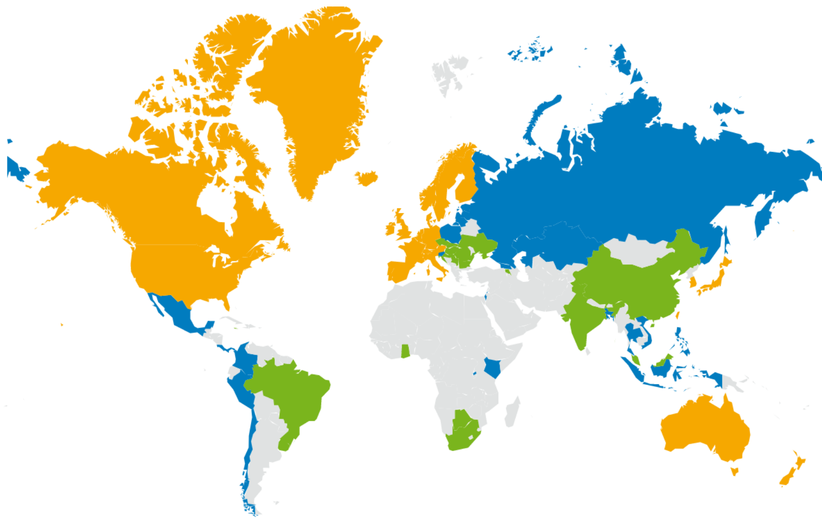
OUR THOUGHTS ON

SHAREHOLDER VALUE CREATION THROUGH CORPORATE GOVERNANCE

THE DUNROSS WAY

2021-11



BREAKOUT NATIONS POSSIBLE BREAKOUT NATIONS OLD WORLD

This is Dunross

Dunross is an independent, global investment company focused on Breakout Nations. At present, Dunross has offices in Cyprus, Luxembourg, United Kingdom and Sweden. Dunross is a dedicated long-term value investor.

EXECUTIVE SUMMARY

THE DUNROSS GUIDE TO SHAREHOLDER VALUE CREATION THROUGH CORPORATE GOVERNANCE

- Open, informative and constructive dialogue with all shareholders.
- Focus on the core businesses.
- Avoid becoming a value trap by focusing on profitability over growth.
- Set appropriate targets for the capital structure.
- Implement and communicate a well-defined dividend policy.
- Never forget to cancel treasury shares.
- Ensure that major transactions are resolved at a shareholder's meeting and not by the board.
- Safeguard shareholders pre-emptive rights in share issues.
- Use existing shareholder base for disposals and spin-offs.
- Independent shareholders should have deciding power on related party transactions.
- Allow minority shareholders to nominate independent directors.
- Introduce transparent and justifiable remuneration policies.
- Disclose all insider shareholdings and transactions.
- Use a transparent voting system at general meetings.

…and last but not least, you're always most welcome to use Dunross as a discussion partner on how to create shareholder value.

OUR THOUGHTS ON SHAREHOLDER VALUE CREATION

Dunross is a long-term value investor in the global equity markets. We focus on finding the best countries to invest in, where we pick companies with a strong franchise, attractive valuation and healthy growth prospects. Given that our holdings are leaders in their respective industries, we, of course, also want them to excel when it comes to shareholder value creation and corporate governance. And, this is where this brochure comes in.

There are many ways to unlock the true value of a company, and one factor often overlooked is through good corporate governance. By applying some very simple principals, it is possible to significantly improve the market's confidence in a company, reduce perceived risks and make the company best in class. In turn, this will lower the cost of capital, make the company more competitive and create more value for all shareholders. This is our guide to Shareholder Value Creation through Corporate Governance – the Dunross way.

