



Food Supply Chain Thematic Engagement

FINAL ANALYSIS FOR AP7
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INTRODUCTION

This is the final analysis prepared for AP7, reflecting on 2,5 years of Food Supply Chain Thematic Engagement. It includes an overview of the current state of play as compared to early 2018, when a pre-study, commissioned by AP7, was made ahead of initiating the engagement. Further, this report presents an assessment of engagement impacts, lessons learned, as well as a commentary on remaining gaps and suggested areas for further efforts and engagement.

As pointed out in the pre-study for the Food Supply Chain Thematic Engagement, agriculture is the sector with the highest prevalence of child labour: 70 % of all child labour globally is found here. There is also an elevated risk and occurrence of forced labour. This engagement, therefore, focused on labour-related challenges in the agricultural part of food supply chains. Making this issue material is the fact that companies are dependent on the workforce for their agricultural supply, often experiencing poor livelihoods, while there is a clear trend of farmers and agricultural workers leaving rural areas in search of better lives. Providing better working and living conditions for rural populations is therefore in companies' long-term interests. Several countries, and likely the EU, are introducing similar legislation to the earlier adopted UK Modern Slavery Act and California Transparency in Supply Chain Act. The implications for companies relying on the agricultural supply chains where labour rights violations are rampant may therefore be costly and also include reputational and legal risks. Alignment with new legal requirements is being established in the industry, particularly in light of the current review of EU mandated disclosures.

Together with AP7 and a global group of investors, Sustainalytics has encouraged food & beverage and food retailing companies to address risks of child labour and forced labour in their supply chains, as well as to remediate other potential adverse labour rights impacts. After being identified in the pre-study as high-risk commodities, particular focus was placed on coffee, rice, sugar, tea and tomatoes. Living income and living wages for smallholder and agricultural workers have been specifically highlighted in the engagement, as this topic was noted in the pre-study as a root cause behind labour rights issues and one on which there was a growing momentum of corporate attention in 2018.

REFLECTIONS ON SECTOR AND TOPIC DEVELOPMENTS

Since the start of this thematic engagement in 2018, it is clear that progress has been made in terms of advancing policies and due diligence of labour rights in agricultural supply chains by almost all companies targeted in the engagement. Leading companies have also advanced their work in terms of mitigating elevated labour rights risks and improving farmer livelihoods. On the latter, quite some progress is noted in the area of living income for smallholders and living wage for agricultural workers, as a mean to get to the root cause behind many labour rights concerns – poverty and insufficient remuneration enabling a decent standard of living.

The pandemic, child labour and vulnerable workers

While the above is positive, and we will dive deeper into some of the mentioned topics later in the report, the COVID-19 pandemic has, of course, both overshadowed and reversed some of the progress made. Not only has it changed consumer demands and created logistical challenges for the food industry, but it has also severely affected those making a living from agricultural production.

“As the pandemic wreaks havoc on family incomes, without support, many could resort to child labour.” ILO Director-General, Guy Ryder.

The International Labour Organization (ILO) and UNICEF estimate that, compared to before the pandemic and economic crisis, the number of people in extreme poverty could have increased by between 40 to 60 million in 2020 alone. The organizations also note that to secure livelihoods, child labour is a likely resort for many households in poverty. While there are variations by country, causal estimates between poverty and child labour, according to ILO and UNICEF, is that a 1 percentage point rise in poverty leads to at least a 0.7 percentage point increase in child labour.¹ In other words, it would mean an estimated increase in child labour globally of 28-42 million children. In this context, one should remember that global estimated levels of child labour when we started this thematic engagement was 152 million, of which more than 70 % were found in agriculture. These are still the latest global estimates issued by the ILO.² One should, of course, be careful to draw exact conclusions from uncertain estimates in 2020, but the general picture of it is clear – the risk of substantially increased child labour in the wake of the global pandemic is very high. It is also likely that agriculture, the sector with the highest prevalence of child labour in ILO’s 2017 estimate, is likely to have taken a big hit from the pandemic. By the time of writing, ILO and UNICEF are developing a simulation model to better understand the impacts of the pandemic on child labour globally. New global estimates on child labour will be released in 2021 by the ILO.³

Migrant workers and other groups at risk of being involved in forced labour risks are also likely to have taken an unproportionate hit by the global economic downturn.⁴ With the above realizations in mind,

¹ https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---ipec/documents/publication/wcms_747421.pdf

² https://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_575499.pdf

³ https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---ipec/documents/publication/wcms_747421.pdf

⁴ <https://www.antislavery.org/covid-19-and-slavery-the-five-big-impacts/>; https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---ipec/documents/publication/wcms_745287.pdf

it makes it more important than ever to address poverty as a root cause both to child labour and as a means to improve livelihood for vulnerable groups. Below we reflect on interesting developments in advancing corporate responses to living income and living wages, as well as highlight a new initiative to address forced labour. We also report on a new corporate initiative against forced labour in the food sector.

