T. ROWE PRICE FUNDS SICAV

# US Smaller Companies Equity Fund – ESG Report

## Providing transparency on Environment, Social and Governance aspects of the Fund

*As at 31 December 2023*

## ESG INTEGRATION APPROACH

- The US Smaller Companies Equity Fund uses ESG integration as part of its investment process. This means incorporating environmental, social and governance factors to enhance investment decisions. Our philosophy is that ESG factors are a component of the investment decision—meaning that they are not the sole driver of an investment decision, nor are they considered separately from more traditional analysis.
- The process of ESG integration takes place on two levels: first, with our research analysts as they incorporate ESG factors into company valuations and ratings, and second, with the portfolio manager as he balances these ESG factor exposures at the portfolio level. Both the analysts and the portfolio manager are able to leverage dedicated, in-house resources to assist in analyzing ESG criteria.
- Our ESG specialist teams provide investment research on ESG issues at the company level and on thematic topics. Additionally, they have built tools to help proactively and systematically analyze the environmental, social, and governance factors that could impact our investments. The foundation of the analysis is a proprietary flagging tool called the Responsible Investing Indicator Model (RIIM). It covers around 6,500 companies and pulls from data sets that are not in the wheelhouse of traditional financial analysis. These data sets include:
  - ESG performance data (e.g., number of accidents, carbon emissions, strength of whistle-blower programs, etc.);
  - ESG targets (e.g., plans to reduce carbon emissions, increase diversity, etc.)
  - ESG incidents and controversies (e.g., environmental fines paid, local community controversies/protests against a company, etc.)
- Our investment process seeks to strike an appropriate balance between risk and return, and we approach ESG considerations in the same manner, considering both financial and non-financial risks. The fund's portfolio manager works collaboratively with investment analysts and with our internal ESG resources to develop an understanding of the key ESG considerations, and to weigh their significance against other aspects of the investment opportunity. The relative importance and impact of ESG factors will vary from company to company, similar to many investment considerations in our bottom up approach.
- The fund is classified as Article 8 according to the Sustainable Finance Disclosure Regulation. Although the fund does not have sustainable investment as an objective, the promotion of environmental and social characteristics is achieved through the fund's commitment to maintain at least 10% of the value of its portfolio invested in Sustainable Investments. The fund avoids issuers whose activities we may consider harmful to the environment and/or society through the application of our proprietary screen, the T. Rowe Price Responsible Exclusion List.

**INVESTMENT OBJECTIVE:** To increase the value of its shares, over the long term, through growth in the value of its investments.

**INVESTMENT PROCESS:** The fund is actively managed and invests mainly in a widely diversified portfolio of shares from smaller capitalisation companies in the United States. Although the fund does not have sustainable investment as an objective, the promotion of environmental and/or social characteristics is achieved through the fund's commitment to maintain at least 10% of the value of its portfolio invested in sustainable investments, as defined by the SFDR. In addition to the E/S characteristics promoted, the fund also applies the investment manager's proprietary responsible screen (the T. Rowe Price Responsible Exclusion List). The fund may use derivatives for hedging and efficient portfolio management. For full investment objective and policy details refer to the prospectus. The manager is not constrained by the fund's benchmark, which is used for performance comparison purposes only.

## RECENT COMPANY ENGAGEMENTS

We maintain a regular dialogue with the management teams of companies represented across the portfolio. Our investment-driven engagement program frequently identifies targets through our proprietary RIIM analysis, governance screening and analysts' fundamental research. While we engage with companies in a variety of different contexts, ESG engagement focuses on learning about, encouraging or exchanging perspectives on the environmental practices, corporate governance or social issues affecting their business.

While most of the meetings we hold with company managements will include some discussion of ESG topics, we differentiate meetings held with a heavy focus on ESG, meaning ESG issues were the sole items on the agenda or made up a meaningful part of the meeting. Agenda items are classified as "meaningful" when they take up a significant portion of the meeting or are a significant factor in the investment case.

The following are selected examples of recent engagements with companies held in or considered for the portfolio. The examples are not meant to be representative of every engagement held, but to illustrate the types of ESG engagements we are having with the managements of our investment companies.

