

WINNERS & SPINNERS

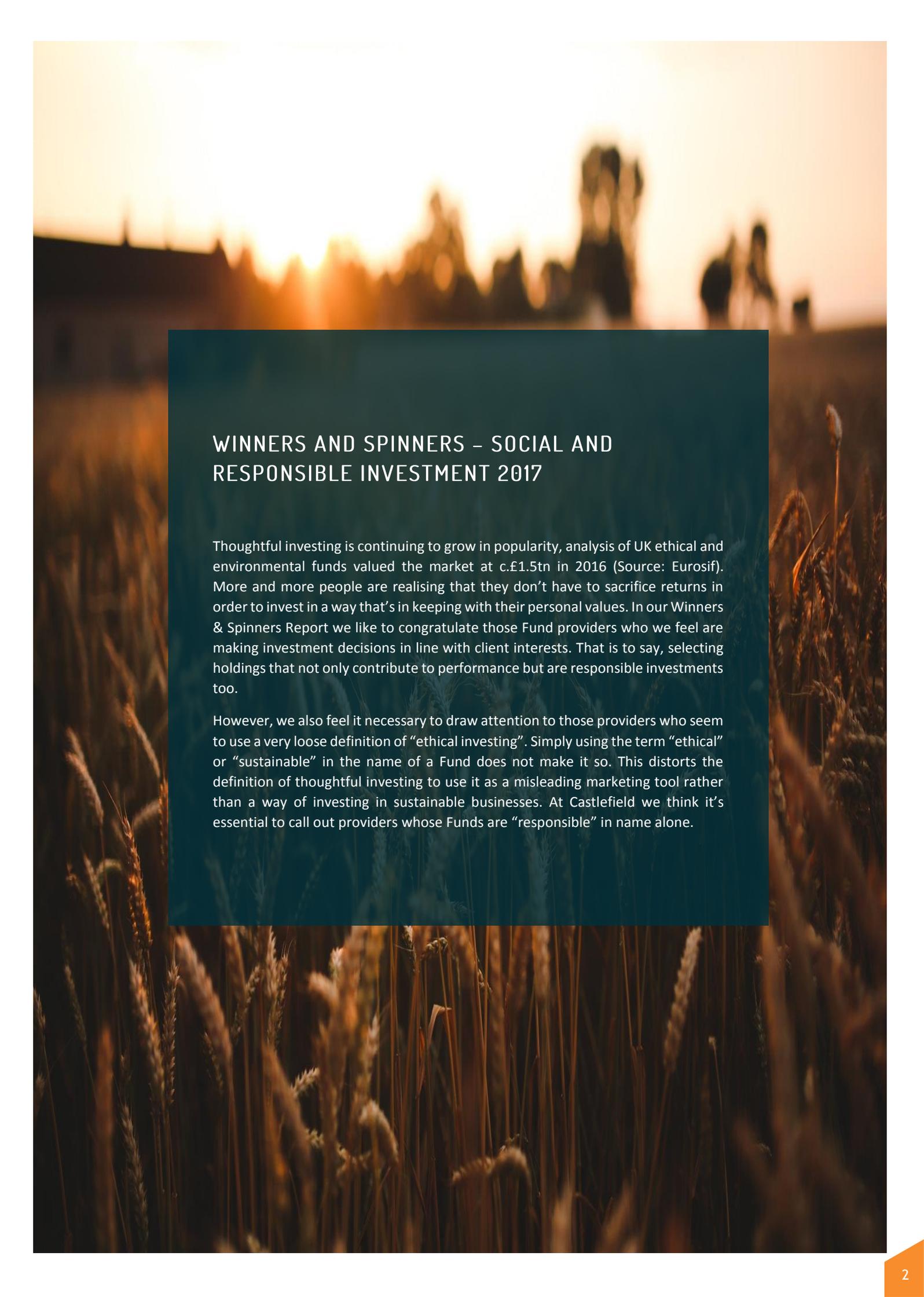
SOCIAL & RESPONSIBLE INVESTMENT 2017



THE THOUGHTFUL INVESTOR

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WINNERS AND SPINNERS – SOCIAL AND RESPONSIBLE INVESTMENT 2017

Thoughtful investing is continuing to grow in popularity, analysis of UK ethical and environmental funds valued the market at c.£1.5tn in 2016 (Source: Eurosif). More and more people are realising that they don't have to sacrifice returns in order to invest in a way that's in keeping with their personal values. In our Winners & Spinners Report we like to congratulate those Fund providers who we feel are making investment decisions in line with client interests. That is to say, selecting holdings that not only contribute to performance but are responsible investments too.

However, we also feel it necessary to draw attention to those providers who seem to use a very loose definition of "ethical investing". Simply using the term "ethical" or "sustainable" in the name of a Fund does not make it so. This distorts the definition of thoughtful investing to use it as a misleading marketing tool rather than a way of investing in sustainable businesses. At Castlefield we think it's essential to call out providers whose Funds are "responsible" in name alone.

THE WINNERS

Environmental and Socially Responsible ‘Winners’ of 2017

Our “winners” are those helping to grow the market for responsible investing by providing funds which respond to demand from today’s responsible investors who want their money to make a positive social and environmental impact.

| FUND SIZE (AS AT 31/08/17) | FUND | CUMULATIVE PERFORMANCE* | | |
|----------------------------|---------------------------------------|-------------------------|------|------|
| | | 1YR | 3YR | 5YR |
| £173.00m | FP WHEB Sustainability Fund (C Acc) | 12.5 | 51.0 | 99.3 |
| £365.16m | Liontrust UK Ethical (2 Acc) | 18.1 | 44.0 | 90.1 |
| £884.76m | Rathbone Ethical Bond Fund (Inst Inc) | 6.5 | 20.5 | 43.8 |

*(Source: FE Trustnet as at 26/09/17)

Past performance is not a reliable indicator of future returns.

1. FP WHEB Sustainability Fund

Thematic Investing for a Sustainable Future

