

WaveStone ESG Report

Quarter ending December 2024

ESG Quarterly: The “S” in Supply Chains: Focus on Modern Slavery

As active investors with fundamental bottom-up research, we spend time understanding the supply chains and operations of the businesses we invest in. In Q2 2024 we did a [research note](#) on supply chains from an environmental perspective, focusing on upstream and downstream emissions (scope 3).

This research note also focuses on companies' supply network, but from a social perspective, specifically modern slavery risks.

The issue

Modern slavery describes situations where workers are subjected to coercion, threats or deception to exploit them and undermine their freedom. Over time Australians are importing a greater proportion of their manufactured goods meaning Australian companies are often exposed to these risks through the offshore suppliers they use, particularly those with complex international supply chains, posing significant legal and reputational risks.

Walk Free¹ and the International Labour Organization (ILO)² have estimated that there are 49.6 million victims of modern slavery in the world today. Of these, 58% of these are from five powerhouse countries of the global economy: India, China, Pakistan, Bangladesh and Uzbekistan. They provide low-skilled labour for industries such as food production, technology and textiles.

Walk Free lists Electronics, Garments, Palm Oil, Solar Panels and Textiles as the top 5 at risk imports by G20 countries.³

- Electronics from China and Malaysia remain the highest value at-risk product imported by G20 countries.
- Labour exploitation is pervasive in the garment industry, which is the second most valuable at-risk product. At-risk garments imported into the G20 are manufactured in Argentina, Bangladesh, Brazil, China, India, Malaysia, and Vietnam.
- Polysilicon, a silica-product derived from quartz sand, is essential to manufacturing solar panels. China is the market leader in polysilicon production and in 2021 about 45% of the world's polysilicon supply originated from the Uyghur region. Multiple reports allege presence of forced labour and abuse of other human rights in the Uyghur region.
- In Malaysia, migrant workers make up the majority of the palm oil workforce, and once on a plantation they can face heightened risks of debt bondage, restricted movement, confiscation of identity documents, and having their wages withheld. Conversely, the Indonesian palm oil industry relies majorly on domestic labour, including internal migrants, however the use of a piece-rate system of pay with no mandatory minimum wage or social protections has led workers to involve their children in the work in order to meet the high harvest quotas and earn a survival wage.

¹ [Global Slavery Index | Walk Free](#)

² [ILO Homepage | International Labour Organization](#)

³ [Importing risk | Walk Free](#)

The above are examples of how modern slavery risks whilst prevalent in low-income countries, can be deeply connected to demand from higher-income countries. The production and movement of goods between countries – from the sourcing of raw materials to manufacturing, packaging, and transportation – creates complex and opaque supply chains, many of them tainted with forced labour.

In our assessments of modern slavery risks, we find that business to consumer (B2C) brands necessitate higher investor due diligence compared to business to business (B2B) brands. For instance, Reliance Worldwide Corporation (ASX: RWC) distributes its products via larger retailers like Home Depot and so is subjected to Home Depot's supplier due diligence and checks, whereas a brand selling directly to consumers such as Kmart would require careful investor due diligence for modern slavery risks.

Why now?

We note progress in company awareness and disclosure since the introduction of Modern Slavery Act in 2018. There is a growing cohort of companies disclosing and explaining advanced actions to manage modern slavery risks.⁴

As companies mature in their identification and reporting of modern slavery risks, we increasingly realise the potential for its presence in operations and supply chains of companies. This poses regulatory, financial, reputational as well as operational risks for companies if not remediated.

For instance, in October 2020, the Federal Court of Australia ordered **Westpac Banking Corporation (ASX: WBC)** to pay a 1.3 billion Australian dollar penalty for breaches of the Anti-Money Laundering and Counter Terrorism Financing Act 2006, some of which involved misuse of Westpac's payment systems to pay for trafficking of children, overseas. This was the highest civil penalty in Australian history.⁵

In 2022, **Ansell Limited (ASX: ANN)** was hit by a lawsuit in the US, alleging it knowingly used a sub-contractor in Malaysia who engaged in modern slavery to make pharmaceutical grade gloves.⁶

We also draw from the below recent regulatory updates that are expected to drive increased focus on supply chain due diligence, transparency and corporate reporting.