Living income – initial momentum has increased in strength

As we embarked on this thematic engagement in 2018 and prepared the pre-study commissioned by AP7, we spoke to several stakeholders specialized in labour rights issues in agricultural supply chains. From such dialogues and our own experience from other engagements initiatives, we could clearly see living income and living wage gaining momentum, and an emerging uptake from some companies of the topic. This was particularly evident in the cocoa sector and the tea industry with the well-recognized Malawi 2020 initiative, among others, on living income and living wages for Malawian tea farmers and workers. Since then, a lot has happened in this area. Several multi-stakeholder networks and collaborations are actively contributing to advancements. During this engagement, we have clearly seen this momentum grow and we have made efforts to further support its development.

There is a wealth of reports and guidance issued in the last couple of years alone. Clearly, there is also an uptake from a growing group of companies, industry initiatives and other standard-setting bodies, on how to develop corporate roadmaps on living income and living wages. Besides further developments in the cocoa and tea sectors, individual companies have also embarked on living income specific initiatives in the rice and coffee sectors. Bonsucro, the standard-setting body on sustainable sugar cane production, is in the middle of reviewing its standard. It appears as if the new version will include stronger provisions on living income and living wages. Sustainalytics has provided input in favour of this.

To further drive developments in the area of living income, in spring 2020, Sustainalytics drafted and coordinated an investor statement on living income and living wages. It was sent to the CEO and Chairpersons of more than 40 food and beverage companies and food retailers globally, among them the companies targeted in this thematic engagement. The aim was to communicate a strong investor commitment to the issue, adding the investor voice and support to a growing number of initiatives, networks, and guiding tools. The statement saw strong investor support, signed by 36 institutional investors globally, with a combined AUM of USD 2.4 trillion. Besides follow-up calls with companies, Sustainalytics also co-hosted a webinar with the Living Income Community of Practice on how to build a corporate roadmap towards living income for smallholders. Ahead of the webinar, a survey was sent to food and beverage companies to better understand challenges and current adoption of living income roadmaps. A challenge highlighted by the companies was to define the business case for living income and a reluctance to make a forward-looking commitment in the area before more progress had been secured from company-led income generating activities among small-scale food producers.

While it is difficult to prove a causal link, Sustainalytics believes that this collaborative thematic engagement has played a role in driving continuous developments in the area of living income – through the investor letter, the survey, bilateral calls with companies as well as the webinar.

New initiative to address forced labour

A considerable new initiative within the scope of this engagement was announced in December 2020. The Consumer Goods Forum (CGF), encompassing some of the largest corporate players in the food sector, announced a collective stance against forced labour with the creation of the CGF's new Human Rights Coalition – Working to End Forced Labour. The coalition, comprising of 20 companies, is a CEO-led initiative to drive collaborative action.

The coalition's work is guided by the CGF's Priority Industry Principles, which were developed to address the core drivers of forced labour:

- Every Worker should have freedom of movement.
- No Worker should pay for a job.
- No Worker should be indebted or coerced to work.

Members have developed a strategy to identify and address actual and potential forced labour risks and impacts in their operations through the deployment of forced labour-focused human rights due diligence systems. The coalition is focusing, but not limiting, its efforts on the risks for forced labour in the palm oil sector. Members will support responsible recruitment using both company leverage within their operations and collective engagement in selected geographies and commodities, also beyond palm oil.

In the wake of the pandemic, a broad coalition and effort on this topic is of course positive news, and necessary to regain what has been lost in terms of labour conditions following the COVID-19 crisis.