Carl-Fredrik Reuterswärd

THE GUIDING AND FUNDAMENTAL PRINCIPLES – ALL SHAREHOLDERS ON THE SAME SIDE OF THE TABLE

For us it is extremely important that the companies we invest in treat all shareholders equally. To demonstrate such a commitment to this principle is very important especially for companies with a dominating shareholder, who might control not only the general meeting, but also the board and management. The reason for this is that the company otherwise may run the risk of being perceived by minority shareholders as managed only for the benefit of the majority shareholder, something that will increase the cost of capital, and decrease company value.

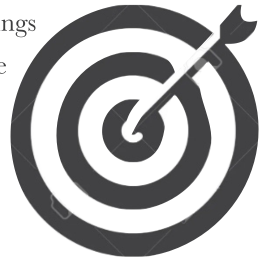
It is important that the companies we invest in treat all shareholders equally

We strongly advocate for dominating shareholders to demonstrate their commitment to create value for all shareholders by taking a few simple but effective measures to align majority and minority shareholders (described in more detail in this booklet), such as: implement a well-defined and constructive dividend policy, give shareholders pre-emptive rights, and let independent shareholders decide on major related party transactions.

FOCUS ON CORE BUSINESS

A company should solely focus on its core businesses, since a strict focus will be rewarded by the market and the company's shareholders. If, however, an amendment to the business-focus is justified, this should be subject to approval at a shareholders' general meeting. Naturally, we also discourage all types of non-core investments and crossholdings that could be viewed as part of a "power strategy".

A company should solely focus on its core business



TRANSPARENCY IS KEY

Misunderstandings are the cause of many troubles, and to avoid these, we encourage companies to be transparent about everything that can be of interest to investors. Even if something is completely clear to the company internally, it might not be so for external investors, so we advocate that companies always explain the background and rationale behind all decisions and suggestions to investors beforehand. This is especially important regarding significant changes such as acquisitions, nomination of new directors, or a proposed mandate to issue new shares. A transparent company will command a lower risk premium and thus have a lower cost of capital, creating more value in the long-term.

There are many ways to accomplish and communicate a company's strategy and goals, for example through quarterly reports, annual reports, press releases, the website etc. One very effective way in our experience, is to arrange regular capital markets days, to which a broad set of people can be invited, such as shareholders, institutional investors and analysts.

We encourage companies to be transparent about everything that can be of interest to investors

DO NOT BECOME A VALUE TRAP

No company ever sets out to become a value trap, i.e. one which over time requires more capital from shareholders than what is returned as dividends, share buybacks and value appreciation. But some companies do end up as value traps anyway. Why? We believe this often has to do with misaligned targets and incentives. For example, if the company has aggressive growth ambitions without adequate profit requirements, and management is incentivized based on such growth, the outcome will inevitably be that revenue and assets will increase but shareholder returns will suffer.

A value trap, is one which over time requires more capital from shareholders than what is returned as dividends and/or share buybacks

In order to avoid becoming a value trap, a company should have a strict adherence to profitable growth, because "growth for growth's sake is the ideology of the cancer cell". As such, we discourage all growth targets and endeavours to increase market share etc. if they are not combined with sustained or increased profitability. Exactly how a company balances growth vs. profitability also becomes a valuable tool in discerning whether the company is actually managed with the sole intention of creating value for all shareholders, or for some other conflicting interests, e.g. as a power base for management, "ego-enhancer" or as an extension of the government.

Growth that in the short run only creates a need for new equity must convincingly be demonstrated as a more profitable strategy in the long run than otherwise, or else it will be regarded by the market as a value trap, resulting in a higher cost of capital.