## Chesapeake Energy (4th Quarter 2023 Engagement)

| | |
|---|---|
| **Focus** | Environmental |
| **Company Description** | Chesapeake Energy Corporation is an energy provider headquartered in Oklahoma City. |
| **Engagement Objective** | We engaged with the company to better understand its emissions reduction progress and strategy as part of T. Rowe Price's commitment to the Net Zero Asset Managers initiative. |
| **Participants** | From Chesapeake Energy: Chief Operating Officer; Investor Relations<br><br>From T. Rowe Price: ESG Associate Analyst |
| **Engagement Outcome** | Our objective in engaging with Chesapeake Energy was to better understand its emissions reduction progress and strategy as part of T. Rowe Price's own Net Zero Asset Managers initiative commitment.<br><br>Chesapeake Energy committed to net zero Scope 1 and 2 by 2035, and it has achieved a 40% reduction in Scope 1 and 2 emissions over the past four years.[1] Scope 3 emissions, which account for 98% of total emissions, are the only kind that are increasing and not covered by the target.[1]<br><br>Toward the goal of emissions reduction, Chesapeake Energy replaced gas-driven pneumatic valves, which is the undertaking that has most significantly reduced its emissions, particularly for methane, and doing this accounted for approximately 85% of progress, or 750,000 tons of carbon dioxide abatement. The company's next phase toward emissions reduction will focus on carbon capture from gas-driven compression and looking at alternative means for power compressors.<br><br>Another focus area for developing technology is detecting and quantifying emissions. About 70% to 75% of Chesapeake Energy's production is continuously monitored. Installing monitoring devices costs from USD 10,000 to USD 30,000 per location in addition to the cost of monitoring and managing the data. However, the company's centralized command center is advantageous as it was an early adopter of real-time location monitoring. Chesapeake Energy is concerned with the Environmental Protection Agency's methane rule, however, in connection with how rapidly the technology for emissions monitoring evolves.<br><br>Chesapeake Energy expects its consolidated emissions intensity to be better than it is as a standalone if it ever completes any acquisitions or that it would have a clear path to improve the emissions of any acquired assets. To this point, the company highlighted Vine and Chief as examples of companies doing a good job managing emissions, with Chesapeake Energy improving emissions through pneumatic releases over the past 18 months.<br><br>Chesapeake Energy also recently formed its Energy Ventures Team to screen opportunities that support the company's net zero ambition. Some of the team's projects include momentum midstream pipeline and carbon capture and storage and a partnership with Eavor Technologies that consists of providing technical expertise on subsurface operations and drilling geothermal wells. The company also shared with us that 100% of its natural gas is certified as Responsibly Sourced Gas, which Chesapeake views as recognition for the level at which it was already operating.<br><br>Our engagement with Chesapeake Energy informed our research. While Chesapeake Energy's Scope 3 emissions and primary business of producing hydrocarbons likely precludes it from fully achieving net zero status, we believe it operates with best practices. |

[1] Scope 1: direct emissions from owned or controlled sources; scope 2: indirect emissions from the generation of purchased electricity, steam, or cooling; scope 3: all other indirect emissions.

## Avery Dennison (4th Quarter 2023 Engagement)

| | |
|---|---|
| **Focus** | Environmental, Governance |
| **Company Description** | Avery Dennison is a materials science company that designs and manufactures labeling and functional materials. |
| **Engagement Objective** | We engaged with Avery Dennison as part of our recurring ESG outreach to get updates on progress and performance. |
| **Participants** | From Avery Dennison: VP Associate General Counsel; VP Innovation & Product Line Manager; VP Financial Planning & Analysis; Lead Director<br><br>From T. Rowe Price: Analyst; ESG Associate Analyst |
| **Engagement Outcome** | The purpose of our engagement with Avery Dennison was to learn about the company's ESG targets and its progress toward them.<br><br>Avery Dennison is working on reaching 70% revenue from sustainability-driven products by 2025, and this will be the company's focus for the next one to two years along with addressing Scope 3 emissions.[1] Addressing Scope 3 emissions will involve the company making progress on methodology and supplier engagement and decarbonizing the supply chain.<br><br>While it does not yet have a target, Avery Dennison is in the early stages of developing a net zero plan, and it plans on focusing on eliminating Scope 1–3 emissions before evaluating other options to achieve net zero, such as through using technology, carbon capture, Power Purchase Agreements, and offsets.[1]<br><br>We discussed sites with alleged soil or groundwater contamination and noted that these investigations include a variety of circumstances and locations, such as one recently settled in Los Angeles that involved thousands of companies dumping waste.<br><br>Part of Avery Dennison's 2030 product sustainability goal is to ensure its products and services quantifiably and demonstrably enable circularity. Some of its related goals include solving problems for industries served, such as reducing food and retail waste.<br><br>Avery Dennison is working on quantifying its impact as it knows anecdotally that its digital labels have helped to reduce waste across the apparel supply chain, for example, so defining and measuring such impact will help its customers achieve their sustainability goals. As such, the company is working on impact around specific use cases in terms of dollars, carbon avoided, and water/waste reduced. Avery Dennison views food waste reduction as a significant area of opportunity with 40% of all foods ending up in landfills.<br><br>The company also spoke to us regarding a few recent and future refreshes within the Board of Directors. In September, Deon Stander took over as chief executive officer from Mitch Butier, who is remaining with the company as chair. Stander has continued with the company's previous strategy that includes being a leader in ESG.<br><br>Avery Dennison's compensation at the executive level includes an ESG component that differs based on the role, and this incentive uses qualitative assessments that are considered annually in light of nonlinear progress on long-term goals.<br><br>This engagement with Avery Dennison has informed our research and demonstrated the company's progress on reducing its environmental footprint and lean toward its strong circular economy. We support Avery Dennison's focus on quantifying impact measurements, and we recommended improving disclosure for the ESG component of compensation with possible consideration for the implementation of standards from the International Sustainability Standards Board. |

