	**Corporate Governance**	Asia Corporate Governance Association
	Climate change	• Asia Investor Group on Climate Change • AIGCC Asian Utilities Engagement Programme • Carbon Disclosure Project • Climate Action 100+
	Biodiversity	• PRI Spring Initiative • Eastspring joined the PRI Nature Stewardship Advisory Committee, a steering group seeking to establish engagement priorities on nature and biodiversity

The exact definitions for above policies are available in the Group Responsible Investment Policy, which is accessible on the linked website.

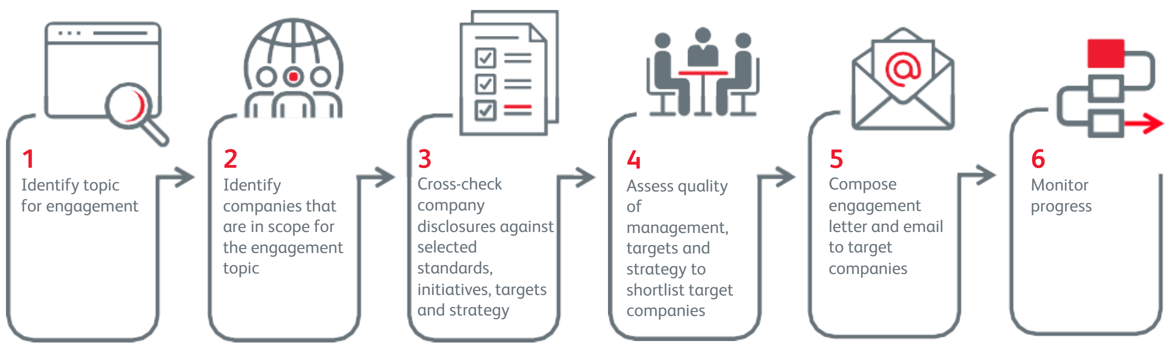
3.1.1 Engagement process

Engagement process

Eastspring's Central Engagement programme enables them to communicate their expectations on material ESG themes to select investee companies. The programme's objectives are based on Eastspring's judgment of materiality to investment portfolios.

To ensure effective engagement, a dedicated Central Engagement team works closely with Eastspring portfolio managers to enhance understanding and minimise misalignment. For each identified material ESG theme, the Central Engagement team follows a six-step process to implement the programme:

Central engagement cycle



Eastspring monitors and reports engagement progress using milestones rated at different levels. Each engagement is pursued continuously, until it reaches the highest milestone, **'Level 5: Company has satisfactorily resolved the issue'**.

As the intended objectives of engagements differ per company, the definition of 'satisfactorily resolved' will also differ. For example, an engagement on sustainable palm oil will be satisfactorily resolved if the company successfully obtains the relevant certification.

Measuring and monitoring progress through these milestones is crucial for active ownership and driving positive outcomes. This process is also essential for the escalation process, detailed further below.

For climate engagement targets, the ratings are communicated annually in the Group Sustainability Report.

Engagement across asset classes

Traditionally, engagement has focused on listed equity assets, as investors assume partial ownership of a company. However, Prudential intends to use its influence as an investor as effectively as possible, extending beyond just equity. Prudential believes investors can also exert influence when financing a company through debt and private company financing.

Engagement through corporate bonds can be particularly effective in Prudential's markets, as debt financing is more relevant in emerging markets[18]. As an insurance company, our allocation to corporate bonds is significant. Additionally, engagement through debt may give easier access to corporate management. Engagement on sustainable finance, especially through labelled bonds with additional sustainability-linked covenants, can be effective due to the prospect of access to additional capital[19].

Therefore, our targets and policies do not differentiate between asset classes and apply to all where feasible. Our target for corporate engagement on climate change is set on the current carbon footprint of the portfolio, which includes both debt and equity.

Prudential's influence on private companies is more limited, as we do not directly invest in these companies. Instead, our engagement focuses on the private asset managers that manage the investment funds in which we invest.