HAVE AN EFFICIENT CAPITAL STRUCTURE

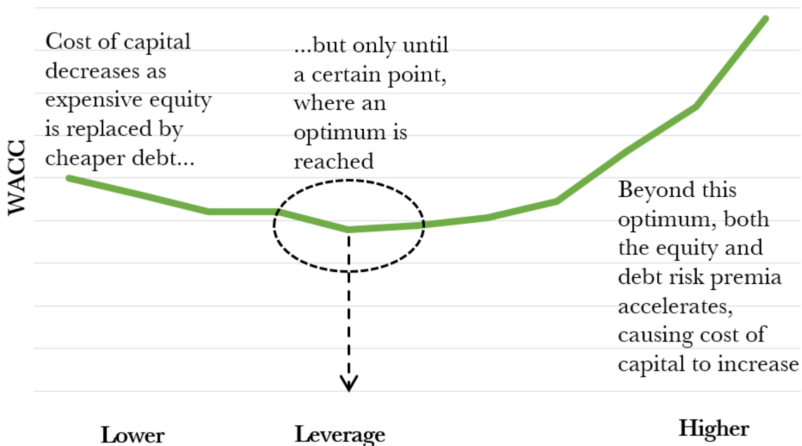
One of the most fundamental corporate governance measures a company should implement is to decide on an appropriate capital structure that sets the framework for the company's total cost of capital, with the objective to minimize both cost of equity and cost of debt.

We don't encourage companies to over-leverage, but rather to take on an optimal amount of debt depending on the business. For example, capital-intensive businesses with high earnings visibility such as infrastructure or real estate generating recurring income, should have a higher amount of debt, whereas highly cyclical companies or those with very lumpy revenue streams should carry less debt.

Examples of other factors that affect the suitable debt level are the interest rate level, the quality of the company's franchise, potentially hidden or overstated values in the balance sheet, as well as political and regulatory risks. The figure below visualizes how a company can minimize the cost of capital (WACC – Weighted

Decide on an appropriate capital structure with the objective to minimize both cost of equity and cost of debt

Weighted average cost of capital



average cost of capital) by optimizing leverage. Note also how the cost of capital accelerates when gearing increases beyond the optimum, something that should be avoided.

From experience, we also know that it's very important that companies set well-founded and sound targets for their capital structure (e.g. debt-to-equity, net debt-to-EBITDA, and/or interest coverage ratio), because the framework affects financing decisions, such as either retaining earnings or distributing dividends. Naturally, these targets also need to be communicated clearly to the market so everyone knows what to expect from the company.

IMPLEMENT A POLICY FOR DIVIDENDS AND SHARE BUYBACKS

A well-defined policy of returning capital to shareholders is one of the most important ways through which a company can communicate financial strength and its commitment to shareholder value creation.

The shareholder remuneration policy should first of all state that all shareholders should be treated equal to the main shareholder. Second, annual dividends should ideally be based on a percentage range of earnings or cash flow, rather than a fixed amount, thereby making shareholders feel that they are part of the company's successes or failures, and not like a bondholder who receives a fixed coupon.

If capital is returned through dividends, dividend payments should be declared together with the record and ex-dividend dates in a timely manner, in order to allow investors to settle any transactions in connection with such payments and eliminate any ambiguity that otherwise may arise.

Share buybacks could be part of the dividend policy and are normally a more cost-effective way to return capital to shareholders compared to cash dividends, since dividend payments almost always

are subject to taxes for shareholders, especially for international investors. Share buybacks are of course only suitable and profitable alternative to dividends if the company's share price is undervalued by the market. However, dividends have an important boundary condition, cancellation, see next paragraph.

In order to increase visibility even further regarding buybacks, the company could, for example, have a policy stating that should its shares trade with a certain discount to its "intrinsic" value (defined in a transparent and credible way), then capital will be returned to shareholders through buybacks rather than dividends.

Dividends should ideally be based on a percentage range of earnings or cash flow, rather than a fixed amount, making shareholders feel that they are part of the company's successes

DON'T FORGET TO CANCEL TREASURY SHARES

If and when a company decides to buy back shares, it is of utmost importance that the acquired shares are cancelled. Otherwise, we don't see buy backs as part of a dividend policy, but as pure speculation. If the company chooses to keep them as treasury shares, investors will not subtract these shares in the denominator when calculating Earnings Per Share (EPS), resulting in an unchanged EPS and no increase in value of the company.

