



WALTER SCOTT

▶ BNY MELLON | INVESTMENT MANAGEMENT

WHY INVESTING IN QUALITY
COMPANIES MATTERS NOW
MORE THAN EVER

FPPTA CONFERENCE

October 2023

AGENDA



INTRODUCTION



WHY QUALITY?



IDENTIFYING AND ASSESSING QUALITY



EVIDENCING QUALITY



CONCLUSION

INTRODUCTION

**BESPOKE EQUITY PORTFOLIO
MANAGER**

**BASED IN EDINBURGH,
SCOTLAND & BOSTON, USA[†]**

**100% OWNED BY BNY MELLON
SINCE 2007**

**\$81.3BN ASSETS UNDER
MANAGEMENT**

284* CLIENT RELATIONSHIPS

**LONGEVITY OF CLIENTS,
STAFF & PHILOSOPHY**



**ALEX
TORRENS**

Alex is Head of Walter Scott North America, a division of BNY Mellon Securities Corporation, and is based in Boston. Alex is also a member of the Investment Management Committee. He first joined the firm before university in 2006 and intermittently worked in different departments. Alex participated in the Walter Scott investment internship in 2009 and joined full time as an Investment Analyst in 2010. He performed investing roles until 2023, as an Investment Manager and Co-Head of the Research team from 2016. Alex holds an MA in Law from the University of Cambridge and an Executive Education certificate from Columbia Business School.



**GUSTAVO
BIKESBAKKER**

Gustavo is a Client Investment Manager. He joined Walter Scott** in 2022, after 11 years at Meketa Investment Group where he contributed to the firm's client services, sustainability and research efforts. Prior to this, he worked as an investment analyst at Ernst Research and Management, a Boston-based hedge fund. Gustavo earned an MS in Finance from Carroll Graduate School of Management at Boston College, an MSM/MBA from the Arthur D. Little School of Management, an Analista de Sistemas degree from the Fundación BankBoston School of Information Science in Buenos Aires, and a Certificate of Advanced Studies in Sustainable Finance at the Haute École de Gestion Geneva.

*As at 30 June 2023. *284 consists of 137 Clients and 147 Fund Investors.*

[†]All operations are based in Edinburgh, Scotland with a client service presence in the United States.

***Whilst an employee of BNY Mellon, Gustavo is 100% focused on supporting Walter Scott clients.*

WALTER SCOTT AND QUALITY

We believe returns derived from investing in the shares of a company will reflect the internal wealth generated by that business

MSCI

“A quality score for each security is calculated by combining Z scores of three winsorized fundamental variables—Return on Equity, Debt to Equity and Earnings Variability. MSCI then averages the Z scores of each of the three fundamental variables to calculate a composite quality Z score for each security, and then ranks all constituents of the parent index based on their quality scores. A fixed number of securities with the highest positive quality scores is determined for each MSCI Quality Index with the goal of achieving high exposure to the quality factor while maintaining sufficient index market capitalization and number of securities coverage.”

