AB SUSTAINABLE GLOBAL THEMATIC PORTFOLIO

ENGAGEMENT REPORT: 2019

During 2019, AB portfolio managers and analysts engaged with the senior management and/or boards of directors of companies in the AB Sustainable Global Thematic Portfolio. We report on our engagement activity on an annual basis. This year, the Thematic & Sustainable Equities team engaged with 43 individual companies on 163 issues, including 22 environmental, 71 social and 70 governance.

Summary reports of a selection of our engagements with companies during the year follow below.

EXAMPLE ENGAGEMENT ON ENVIRONMENTAL/GOVERNANCE ISSUES

We spoke with Procter & Gamble about environmental and governance issues.

+ Procter & Gamble (consumer goods company). We met with the director of Global Sustainability and investor relations (IR) from Procter & Gamble to discuss alignment with the United Nations (UN) Sustainable Development Goals, palm oil sourcing and executive compensation.

After an earlier meeting with the CFO, we wanted to ask management follow-up questions regarding environmental, social and governance (ESG) issues. Procter & Gamble disclosed how it is aligned with each of the 17 Sustainable Development Goals by, among other things, increasing recycled product packaging, reducing greenhouse gas emissions in its supply chain, and helping with disaster relief initiatives and philanthropic activities. We expressed that we want the company to focus on the goals that are most emblematic of its business rather than discussing extracurricular activities. Management understood our concern and directed us to the company's new 10-year plan, Ambition 2030. The objective of this plan is to have 100% of the company's leadership brands (brands with global sales of over US$1 billion) enable and inspire responsible consumption. Each brand will design a sustainability campaign (some examples include the "Shave Your Toxic Masculinity" and "Like a Girl" ad campaigns) but will have underlying social and environmental criteria to track impact and progress. Some of the environmental brand fundamentals include recycled/reusable packaging, use of bio-based materials in packaging, reporting on Scope 1, 2 and 3 greenhouse gas emissions, and usage of renewable electricity in production processes. The company has already committed to its science-based target of a 50% reduction in operations emissions by 2030. Ambition 2030 further supports these environmental efforts and lays out targets and tracking metrics.

Procter & Gamble spent US$1.9 billion in 2018 on research and development. We asked if management could estimate how much was geared toward sustainability improvements and enhancements. While management did not provide a numerical answer, it explained that sustainability and innovation are intertwined at the company and that the majority of that spend could be recognized as sustainability-oriented. Management highlighted its EC30 clean product pilot, which includes dry hand soap and laundry detergent that reduce the amount of water needed to activate the cleaning product and do not require any plastic packaging. More applications, such as face wash, are expected to be rolled out in the coming months.

Raw material sourcing (palm oil) and labor practices (suppliers) are two of the more notable ESG risk factors affecting Procter & Gamble. We wanted to better understand how management is addressing/mitigating these risks. When harvested properly, palm oil is very efficient versus other vegetable oils. The company's largest palm oil suppliers are in Malaysia. In addition to adhering to the Roundtable on Sustainable Palm Oil certifications and standards, the company recently piloted a program called the Learning Farm Model aimed at improving the lives of farmers in Malaysia. The company enlisted the help of nongovernmental organizations Proforest and International Plant Nutrition Institute as well as researchers from Massachusetts Institute of

Technology to train the farmers on better agricultural practices, nutrient management and how to sustainably increase oil yields. The program delivered yield improvements of 30%–50%, grew a peer-to-peer learning network and increased the incomes of farmers without having to expand or harm any of the farming land. The company is now scaling this initiative across all its suppliers, targeting the higher-risk locations and working with the World Wide Fund for Nature and Conservation International to share best practices. Management mentioned that it reserves the right to terminate contracts immediately due to human rights violations that are detected, but the company finds it more productive to work with the suppliers on infractions to improve labor conditions. We reduced the risk score on the company's raw material sourcing, given its expansion of sustainable palm oil practices.

Finally, we discussed whether the company would consider integrating sustainability/ESG targets into its executive compensation plan. Procter & Gamble's chief sustainability officer is the only executive with explicit sustainability targets built into her compensation plan. The company continues to integrate sustainability across the business. Currently, the year-end business reviews now include sustainability as a measure of performance for all executives that report to the CEO. Management assured us that sustainability is one of many performance factors for the company, but the company currently lacks a formal algorithm.

EXAMPLE ENGAGEMENT ON SOCIAL ISSUES

We met with Amazon.com regarding social issues.

+ Amazon.com (e-commerce company). We spoke with the director of IR of Amazon to discuss the company's labor and supply chain practices following negative press.

