

Russia's war on Ukraine

Active Ownership in times
of conflict

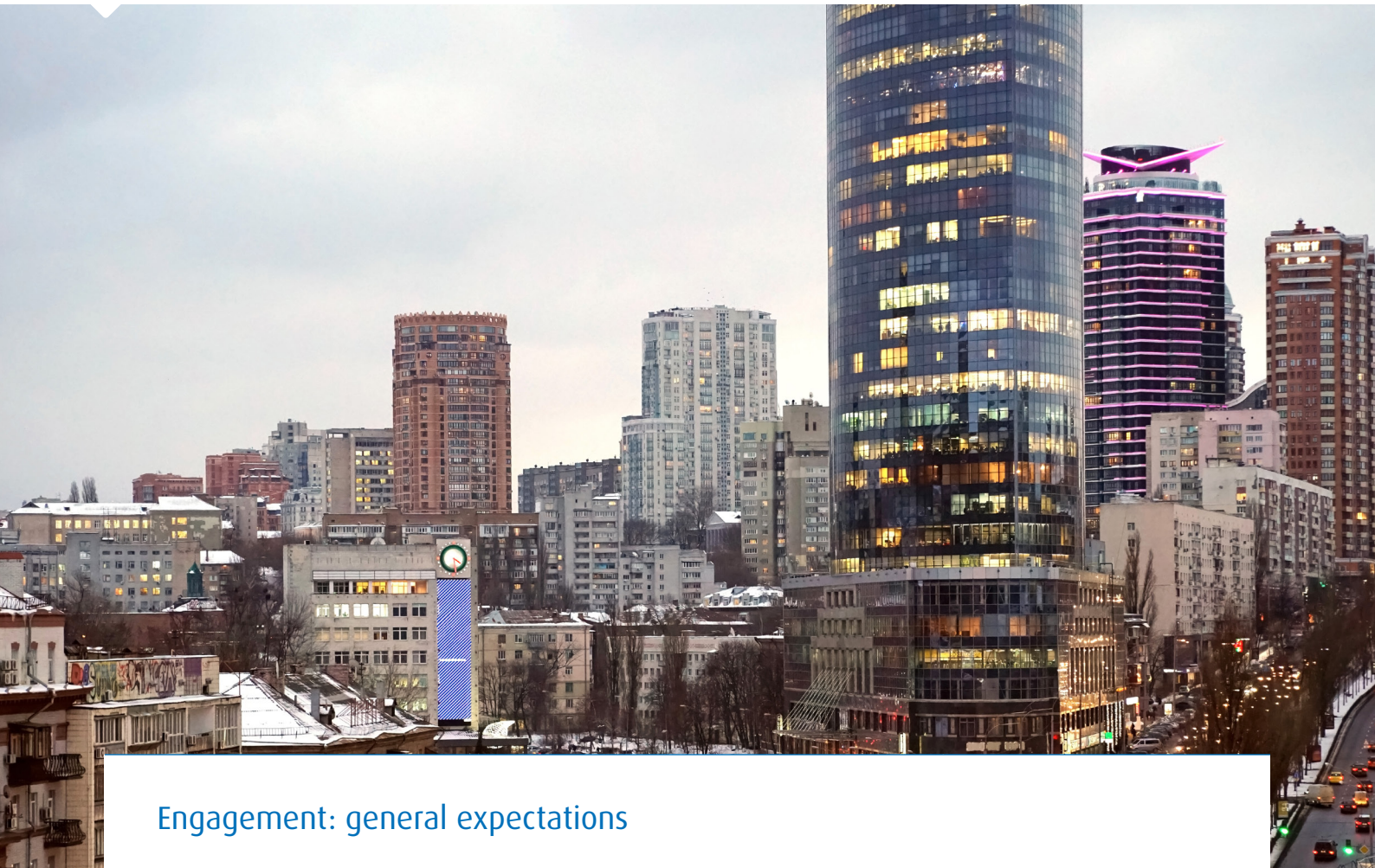


Introduction

We deeply regret the scenes of terror we are witnessing in Ukraine, and the new era of geopolitical insecurity that it heralds. We are working quickly to review the wide-ranging implications of these developments for our clients and assess the most appropriate and constructive actions to take as responsible investors.