A regular feature in our Winners section, the WHEB Sustainability Fund continues to impress with its commitment to sustainable investing and excellent transparency. WHEB publish the full list of Fund holdings so investors can see exactly which companies they are exposed to and the annual investor conference is a great opportunity for investors to meet the management team. This fund is deservedly popular among SRI investors. The managers have a good track record and they convey a strong impression of always trying to do better both within their own business and, through dialogue and engagement, with the companies in which they invest.

Managers select holdings that come under one of nine investment themes and companies providing solutions to sustainability challenges. The four social and five environmental themes presented in the adjacent diagram encompass the companies which are providing solutions to the most serious challenges we face. These themes form the basis of WHEB’s investment universe.

Not only do WHEB select holdings based on their potential to have a positive impact, they have recently launched an Impact Calculator as an innovative way of educating consumers as to how their investments are delivering on that potential. We feel that the WHEB Fund serves as a good example delivering strong positive financial performance without compromising on values.



(Source: WHEB)

Top 10 Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|--------------------------|-----------|
| STANTEC INC | 2.30 |
| XYLEM INC | 2.26 |
| LITTELFUSE INC | 2.21 |
| INTERTEK GROUP | 2.15 |
| AGILENT TECHNOLOGIES INC | 2.15 |
| ANSYS INC | 2.15 |
| ORPEA | 2.13 |
| A.O. SMITH | 2.12 |
| GRAND CANYON | 2.11 |
| TE CONNECTIVITY | 2.11 |

We can see companies such as A.O. Smith Corporation in the top ten holdings. This is an example of a position that fits into WHEB's resource efficiency theme. The company develops energy-efficient products to heat and clean water. The company is one of the world's leading manufacturers of residential and commercial water heating equipment and boilers. A.O. Smith also manufactures water purification products for residential and light commercial applications.