[1] Scope 1: direct emissions from owned or controlled sources; scope 2: indirect emissions from the generation of purchased electricity, steam, or cooling; scope 3: all other indirect emissions.

## ESG RIIM PROFILE

The T. Rowe Price Responsible Investing Indicator Model (RIIM) rates companies, governments and securitized assets in a traffic light system measuring their environmental, social, and governance profile and flagging issuers with elevated risks. For certain types of investments, including, but not limited to, cash, currency positions, and particular types of derivatives, an ESG analysis may not be relevant or possible due to a lack of data. Where ESG considerations are integrated into the investment research process, we may conclude that other attributes of an investment outweigh ESG considerations when making investment decisions.

| | Portfolio | | Benchmark | |
|---|---|---|---|---|
| | No. of securities | % weight | No. of securities | % weight |
| Green | 105 | 62.9 | 2,089 | 82.3 |
| Orange | 66 | 35.6 | 335 | 16.8 |
| Red | 1 | 0.1 | 26 | 0.6 |
| Not in scope | 2 | 0.3 | 17 | 0.4 |
| Not covered | 0 | 0.0 | 0 | 0.0 |
| Cash | 1 | 1.1 | 0 | 0.0 |
| **Total** | **175** | **100.0** | **2,467** | **100.0** |

● No/few Flags ■ Medium Flags ▲ High Flags

The comparator benchmark of the Fund is the Russell 2500 Net 30% Index. The manager is not constrained by the fund's benchmark, which is used for performance comparison purposes only.

## SUSTAINABILITY INDICATOR

The fund is classified as Article 8 according to the Sustainable Finance Disclosure Regulations (SFDR).

The sustainability indicator used by the fund is a minimum of 10% of the value of the fund's portfolio held in securities that the investment manager identifies as sustainable investments.

The percentage exposure of the fund to sustainable investments is:

| | Target Minimum Exposure % | Fund Exposure % |
|---|---|---|
| Sustainable Investments | 10.0% | 21.7% |
| Environmental Objectives | 0.5% | 4.5% |
| Social Objectives | 0.5% | 17.2% |

**RISKS - The following risks are materially relevant to the fund (refer to prospectus for further details):** Small and mid-cap - Small and mid-size company stock prices can be more volatile than stock prices of larger companies.

**General fund risks - to be read in conjunction with the fund specific risks above.** Equity - Equities can lose value rapidly for a variety of reasons and can remain at low prices indefinitely. ESG and sustainability - ESG and Sustainability risk may result in a material negative impact on the value of an investment and performance of the fund. Geographic concentration - Geographic concentration risk may result in performance being more strongly affected by any social, political, economic, environmental or market conditions affecting those countries or regions in which the fund's assets are concentrated. Investment fund - Investing in funds involves certain risks an investor would not face if investing in markets directly. Management - Management risk may result in potential conflicts of interest relating to the obligations of the investment manager. Market - Market risk may subject the fund to experience losses caused by unexpected changes in a wide variety of factors. Operational - Operational risk may cause losses as a result of incidents caused by people, systems, and/or processes.

## ADDITIONAL DISCLOSURES

## IMPORTANT INFORMATION

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