- [Government's response to the Australian Modern Slavery Act Review](#)⁷;
- the appointment of Australia's first Anti-Slavery Commissioner⁸; and
- the [EU Corporate Sustainability Due Diligence Directive \(EU CSDDD\)](#)⁹, that are expected to drive increased focus on supply chain due diligence, transparency and corporate reporting.

In this research note we aim to cover an overview of the topic, the observed current state of disclosure and management of modern slavery risks for ASX companies and looking ahead engagement with companies.

Modern Slavery – Taking Value at Risk Approach

Our approach to assessing modern slavery related risks within a company's business activities considers potential value at risk for a business, along with an ongoing assessment of any serious allegations or breaches of human rights. Businesses that do not manage modern slavery risks effectively throughout their business activities are exposed to legal, reputational and financial risks. In particular, regulatory risk is growing and compliance costs for supply chain due diligence and disclosure are expected to rise.

For instance, **Coles Limited (ASX: COL)** noted an investment of >\$3.79m in the past three years to fund independent ethical audits (In FY24, 1,239 independent ethical audits were conducted on in-scope tier one and two suppliers; 1129 in FY23 and 911 in FY22).

⁴ [MSD ASX100 FY2023 111124.pdf - Google Drive](#)

⁵ [Westpac ordered to pay \\$1.3 billion penalty | AUSTRAC](#)

⁶ [Ansell responds to forced labour allegations against a supplier - Australian Manufacturing Forum](#)

⁷ [Australian Government response to the review report of the Modern Slavery Act 2018 \(Cth\)](#)

⁸ [Appointment of Australia's first Anti-Slavery Commissioner | Our ministers – Attorney-General's portfolio](#)

⁹ [Corporate sustainability due diligence - European Commission](#)

We concur with the findings of the recent Modern Slavery Act Review¹⁰, which covers weaknesses in the state of existing corporate disclosure as below:

Common weaknesses were: failing to address known modern slavery risks and products; failing to describe modern slavery risks beyond Tier 1 of supply chains; providing only a basic or unclear description of modern slavery risks; giving an inadequate explanation of risk assessment methods and grievance mechanisms; and not consulting with civil society groups in modern slavery risk assessment.

From an investor perspective, we view enhanced due diligence and disclosure requirements on this topic led by regulatory changes as overall positive.

We expect our portfolio companies to undertake appropriate due diligence across their business activities to proactively identify, assess, remediate and report modern slavery risks. Our engagements with companies aims to focus on the *effectiveness* of their modern slavery programs in place. For instance, we understand that for several companies, their outreach and engagement beyond Tier 1 suppliers is still evolving. We also understand that there can be practical impediments in supply chain mapping and product tracing. Some large organisations have tens of thousands of individual suppliers. Beyond tier 1 of the supply chain the business environment can be opaque and beyond the direct knowledge or control of the Australian company or even its tier 1-2 suppliers. In our view, gaining supply chain visibility across multiple tiers can also significantly benefit companies in achieving overall operational efficiency and competitive advantage.

Case Study: Coles Limited- Looking for Modern Slavery Risks beyond Tier 1¹¹

In May 2023, there were numerous media reports relating to serious allegations of human rights violations within a number of tea supply chains. Concerns raised included wages, unsafe working conditions and sexual harassment across multiple tiers within the supply chain, including down to tea estates.

Based on the concerns raised, Coles reached out to its suppliers to understand if the allegations raised were within its supply chain. It was confirmed that some were.