It is of utmost importance that the acquired shares are cancelled

Furthermore, a buy-back program without cancellation of treasury shares will be interpreted as if the company will sell the shares back into the market eventually, thereby creating an overhang that will negatively impact the cost of equity, and the company's value. Or even worse, the treasury shares could be interpreted as a power tool by the management or the controlling shareholder and create suspicions from investors regarding the company's underlying intentions.

Should local regulations for some reason not allow cancellation of treasury shares, or make it practically impossible, the company should not buy back shares at all.

LET SHAREHOLDERS DECIDE ON MAJOR TRANSACTIONS

All major transactions by the company – be it asset disposals, share issues, acquisitions etc. – should be resolved at a general shareholders meeting, where all shareholders can vote (except of course when it comes to related party transactions, where only unrelated shareholders should be allowed to vote). As such, the board of directors should not be given any wide-ranging mandates, such as the right to do share issues or to conduct major transactions, because this will create mistrust from investors.

Major transactions should be resolved at a general meeting

PRE-EMPTIVE RIGHTS

Shareholders should always be entitled to pre-emptive rights, i.e. the right of existing shareholders to have the first right of refusal to subscribe to any new shares issued by the company. To allow existing shareholders the possibility to take part of a share issue is not only fair, but more importantly, will lower investors' perceived risk of being diluted by directed share issues to other parties.

Shareholders should always be entitled to pre-emptive rights

USE EXISTING SHAREHOLDERS FOR DIVESTMENTS

As with share issues, we also believe that the company should apply the same pre-emptive rights principles on disposals and spin-offs. If a company decides to divest a part of its business, the board should always consider the option to either sell the business to the parent company's shareholders by using purchasing rights allocated on a pro rata basis, or to distribute the shares as a special dividend and list the divested business separately.

Creates the possibility for the company to use the shareholder base to get a wider distribution of the shares

In this way, shareholders can decide for themselves if they want to be owners of the divested business or not, and it also creates the possibility for the company to use the shareholder base to get a wider distribution of the shares, thereby ensuring liquidity in the divested business's shares. Remember that the shareholder base is a valuable asset.

BE VERY CAREFUL WITH RELATED PARTY TRANSACTIONS

To the largest extent possible, avoid related party transactions: disposals, acquisitions, loans, guarantees etc., involving shareholders, board members, management or companies related to any of these. If, however, related-party transactions are being pursued anyway, there must be a transparent framework in place which clearly states who can decide on such transactions on the company's behalf and how the terms should be negotiated. In this regard, we advocate that the board should always hire a truly independent expert to assess the fairness of any major related party transaction.

Avoid related party transactions: disposals, acquisitions, loans, guarantees etc.

The connected shareholder should be restricted to vote on related party transactions, so that the decision on the transaction only rests with the independent shareholders.

NOMINATE TRULY INDEPENDENT DIRECTORS

When nominating independent directors, we urge companies to think long and hard about which candidates to propose, because they will be the voice of the minority shareholders on the board. As such, it is not enough for candidates to be classified as independent on paper. For this reason, the board should consider whether they can be viewed as credible and truly independent, because in our view a de facto independent board member will bring more value to the board's work than someone who might fit the bill but in the end just thinks and votes like all the other board members.

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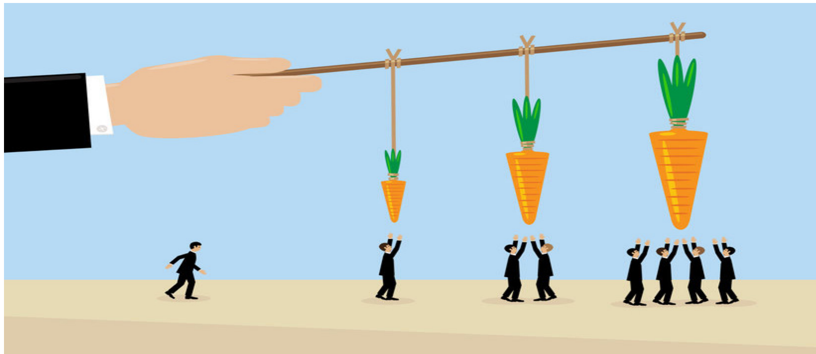
Nomination of independent directors should ideally be approved by the minority shareholders of the company. Alternatively, the minority shareholders should be represented in the nomination committee appointing the independent directors.