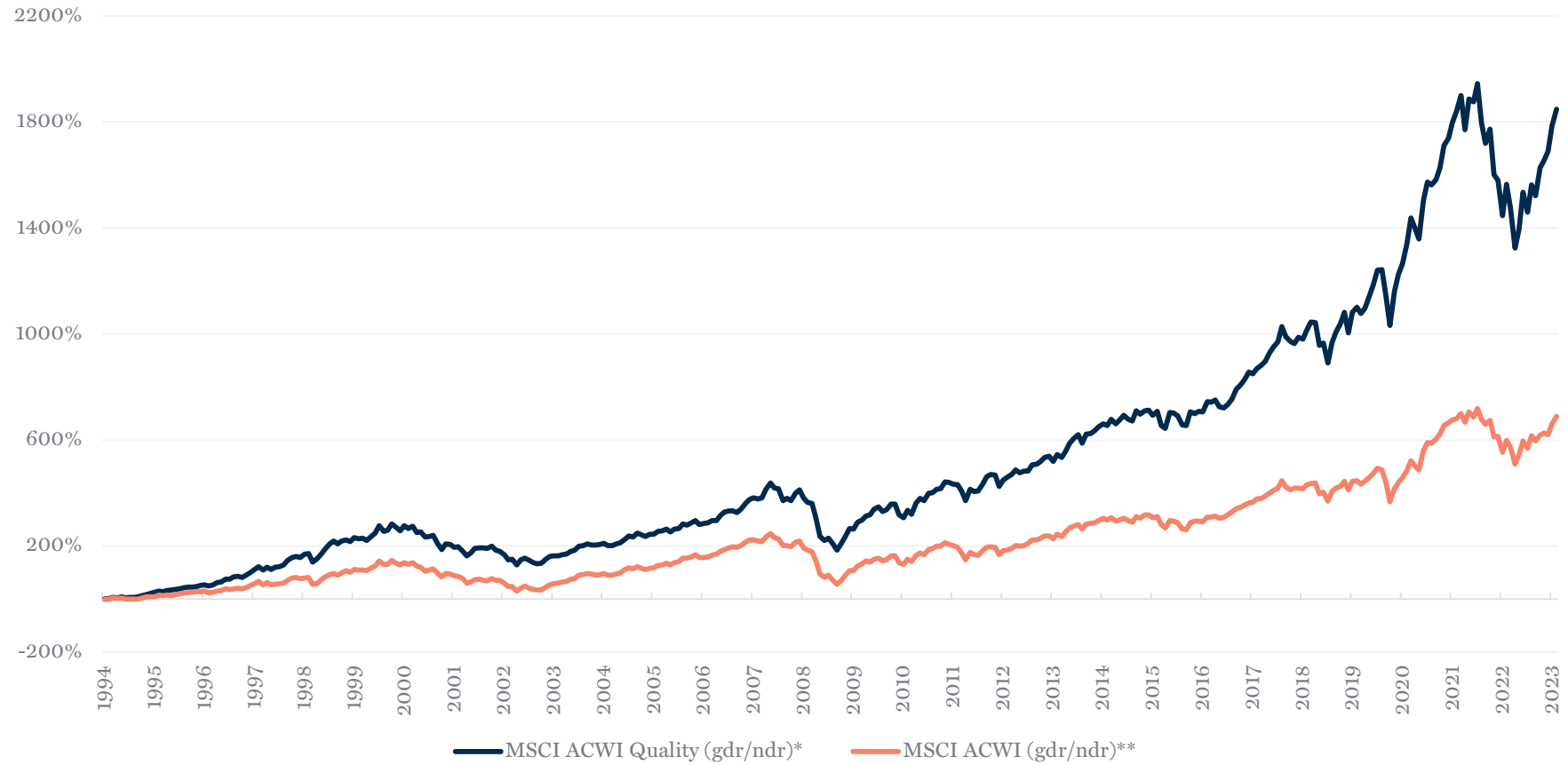
OUR PHILOSOPHY

We believe the interests of all our stakeholders are best served by actively investing in responsibly managed companies capable of delivering exceptional levels of wealth generation

Source: MSCI, Walter Scott.

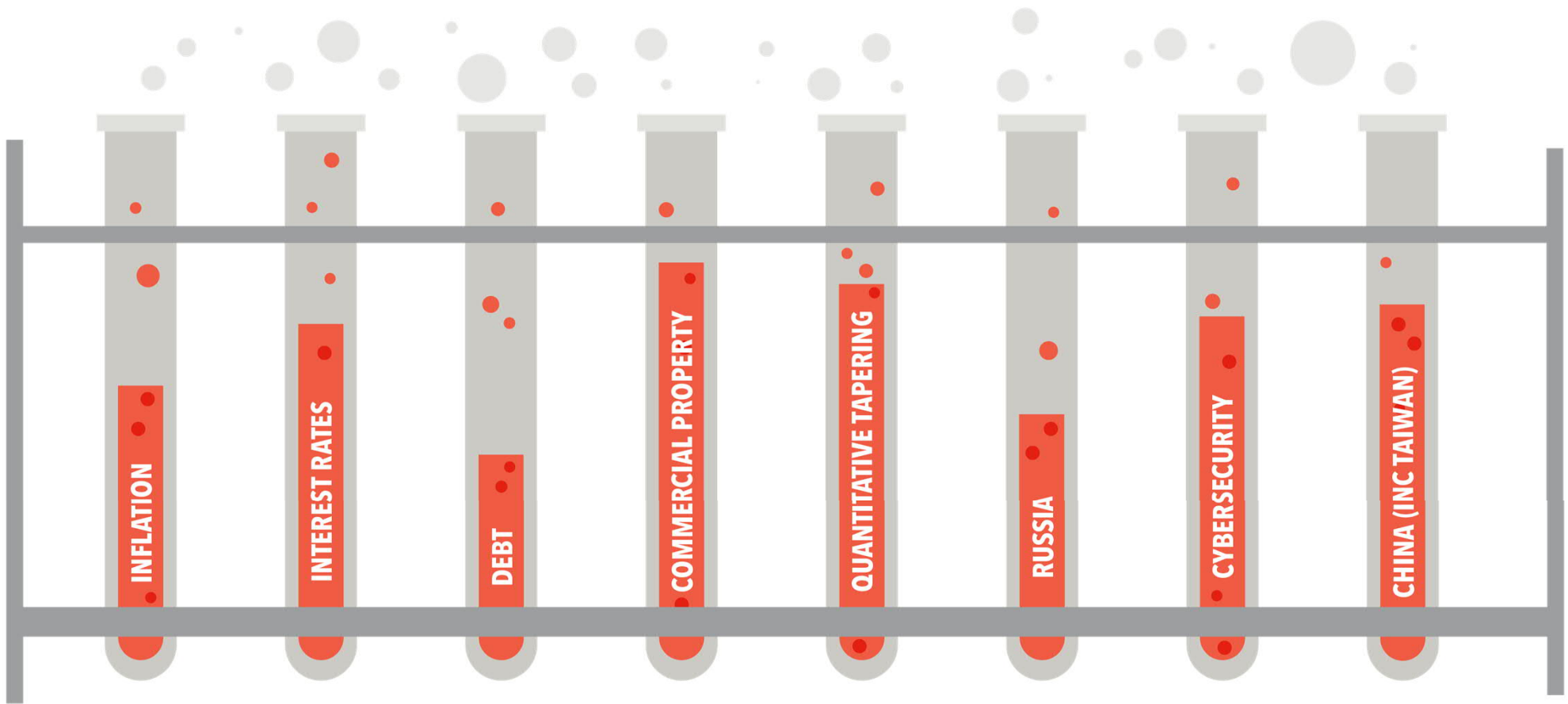
WHY QUALITY?