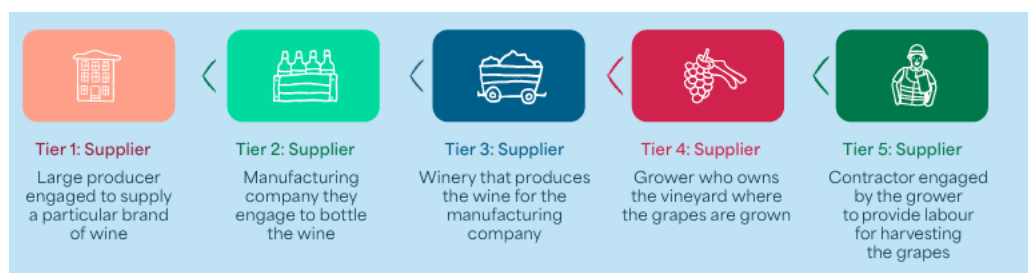
On one site, the allegations of sexual harassment were confirmed, and action was taken as a result. This included putting in place support for the people impacted – such as enhanced welfare structures for workers and doubling the size of the welfare team; offering free private counselling and psychosocial support to all workers onsite; strengthening contractor management; and a campaign to build awareness and trust in a confidential whistleblowing line.

Current State of disclosure and management of Modern Slavery Risks

Progress in the understanding of modern slavery risks has steadily improved over the years. Case examples of how companies are showcasing this in their disclosures is as below:

Detailed supply chain descriptions: Companies are providing more comprehensive descriptions of their supply chains, including information about suppliers beyond Tier 1.

For instance, Endeavour Group 2024 Modern Slavery Statement¹² (ASX: EDV) describes its wine supply chain could look like below beyond Tier 1:



¹⁰ Page 26, Report of the statutory review of the Modern Slavery Act 2018 (Cth) The first three years

¹¹ Coles Modern Slavery Statement.pdf

¹² Page 12, 2024-Endeavour-Group-Modern-Slavery-Statement.pdf

Risk identification and assessment: Enhanced processes for identifying and assessing risks in accordance with the United Nations Guiding Principles (UNGP) are being implemented. The UNGPs are the recognised global standard for preventing and addressing business related adverse human rights impacts such as modern slavery.

For instance, **Commonwealth Bank’s 2024 Modern Slavery Statement**¹³ (ASX: CBA) uses UNGP to report on how they assess and address modern slavery risks across their business as an employer, a procurer of goods and services and a provider of banking products and services.

Supplier due diligence: There is an increased focus on conducting due diligence on suppliers to ensure they comply with modern slavery laws and standards. Some companies have even reported terminating supplier relationships based on non-cooperation, although a majority are attempting to work through the issues.

For instance, **Aristocrat Leisure Limited (ASX: ALL)** has a formal supplier due diligence process¹⁴ composed of two key steps as below:



Key performance indicators (KPIs): Companies are developing robust KPIs to measure the effectiveness of their modern slavery actions.

For instance, **Collins Food Limited (ASX: CKF)** outlines key KPIs in relation to its path forward in addressing modern slavery risks in its business¹⁵

Future Action	KPI	Status
The work of encouraging new and existing supply partners to register with Sedex is ongoing.	KFC Australia’s goal is to have all supply partners, who meet the registration threshold, registered with Sedex.	This is an ongoing task that will remain relevant as new supply partners are engaged.
KFC Australia will review its due diligence system in the context of the United Nations Guiding Principles on Business and Human Rights.	Review of system completed by the time of publishing the next modern slavery statement.	This is an ongoing body of work, that KFC Australia is considering outsourcing to ensure that it is completed by the time of the next statement.
KFC Australia continues to work on developing key performance indicators in relation to our modern slavery mitigation strategies, and documented remediation processes and policies.	To have a board approved set of KPIs relating directly to modern slavery mitigation.	This is an ongoing body of work, that KFC Australia is considering outsourcing to ensure that it is completed by the time of the next statement.
Maintain compulsory modern slavery training for new starters, and annual compliance training for all team members on the whistle-blower and open policy.	KFC Australia’s goal is to ensure that all new RSC staff receive modern slavery training within six (6) weeks of commencing employment, that all RSC door staff receive modern slavery training every two (2) years, and that all team members are reminded annually of the whistle-blower and open door policy.	This is an ongoing commitment.
Complete a review of all of KFC Australia’s employment and team member related policies, applying a modern slavery prevention lens.	To have completed a review of KFC Australia’s employment and team member related policies during 2024.	This work commenced in 2023 with the whistleblower policy, and is an ongoing body of work.
Include modern slavery related provisions in Yum! (global) contract templates.	To have included in the master services agreement template being utilised at a global level provisions requiring Sedex registration by global supply partners and their subsidiaries (as appropriate).	While KFC Australia does not control this work, the request has been lodged and the work is ongoing at the Yum! level.