Milestone 1
Raised awareness of issue with company

Milestone 2
Dialogue in process

Milestone 3
Company has agreed to address the issue

Milestone 4
Company has developed or are planning to implement a plan to address the issue

Milestone 5
Company has satisfactorily resolved the issue

Lessons learned during climate engagement

In 2021, Prudential set a target to engage with companies responsible for 65 per cent of the absolute (financed) emissions in our investment portfolio. Eastspring has been engaging with these companies, many of which are in Asia. Eastspring shares their lessons learned in their 2023 Responsible Investment report, and has found:

- Effective engagement is inherently long-term engagement
- Awareness translates to action
- Progress needs to be contextualised for different economies

18 World Bank Group, Corporate Borrowing in Emerging Markets: Fairly Long Term, but Only for a Few, 2018
19 Jan 2023 EMTI (eu-asean.eu)

Escalation process

To increase the impact of our engagement approach, issues can be escalated. Judgement is applied in all engagements, and the strategy for escalation is determined on a case-by-case basis due to the unique circumstances of each situation. The following are typical engagement escalation measures that Eastspring may choose to employ:

- Direct dialogue with management
- Collaborative engagements
- Proxy voting
- Shareholder resolutions
- Divestment as a last resort

We continue to engage after divestment

Prudential's coal policy mandates divestment from all direct investments in businesses that derive more than 30 per cent of their income from coal (whether mining or energy production). This policy balances our stewardship duties in emerging markets while allowing companies in those markets to phase out coal in a just and inclusive manner.

To support this, Eastspring continues to engage with excluded/divested coal companies, encouraging them to continue to decarbonise and potentially return to the investable universe. Additionally, Eastspring engages with these companies on financing their transition through labelled bonds and setting Paris-aligned targets, as Prudential has an exemption policy for these circumstances.

3.2 Proxy voting policy

Prudential's voting rights are exercised by the managers who invest on behalf of Prudential, one of which may be Eastspring. Eastspring's voting policy is set out in this section.

An active and informed voting policy is a core part of our direct equity investment philosophy and approach to active ownership. As a starting point, we are supportive of the boards and executive management of companies in which we invest. However, when companies consistently fail to achieve our reasonable expectations, we will consider promoting changes through proxy voting.

Eastspring follows a principles-based approach, considering all votes within the guidelines set out in the Eastspring Group Responsible Investment Policy (available in the download section on the website). They consider issues, meet with company leadership if necessary and applicable to the investment strategy, and vote accordingly. Where possible, they seek to discuss any contentious resolutions with investee companies before voting.

3.2.1 Guidance on Climate Mitigation

The principles-based voting approach allows flexibility for portfolio managers to vote as they see fit. However, with increasing strategies and shareholder proposals on climate change that are put to vote, Prudential has formulated additional guidelines on climate change. In addition to following this guidance, Eastspring also engages with proxy advisors regularly to ensure conscious voting.

Climate proposals by management

We are increasingly aware of climate proposals by management of corporates, especially as part of the 'Say on Climate' initiatives. Prudential generally votes (through its asset managers) in favour of decarbonisation strategies aligned with the Paris Agreement. Asset managers assess proposals case-by-case, considering:

- Application of the 'common but differentiated responsibilities' principle of the Paris Agreement, especially when voting on proposals by corporates operating in emerging markets. In practice this means that the climate proposal is in line with a decarbonisation pathway that is considered fair for a country at a specific stage of economic development
    - The fair share concept of decarbonisation is difficult to quantify, but principles are set out by Climate Action Tracker, the ASCOR project and the Climate Equity Reference Project
- Decarbonisation strategies should cover scope 1, 2 and where possible, material scope 3 carbon emissions. Materiality of scope 3 should be determined via a relevance assessment that considers factors such as size, influence, risk, and sector guidance[20]
- Clear prioritisation of emissions reduction activities and initiatives over offsetting
- Support from a capital expenditure plan
- Disclosure of climate-related financial risk, preferably aligned to the TCFD recommendations

Shareholder proposals

Prudential generally votes in favour of shareholder proposals that are in line with the Paris Agreement and takes the above considerations into account. We may vote against proposals that are unrealistic or disadvantageous to the company compared to competitors or government.

20 Corporate Value Chain (Scope 3) Accounting and Reporting Standard

3.3 Asset manager engagement

As an asset owner, engaging with asset managers is crucial to ensure that they align their stewardship activities and public messaging with our long-term interests. Asset managers make several decisions on behalf of asset owners within the boundaries defined by the asset owner. These decisions range from deciding which securities to invest in, engaging with corporates and voting.

In addition, asset managers have their own approaches to policy engagement and public advocacy and are very active participants in the financial industry. On climate, this influence has prompted the establishment of the net zero Asset Manager Initiative.

Prudential and Eastspring, as affiliated companies with the Prudential plc group, are aligned in our approach to active ownership. Prudential engages with its external asset managers on ESG expectations and specific requirements on Responsible Investment (e.g. exclusions, need for ESG-integration, decarbonisation and other Sustainability targets). This engagement extends beyond ESG integration into the manager selection process, as detailed in the Group Sustainability report. For asset managers new to certain engagement themes, Prudential arranges ad hoc working sessions to provide further guidance to ensure effective integration.