Cumulative USD Performance 30 June 1994 to 31 July 2023



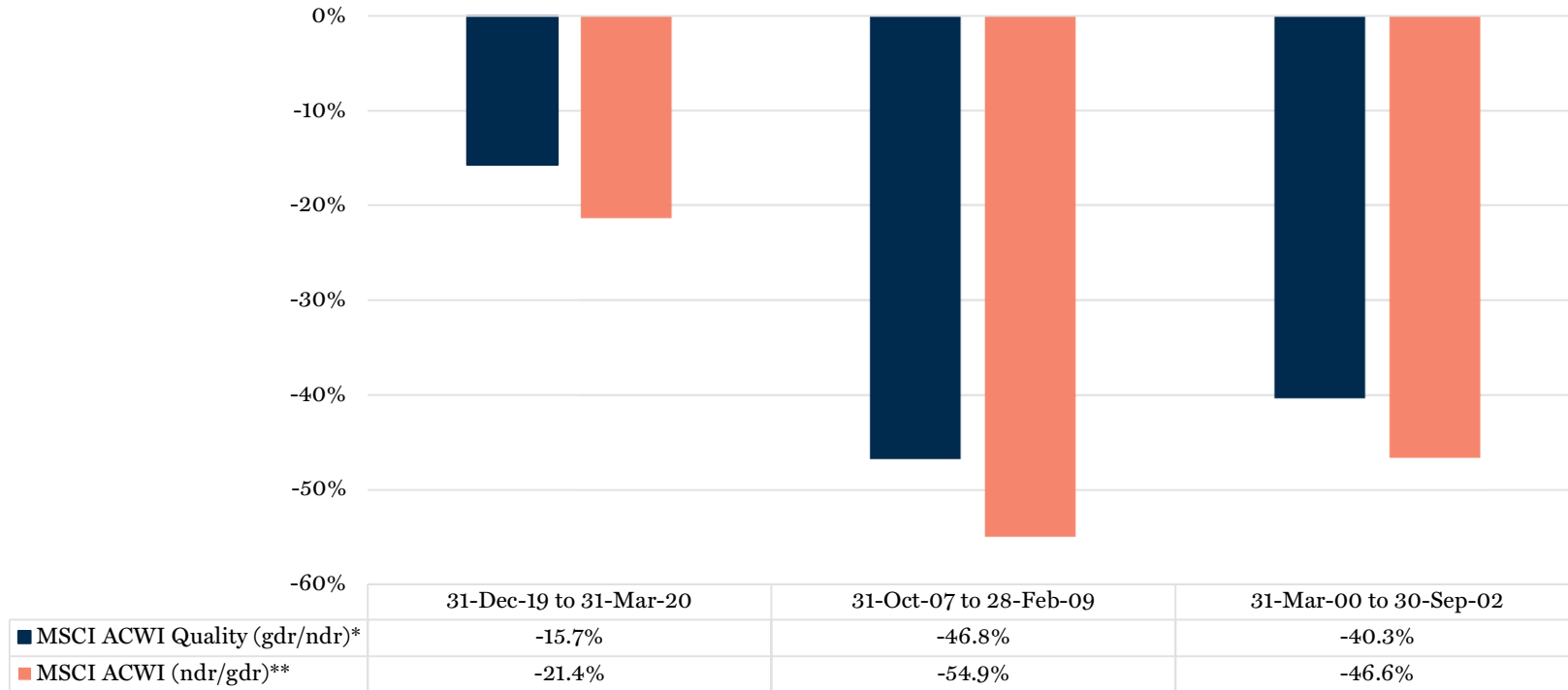
Source: MSCI. *MSCI ACWI Quality was inceptioned in December 2012. Periods before that point use backdated data using the same methodology. MSCI ACWI Quality (gdr) from 30 June 1994 until 31 December 2000, MSCI ACWI Quality (ndr) thereafter. **MSCI ACWI (ndr) data is only available from 1 January 2001. The period from 30 June 1994 until 31 December 2000 uses MSCI ACWI (gdr) figures.