We asked about the company's policy on product sourcing, including what type of standard procedures it has in place, how it enforces them, how often it conducts random auditing and what its response is once a product is deemed to have been produced by sellers who did not comply with company standards. Management requires that all facilities engaged in the production of Amazon products meet and maintain, at a minimum, a basic set of requirements to qualify for initial and continued production. The company is strongly committed to ensuring that the products and services it provides are produced in a way that respects human rights and the environment and protects the fundamental dignity of workers. The company engages with suppliers that are committed to these same principles, and it sets exacting standards for suppliers of goods and services for the company and its subsidiaries. These standards are derived from the UN's *Guiding Principles on Business and Human Rights* and the Core Conventions of the International Labour Organization (ILO), including the ILO Declaration on Fundamental Principles and Rights at Work and the UN's *Universal Declaration of Human Rights.* Suppliers include, but are not limited to, product suppliers in the company's supply chain (such as licensees, manufacturers and producers) and suppliers supporting the company's retail operations (such as third-party labor agencies and transportation service providers). Suppliers must comply with all applicable laws and the Amazon Supplier Code of Conduct (Supplier Code), even when the Supplier Code exceeds the requirements of applicable law. To ensure that these standards cascade throughout the supply chain, the company expects suppliers to consistently monitor and enforce the standards in their own operations and supply chains, and make improvements to meet or exceed the company's expectations and those of its customers. Suppliers are required to disclose any subcontractors or labor agents upon request. They are also expected to hold their subcontractors and labor agents to the standards and practices covered by the company's Supplier Code. Suppliers with subcontracted production are required to work with their subcontractors to adopt and raise awareness of the Supplier Code. Management recognizes that suppliers in deeper tiers of the supply chain and suppliers in informal sectors may take more time to align with these standards. Management is committed to working with suppliers to help them understand Amazon's policies.

We also asked IR to clarify whether there are different procedures for first- and third-party sellers. The company requires that all products sold on its marketplace be manufactured in a manner that meets or exceeds the requirements outlined in the company's Supplier Code. The company takes a risk-based approach to monitoring suppliers; it does not have full visibility into the supply chains of non-Amazon branded products. It relies on reputable brands to monitor their own supply chain.

We also wanted to better understand how management ensures that third-party sellers comply with the Supplier Code as the number of third-party sellers grows. Management believes that good working conditions lead to good business. It expects all suppliers and service providers to behave in a lawful and responsible manner, protect the environment, act safely and responsibly and safeguard workers' rights. While Amazon does not have full visibility into the supply chains of non-Amazon branded products, it takes action when an issue is escalated. For example, in 2018, Amazon removed all products known to be made with cotton sourced from Uzbekistan and Turkmenistan, countries known to use government-mandated forced labor.

In terms of the consequences for sellers that are non-compliant, Amazon operates a policy of continuous improvement and is committed to working with suppliers to improve protections for their workers and workplaces. Amazon reserves the right to terminate a relationship at any time for failure to meet the Supplier Code; however, it strives to always put the interests of workers first.

We discussed with IR how Amazon benchmarks its practices versus peers and how it has strengthened management and board oversight in recent years. The company regularly benchmarks itself against peers and industry partners. To ensure that its policies and programs incorporate internationally recognized human rights standards, it conducts formal benchmarking with industry and multilateral groups to design, operate and continually improve its risk assessment and audit program. It reviews its Supplier Code against policies developed by industry initiatives (such as the Responsible Business Alliance) and further developed its standards in consultation with Nest, Business for Social Responsibility, Impactt Limited, and Verité.

Finally, we asked management how it assesses the reputational impact from negative press. IR explained that the company monitors media coverage and takes supply chain allegations seriously. Whether the company encounters social responsibility concerns within its own supply chain or the supply chains of other brands, it works quickly to notify the appropriate brand owner, factory, local nonprofit organization and investigators to take appropriate action. Amazon has removed all products identified in recent press as brands sourcing from factories deemed ineligible under the Supplier Code, until the brands can demonstrate that they are not sourcing from ineligible factories and are holding suppliers to the same safety standards Amazon holds in its supply chain.

Despite all these procedures being in place, as third-party sellers become a much larger part of the overall business, we feel that it will be increasingly challenging for Amazon to maintain oversight of its supplier's sourcing. After careful consideration, we sold our position in Amazon after these conversations.

EXAMPLE ENGAGEMENTS ON SOCIAL/GOVERNANCE ISSUES

We spoke about social and governance issues with Proofpoint and QIAGEN.

