



## Appendix 2

# Morningstar Investment Management

## Asset Stewardship Principles

Morningstar Investment Management's mission centres on helping investors reach their financial goals. We believe in the careful and responsible management of client's assets. In addition to the requirements set out in our Corporate Governance Policy, Morningstar Investment Management has developed these principles to exercise effective asset stewardship on behalf of investors.

### How we align our purpose and values with our duty to clients

Our investment principles, which drive our investment decision-making, also aligns our purpose and values with our duty to clients. These seven investment principles guide our thinking, behavior and decision-making and have been inspired by the most experienced and successful investors in the last century.

We put investors first

- We believe the firms that put investors first win in the long term because their investors win.
- Since 1984, Morningstar, Inc. has been helping investors reach their financial goals. Our fiduciary duty to our investors is paramount.

We're independent-minded

- To deliver results, we think it's necessary to invest with conviction, even when it means standing apart from the crowd.
- Our research shows that making decisions based on fundamental analysis, rather than short-term factors and sentiment, delivers better long-term investment results.

We invest for the long term

- Taking a patient, long-term view helps to ride out the market's ups and downs and take advantage of opportunities when they arise.
- Investing with a multi-decade horizon aligns with investors' focus on increasing their purchasing power over their lifetimes.
- The long term is the only period where fundamental, valuation-driven investing works.

We're valuation-driven investors

- Anchoring decisions to an investment's fair value, or what it's really worth, leads to greater potential for returns.
- Valuation-driven investing through a long-term focus on the difference between price and intrinsic value enables investors to get more value than they're paying for.



We take a fundamental approach

- Powerful research is behind each portfolio position we hold, and we understand what drives the cash flows of every investment we analyse.
- Fundamental investing incorporates a focus on the future earnings of an investment and not just its prospective price change.

We strive to minimise costs

- Controlling costs helps investors build wealth by keeping more of what they earn.
- Investment returns are uncertain, but costs are not.

We build portfolios holistically

- To help manage risk and deliver better returns, truly diversified portfolios combine investments with different underlying drivers.
- Portfolios should be more than the sum of their parts.
- True diversification can have a powerful impact on a portfolio's risk-adjusted returns—but simply holding more investments isn't the same as true diversification.

### **Key Management and Investment Personnel**

Morningstar Investment Management is led by the following senior management and investment professionals:

Managing Director, Asia Pacific

- Develops business strategy and oversees its implementation
- Works with senior management to deliver investment outcomes and service to clients
- Responsible Manager

Chief Investment Officer, Asia Pacific

- Develops Morningstar Investment Management's investment capabilities and thought leadership profile
- Chairs the Asia Pacific Investment Policy Committee
- Responsible Manager

Chief Operating Officer

- Leads all aspects of business operations, investment operations and product management.
- Chairs the Due Diligence Committee
- Responsible Manager



## **Management of client assets in accordance with investment strategies**

The Asia Pacific Investment Policy Committee oversees the delivery of investment management and investment advisory services to clients in the Asia Pacific region. The Committee's primary purpose is to have oversight of all policies, procedures and decision-making required to efficiently execute investment management and investment advisory services and ensuring client assets are managed in accordance with approved investment objectives and guidelines. The Committee is also responsible for resolving any conflicts of interest arising from investment management activities in accordance with our conflicts of interest policy.

The Committee delegates authority for certain investment management oversight activities to various sub-committees: the Asset Allocation Sub-Committee, the Portfolio Construction Sub-Committee, and the Manager & Security Selection Sub-Committee.

## **Internal Governance – Client Assets**

Morningstar Investment Management's approach to key aspects of internal governance and management of business activities which could impact client assets is set out below.

### Error correction policy

All Morningstar Investment Management's Managed Funds are unit priced by our external custodian and administrator (JPMorgan) and have tolerance levels applied against a benchmark movement. Where a tolerance level is exceeded, JPMorgan will provide evidence to support the excess which Morningstar Investment Management considers when performing their unit price review. Any other unit price discrepancies determined by Morningstar Investment Management are raised to JPMorgan for investigation and resolution prior to Morningstar Investment Management releasing unit prices to the market. Unit pricing errors are dealt with in accordance with our Unit Pricing Policy.