SET INCENTIVES THAT GIVE THE RIGHT RESULTS

Directors and management should be satisfactorily rewarded if they do a good job, but not if they don't deliver. To understand what is expected of management, their pay should be tied to the company's financial targets (which of course also need to be clearly communicated), and all remuneration policies must be made available for shareholders. We also advocate that shareholders should vote on remuneration policies at the general meeting with regular intervals.

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The financial targets and bonus criteria must be relatively bold and aggressive, thus making it clear that bonus should only be paid out if the goals are reached, thereby avoiding excessive pay for sub-par performance. By being transparent on pay and setting remuneration – whether being cash, options or shares appropriate lock-up periods – at a long-term performance-based and morally justifiable level, investors will feel increased confidence in the management and the company.

Management and directors should also be encouraged to acquire shares in the company at market price, making their long-term interests more aligned with that of shareholders.

DISCLOSE HOW INSIDERS TRADE

Even if it's not required by stock market regulations, we advocate for companies to keep investors informed about all transactions in a company's share conducted by major shareholders and members of the board and management. Exactly how this should be done (if not regulated) is up to the company, but the important thing is that investors receive transparent and frequent updates on how insiders act.

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USE A TRANSPARENT VOTING SYSTEM AT GENERAL MEETINGS

We encourage companies to use a ballot system at general meetings of shareholders – either in paper or digital – and not conduct voting by show of hands or any other outdated method. By properly counting the number of votes present and the number of votes cast for each agenda item, the company doesn't only ensure a fair decision-making process for shareholders, but also safeguards a very important feedback loop: if the board of a company doesn't know what exact percentage of shareholders support or disapprove of a certain measure, it may continue proposing matters that in fact are quite unpopular but can be misinterpreted as having broad-based support in a show-of-hands situation.

By properly counting the number of votes, the company ensure a fair decision-making process for shareholders, and safeguards feedback

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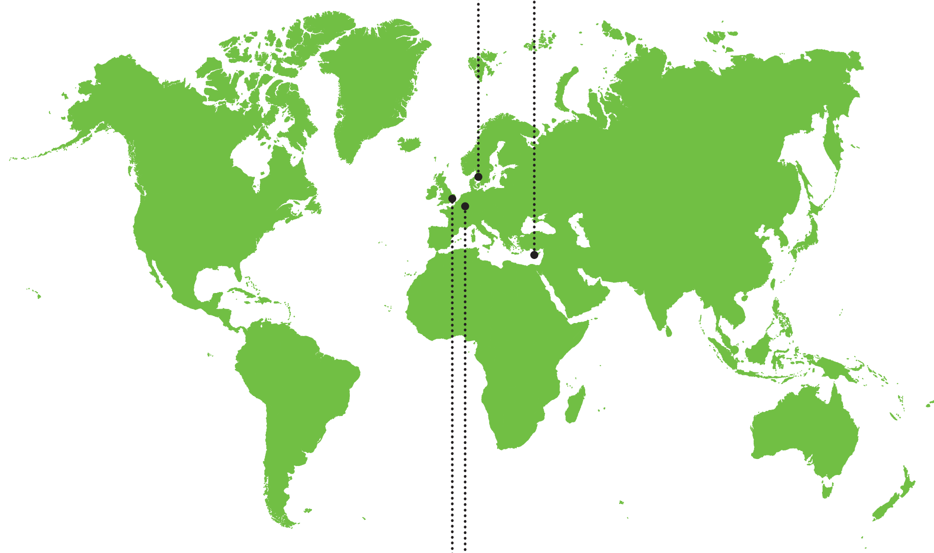

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