In addition to bilateral engagement with external asset managers, Prudential actively participates in collaborative asset manager engagements through the Engagement Track of the net zero Asset Owner Alliance (NZAOA). The NZAOA engages asset managers on[21]:

- Their voting practices
- Their climate policy engagement
- Expectations on their corporate engagement practices

21 The expectations of the NZAOA are set out in respective papers available on the website

3.4 Policy engagement

In each of our markets, Prudential proactively engages and maintains strategic and working relationships with local policy stakeholders. We believe in the critical role that government and its key institutions – ministries, central banks and regulators – play in developing a bespoke position and plan on net zero. These are crucial in ensuring realistic pathways to national energy transition goals and managing climate risk. Policy engagement is therefore key to our engagement approach.

Historically, Prudential has played a proactive and supportive role collaborating with governments and regulators globally, including in the UK, Asia and Africa, on a range of policy and regulatory issues as governments and regulators have sought to ensure their financial sectors were 'fit for purpose' and could support their own national development objectives. Our past engagements included capacity building, best practice-sharing across jurisdictions and domestic capital market development. The development of sustainable finance strategies and instruments with our policy stakeholders is the next important step on this journey.

We engage proactively in several key areas, including:

- Development of domestic guarantees to channel climate finance,
- Regulatory reform,
- Labelled bond markets and other vehicles to mobilise finance (including through blended finance).

As a major provider of Takaful (Sharia Compliant) insurance in Asia, Prudential also believes we have a role and responsibility in supporting the development of sustainable Islamic finance in markets where these products are prominent.

We acknowledge that a strong element of mobilising the right money to the right places needs partnerships, including with industry associations and through an active engagement strategy with governments. We are working bilaterally and multilaterally to engage our stakeholders to support these journeys. This includes support for transitional finance in markets at different stages of development compared to more developed markets.

We believe that blended finance will be of increasing interest to policymakers in Asia and Africa in 2024 and beyond, and we aim to build out our work in this area. Prudential's chair, Shriti Vadera, is currently co- chairing with Mark Carney the World Bank Private Investment Lab, focusing on leveraging private finance for investment in emerging markets.

We are working to support messaging on multilateral development bank (MDB) reform to unlock real potential for practical partnership in mobilising finance. This is not new; we have some experience in blended finance. But we believe much can be done in partnership with public or MDB partners to structure these projects, and navigate local legal and regulatory barriers before institutional investors can contribute meaningfully.

Prudential's role in Vietnam's Just Energy Transition Partnership

In December 2022, Prudential was announced as the insurance partner on the private sector working group for Vietnam's Just Energy Transition Partnership (JETP). We are proud to support Vietnam in achieving their ambitious net zero targets.

The JETP aims to ramp up renewable energy and accelerate the phasing down of fossil fuels, while investing in transition-aligned jobs and industries of the future. Alongside providing the long-term asset owner perspective, we contribute local knowledge through the involvement of colleagues from Prudential Vietnam and Eastspring Vietnam, as well as support from Prudential's head office.

For a detailed update on our policy and regulatory engagement activities and initiatives throughout the year, please see our 2023 Sustainability Report.

Workshop in Vietnam: Accelerating the development of the labelled bond market

Prudential and Climate Bonds Initiatives (CBI) organised a labelled bond and transition investment workshop on 6th July 2023 in Vietnam. The workshop aimed to gather feedback from market participants to understand the challenges and issues in scaling up the labelled bond market in Vietnam.

The workshop identified key issues and initial considerations for solutions to discuss with the Vietnamese government:

- **National taxonomy and standards** for green bond issuance, disclosure and reporting regime are needed to advance the development;
- **Capability enhancement** of stakeholders and establishment of an ecosystem (consulting companies, rating agency, financial advisors);
- **Supply and demand drivers:** intervening to close the yield gap between issuers and buyers to initiate the market; and
- **Reporting and disclosure requirements:** that appropriately consider and account for multinationals, mid-sized corporates, and small and medium-sized enterprises.

Prudential plc
Powering change: unleashing stewardship as an asset owner for a just and inclusive transition (September 2024)

www.prudentialplc.com

Lead author

Liza Jansen
Head of Responsible Investment
Prudential plc

Supporting authors

Enci Wang
Senior Manager, Responsible Investment
Prudential plc

Diana Guzman
Chief Sustainability Officer
Prudential plc