Cumulative Performance (as at 26/09/17)



26/09/2012 - 26/09/2017 Data from FE Analytics

FP WHEB Sustainability C Acc

IA Global

(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

2. Liontrust UK Ethical

Looks for companies that improve people's lives

The Liontrust Sustainable Futures team use rigorous screening criteria and the SRI process is central to the management of the Fund. This process is used across the Liontrust Sustainable Future range but the UK Ethical Fund is slightly different in that it uses stricter selection criteria. The process is primarily positive, seeking those companies that benefit society. However, there are negative screens in place too. The investment team have identified thematic trends and attempt to identify companies that fit into these themes but also believe there are some business activities that are not consistent with long-term and sustainable value creation, and hence see the need to avoid investing in companies with significant exposure to these activities. The thematic approach looks for those companies that improve people's lives through medical, technological or educational advances; improving resource efficiency; and helping to build a more stable, resilient and prosperous economy. The Fund is one of very few that excludes any companies involved in animal testing for both medical and non-medical purposes, making it suitable for investors who disagree with any form of animal testing for whatever reason.

Top 10 Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|------------------------------|-----------|
| LONDON STOCK EXCHANGE GROUP | 6.00 |
| PRUDENTIAL PLC | 5.38 |
| LEGAL & GENERAL GROUP | 5.07 |
| KINGSPAN GROUP | 5.06 |
| WORLDPAY GROUP PLC | 4.91 |
| SOPHOS GROUP PLC | 4.63 |
| COMPASS GROUP PLC | 4.51 |
| JARDINE LLOYD THOMPSON GROUP | 3.81 |
| PARAGON GROUP OF COMPANIES | 3.76 |
| CREST NICHOLSON HLDGS PLC | 3.76 |

Cumulative Performance (as at 26/09/17)



- Liontrust UK Ethical 2 Acc
- IA UK All Companies

(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

3. Rathbone Ethical Bond Fund

Bonds must meet strict criteria ethically and financially

A variety of negative screening criteria are used to ensure that issuing companies that engage in practices that are considered unethical are excluded. As well as passing the negative screens, issuers must also meet at least one of the positive ethical criteria in order for the holding to be considered investable. This ensures that companies are not only avoiding bad business practices but are in fact contributing to society and/or benefiting the environment.

The SRI process is undertaken by the specialist ESG arm of Rathbones. Companies not passing the negative screening criteria are automatically excluded, and these are: alcohol production, animal testing (including a medical and non-medical screening policy), armaments, environmentally unsustainable or high-impact activities, gambling, nuclear power, pornography and tobacco. In addition to the negative screen, companies are screened for demonstrating progressive or well-developed practices or policies in the following areas: corporate community investment, employment, human rights, management of environmental impacts and provision of beneficial products and services.

Top 10 Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|---|-----------|
| EUROPEAN INVESTMENT BANK 6% BDS 7/12/2028 GBP1000 | 2.9 |
| STANDARD LIFE ABERDEEN 6.75% PERP | 2.24 |
| BPCE SA 5.25% BDS 16/04/29 GBP100000 | 2.03 |
| RSA INSURANCE GROUP 5.125% 10/10/2025 | 1.85 |
| ROYAL LONDON 6.125% 30/11/1943 | 1.81 |
| ROYAL LONDON 6.125% 13/11/2028 | 1.75 |
| PHOENIX GROUP 6.625% 18/12/2025 | 1.66 |
| AXA 5.625% 16/01/1934 | 1.64 |
| INVESTEC PLC 4.5% 05/05/2022 | 1.64 |
| STANDARD LIFE ABERDEEN 5.5% 12/07/2027 | 1.59 |

Cumulative Performance (as at 26/09/17)



26/09/2012 - 26/09/2017 Data from FE Analytics

- Rathbone Ethical Bond Inst Inc
- IA Sterling Corporate Bond

(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

THE SPINNERS

Environmental and Socially Responsible ‘Spinners’ of 2017

| FUND SIZE (AS AT 31/08/17) | FUND | CUMULATIVE PERFORMANCE* | | |
|----------------------------|--|-------------------------|------|------|
| | | 1YR | 3YR | 5YR |
| €565.56m | The Vanguard SRI European Stock Fund (Acc GBP) | 17.5 | 35.6 | 75.6 |
| £150.86m (26/09/17) | Aberdeen Ethical World Equity Fund (I Acc) | 11.1 | 25.6 | 51.2 |
| £485.66m | Friends Life Stewardship Fund (NGP) | 9.7 | 23.1 | 65.0 |

*(Source: FE Trustnet as at 26/09/17)

Past performance is not a reliable indicator of future returns.

