

# Conflict risk: an engagement update

In recent years, we have seen increasing global attention on geopolitical risk. As a result, we have been engaging our investee companies with ties to Conflict-Affected High-Risk Areas (CAHRAs).

As outlined in our previous conflict risk pieces on [Myanmar](#) and [Russia's war on Ukraine](#), we focus on how they are mapping their operations and supply chains, conducting human rights due diligence and ensuring they are upholding the UN Guiding Principles on Business and Human Rights. While we note that the following countries are not the only ones impacted by ongoing geopolitical conflict, we focus on the areas where we have the most exposure and, thus, the greatest investor impact.

## Myanmar

1 February 2023 marked the second year of Myanmar's coup, and the situation has continued to deteriorate, with increased acts of violence in violation of international human rights law. This includes increased military censorship and surveillance,

which undermines access and freedom of information and expression. Since the coup, we have engaged with nine companies with operations in Myanmar.

### KDDI

**KDDI** is one of Japan's leading telecommunications companies. It has been working in Myanmar with **Myanma Posts and Telecommunications (MPT)**, a local telecommunications company supporting its telecommunications services in the country. Given the complexity and gravity of the issues of internet shutdowns and intercept surveillance, we escalated dialogue to senior executives. Through the engagement, we learned that **MPT** runs the day-to-day operations, resulting in **KDDI** having limited power to influence change. **KDDI** can only request that **MPT** uphold human rights principles, but ultimately the decisions



are made by **MPT**. Although the company was open to dialogue, we were not assured that its operational structure in Myanmar provided it with sufficient leverage to avoid complicity in human rights abuses. As a result, we divested from **KDDI** in the responsible fund.

### Daiwa House Industry Co Ltd

**Daiwa House** is Japan's largest homebuilder. Its subsidiary, **Fujita Corporate**, has exposure to Myanmar through a joint real estate development project also known as the Y Complex project. The company was scrutinised as the land lease payments allegedly became a source of funding for the Myanmar military. The company has reiterated that it had made no rent payments to the military since 1 February 2021. Following our initial outreach, the company promptly responded to our additional information requests on upholding human rights standards. However, it remains unclear whether the company has conducted human rights due diligence.

### Sudan

It has been over a year since the military coup in Sudan and there have been recent positive developments, with the UN welcoming the talks between Sudanese political parties aiming to reach an agreement to form a civilian government. Given

**MTN Group's** role as a leading telecommunications provider in Africa, with a subsidiary in Sudan, we reached out to the company to understand its approach to the conflict.

### MTN Group

The company faced scrutiny in previous years for blocking access to the internet and fixed line services. Since then, we have seen good progress. The company joined the Global Network Initiative, published transparency reports and improved its ranking position in the Ranking Digital Rights Benchmark. We reached out to **MTN Group** to better understand its approach to heightened human rights due diligence, its proactive approach for monitoring new conflicts and escalation, and how the company upholds its human rights principles amid pressures from the military to shut down internet impacting users' freedom of expression.

### Russia & Ukraine

#### Updated: Industry impacts and angles of engagement

There are engagement-specific angles to certain industries with elevated exposure to the war in Ukraine, as well as to the sanctions against Russian companies and individuals. The following sets out examples of these specific impacts as well as engagement perspectives.

Impact (Situation evolved)	Company example
<b>Agriculture</b>	
<ul style="list-style-type: none"> <li>■ Agriculture production and exports continue to be significantly impacted by the war due to route disruption, leading to increased logistic costs.</li> <li>■ Fertiliser prices have been skyrocketing as the price of natural gas, a key input to fertiliser production, is also soaring.</li> <li>■ All of this impacts food security, especially in lower-income countries that depend on exports from Russia and Ukraine.</li> </ul>	<ul style="list-style-type: none"> <li>■ Given the importance of food security as a basic human right, agriculture companies continue to operate essential food facilities in Russia.</li> <li>■ Other agriculture companies in Ukraine are experiencing logistical disruptions to supply routes. Production facilities are running at lower utilisation rates as companies are unable to export goods.</li> </ul>

## Hotels

- Western-based hotel chains have suspended and withdrawn potential new developments or investments in Russia. Others have also closed their corporate offices in Russia.
- Companies have prioritised the safety of workers, including providing pay to impacted team members in Russia.
- The companies we spoke to state that many of their hotels are operated by third parties, where the franchise and management agreements are often lengthy and complex. Companies are currently evaluating their contracts but it is not clear to what end.

## Consumer staples

- Of the sectors in the S&P 500, consumer staple companies have the most exposure to Russia.
- In direct operations, companies are prioritising the safety of workers in Ukraine and Russia. Those with supply chains in Russia are working to mitigate further exposure to the region.
- Many consumer goods and retail companies are suspending, winding down or exiting operations in Russia.
- Companies that have staff in the country continue to support staff through the provision of pay.
- Some supermarkets are also removing products that are sourced from Russia. Other fashion retailers are stopping the delivery of goods to the country.