Russia's military invasion of Ukraine has severe implications for human rights and presents significant challenges to businesses with ties to both countries. These include protecting workers in Ukraine, managing supply chain disruptions, and spikes in energy, food, and commodity prices, among others. On the other hand corporations are facing significant operational and reputational risk from continued presence in Russia and are under pressure to take rapid action.

Divestment is one potential response from the investor community to the crisis in a bid to isolate Russia, but engagement with companies with exposure to the region is also critical. In this note we provide an insight into our initial dialogues and the questions we believe should be asked.



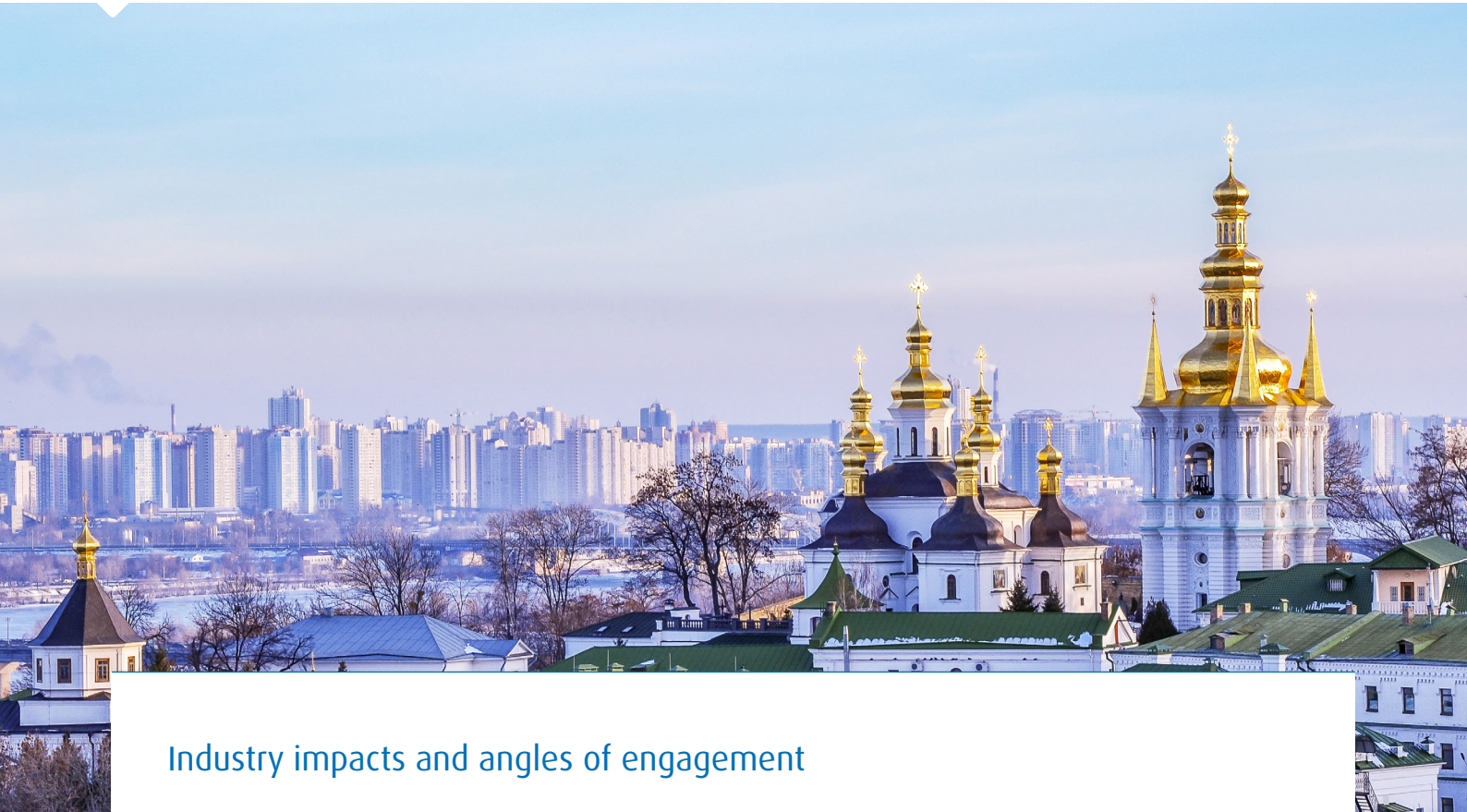
Engagement: general expectations

In the immediate crisis, when engaging with a company with direct operations or supply chains in Ukraine we are asking about:

- › Safeguarding of companies' workforce and their families and support of evacuation of staff as appropriate
- › Engagement, as much as feasible, with local stakeholders to understand how the company can offer humanitarian support and assistance
- › Engagement with suppliers linked to Ukraine to support employees in its supply chain and share considerations around business continuity/ alternative suppliers

In addition on engaging companies with exposure to operations or key supply chain in Russia:

- › Identify whether its businesses are linked to Russian state-owned or affiliated companies participating in or financing the conflict
- › Analyse the immediate impacts of sanctions on Russia on its business operations and supply chains
- › Assess potential reputational damage and loss of brand value of continued presence in Russia
- › Develop integrated human rights due diligence assessments to understand the impact of its business activities and take steps to mitigate and prevent them
- › Conduct a human rights due diligence assessment to ensure a responsible exit and mitigate unintended consequences for those choosing to exit or suspend operations
- › Understand the status of any significant legal/ contractual obligations that may complicate any exit



Industry impacts and angles of engagement

There are angles to engagement specific to certain industries with elevated exposure to the war in Ukraine as well as to the sanctions against Russian companies and individuals. The following sets out

examples of these specific impacts and engagement angles. We will report further on the breadth and outcome of our engagement conversations as the situation develops:

Industry	Impact	Company examples
<p>Agriculture</p>	<ul style="list-style-type: none"> • Russia and Ukraine are significant food producers, notably of wheat, corn and vegetable oils. The invasion has led concerns over the health and safety of staff and impacts on food supply, prices and food security. • Long term: There is also a risk of increased negative environmental impact including biodiversity loss as pressure to increase crop yields might lead to increased use of fertilisers and pesticides. 	<ul style="list-style-type: none"> • We will engage with food producers to understand how they manage risk to people in Ukraine operations and supply chains, and how the potential shortages will affect sourcing patterns and practices to compensate production elsewhere.
<p>Hotels</p>	<ul style="list-style-type: none"> • Companies need to ensure protection as far as possible of staff and guests and implementation of clear policies, contingency plans and monitoring of events for areas affected by the conflict. 	<ul style="list-style-type: none"> • We engaged with InterContinental Hotels Group on its measures to ensure health and safety for its staff in Ukraine and the potential impact of current and potential sanctions against Russia. The Group has no owned hotels in Ukraine, one is managed, and another is franchised, and currently used by the media and the Ukrainian government. The company is in close communications with its teams on the ground to provide support and ensure the safety of its colleagues and guests. It is currently seeking further details on how its sanction may impact operations and support.