+ Proofpoint (enterprise security company). We met with IR from Proofpoint to educate the company on ESG issues and suggest areas in which it could improve disclosures and demonstrate value creation for its stakeholders.

Proofpoint is a leading cybersecurity firm with a people-centric vulnerability model. It is a high-growth company that operates in a competitive environment for talent, is considered frugal and is starting to engage with some shareholders on ESG issues. It lacks a corporate social responsibility (CSR) report and consistent, measurable ESG metrics that are shared externally.

Our initial conversation started with a discussion around a recent convert offering but changed to a discussion on ESG. IR had started to receive inbound inquiries to set up ESG-focused calls, but management had a lack of understanding of the topic. We discussed the evolution of ESG and responsible investing, the UN Sustainable Development Goals, and how Proofpoint fits in a world where the role of a company is greater than delivering financial returns.

In a follow-up email, we made several suggestions to the company. While Proofpoint has an extensive set of customer success stories on its website that detail the pain points it addresses, it fails to share consistent business metrics on the value it provides that can be tracked over time. We recommended that the company consider publishing a CSR report and provided IR with an example. We did not stress the volume of information and statistics shared, but instead focused on the quality of the metrics targeted by the other company and how they relate to the value the company seeks to create through the products offered to its customers.

We also provided some examples of relevant metrics that the company might consider sharing to demonstrate improvements in employee satisfaction and diversity, encouraging management to have specific external goals. Attracting and retaining key talent is crucial for the firm.

We noted the Business Roundtable's recent revision to its definition of a corporation: one that serves all stakeholders, including customers, employees, suppliers, communities and shareholders. We encouraged the company to consider becoming a signatory if the Business Roundtable's definitions align with its values and intentions as a firm.

Finally, we discussed executive compensation and including more ESG metrics in the company's compensation plan with specific targets. Currently in its proxy, Proofpoint lists 39 performance metrics that are considered, only two of which could be considered ESG issues (workforce diversity and succession planning), with no details on criteria or specific goals. We shared data on the percentage of companies that currently incorporate ESG metrics in compensation plans and data demonstrating that companies with improving ESG metrics tend to experience stock appreciation over time.

The goal of this engagement was both educational and a call to action (CSR report, external metrics around employee satisfaction, diversity and enhancements to future compensation plans). We plan to follow up on these suggestions in future meetings and will track progress in the next six to 12 months.

+ QIAGEN (sample and assay technologies provider). In early 2019, we met with the CFO and head of IR of QIAGEN as part of the management team's road show after the company published its 2018 results. We spoke to management about human capital risk, accounting, diversity, quality control and executive compensation.

QIAGEN has built a leading position in sample-preparation technologies for DNA sequencing and other molecular testing applications, which benefits from steady, secular growth opportunities and attractive margins, given the high proportion of sales from consumables. Over the past several years, QIAGEN has expanded its product lines across areas such as Next-Generation sequencing, point-of-care diagnostics and bioinformatics. The company has accomplished this through a series of tuck-in acquisitions and organic investments.

We had some concerns about the company's growing gap between profitability and cash flow. Management explained that costs associated with M&A, ongoing restructuring with slower-growing segments of the business, and capital investments to support the upcoming launch of new products have led to this gap. Management addressed our concerns by explaining that the cash-flow profile of the company is poised to improve over the next few years as QIAGEN makes progress toward its corporate goal of US$600 million of yearly operating cash flow by 2020. The guidance assumes that elevated M&A costs subside, along with one-off royalty costs, such as a US$30 million payment in 2018. We will be closely watching for these improvements to materialize in the coming year.

Given the high-value nature of QIAGEN's products and their role in patient care, it raises the potential risk of adverse quality-control issues or recalls. Management reiterated that the company has not experienced a regulatory warning in several years (since 2016) and believes that the company has strong quality-control practices in place. Also noteworthy, the financial costs associated with product recalls are quite low due to high gross margins and intellectual-property royalties that do not need to be paid on de-distributed products.

We also discussed a concern about human capital and retention. To be successful, QIAGEN relies on a highly skilled workforce, which creates a human capital risk as the company seeks to retain and attract quality personnel. Management believes that having bioinformatics sites strategically located in areas with the requisite talent helps in recruiting efforts.

We touched on executive compensation and board diversity. Management shared that the short-term cash portion of the compensation for QIAGEN's CEO and CFO includes ESG-sounding metrics. However, we asked for greater transparency around the company's goals and progress, which it acknowledged and believes would be possible in the future. Management also acknowledged that the board still lacks best-in-class diversity, with only two women on a seven-member board and five out of seven members being American.