Human rights due diligence legislation rapidly developing

If the pandemic is the main negative development this year, a more positive one is the rapidly evolving legal landscape on human rights due diligence. A growing number of countries, e.g. the UK, the Netherlands, France, and Australia, already have legal requirements on corporate human rights due diligence of some kind, most of them focused on reporting requirements. Similar legislations are also underway in Germany. Since the end of 2019, the odds for EU-level human rights due diligence legislation has substantially increased, and it is likely that such a legislation would be adopted in the latter part of 2021.⁵

There seems to be a good level of support also from businesses. Companies we are and have been in dialogue with primarily point to how the legislation would level the playing field. Support is also evident from 26 companies which, in 2020, issued a public statement in support of such EU wide legislation. This was followed by a similar statement by a large group of investors.

All in all, it has been an intense period of both positive and negative developments in relation to labour rights and livelihood for farmers and workers in our global food system. Significant challenges remain, not the least as we are still in the middle of the pandemic. At the same time, legal developments and increased private sector action speak to a more positive outlook.

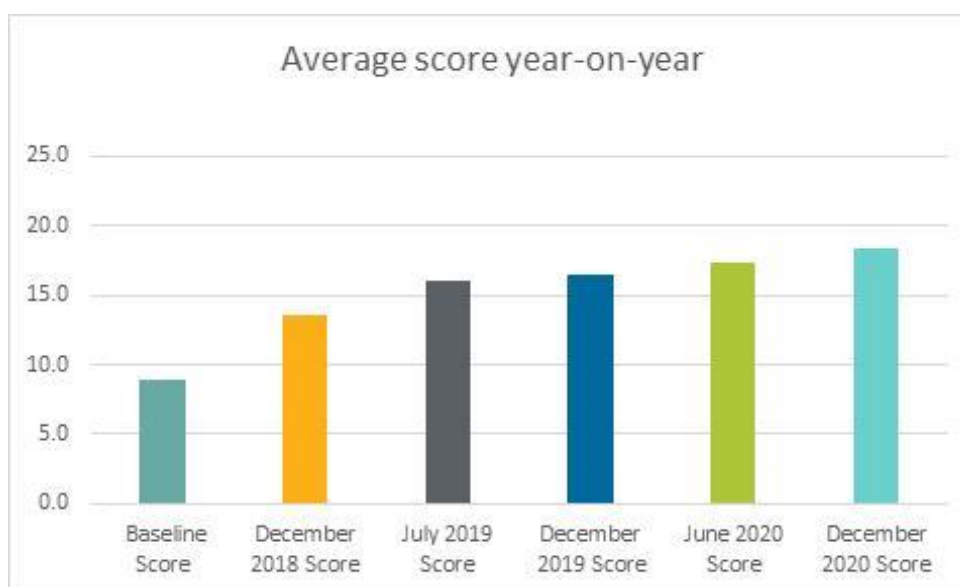
⁵ <https://shiftproject.org/resource/mhrdd-europe-map/>

ASSESSMENT OF ENGAGEMENT IMPACTS

The overall progress of the engagement

As we ended this engagement some interesting conclusions could be drawn vis-à-vis where we started. Adding up the scores for each of our five KPIs, the maximum possible score is 28. When we issued our baseline report in June 2018 the average score for the targeted companies was 8.9. By the time of our first biannual report in December 2018, the average had increased to 13.6. This early and substantial increase can largely be attributed to the fact that we had held the first round of engagement calls and meetings with most companies and had received substantially more information in this direct contact with the companies, compared to the publicly available material that we created the baseline report on. An important take-away from this is that improved disclosure is a fairly low-hanging fruit for companies to showcase and get credit for the work they actually already conduct and that this is an important point for investors to encourage in their endeavour to get access to as complete information as possible of their investee companies. The need for transparency and improved public reporting, in particular, have indeed been pointed out to companies throughout this engagement.

The first six months between the baseline and first biannual report aside, the progress does not have a public reporting bias as our assessment from that point onwards considered both public reporting and information obtained in direct dialogue with the companies. As is evident in Graph 1 below, substantial progress has taken place with average scores increasing from 13.6 in December 2018 to 18.4 in December 2020. Worded differently, it means we started with 39% of our KPIs being fulfilled when reviewing public reports for the baseline study. By the time of our first biannual report, having obtained additional information from dialogues with the companies, fulfillment had increased to 49% in December 2018. As we conclude the engagement in December 2020, we have reached an average level of fulfillment of 65% by the 17 companies targeted in the engagement, i.e., an improvement from the baseline of 26%. From the first biannual report, we have seen an improvement of 16%.