Industry	Impact	Company examples
Consumer staples	<ul style="list-style-type: none"> Many consumer staple companies have factories and warehouses in Ukraine. Employee safety is vital in these facilities, companies must ensure that this is their top priority. 	<ul style="list-style-type: none"> We spoke to Procter & Gamble on its social supply chain management. In Ukraine, two of its manufacturing sites have been shut down. It is building inventory elsewhere to compensate; this will ensure staff safety while producing and providing necessities to local relief efforts. In Russia, the company is assessing the risk of the government seizing private assets.
Energy	<ul style="list-style-type: none"> Russia is the world's third largest oil producer and biggest gas exporter, with the sector contributing ~40% of federal budget revenue. At the time of writing sanctions exclude energy exports, however there is increasing discussion of the US and EU banning Russian oil imports. Banning gas imports appears to remain off the table for now, given the EU's reliance on gas and already high prices driving a cost of living crisis. Energy companies are keen to disassociate themselves with the financial and operational risks of investing in the country. However, significant write downs of Russian assets and portfolio changes will impact earnings over the next few years. Companies must navigate these challenges whilst also potentially needing to seek alternative supplies for refineries and customers in regions that may ban Russian oil or even gas imports. 	<ul style="list-style-type: none"> Majors like Shell, BP, ExxonMobil and Equinor have decided to exit their joint ventures in Russia, mostly with state owned enterprises, and stop new investments in the country. At the time of writing, TotalEnergies has decided to stay; however, it will not provide capital for new projects in Russia. We will also be engaging with the sector to emphasise our support for and the ongoing necessity of energy transition efforts. Current high prices must not be seen as a pretext for postponing transition plans or reallocating capital away from low carbon sources back to fossil fuels. This would risk derailing decarbonisation efforts and perpetuating reliance on fossil fuels and the associated geopolitical instability they bring.
Semiconductors	<ul style="list-style-type: none"> Supply chain disruptions have been at the heart of the semiconductor industry for the past 2 years due to the chip shortage. Ukraine is the largest supplier of noble gases; these are key materials for the semiconductor etching process. Once again, the industry may be affected by these material shortages. 	<ul style="list-style-type: none"> ASML states that it sources less than 20% of the gas from the region but it is looking at alternative sources to ensure no disruptions in its supply chain. We will engage with semiconductor companies to understand how they are diversifying their supply chain to reduce supply chain disruptions.
Internet platforms	<ul style="list-style-type: none"> Social media platforms have been instrumental in disseminating information on the invasion. However, given the spread of misinformation, these platforms have a duty to protect users from inaccurate information and user security without hindering freedom of expression. 	<ul style="list-style-type: none"> We reached out to Meta Platforms, owner of Facebook, Instagram and WhatsApp, to understand the measures taken to ensure responsible speech online. We want to better understand how the company is using technology to scale up the work of its content review teams, and its measures to ensure the privacy and data security risks.
Banks	<ul style="list-style-type: none"> International banks might be exposed to the war through direct operations on the ground, offshore support teams (e.g. tech development), or credit and underwriting exposure to either Ukrainian or Russian financial institutions or corporates Compliance with international sanctions is at highest priority 	<ul style="list-style-type: none"> We engaged a Nordic bank which had exited Russian and Baltic operations given its historic Anti-Money Laundering scandals. Its exposure remains at 0.1% non-core exposure, which only signifies a small portion of risk. Future engagement with the sector will include those banks that had significant Russian lending and underwriting exposure

Industry	Impact	Company examples
Aviation	<ul style="list-style-type: none"> Commercial airlines were scrambling to rescue aircraft and protect staff who have been stranded in Ukraine after flights were suspended. Flight route changes due to airspace blockages will impact environmental footprints and prices 	<ul style="list-style-type: none"> We reached out to Wizz Air to understand its plans to withdraw staff and assets from Ukraine safely. After commercial flights were suspended, the company scrambled to rescue four aircraft and staff stranded in Ukraine. It will evacuate at the earliest opportunity its Ukrainian based crew, their immediate families, and any families of Wizz Air Ukrainian nationals who wish to leave the country.
Automobiles	<ul style="list-style-type: none"> Several large automobile companies communicated their temporary exit from producing or selling in Russia Commodity supply chain challenges further exasperated by the war, and related sanctions and transport hurdles 	<ul style="list-style-type: none"> We engaged with Toyota that highlighted the biggest impact as being challenges with commodity sourcing; this has been exacerbated by commodity price inflation and supply chain disruptions before the war. They have temporarily stopped production and sales in Russia due to ethical reasons and the inability to deliver production parts and components to Russia.

Wider economic impacts

Energy and the net zero transition

The status of Russia as a major fossil fuel exporter has led to widespread spikes in prices, at a time when European gas prices had already seen significant increases due to other supply factors. The prospect of sanctions is now very much on the table. At the time of writing the US has announced a ban on all energy imports, with the UK due to end oil imports by the end of 2022. In Europe, banning gas imports appears to remain off the table for now, given that Russia makes up 40% of imports – but the EU has laid out a plan to significantly reduce this dependence.