WHY QUALITY?



WHY QUALITY?

3 Most Significant Drawdown Periods 30 June 1994 to 31 July 2023



Source: MSCI. *MSCI ACWI Quality was inceptioned in December 2012. Periods before that point use backdated data using the same methodology. MSCI ACWI Quality (gdr) from 30 June 1994 until 31 December 2000, MSCI ACWI Quality (ndr) thereafter. **MSCI ACWI (ndr) data is only available from 1 January 2001. The period from 30 June 1994 until 31 December 2000 uses MSCI ACWI (gdr) figures.

WHAT DOES QUALITY LOOK LIKE TO US?



EXCELLENT MANAGEMENT AND CULTURE

- Exemplary capital allocation
 - Foster sustainability
 - Think long-term
 - Integrity



GROWTH OPPORTUNITIES

- Growing markets
- Market share gains
 - Organic-led



CONTROL OF DESTINY

- Not reliant on economic cycle
- Lack of substitution risk
 - Limited supplier or customer concentration
- Rational competition



BARRIERS TO ENTRY

- Technology leadership/innovation
 - Economies of scale
 - Network effects
 - Brand strength
- High switching costs



NICE TO HAVES

- Virtuous cycles
- Pricing power
- Recurring revenues
- Low-cost, mission-critical
- Friendly middlemen
- Relative obscurity

IDENTIFYING AND ASSESSING QUALITY

Our proprietary process breaks an individual company into key constituent parts. It forces rigour and rationality over any bias

SEVEN SISTERS SAMPLE

Stock champion:

Company Business Comment

History of the company, when it was founded, what are its key principal business lines etc.

Market share data and trends in share

Does it drive growth organically or through M&A?

Does the company possess pricing power? If so, why?

Comment on margins and whether they reflect this pricing power, if not, why not?

Integrity

Desired six methods

Qualified statement

Outright liabilities

Off-balance sheet

Indirect selling

Treatment of minorities

Environmental, social & governance considerations*

- Accounting standards
- Audit statement – Qualified or not?
- Who is the auditor? How many years have they used the current auditor?
- Off-balance sheet vehicles?
- History of ownership, management ownership, treatment of minority shareholders?
- Any other black marks on the company through its history?
- Board structure / Independent director representation / separation or CEO and Chairman roles?
- Environmental footprint / CO2 emission reduction targets / Other "E" factors to be aware of / "E" ratings by third party Informa provides etc.
- Social considerations – Usually taken from company Sustainability report

Market Position

Market share/growth

Small membership growth

Set-backs/fragmented

Cyclical/steady growth

Barriers to entry

Technical disruption

Customer/supplier concentration

Fashion orientation

- What kind of market is this – High growth / Low growth?
- Is the industry controlled by a small number of big players or is it highly fragmented?
- Cyclicality of industry (peak to trough growth rates) and cyclical nature of company growth?
- Is this a high barrier to entry industry? If so, why?
- Is the industry exposed to technological disruption
- Who are the key customers?
- % of revenues accounted for by top 5 customers etc
- Is this an industry driven by consumer fads?

Profitability

Sustainable return structure

Price/sellprice ratio

Cash flow sufficiency

Margin trends

- IRR - % Internal Rate of Return
- ROE - % Return on Equity
- Does the current return structure appear to be sustainable?
- Does it cover Capex and other requirements?
- Cash flow generation – does it cover Capex and other requirements?

Financial Control

Balance sheet stability

Debt structure/currency/duration

Balance between retained earnings and paid up capital

- Balance sheet analysis commentary – Net debt to Equity / Leverage ratio / Interest coverage / Credit rating and Outlook
- If there is debt, is it fixed or floating?
- Debt duration / average cost of debt / maturity profile

Management

Information on listing

Average daily trading volumes

Single class of stock or multiple?