## Energy

- Since the invasion of Ukraine, we have seen a “trilemma” between energy security, energy equity, and energy sustainability.
- Many countries, including the EU, the UK and the US, now have various sanctions and price caps to restrict the import of Russian oil and gas. While the EU has not agreed on a ban of Russian gas due to its dependence, and, thus, rippling effects on already soaring energy prices, it has new policies to move away from reliance.
- Energy companies have announced significant profits following high oil prices, presenting greater scrutiny regarding these companies’ taxation as people are impacted by the cost-of-living crisis linked to energy bills and fuel.
- While **Equinor** was the first company to completely exit Russia, more recently, energy companies are facing complexities with exits. **Shell** experienced a write-down from the sale of its Russian oil project and, alongside **BP**, these companies are awaiting approval of their sale from Russian authorities.
- To ensure energy companies continue with their decarbonisation efforts, we continued our engagement with major energy companies like **Shell**, **BP**, and **ExxonMobil** on their climate strategy roadmap to ensure they do not lose sight of the energy transition.

## Semiconductors

- Despite sanction efforts targeting semiconductors, Western semiconductor chips have been found in Russian military equipment, including missiles.
- This is due to the dual use of these chips, being used both for military and civilian purposes and the difficulty in sales channels traceability through third party distributors.
- We engaged with five semiconductor companies to understand the companies’ approach to customer due diligence beyond export control compliance processes.

## Internet platforms

- Internet platforms continue to be a vital source of information and narrative on the ground in Ukraine and disseminating information on the war.
- Russia has banned **Meta**’s platforms, Facebook and Instagram, citing them as carrying out ‘extremist activities’.
- Internet platforms must protect freedom of information while ensuring that users are aware of the spread of disinformation.
- Meta took down networks in Russia for violating its policy on coordinated inauthentic behaviour. These websites impersonated legitimate news organisations amplifying Russian propaganda rhetoric.



### Banks

- Western banks are struggling to exit Russia following a new law introduced by the Russian government requiring their approval for deals by foreign owners.
- Banks are also seeing increased credit, cyber and compliance risk and many have stepped up governance processes with daily crisis committees and support teams.
- In July 2022, **HSBC Group** agreed to sell its Russian stake to Expobank. Following this, we spoke to the company on its approach to managing increased geopolitical tensions. As a result of the conflict risk, the company has altered its portfolio and exited businesses that were deemed as non-core.

### Automobiles

- The impact of the Russia and Ukraine war on the automotive industry has been compounded by the semiconductor shortage.
- Critical components are produced in Ukraine and Russia causing severe delays in production times.
- The effect of sanctions in Russia continues to impact inventories and supply chains, forcing the suspension of automobile manufacturing at facilities outside of Russia.
- Most foreign automotive brands have exited from Russia — only three domestic and 11 Chinese companies remain.<sup>1</sup>
- Other manufacturers impacted by the raw material, component and chip shortages are working on various business continuity strategies such as regionalisation, better supply chain monitoring systems and supply chain diversification.

## Semiconductors under the microscope

After news reports about western semiconductors being found in Russian missiles in the war against Ukraine, we reached out to semiconductor companies to understand their approach to customer due diligence. We understand that these companies manufacture dual-use components

(i.e. components that are available for both civilian and military use), and it can be challenging to monitor components that are deployed and reused after the primary sale. Nonetheless, given the severity of human rights atrocities, we engaged to understand their approach to end-use customer due diligence to ensure that products do not end up in the wrong hands.

Response	Detail
<b>Texas Instruments Inc</b>	
Responded	Following an internal review, the company identified the component found in missiles was an obsolete device manufactured in 1998. The company provided further information on its export control compliance process and mentioned it was working to improve it. The company also mentioned working with distributors to identify red flags and conducts frequent audits of its export control, customers and suppliers.
<b>Analog Devices Inc</b>	
Responded	The company stated that its internal investigations are ongoing. <b>Analog Devices</b> took a strong position on Russia and did not sell to Russia, even on components that were authorised. To ensure compliance, the company conducts audits both on an annual basis.

<sup>1</sup> [bne IntelliNews - Only 11 foreign car brands left in Russia out of 60 before the war](#)

Response	Detail
<b>Infineon Technologies AG</b>	
Responded	The company stated that it implemented proper measures and sanctions against Russia in the Ukraine war which includes technical support. The company states that it complies with laws and has robust export control compliance.
<b>NXP</b>	
Responded	The company reiterated its adherence to all export control controls. The challenge for the company and the whole industry is that the products found in weapons are very old, sold through normal and legitimate distribution channels, and found in civilian products such as washing machines. <b>NXP</b> elaborated on how it strengthened its distribution channel management. It records sales by customer names and product lines daily. The company also audits customers and distributors and educates them on human rights and why they cannot sell to those on trade restriction lists.

## Outlook

Navigating geopolitical uncertainties will be an engagement theme that will continue throughout 2023. Companies are increasingly re-evaluating their global operations and supply chains to minimise business disruptions from possible escalations of conflicts. This rapid rise in global fragmentation will have repercussions

for the worldwide economy. As geopolitical risks intersect with ESG risks, we will continue to build on our engagement with investee companies to understand how they are actively assessing and mitigating the impacts of the conflict on their own operations and supply chains, but also their part in the conflict.

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