¹³ Page 13, <https://www.commbank.com.au/content/dam/commbank-assets/about-us/docs/2024-Modern-Slavery-Statement.pdf>

¹⁴ Page 27, [Modern-Slavery-Statement-2023_FINAL.pdf](#)

¹⁵ Page 24, [Modern Slavery Statement 2024](#)

External collaborations: Fostering collaborations with external organisations to address modern slavery risks is becoming more common.

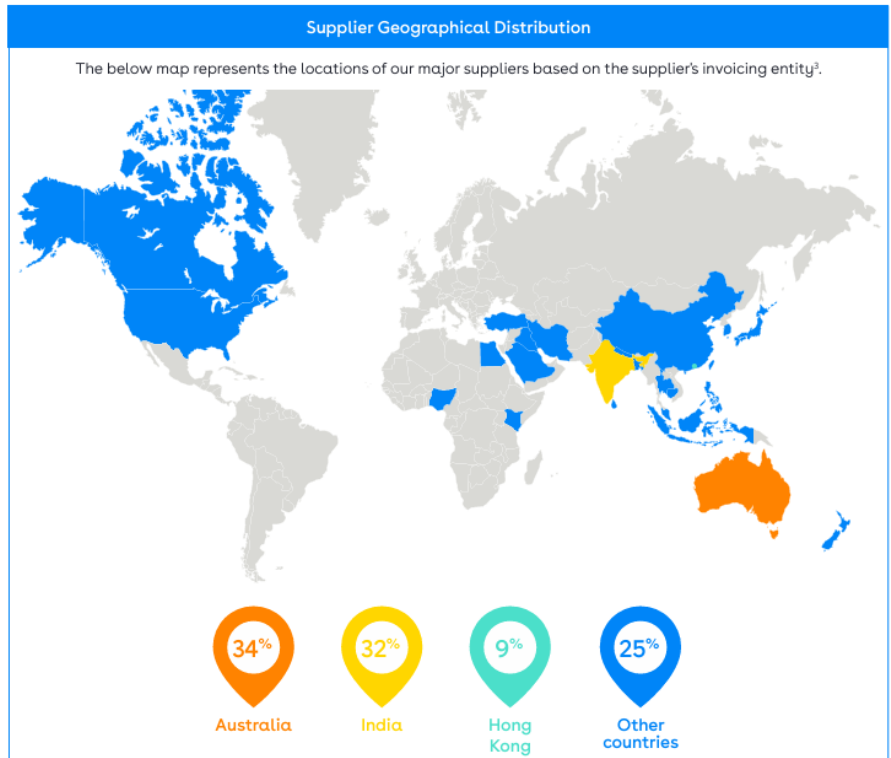
For example, during the year, Wesfarmers Health within the **Wesfarmers Limited (ASX: WES)** partnered with Australian Red Cross to boost workers' knowledge of workplace protections by promoting the Work Right Hub¹⁶. This collaboration focused on domestic suppliers and factories to inform and empower workers. Workers with these suppliers and factories can now anonymously access the Work Right Hub's multilingual decision tree tool by scanning a QR code, allowing them to access information on their workplace rights and protections and directing them to support services

Grievance channels and remediation processes: Having remediation processes demonstrates a commitment to continuous monitoring and providing remedy pathways when risks are identified. The UNGPs set out the effectiveness criteria for grievance mechanisms, which at a high level highlights the necessity of enabling trust from the stakeholder groups and ensuring that the grievance mechanism is accessible to all stakeholder groups.