Graph 1: Average score year on year for all companies

Company progress

A diverse picture appears in terms of final scores for companies targeted in the engagement. The best-performing company finished with a score of 25.3 out of maximum 28. The lowest scoring company finishes with a score of 11.3. Looking at the scores and summarizing the output from engagement meetings with the companies, three segments of leading, mid-level and lagging companies have crystalized:

- **Leading companies** are typically piloting innovative and cutting-edge interventions in their agricultural supply chains to mitigate labour rights risks and work towards living income and living wages. They have robust due diligence processes in place.
- **Mid-level companies** have due diligence procedures in place and might be doing some ad hoc forms of mitigative work.
- **Lagging companies** have policies in place on labour rights and might have some due diligence procedures, but not very comprehensive and lack a plan to mitigate identified risks.

Notably, a number of the ‘leading companies’ started in 2018 as ‘mid-level companies’. Those companies have strengthened their labour rights due diligence since 2018 and have made considerable efforts in mitigative work to address labour rights risks in their supply chains. Companies that already in 2018 were industry leaders took additional steps in addressing labour rights issues in their agricultural supply chains. Some lagging companies also developed into mid-level companies.

Similarly, there is a variation in terms of fulfillment of the five KPIs set up to measure progress by the companies targeted by the engagement. KPI 1 on supplier code of conduct on the respect of human rights and KPI 4 on remediation of adverse labour rights impacts were completely fulfilled by all targeted 17 companies by the end of the engagement in December 2020. KPI 2 on labour rights due diligence has improved considerably since the start of the engagement, with 75% fulfillment at the end of the project. The least successful KPIs are KPI 3 on mitigation of elevated labour rights risks and KPI 5 on prioritizing collaboration on labour rights risk - both KPIs have improved from 25% to 50% level of fulfillment. These are by far the most demanding areas in terms of capacity, as we asked for substantial mitigative and collaborative measures throughout the companies’ various agricultural supply chains. However, several leading companies are making relatively extensive such efforts.

ENGAGEMENT ACTIVITIES AND LESSONS LEARNT

In the course of this thematic engagement, Sustainalytics, together with participating investors, conducted 75 engagement meetings, including several in-person meetings. Sustainalytics also sent approximately 600 emails and have drafted, sent, and coordinated responses to a living income and living wage investor statement. In addition, Sustainalytics organized an engagement trip to visit Italian food producers and hosted a follow-up virtual roundtable to share experiences and good practices in addressing labour rights issues in this context. Sustainalytics have also helped organize a living income survey and webinar and developed good practice material on living income and labour rights due diligence to share good practice and guidance to companies targeted in this engagement. Below we provide a selection of our engagement efforts and offer some reflections.

Good practice trip to Italy

A highlight during this thematic engagement was Sustainalytics' investor trip to Italy in September 2019. We spent a week there, together with AP7 and a group of institutional investors, to better understand the challenges to labour rights and solutions in the Italian agricultural sector. The objective was to further improve how we could engage investee companies to strengthen the respect of labour rights in agriculture and spur further action. During the trip, we connected with a variety of stakeholders, including tomato producing companies, farming cooperatives, labour unions, Italy's Ministry of Labour, the International Organisation for Migration, civil society organizations and others.

We learnt about several challenges contributing to a precarious situation for agricultural workers in Italy, not limited to tomato production. Overall, it was clear that the vast majority of workers are migrant workers, either with a work permit obtained specifically to work in agriculture, or migrants without permits having to accept work without legal contracts and secure conditions. For the workers without permits, there is no way they can then get a permit while staying in Italy, even if they are offered a job with a legal contract. They are then left in the limbo of accepting poor working conditions without a legal contract or to return to their home country.

For those with a contract, we understood that it was not uncommon to get paid for only a part of the hours worked. Workers, with or without contracts and permits, often live in ghetto-like accommodation and there have been widespread reports of the mafia (the so-called Caporalato) controlling workers' transport and overcharging as a rule. Several fatal incidents have happened over the years while transporting workers in overcrowded and unsafe vehicles. It is not difficult to understand that in vulnerable positions without valid permits and wary of criminal groups, migrant workers are unlikely to report abuse or systematically poor working conditions.