1. The Vanguard SRI European Stock Fund

Vanguard offer two different SRI passive vehicles in their “range”. As one of the largest providers of passive products this serves to indicate the limited availability of passive options that are aimed at Thoughtful Investors. The fund is designed to achieve the performance of the FTSE Developed Europe Index by investing in a sample of the index securities that pass a screening process for “socially responsible” investing. The fund will not hold stocks of companies in the index that do not meet specific “socially responsible” criteria. Despite the screening processes employed by Vanguard we can see from the holdings listed below that companies that we would not consider to be “socially responsible” have made their way into the fund.

Top 10 Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|--------------------------|-----------|
| ROYAL DUTCH SHELL | 3.1 |
| NESTLE | 2.9 |
| NOVARTIS | 2.3 |
| ROCHE | 2.1 |
| UNILEVER | 1.8 |
| BRITISH AMERICAN TOBACCO | 1.5 |
| SANOFI | 1.3 |
| BAYER | 1.2 |
| BANCO SANTANDER | 1.2 |
| ALLIANZ SE | 1.1 |

The principle activity of British American Tobacco (BAT) is the manufacture of cigarettes and other tobacco products. The World Health Organisation says, “Tobacco use kills more than 7 million people every year and costs households and governments over US\$1.4 trillion through healthcare expenditure and lost productivity.” As well as the adverse impacts on human health through the use of their products, BAT sources tobacco from suppliers in countries with human rights concerns. The NGOs Human Rights Watch and Swedwatch have documented serious human rights abuses in BAT’s supply chain in the last year. Human Rights Watch identified in 2016 several incidents of child labour in Indonesia, where BAT owns one of the country’s largest tobacco manufacturers. They found many of the farm workers lack even basic equipment to protect themselves from the risks of nicotine exposure. On top of the tragic human cost of their main output and their limited ability to mitigate against

human rights risk in the supply chain, BAT use non-medical animal testing for the development of cigarettes and tobacco products (Source: Ethical Screening).

Another holding that seems at odds with the remit of the fund and flies in the face of the social criteria is Royal Dutch Shell. Shell's business operations have significant environmental impacts including toxic air emissions and contamination of water resources; destruction of natural habitats; and high consumption of energy and water. Shell is involved in environmentally high risk activities such as deep-water drilling, fracking and the extraction of heavy oil from tar sands. They also have exploration activities within the ecologically sensitive Artic Circle. There have been a high number and volume of oil spills from their operations, the occurrence of these serious incidents shows they are unable to mitigate the risks of their environmental impacts. Alongside the environmental problems with this holding there are also problems with human rights, with Shell implicated in many human rights violations. One of the more recent cases that has been widely publicised was spills in the Niger Delta which affected the Ogale community of about 40,000 people in Rivers State, on the coast of Nigeria. They claim that Shell's spills in the area since 1989 have meant they do not have clean drinking water, farmland or rivers (Source: Ethical Screening).

There has been a lack of consideration when creating this passive vehicle. Investors looking for passive SRI options with Vanguard will still be exposed to sectors such as tobacco and fossil fuels. In short, the creation of this fund feels more like a box ticking exercise than a real attempt to provide a passive option that meets the needs of those who wish to incorporate their values into their investment decisions.

Cumulative Performance (as at 26/09/17)



(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

2. Aberdeen Ethical World Equity Fund

This Fund is becoming a “Spinners” list regular. Both negative and positive criteria are applied as a means to achieving their stated aim but it is difficult to see how some of the holdings that make up the Fund can be considered ethical.