In early November, we had the opportunity to meet with the head of the Supervisory Board as well as the director of IR. Our goal of the meeting was twofold: to follow up on our previous meeting as well as address new concerns that had surfaced. Over the past seven months, QIAGEN's stock had declined more than 20% on an absolute basis and underperformed its peers. We engaged with management to understand what actions management and the board were taking on behalf of shareholders to improve performance at QIAGEN.

QIAGEN had experienced a series of setbacks, including a restructuring of its commercialization joint venture in China, due to slower-than-expected demand; a restructuring of its global sales force; the curtailing development activities supporting the GeneReader Next-Generation sequencing platform, leading to a US$250+ million write-down; slower-than-expected sales growth in 3Q19; and the resignation of CEO Peer Schatz, who had run the company for approximately 15 years.

To address these setbacks, management took time to walk us through its assessment of the issues and future next steps.

Regarding the search for a new CEO, the board is considering both internal and external candidates. It is looking for an individual who is an “operator” as opposed to a “visionary.” The board expects the search to take approximately six months. Management was very positive about the level of the board’s engagement going forward. Senior leadership executives were described as “energized” about the future of the company. Management also noted that it does not expect any further high-profile departures until a new CEO is appointed. We viewed this information as materially positive from a governance risk perspective.

Prior to the CEO’s departure, the company often overpromised and underdelivered on its performance metrics, internally and externally. Management acknowledged this and plans to provide more realistic guidance to the financial markets. As the company embarks on 2020 planning, it will aim to improve its internal communications. We note that 2020 revenue estimates have declined to more reasonable levels. However, market sentiment toward the stock remains poor.

Regarding compensation plans for the CEO, management noted that QIAGEN will “start with a clean sheet of paper.” Simplicity will be a key theme, with a focus on metrics such as revenues, profits and cash flow. Management also intends to include softer metrics, such as culture and product development. We suggested that management consider tying compensation to ESG-related metrics, which would include culture and research and development.

We discussed with management how the ongoing restructuring has not been positive for employee morale. Management acknowledged that there could have been better sequencing and communication of the restructuring at the company. Management believes that a pause in restructuring will help boost employee morale. While there have been no negative posts on external company and job review sites, we will continue to monitor the situation over the coming months. From a customer perspective, we were pleased to hear that customers have reacted positively to a recent product restructuring (GeneReader) and new partnership (Illumina).

As a result of these conversations, we have improved the social governance risk scores for QIAGEN. That being said, we will continue to monitor communication, CEO search status and employee morale.

EXAMPLE ENGAGEMENT ON GOVERNANCE ISSUES

We engaged with Kingspan on governance issues.

+ Kingspan (building materials company). Ahead of the company’s annual shareholder meeting, we met with a member of the board at Kingspan to better understand the proposals that were up for consideration.

We wanted to address questions we had regarding the composition of the board of directors, chair succession planning and executive compensation.

In our meeting with management, we expressed our concern regarding the percentage of independent directors (50%) versus our minimum threshold recommendation (50.01%). The board member said that two of the directors were, in his opinion, being penalized for financially immaterial relationships (brokerage and legal fees). He also noted that one of the non-independent board members would be retiring soon, which will make independence less of an issue going forward.

Board member evaluation is another topic we discussed with management. We wanted clarity around the processes in place. Management explained that the individual members are evaluated on a more informal basis. Related-party transactions are formally gathered and cross-checked. Directors must also disclose other directorships; this information is formally gathered and collated for the board. We also learned that there is an external evaluation of the board (but not independent directors). Management confirmed that the directors are operating in an independent manner during debates and discussions.

We also discussed diversity of management and the board. Management relayed that it currently has an outstanding board member search for candidates with more international experience as well as female representation. We also learned that the CEO is very focused on diversity within the organization generally. He would like to create more opportunities for women, especially in high-profile lead roles. At the time, the CEO had three female direct reports, one of whom is the head of Talent and Development.

Management shared its plans for succession planning for the chair of the board. The current chair has been at the helm for 39 years. It is a topic frequently discussed by the non-executives as well as the Nominating and Governance Committee. While it will be a loss for the company when he retires, there is a clear succession plan in place.

We also spent time discussing executive compensation with management. We had some concerns regarding compensation, specifically for two executives. Management noted that the executives were not comfortable with retirement at their current pension plan levels. For new appointees, management expects the pension plan range to be 20–25%, the higher threshold for executives coming from a defined benefit plan. It also confirmed that there are no plans to change executive compensation in the near future.

As a result of our meeting with the board member, we decided to vote for the proposals at the annual shareholder meeting.

Please refer to the following legal disclosures.

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