ADR level

- Who are management? Previous experience and current tenure and competency of management
- Do we have access to management, view on the transparency and competency of management
- Information on listing information
- Average daily trading volumes
- Single class of stock or multiple?
- Valuation metrics

COMPANY NAME
Last Modified Date:
Approval Status: Approved

EMERSON TABLE	2015	2016	2017	2018	2019	2020	1 Year %
Revenue	120,000	125,000	130,000	135,000	140,000	145,000	14.2%
Operating Profit	35,000	38,000	41,000	44,000	47,000	50,000	14.2%
Net Income	30,000	33,000	36,000	39,000	42,000	45,000	14.2%
Free Cash Flow	30,000	33,000	36,000	39,000	42,000	45,000	14.2%
Capital Expenditure	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)	(100%)
Debt	(45,000)	(45,000)	(45,000)	(45,000)	(45,000)	(45,000)	(100%)
Equity	75,000	80,000	85,000	90,000	95,000	100,000	14.2%
Market Cap	180,000	190,000	200,000	210,000	220,000	230,000	14.2%
EV/EBITDA	12x	12x	12x	12x	12x	12x	100%
EV/FCF	10x	10x	10x	10x	10x	10x	100%
EV/EBIT	15x	15x	15x	15x	15x	15x	100%
EV/Operating Profit	18x	18x	18x	18x	18x	18x	100%
EV/Net Income	20x	20x	20x	20x	20x	20x	100%
EV/Free Cash Flow	22x	22x	22x	22x	22x	22x	100%
EV/Debt	3x	3x	3x	3x	3x	3x	100%
EV/Equity	2.4x	2.4x	2.4x	2.4x	2.4x	2.4x	100%
EV/Market Cap	0.7x	0.7x	0.7x	0.7x	0.7x	0.7x	100%

COMPANY NAME - Integrity, Sustainability and Governance Summary

Include a clear bullet-point summary, containing the most material integrity, sustainability and governance opportunities, risks and engagement initiatives

Opportunities:

- Working Capital & Supply Chain
- AC (PRODUCTION) EFFICIENCY
- AC (PRODUCTION) COST OF SALES
- ENVIRONMENTAL COMPLIANCE
- ASSET PRODUCTIVITY
- CASH FLOW IMPROVEMENT

Risks:

- INTERNAL RATE OF RETURN
- CHANGE IN WORKING CAPITAL POLICY
- CAPEX'S VALUE
- CASH ACQUISITIONS & SHARE
- NET FINANCIAL COST
- LIQUID PROFIT & NET DEBT
- NET DEBT & SHAREHOLDERS PERIOD

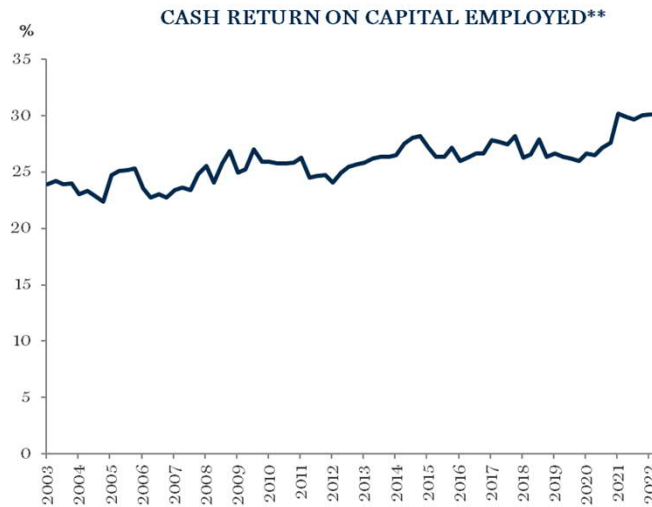
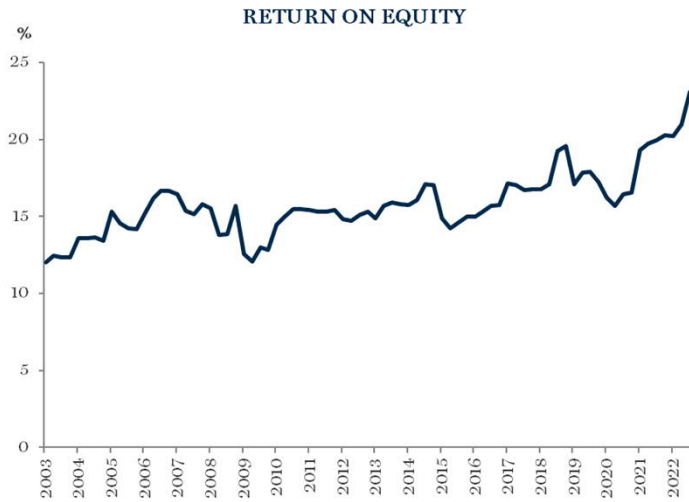
Examples being	2015	2016	2017	2018	2019	2020
CO2 emissions from transportation	100	100	100	100	100	100
Renewable energy use (production)	100	100	100	100	100	100
Total Carbon Footprint	100	100	100	100	100	100