This dramatic shift in energy markets is already dividing opinion around the implications for the net zero transition. On one side, there is the view that it makes the imperative for rapid action even greater, as growing our renewable energy resource and taking steps on energy efficiency will reduce our dependence on imported oil and gas. On the other are those who argue that high energy prices mean we cannot afford the necessary expenditure to make the transition

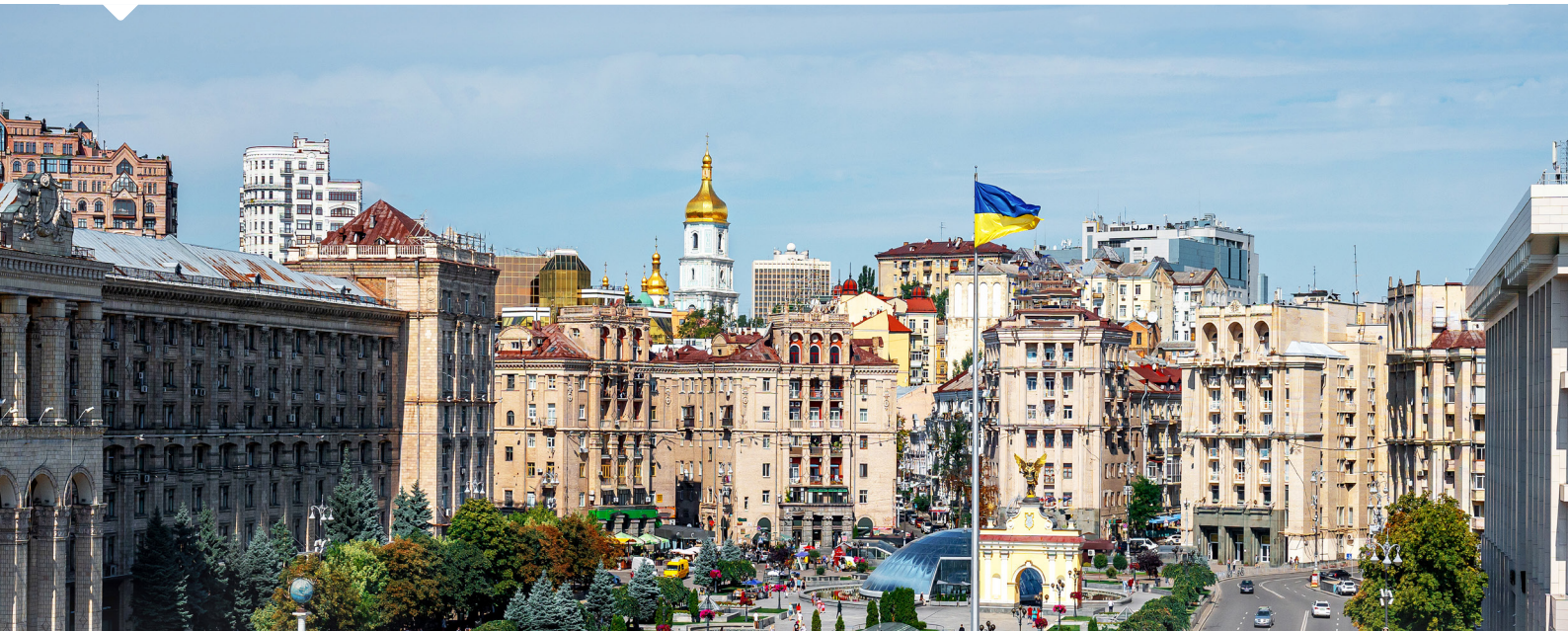
happen, and that we should fall back on existing infrastructure including coal.

In our engagement both with companies and policymakers, we will press the case for a continued push toward net zero, maximising the co-benefits in terms of energy security – now is not the time to reverse direction.

Cost of living

Having said this, the cost of living implications of the crisis are very real. As well as skyrocketing energy prices, the invasion also has major implications for food prices, given Ukraine’s key role in agricultural production, and for the supply of certain metals and minerals.

Very clearly there is a key role for government policy here, to cushion the blow of higher prices on the vulnerable. Corporates, too, could play a supportive role by providing support for lower-wage employees and customers who may struggle to pay the bills.




Outlook

The escalating violence in Ukraine is devastating, and we, as responsible investors, stand with Ukraine. We are challenged to make hard choices; on the one hand, we are engaging with companies exposed to Russia and Ukraine to gain insights into the complexities on the ground and press for effective management of human rights and supply chain risks. On the other, we support companies

that choose to suspend operations in Russia responsibly whilst being conscious of any unintended consequences. There is no one-size-fits-all approach given companies' broad range of situations. The crisis is incredibly volatile, and we will adapt our approach to engagement and report in greater depth on the results of our engagement in due course.

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