In general, performance calculation errors are rare. Unit Pricing errors would be the primary cause of performance calculation errors. If a performance calculation error is identified, performance is recalculated and reports re-released subject to the materiality.

### Brokerage and commissions

Brokerage and commissions are a key consideration for the Morningstar Investment Management investment process and we aim to minimise transaction activity, reducing the transaction costs including brokerage and commissions.

Where Morningstar Investment Management appoints an external manager to manage a portfolio, we apply a long-term conviction-led approach that involves high thresholds for initial due diligence research but once appointed, typical holding periods for managers are in excess of 5 years. A major cost of multi-manager investing is excessive and regular manager switching; and this approach minimises costs



associated with high manager turnover. We require underlying managers to account to Morningstar Investment Management for any fees, brokerage and commissions, income or the value of any other benefit (called 'soft dollar receipts') which it or its related party may receive in relation to the investment of the portfolio.

We undertake detailed monitoring of implementation costs including transaction costs such as brokerage, commission and custody settlement in conjunction with our annual Product Disclosure Statement (PDS) updates.

#### Equitable asset valuation and pricing

Asset valuation and unit pricing for the Morningstar Investment Management Managed Funds is outsourced to JPMorgan.

JPMorgan prices securities in accordance with their Global Fund Services Australia and New Zealand Pricing Policy which documents the baseline pricing practices and controls for fund accounting. All security pricing activities fall under the oversight of JPMorgan's global pricing committee. The instruments covered by their policy are exchange traded assets, fixed income securities and bonds, foreign exchange rates, market indices and OTC instruments.

JPMorgan generates the Net Asset Valuations of all portfolios held within our funds. These valuations are incorporated into the overarching fund valuation and unit priced accordingly against the units issued held by the unit registry. Once JPMorgan strikes unit prices for the Morningstar Investment Management funds, these prices are released to Morningstar Investment Management's Investment Operations team to review. Investment Operations performs a unit pricing tolerance check on a daily basis to ensure that the unit prices are reasonable and have moved in accordance to the contribution of the underlying investments. Once movements are confirmed correct, Morningstar Investment Management releases the unit prices to the market.

#### Best execution and trade allocation

To implement our investment strategies, we may design portfolios or appoint external managers to manage particular assets. For portfolios constructed internally, we use implementation managers to execute trades.

Capital allocation decisions are implemented across strategies and managers with a focus on achieving the best execution at all times. We strive to deliver the most consistent and efficient implementation of a portfolio. Transaction costs are a key detractor of performance, so a strong focus on portfolio implementation is key to minimising these costs.

Our external managers, including implementation managers, face brokers in the market. In accordance with the agreements we have with these managers, execution and allocation of trades must be done in good faith, on an arm's length basis and in accordance with the managers own Best Execution and Trading Policies.



Implementation and external managers' middle offices facilitate the support for trade execution. Managers leverage software providers such as Global Trading Support Services (GTSS), integrated with FX Connect, and proprietary trade management systems which provides seamless connectivity from trade execution to settlement, including direct connectivity via Financial Information eXchange (FIX) from front office to middle office trade processing as well as via the SWIFT network to a full community of custodian banks for the purposes of settlement notification.

## **Asset Stewardship**

Morningstar's approach to providing effective asset stewardship on behalf of clients lies in its approach to initially assessing and undertaking due diligence on appropriate investments. This is supplemented by ongoing monitoring, engagement and communication which considers both financial and non-financial matters. Our approaches across both internally managed strategies and external managers are summarised below:

### Internally managed strategies

A primary focus of our internally managed, direct equity investment process is to identify and monitor how the companies, in which we are invested, manage their capital for the benefit of their shareholders. Our quality and valuation metrics are built upon the actual financial performance of companies in the context of the industries in which they operate. We also monitor and incorporate the propensity and ability of corporate management to return capital directly to shareholders. Another key component of our process is our qualitative assessment of company management through internal and external research analyst reports, company reports, and media reports.