- Environmental Considerations**
- Water
 - Natural resource usage
 - Biodiversity
 - Circular economy
- What are the company's material environmental risks?
- What environmental targets are in place?
- How well does the company manage its use of natural resources?
- Carbon Risk and Climate Change**
- Carbon Risk and Climate Change
 - Physical risk
 - Transition risk
 - Financial risk
- Does the company measure its climate impact?
- Are measures in place to reduce the company's climate impact?
- Does the company have a transition strategy in place?
- Human and Social Capital**
- Board and culture
 - Conduct and culture
 - Cyber security
 - Diversity
 - Human Capital
 - Management/labour rights
 - Supply chain management
 - Tax
 - Community engagement and social license
 - Product safety
- Does the company culture support diversity and inclusion?
- Has the company experienced quality or safety issues and if so, what measures have been put in place to mitigate these?
- How well does the company know its supply chain? Is it audited?
- What controls are in place to ensure cyber security / data privacy?
- Is the board of directors sufficiently independent?
- Does the board of directors have the individuals with the requisite skills and experience to ensure effective and inclusive decision-making?
- Is executive remuneration proportionate, well-structured and aligned with long-term sustainable value creation?
- How are minority shareholders treated?

Information Classification: Internal
T200 bullet point added Dec-14

COMPANY EXAMPLES

EVIDENCING QUALITY GLOBAL PORTFOLIO CHARACTERISTICS AS AT 30 JUNE 2023

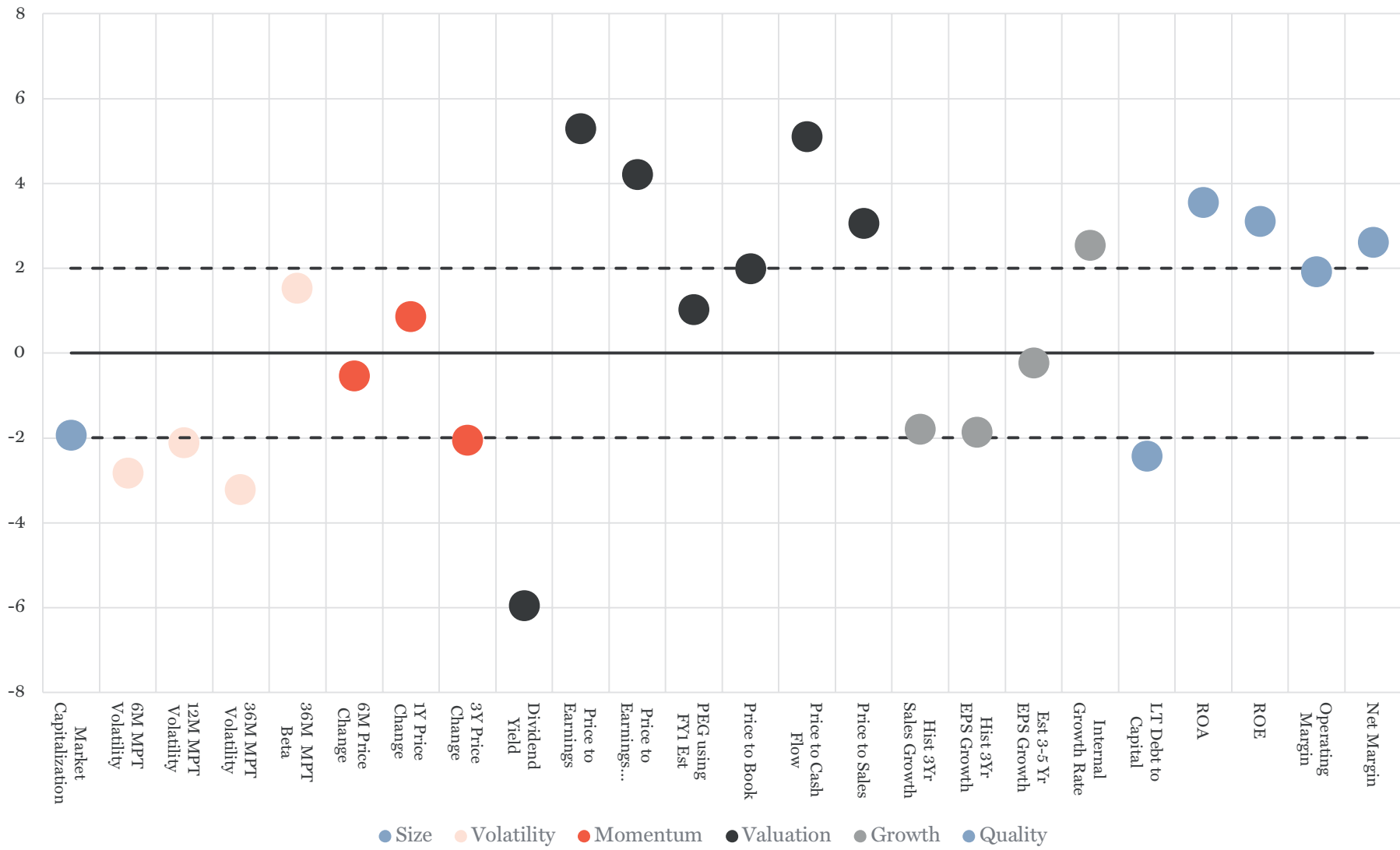


	Representative Portfolio	MSCI ACWI
ROE*	23.1%	14.4%
CROCE**	29.7%	18.2%
Operating Margin	17.4%	12.4%
Net Debt to Equity***	24%	81%
P/E	29.2x	19.3x
Dividend Yield	1.2%	2.1%
Number of securities	49	2,935
Turnover (12 months)	7%	-
Active Share	86%	-