For instance, **Woolworths Group Limited (ASX: WOW)** provides a good description of its grievance channels and remediation processes in its 2024 Modern Slavery Statement¹⁷. It has a *Supplier Speak Up* channel; in FY24 the company investigated a total of 73 human rights related grievances raised by workers across their supply chain, including grievances raised by workers in cleaning and trolley collection supply chain. This was an increase from F23, when 46 grievances were investigated.

Mapping Geographic spread of sourcing: A number of ASX companies now provide disclosure on their geographic exposure to high risk locations.

IDP Education Limited (ASX: IEL), as an example, provides disclosure of its geographic exposure for both its employees and suppliers in high-risk locations. The company identifies it has direct employees in high-risk geographies including: Pakistan, Nigeria, Cambodia, Egypt, Philippines, India, Turkey, Kenya, Bangladesh, Sri Lanka, Saudi Arabia. All these countries have a Global Slavery Index "Vulnerability Rating" over 50. However, due to its nature of business, the company notes that vast majority of IDP employees are engaged in professional or office-based roles. In regards, exposure to suppliers the company details this as below:



Source: *IDP 2024 Modern Slavery Statement*

¹⁶ Page 18, wesf-mss_2024_20241120_final_interactive_spreads.pdf

¹⁷ Woolworths Group 2024 Modern Slavery Statement.pdf

Investor Engagement Looking Ahead

Assessing how a company responds to any identified actual or potential instances of modern slavery in supply chains, and the steps taken to prevent further instances, should be of more importance than just the occurrence itself. Therefore, as responsible investors, it is vital that we proactively engage with companies, advocating for better practices and transparent disclosures.

Some engagement questions that can help initiate dialogue and evaluate a company's efforts:

- a. **Risk Assessment:** How does the company identify and assess modern slavery risks within its operations and supply network?
- b. **Policies and Procedures:** What policies and procedures are in place to prevent modern slavery, and how are they enforced?
- c. **Training and Awareness:** Does the company provide training to employees and suppliers on recognizing and preventing modern slavery?
- d. **Grievance Mechanisms:** Are there effective grievance mechanisms for workers to report modern slavery, and how are these handled?
- e. **Remediation Processes:** What steps does the company take to remediate any instances of modern slavery found in its operations or supply chains?
- f. **Transparency and Reporting:** How transparent is the company in its modern slavery statements and reports, and what improvements are planned?
- g. **Collaboration:** Does the company collaborate with external organizations or participate in industry initiatives to combat modern slavery?
- h. **Performance Metrics:** What metrics does the company use to measure its performance in addressing modern slavery, and how are these reported?

These questions can help investors gain a deeper understanding of a company's commitment to addressing modern slavery and encourage continuous improvement.

Carbon Emission and Intensity Tracker:

WaveStone – Australian Share Fund (WASF)	Carbon Emissions		
	Portfolio	Benchmark	Difference
Carbon Emissions Scope 1+2 (tonnes CO2e/USD M invested)	68.3	117.5	-41.9%
Carbon Intensity Scope 1+2 (tonnes CO2e/USD sales)	86.7	166.5	-47.9%

Source: MSCI ESG (as at 31/12/2024)

Benchmark is the S&P ASX 300 Accumulation Index

Engagement

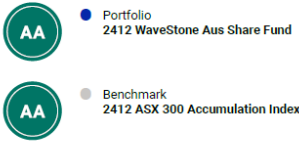
ESG-related Engagements during the Quarter

Company	ESG Category	Topics
SDF	Social Governance	Four Corners Report, ACCC investigation, CEO and Chair Succession
RIO	Social Governance	Discuss approach to Traditional Owners' engagement and related approvals
ANZ	Environment Governance	Shareholder proposal on climate, remuneration incentives, APRA operational risk capital impost, ASIC investigation into markets
IEL	Governance	Remuneration incentives
CSL	Social Governance	Performance of the ELT and drivers of group strategy, guidance and consensus expectations, plasma donation fees and donor experience of RIKA
FPH	Governance	View of the new Chair; Succession planning and long range planning for the business
COH	Governance	Succession planning, profitability and reinvestment balance
EDV	Governance	Chair meeting following CEO departure
WES	Governance	Chair succession. Priceline/Chemist Warehouse management progress
BHP	Environment Social Governance	Climate targets ahead of CTAP vote, commodity exposure, M&A, Board and Governance, fatalities and link to remuneration, Samarco settlement, Australian government policy