The problems seem to be most elevated linked to agricultural products that are hand-picked, rather than machine-harvested, as the latter is less labour-intensive. Poor working conditions seem to occur throughout Italy but are more widespread in the south. Some improvements have been visible in tomato production, not least since more and more tomatoes are machine-harvested. Labour conditions in tomato production have also seen progress as it has been increasingly highlighted in the media. However, these issues are not limited to the tomato sector and workers within other less exposed, hand-picked crops are most likely worse off, with less media and NGO coverage.

Roundtable and meeting after Italy

Drawing on experiences from the trip, in November 2019, Sustainalytics invited a large number of food and food retailing companies, as well as other stakeholders to a virtual roundtable looking at potential solutions to labour rights challenges in the Italian agricultural sector, in particular on how downstream actors can contribute to those. The Ethical Trade Initiative's (ETI's) Italy working group presented its work, as did Oxfam on its human rights impact assessment of the Italian tomato supply chain and subsequent recommendations. In later engagement dialogues, we highlighted to companies, where relevant, the opportunity to join the ETI working group, as well as to look closer on how sustainability and procurement teams within a company can align practices. What we could see in Italy, and other markets is that when a procurement price is too low, it does not enable suppliers to pay appropriate salary levels, or contract aligned salaries to agricultural workers. Closer cooperation between sustainability departments and procurement departments could help overcome this by introducing a system identifying when a price is too low, or what questions or indicators procurement staff should be aware of to enable a fair price and decent salary levels throughout supply chains. This would ultimately support the aim of providing farmers and agricultural workers with living income and living wages.

Focus on living income and living wages: Investor statement, survey, webinar and engagement meetings

In spring 2020, Sustainalytics developed and coordinated an investor statement on living income and living wages, sent to the CEOs and Chairpersons of more than 40 food and beverage companies and food retailers globally, among them the 17 companies targeted in this engagement. In doing so, we expanded our approach to the broader food industry to increase the impact created and drive wider awareness across the whole sector. The aim was to communicate a strong investor commitment to the issue, adding the investor voice and support to a growing number of initiatives, networks and guiding tools in the area. The statement received strong investor support, signed by 36 institutional investors globally with a combined AUM of USD 2.4 trillion. AP7 was one of the signatories.

Following the statement, we had follow-up calls with the companies targeted in this engagement and beyond, discussing commitments to living income and living wages, the extent to which companies are already working towards living income and living wages in their supply chains, as well as what they can do to further such efforts.

Some leading companies are piloting living income or living wage specific efforts in their agricultural supply chains. These companies have or are building, dedicated living income and living wage strategies, roadmaps or similar. However, most companies struggle with even getting started with related efforts. To assist companies in developing their responses to the living income and living wage challenge, Sustainalytics also co-hosted a webinar with the Living Income Community of Practice on how to build a corporate roadmap towards living income for smallholders. Ahead of the webinar, a survey was sent to food and beverage companies to better understand challenges and current adoption of living income roadmaps.

Sustainalytics has participated in several virtual workshops and webinars on the topic and continues to provide an investor perspective on the Living Income Community of Practice Advisory Board.⁶ We also see an increasing number of commodity and/or industry-specific initiatives on living income and living wages, such as a Dutch retailer initiative on living wages in the banana supply chain. Leading companies on living income and living wages recognize the need for such collaborations as it brings scale in the response and alignment in requirements towards common suppliers. Sustainalytics also provided feedback to a revised certification within the sugar sector, with a proposed inclusion of living wages for sugar cane workers.

Sustainalytics' good practice materials and efforts to connect companies

Having seen less advanced companies, from a labour rights perspective, struggling with the area of labour rights due diligence, we launched a quick guide in 2019, including investor expectations on the topic. The two-pager intended to provide a step-by-step guide, including various good practice examples and other useful resources for companies. A similar guide was also launched on living income and living wages, aimed at challenging more advanced companies in the Food Supply Chain Thematic Engagement to implement a living income and living wage approach to tackle the root causes of labour rights risks and adverse impacts in their supply chains. The two-pagers have been shared frequently with the companies in this engagement and have received appreciative comments.

Throughout dialogues with many companies, Sustainalytics has explicitly asked and offered to connect like-minded companies wanting to work in similar commodities on labour rights challenges. The investor trip and roundtable on labour rights in the Italian agricultural sector had similar objectives where we invited not only investors but also companies to participate.

