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DECATUR ESG IMPACT REPORT

ESG Investment Policy Approach

Recently, I was meeting with an asset owner discussing environmental, social, and governance (ESG) factor integration into the investment processes. The asset owner stated that the current ESG scores are flawed since the scores reflect self reported corporate measures, unaudited, and are incomparable across companies. Also, third party providers of ESG scores have a very low correlation, meaning that firm A may receive a high ESG score by one provider, but a low score in another. Therefore , we do not have a ESG standard to evaluate all firms.

> …. ESG INTEGRATION WITH CLIENT'S OBJECTIVES IS ESSENTIAL

Actually, I agree with this asset owner. As an asset manager, my objective is to select the best stocks for my clients' portfolios that meet the clients' objectives. A particular ESG score may not be materially relative to the company under review if it does not impact the firm's performance in meeting my clients' objectives. Therefore, it is important to define the clients' objective as it relates to ESG integration. We believe that there are three legs to a solid ESG integration stool.

ESG Portfolio Solution

Many asset owners, clients, have identified certain targets that they want reflected in their portfolios. For example, the client wants to maximize performance and wants to reduce carbon intensity of the portfolio compared to a designated benchmark. It is understood that the primary objective is performance, over a market cycle, and a secondary objective is reduction of carbon intensity. Also, this requires that the client and manager define the appropriate ESG factors to include in periodic reports. For example, currently 35% of 2,459 firms in the All Country World Index (ACWI) report total carbon emissions in metric tons. This self reported measure can be scaled by annual or trailing twelve month revenues to provide a carbon intensity measure that can be compared across firms and industries. While this approach still depends on self reporting, as long as the client and manager are aware of the definition and source, this is a workable solution.

ESG Proxy Policy

The voting of proxies in accordance with the clients' objectives is an effective method to hold firms accountable. Also, shareholders' resolution that support, in our example, reduction of carbon emissions, would be in agreement with the client's objective and manager would vote in support. Again, the primary objective is to vote the proxies in a manner that promote long term financial performance.

ESG Firm Engagement

The third leg of the stool is firm engagement. Again, prioritizing the client's objectives, the manager will engage with firms accordingly. As an asset manager, we have found collaboration with other asset owners and managers that are signatories of the Principals of Responsible Investment (PRI) to be very positive. For our example, the initial firm engagements could focus on getting the portfolio companies to report their carbon emissions.

Conclusion

As the ESG integration evolves, we are finding that no one solution will fit every client. Therefore, it is important that both the asset owner and manager understand the purpose of ESG integration and the designated measures.