*Source: Walter Scott, FactSet, MSCI. A representative global portfolio was used to illustrate this strategy. *Walter Scott defined methodology which may vary from MSCI index figures. **Cash Return on Capital Employed calculation excludes Financials and Real Estate holdings. ***Net Debt to Equity ex Financials. Past performance is not a guide to future performance and returns may also increase or decrease as a result of currency fluctuations. Full details of characteristics calculation methodology available upon request.*

EVIDENCING QUALITY

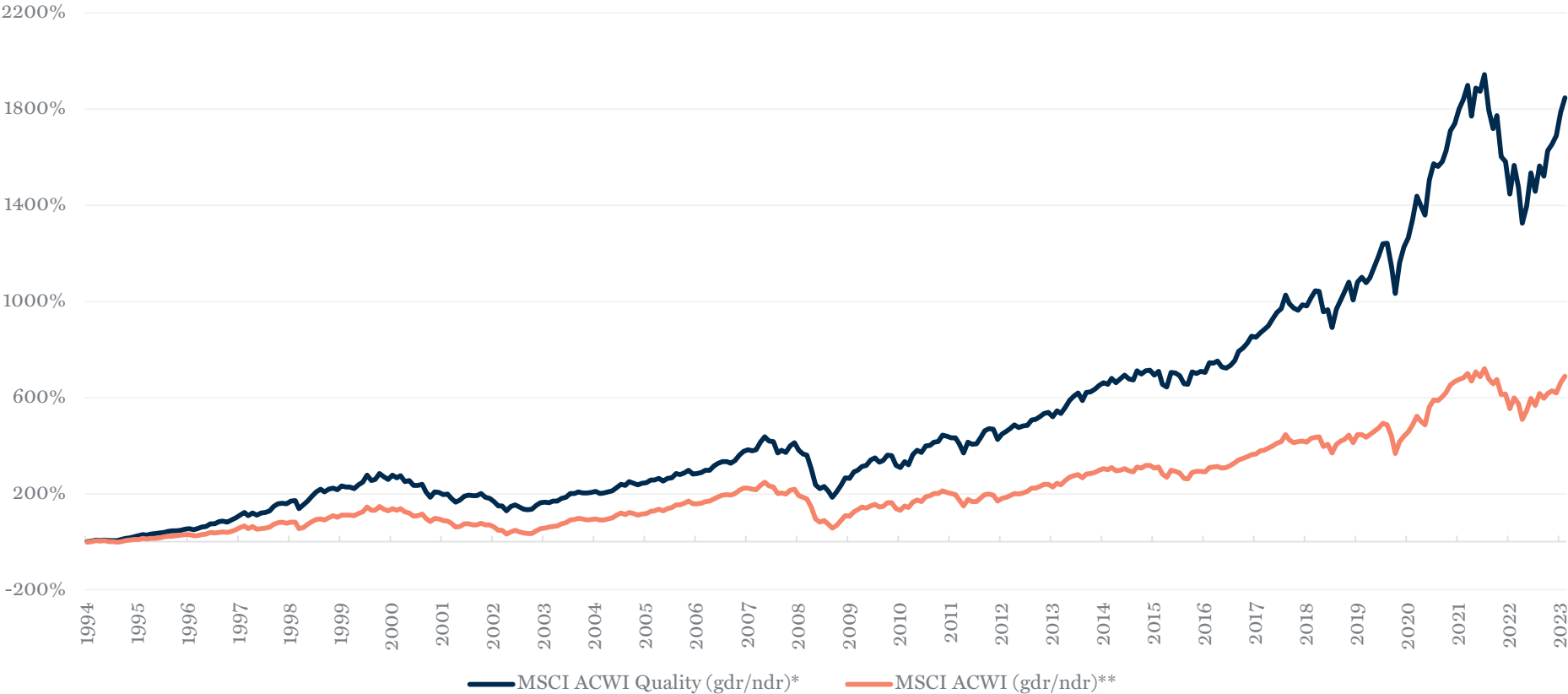
REPRESENTATIVE GLOBAL PORTFOLIO VS MSCI ACWI - CHARACTERISTIC TILT AS AT 30 JUNE 2023



Source: FactSet. Full details of characteristics calculation methodology available upon request.