The engagement activities described above all supported the success of this engagement. The many bilateral meetings held with companies allowed us to maintain a continuous focus and pressure on the topics of child labour, forced labour, living income and living wages. The trip helped build a deeper understanding of conditions and complexities on the ground in agricultural supply chains, which in turn contributed to credibility and better-informed recommendations when engaging with companies. In the area of living income and living wages, we deliberately sought input and collaborations with like-minded organizations to support a broader drive on the topic and to support the growing momentum jointly built up with a number of stakeholders. With the conclusion of this thematic engagement, along with its bilateral dialogues with companies on these topics, we have also sought to link companies to the network of expert stakeholders, to facilitate continuous and growing active involvement by the private sector.

Concluding the positives from the engagement activities above, we believe that the success of this thematic engagement, in short, has been thanks to:

- Active involvement by investors.
- Understanding the companies, the sectors and topics we have engaged on, including the latest trends and overall developments.

⁶ <https://www.living-income.com/>

- A continuous drive in dialogues, and finding new ways of sharing good practices and linking companies and their actions with each other, for example through the investor trip to Italy, the roundtable, the living income webinar and in bilateral dialogues.
- Having a clear focus, primarily in the latter half of the engagement, on living income and living wages, addressing root causes of labour rights issues, and at the same time using and adding to the momentum in the area.
- Maintain an active network of stakeholders beyond like-minded investors and drive core issues together with those, not only to build leverage and have a greater impact but also to ensure companies are linked to such networks as time-bound investor engagements like this one are concluded.

MAIN GAPS AND SUGGESTIONS ON FURTHER EFFORTS AND ENGAGEMENT

There are still gaps in companies' respect of labour rights in their agricultural supply chains. While most of the targeted companies in this engagement have good labour rights due diligence in place, a good deal remains to be done to close gaps in terms of mitigating labour rights risks in agricultural supply chains, and in collaboration between companies and other stakeholders to scale mitigative measures. Further engagement is likely to be most relevant with a strong focus on this area, and less on having policies and systems in place to identify labour rights risks. In terms of risk mitigation, living income and living wages for smallholders and agricultural workers require increased attention and efforts to succeed. Experiencing the growing momentum, this would be a suitable focus for any engagement addressing social issues in agriculture.

For investors wishing to continue the path of this engagement, a few collaborative engagement endeavours are recommended, both from Sustainalytics and other investor groups:

The Platform Living Wage Financials

*"The Platform Living Wage Financials (PLWF) is an unprecedented alliance of 15 financial institutions that encourages and monitors investee companies to address the non-payment of living wage in global supply chains. As an investor coalition with over €2.6 trillion of Assets Under Management and advice, we use our influence and leverage to engage with our investee companies."*⁷

Sustainalytics' Thematic Engagement on Child Labour in Cocoa

Targeting the largest cocoa and chocolate companies in the world to address the issues of 1.5 million child labourers in the two leading cocoa producing countries globally – Ivory Coast and Ghana. Open for investors to join and will run until 2022.

Sustainalytics' Thematic Engagement on Modern Slavery

Targeting the textile and construction sectors to address the risks of modern slavery in these industries including the supply chains. Open for investors to join and will run until 2024.

Sustainalytics' Thematic Engagement on Feeding the Future

Targeting environmental impacts in food production, including climate change and biodiversity, and looking to future-proof the sector through more regenerative practices, and aligned with changing consumer demands. Open for investors to join and will run until 2024.

⁷ <https://www.livingwage.nl/>

About Sustainalytics

Sustainalytics, a Morningstar Company, is a leading ESG research, ratings and data firm that supports investors around the world with the development and implementation of responsible investment strategies. For more than 25 years, the firm has been at the forefront of developing high-quality, innovative solutions to meet the evolving needs of global investors.

Today, Sustainalytics works with hundreds of the world's leading asset managers and pension funds who incorporate ESG and corporate governance information and assessments into their investment processes. Sustainalytics also works with hundreds of companies and their financial intermediaries to help them consider sustainability in policies, practices and capital projects. With 16 offices globally, Sustainalytics has more than 650 staff members, including more than 200 analysts with varied multidisciplinary expertise across more than 40 industry groups.

For more information, please visit www.sustainalytics.com.



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