### External managers

Our due diligence process for evaluating managers and/or strategies combines quantitative data analysis with a qualitative assessment of a strategy's personnel and resources, investment philosophy and process, and firm stewardship. We acknowledge that truly skillful managers are not a commodity, but rather, a scarce resource. Accordingly, our critical focus in researching managers is to assess and identify key areas where a comparative advantage exists and whether it can be sustained.

In this context we focus on the following:

- **People** – We view people as the most important area and look for investors with stable teams with proven track records, bring a different perspective and have their interests aligned with clients
- **Philosophy and Process** – We look for a strong and well-defined investment philosophy that suits the people, is repeatable, has a long-term fundamental approach, and is underpinned by a robust approach to risk management

- **Firm** – It’s also imperative that a firm enables quality people to operate effectively and puts investors first. Most important is that the firm provides alignment between clients and the fund managers, the structure is conducive to investment independence, is appropriately resourced with good culture to retain its key people

Our process is designed to keep abreast of any changes occurring with the direct investments or the managers we invest with. This is done through regular monitoring and frequent contact and engagement with the management and fund managers of the respective companies. Our team continues to evaluate the investment options based on the same process used in the review and selection stage, but we understand that the ongoing due diligence of an investment option presents different challenges. Therefore, Morningstar Investment Management focuses on specific issues or events that could change its opinion of the investment option and challenge its original investment thesis.

The ongoing monitoring process focuses on the following issues:

- Regulatory issues
- Organizational and/or manager changes
- Management team updates
- Style and process consistency
- Portfolio characteristics
- Risk-adjusted performance
- Asset growth

Morningstar Investment Management is constantly developing and evolving our skills and capabilities to ensure our approach to asset stewardship is best practice in Australian and global investment markets. Morningstar continues to invest further in areas of ever increasing relevance to investors including behavioural science and environmental, social, and governance (ESG) research.

Morningstar Investment Management does not explicitly take into account ESG considerations when making investment decisions or selecting external managers. However, we believe that there are links between an organisation’s environmental and social impacts, the quality of its corporate governance, and its long-term business success. Further to our investment principles, we believe ESG factors provide additional insights into areas of potential risk and opportunity that may impact the valuation, performance and reputation of the investments we make

Another area of client asset stewardship which is of increasing importance is the approach to proxy voting. Morningstar recognises that voting rights have economic value and that the exercise of such voting rights is a fiduciary duty. We generally require appointed investment managers to manage stock specific governance matters. Morningstar Investment Management believes that its appointed managers are in a better position to manage the proxy voting requirements in respect of their portfolio holdings.



Our investment manager agreements generally require the appointed fund manager to vote on resolutions put to shareholders in accordance with their proxy voting policy. In some instances, as part of an investment mandate, we will authorise our investment managers or agents to exercise our voting rights in accordance with our proxy voting principles. To supplement these principles Morningstar can choose to engage with other investors, industry groups and/ or industry associates and bodies to formulate an approach to ensure securing the best client outcomes. In all circumstances, we retain our voting and other rights in relation to Scheme investments and reserve the right to override a manager's ability to exercise such right.

Morningstar Investment Management manages proxy voting in accordance with its Proxy Voting Policy.

To ensure transparency to investors Morningstar Investment Management produces a range of periodic (monthly, quarterly and annual) and ad-hoc reports and presentations consistent with regulatory and compliance requirements and client service level commitments. These form an essential pillar of Morningstar's client and investor engagement. Performance reports and presentations are developed in-house using proprietary and third-party software, leveraging our internal systems and databases. Morningstar Investment Management assigns 'owner' and 'reviewer' responsibilities for each report in accordance with our publication approval process. This ensures that client reports are comprehensively reviewed by the relevant stakeholders at the appropriate stage of production. Finally, reports are communicated to clients via email, website, third party platforms and/or our proprietary adviser portal (Information Library).

Morningstar Investment Management is well-resourced and adept at communicating in a client friendly manner. Our focus is on presenting the potentially difficult world of investing in a way that can be understood and appreciated by the investor, resulting in better investor engagement. In addition, wherever possible, our communication encompasses behavioural finance principles, helping investors to stay the journey and achieve their longer-term investment objectives.