Top Ten Fund Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|------------------------------|-----------|
| TSMC | 3.6 |
| AIA GROUP | 3.2 |
| VISA | 3.2 |
| BANCO BRADESCO | 3.1 |
| EOG RESOURCES | 3.0 |
| ORACLE | 2.9 |
| DAITO TST CONSTRUCTION CO | 2.8 |
| EXPERIAN | 2.8 |
| COMCAST | 2.5 |
| SINGAPORE TELECOMMUNICATIONS | 2.5 |

One of the largest holdings in the Fund is EOG Resources. EOG Resources is one of the largest independent crude oil and natural gas companies in the US; which is a concern in itself but furthermore they have faced accusations of illegal burying of waste and in 2011 a blowout occurred at one of their wells, resulting in natural gas and 35,000 gallons of drilling wastewater leaking into the ground over a period of 16 hours. The company also use a technique called flaring, which Friends of the Earth claim is a human rights violation, damaging the livelihoods and health of communities (health risks include premature death, respiratory illnesses and cancer). The extent of EOG flaring reached its peak in 2014 when pictures taken from space were published of the Bakken Shale Oil Field in North Dakota.

EOG Resources is one of the largest producers in the Bakken Shale region. During the 2014 boom in the region the flaring activity in this area was shown to light up the night sky as if the fields were a city. The ethical investment criteria outlined by the company state that managers will, “avoid investing in companies which demonstrate a pattern of non-compliance with local environmental regulations or which significantly contribute to environmental problems. Specific negative screens for this category include fines for offences or repetitive breaches of water pollution regulations, and / or dumping waste (including hazardous waste) in inappropriate areas.” There are also positive criteria employed which hope to favour companies that contribute to the environment. It’s hard to see how EOG resources meets the criteria set by Aberdeen Asset Management (now Standard Life Aberdeen following a merger with Standard Life).

A team from Aberdeen made time for a teleconference with us. They explained that EOG Resources were eligible for inclusion due to their policy of only excluding companies who have been involved in at least 3 significant incidents on a rolling 3-year basis. The process employed means that, should their external research provider flag such a case, that the responsible investment team will discuss the company at their weekly meeting and decide whether the incidents were sufficiently harmful to classify as “significant”. It is this application of their negative screening process that has allowed EOG Resources to be included in the Fund. At Castlefield we don’t feel this is sufficiently robust to prevent Thoughtful Investors gaining exposure to certain industries and companies engaging in activities that are at odds with their values.

Cumulative Performance (as at 26/09/17)



- Aberdeen Ethical World Equity I Acc
- IA Global

(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

3. Friends Life Stewardship Fund

The Friends Life Stewardship Range is now managed by Schroders Investment Management. The Investment remit of the fund includes both positive and negative ethical criteria, which say that they will exclude companies with poor environmental practices and those implicated in human rights abuses whilst favouring those that “meet the Stewardship funds' positive criteria by actively addressing climate change through, for example, renewable energy and energy efficiency.” The managers also seek to favour companies that employ environmentally sustainable management systems.

Top Ten Fund Holdings (as at 31/08/17)

| HOLDING | % OF FUND |
|--------------------------|-----------|
| HSBC HLDGS | 7.59 |
| GLAXOSMITHKLINE | 6.25 |
| UNILEVER | 5.23 |
| VODAFONE GROUP | 4.47 |
| RIO TINTO | 4.42 |
| LLOYDS BANKING GROUP PLC | 4.24 |
| PRUDENTIAL PLC | 3.83 |
| ASTRAZENECA PLC | 2.79 |
| RELX PLC | 2.77 |
| STANDARD CHARTERED | 2.74 |

The top ten holdings include the large mining company Rio Tinto, with BHP Billiton making up a smaller portion of the Fund (as at the last publication of their full list of holdings in December 2016).