SUMMARY

Cumulative USD Performance 30 June 1994 to 31 July 2023



Source: MSCI. *MSCI ACWI Quality was inceptioned in December 2012. Periods before that point use backdated data using the same methodology. MSCI ACWI Quality (gdr) from 30 June 1994 until 31 December 2000, MSCI ACWI Quality (ndr) thereafter. **MSCI ACWI (ndr) data is only available from 1 January 2001. The period from 30 June 1994 until 31 December 2000 uses MSCI ACWI (gdr) figures.

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On behalf of us all,

THANK YOU

APPENDIX

1. DEFINITION OF FIRM

Walter Scott & Partners Limited (“Walter Scott”) is an investment management firm authorised and regulated in the United Kingdom by the Financial Conduct Authority in the conduct of investment business. Walter Scott is a non-bank subsidiary and 100% owned by The Bank of New York Mellon Corporation. All operations are based in Edinburgh, Scotland with a client service presence in the United States. Walter Scott is responsible for portfolios managed on behalf of pension plans, endowments and similar institutional investors. Total assets under management were US\$81.3 billion as at 30 June 2023.

2. PRIVACY NOTICE

Personal information may be collected by Walter Scott following attendance at, or registration to attend, a Walter Scott, affiliate or partner event and will be used solely for the purpose of facilitating the provision of investment management services and managing business relationships. For more information about how Walter Scott collects, uses and shares personal information and an individual’s legal rights (including opt-out rights), please see the full privacy notice which is available on the website: www.walterscott.com/privacy-policy.

3. LEVERAGE, DERIVATIVES AND SHORT POSITIONS

Walter Scott does not generally use derivatives, but American style currency options have been used occasionally for hedging purposes (most recently held in 2007). Walter Scott does not use leverage or short positions.

4. FIRM POLICIES

Policies for valuing portfolios, calculating performance, and preparing GIPS Reports are available upon request.

5. BENCHMARK DEFINITIONS

Walter Scott compares its composites against the published MSCI indices as shown in this presentation. Further information on these indices can be found at: www.msci.com

6. COMPLIANCE STATEMENT

Communication of performance figures reflected in this document must be on a one-on-one basis, private and of a confidential nature. They may not be disseminated to the public in any print, electronic or other medium, including a web-site or any database of general circulation. The following disclosures must be provided in writing when onwardly communicating these performance figures.

Unless otherwise stated performance figures do not reflect the deduction of investment advisory fees.

Returns will be reduced by investment advisory fees and any other expenses that may be incurred in the management of an account.

7. IMPORTANT INFORMATION

7.1 Walter Scott’s Investment Approach

This presentation contains certain statements based on Walter Scott’s experience and expectations about the markets in which it invests its portfolios and about the methods by which it causes its portfolios to be invested in those markets. Those statements are not guaranties of future performance and are subject to many risks, uncertainties and assumptions that are difficult to predict. The information in this presentation is subject to change and Walter Scott has no obligation to revise or update any statement herein for any reason. The opinions expressed in this presentation are those of Walter Scott and should not be construed as investment advice.

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Some information contained herein has been obtained from third party sources that are believed to be reliable, but the information has not been independently verified by Walter Scott. Walter Scott makes no representations as to the accuracy or the completeness of such information and has no obligation to revise or update any statement herein for any reason.

7.3 Performance Statement

Past performance is not a guide to future returns and returns may increase or decrease as a result of currency fluctuations. The objective mentioned may therefore not be reached. Many factors affect investment performance including changes in market conditions, interest rates, currency fluctuations, exchange rates and in response to other economic, political, or financial developments. Investment return and principal value of an investment will fluctuate, so that when an investment is sold, the amount returned may be less than that originally invested. This presentation does not represent and must not be construed as an offer or a solicitation of an offer to buy or sell securities, commodities and/or any other financial instruments or products. This presentation may not be used for the purpose of an offer or solicitation in any jurisdiction or in any circumstances in which such offer or solicitation is unlawful or not authorised.

7.5 Performance Indices

Comparisons to the indices have limitations because the volatility and material characteristics of the indices represented in this presentation may be materially different from that of the portfolio managed by Walter Scott. Because of these differences, investors should carefully consider these limitations when evaluating the performance in comparison to benchmark data as provided herein. Where referencing MSCI or any other index performance figures:

The MSCI data is comprised of a custom index calculated by MSCI for, and as requested by, Walter Scott & Partners Limited. The MSCI data is for internal use only and may not be redistributed or used in connection with creating or offering any securities, financial products or indices.

APPENDIX

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7.6 Benchmark Definitions

MSCI ACWI

The MSCI All Country World Index (ACWI) captures large and mid cap representation across 23 developed and 24 emerging markets countries. With approximately 2,800 constituents, the index covers around 85% of the global investable equity opportunity set. Further information can be found at www.msci.com

WALTER SCOTT

 BNY MELLON | INVESTMENT MANAGEMENT

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