MSCI ESG Ratings*

Portfolio : 2412 WaveStone Aus Share Fund
 Benchmark : 2412 ASX 300 Accumulation Index
 Currency : USD

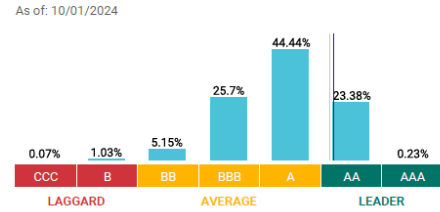
MSCI ESG Ratings



How the MSCI ESG Rating is calculated

	Portfolio	Benchmark
Weighted Avg ESG Score	7.47	7.39
ESG Quality Score	7.47	7.39
ESG Rating	AA	AA

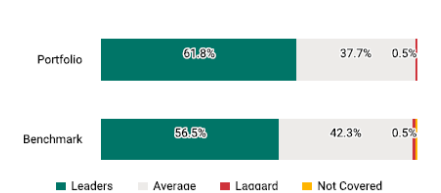
Distribution of MSCI ESG Fund Ratings Universe



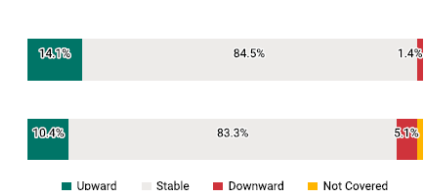
Portfolio ESG Rating Summary

ESG Quality	Leaders 1.15% above benchmark
ESG Ratings Distribution	Leaders 5.30% over benchmark Laggards 0.15% under benchmark
ESG Ratings Momentum	Upward momentum 3.75% over benchmark Downward momentum 3.69% under benchmark

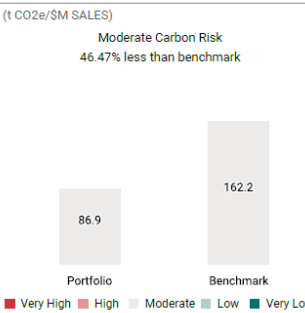
ESG Ratings Distribution



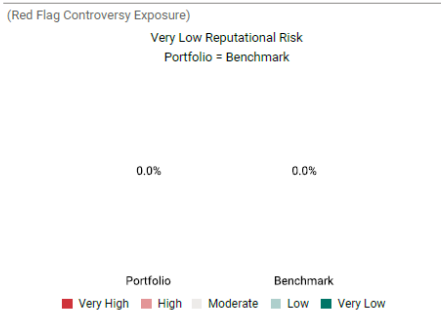
ESG Ratings Momentum



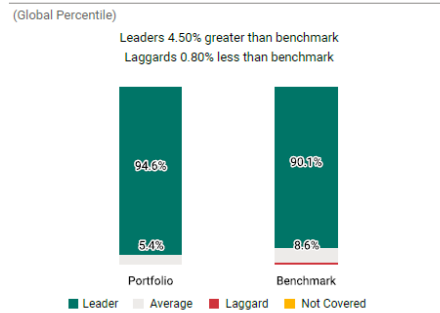
Carbon Risk



Reputational Risk



Governance Risk



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Memberships and initiatives

- Principles of Responsible Investment (PRI)
- Climate Action 100+
- 40:40 Vision

Links to WaveStone Policies

- ESG Policy: **WaveStone ESG Policy**
- ESG Activity Report: **WaveStone ESG Activity Reports**
- Proxy Voting Policy: **WaveStone Proxy Voting Policy**
- Proxy Voting Records: **WaveStone Proxy Voting Records**
- Engagement Policy: **WaveStone Engagement Policy**
- **WaveStone PRI Transparency Report 2023**
- **WaveStone PRI Assessment Report 2023**

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