Rio Tinto's activities have considerable environmental impacts. Third party environmental organisations have expressed concerns about some of the company's projects, such as the Oyu Tolgoi mine which is located in the ecologically sensitive South Gobi Desert. In 2013/14 Rio Tinto reported an environmental incident relating to a spill of acidic uranium slurry at the company's majority-owned Ranger uranium mine, adjacent to the Kakadu National Park in Australia. It is also worth noting that Rio Tinto is one of the world's largest producers of uranium and the investment policy of the Friends Life Stewardship Fund states that it will exclude companies “with any involvement in uranium extraction”.

The exclusion criteria of the fund include a section on companies in extractive industries. Companies are excluded where they derive more than 25% of turnover from operations. Rio Tinto owns and operates coal mines, however the revenue generated by these operations is below the rather generous limit allowed by the Fund. Revenue from coal accounted for around 7.6% of overall company revenue in 2016 but due to the large size of the company the quantum is still significant even though it is not captured by the exclusion criteria.

There is also evidence that Rio Tinto is exposed to human rights risks. The company has interests in countries which human rights organisations have identified as having significant human rights concerns. Rio Tinto has a history of abuse of workers and indigenous peoples. This also goes against the investment policy of the fund which states that it will exclude companies that fail to protect human rights or labour standards. Recent concerns relate to the Grasberg mine, in West Papua, Indonesia. Community relations issues have emerged following allegations from local people that they have been excluded from agreements with the company, that they have been forced to surrender land, and have suffered violence at the hands of the military security forces at the mine. After selling the company's interest in the Bougainville Copper mine in Papua New Guinea, Rio Tinto stands accused by the provincial government of attempting to avoid legal costs relating to alleged human rights breaches and environmental harm. This also goes against the ethical criteria of the fund which state that they will exclude companies from the fund that fail to take serious and lasting remedial action when problems occur.

BHP Billiton also manages to make its way in to the fund. BHP Billiton's operations also have environmental impacts. These negative impacts include habitat destruction, energy use, water use, production waste and emissions. These impacts are cause for particular concern in areas of high biodiversity or water stress.

A BHP Billiton joint venture at the Minas Gerais mine in Brazil was the site of a dam burst in 2015. This industrial catastrophe, in which 19 people died, led to mudslides which contaminated hundreds of kilometres of the Doce River with arsenic and mercury. Local drinking water sources were contaminated, including the only source available to the indigenous Krenak community. The company is facing several liability claims and is in the process of negotiating a deal on damages resulting from the collapse of the dam. Other human rights concerns involve the Cerrejón mine in Columbia. Concerns levelled against the company include the use of excessive force by private security forces guarding the site; poor working conditions; the health impacts of environmental contamination on local communities; and the social impacts of dividing indigenous people's lands (Source: Ethical Screening).

BHP Billiton is the world's largest exporter of metallurgical coal and a major producer of thermal coal. In the financial year ending June 2016, the revenue from BHP Billiton's coal business represented 14.5% of overall company revenue. Meaning that despite being one of the biggest global operators in coal, even BHP fail to be captured by the allowances outlined in the "ethical" criteria of the Friends Life investment policy. As well as their coal operations, BHP Billiton is one of the world's top producers of uranium. Again, the rigidity with which the investment management team apply their own criteria must be questioned, as uranium extraction should render a company excluded from the investable universe.

When we contacted the Friends Life Stewardship team they were able to tell us that they consider the Rio Tinto and BHP exposure to uranium extraction as a negligible and non-strategic part of the business. They were also able to tell us that these large mining companies were eligible to be removed from the exclusion list because their exposure to the negative screening criteria is minor and they believe that the companies make a positive contribution to society.

We are of the view that the negative screening applied should not be interpreted with this level of flexibility.

Cumulative Performance (as at 26/09/17)



(Portfolio and performance data from FE Trustnet) Past performance is not a reliable indicator of future returns.

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Friends of the Earth

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111 Piccadilly
Manchester M1 2HY
0161 233 4890
castlefield.com