Sustainable Investing | Fact vs. Myth

CARILLON TOWER ADVISERS

What's in a name?

Sustainable investing, sustainable and responsible investing (SRI), ESG investing, socially responsible investing (also SRI), impact investing, green investing, ethical investing, values-based investing. Although these are different terms, they simply reflect different approaches to the practice of incorporating environmental, social, and governance (ESG) factors into the investment decision-making process. Regardless of the name, it is all about making a difference with your investment dollars.

What is ESG?

Environmental – **S**ocial – **G**overnance – ESG. These three letters seem simple enough on their own, but when you put them together, they potentially can have significant impact on a company's reputation, bottom line, and long-term value.

Active Ownership

A vital aspect of sustainable investing is active ownership. This includes proxy voting and corporate engagement.

Proxy Voting

As shareholders in a company, equity investors have a say in its operations, primarily through proxy voting. Through voting proxies, shareholders have a voice in addressing environmental and/or social concerns such as increasing board diversity, improving transparency, and mitigating the negative impacts of climate change.

Corporate Engagement

Investors can engage with companies on issues of concern, either directly or as part of a pooled engagement effort with other investors. Engagement can take many forms, including calls, letters, and/or e-mails with company management, and depending on the issue, may take several years before results are realized. However, positive change through engagement is possible.

Fixed Income, Too

While much of the focus of sustainable investing has been on equities, the same principles apply to fixed income. In fundamental credit analysis, particularly for corporate bonds, ESG integration is nothing new. What is new, however, is the growing field of green bonds, social bonds, and sustainable bonds. In the field, bond proceeds are used for specific environmental and/or social purposes, e.g., developing a renewable energy project, upgrading a water system, building affordable housing.

Moreover, credit rating agencies such as S&P and Moody's have updated their methodologies to incorporate ESG issues into the rating process. Credit ratings have a material impact on the interest expense for companies and municipalities, and changes in credit ratings can positively or negatively impact total returns for a bond.

Myth

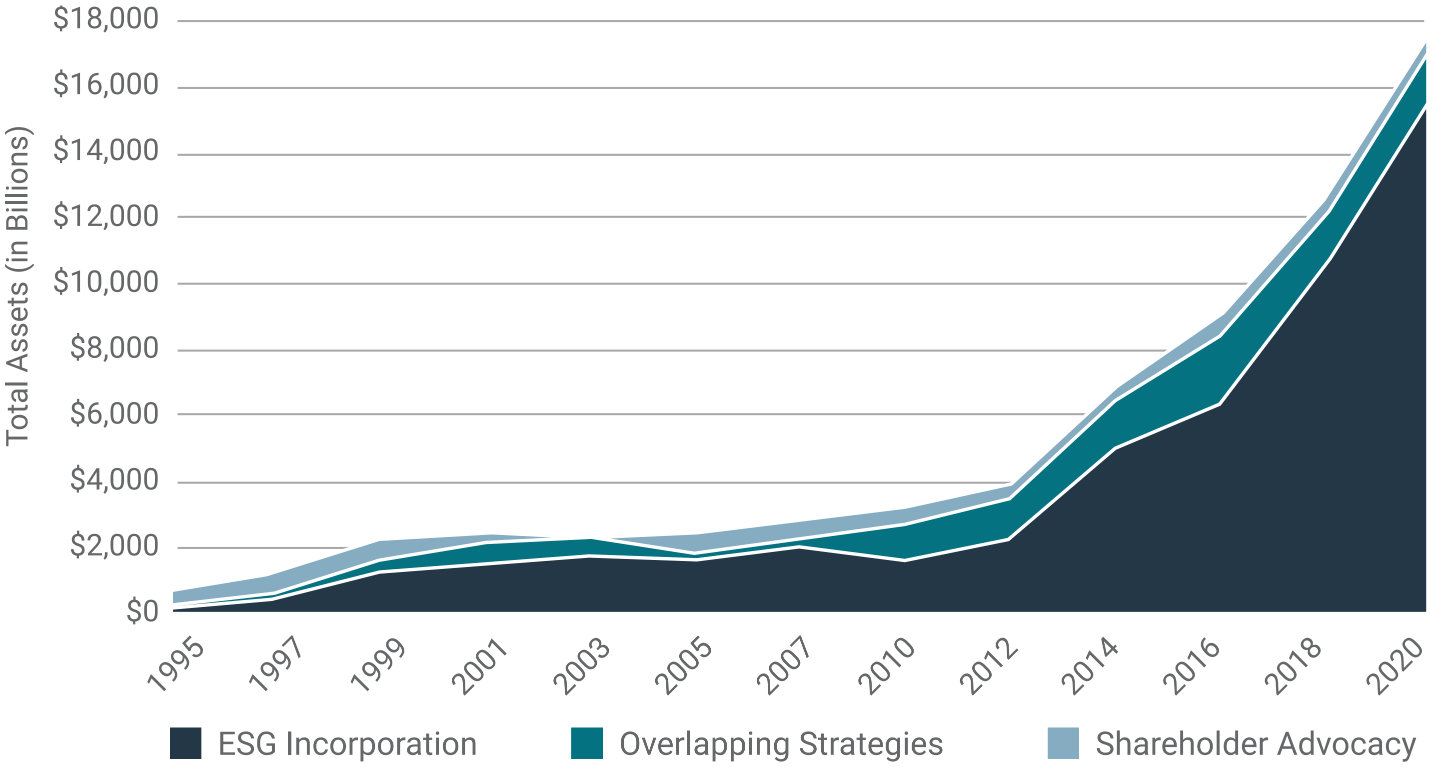
"It's a passing fad."

Actually, this kind of investing has been around for a *long time* – the Quakers avoided investments in enterprises associated with the slave trade. However, in its current form, it has been around since the late 1970s and early '80s.

A growing trend

Incorporating ESG considerations in the investment decision-making process has been gaining significant traction in the U.S., particularly in recent years.

Report on U.S. Sustainable and Impact Investing Trends 2020



Source: US SIF, "Report on US Sustainable, and Impact Investing Trends, 2020"

Myth

"You will sacrifice performance."

Multiple studies, including sweeping meta-studies, have shown that there is a modest correlation between outperformance and corporate sustainability practices. While correlation is not causation, it does make sense when viewed through a risk management lens as well as through the lens of long-term value creation.

Why is it important?

As with any investment discipline, there are both opportunities and risks. Viewing investments through an ESG lens, it is possible to discern risks and opportunities perhaps more clearly.

Risks

Evaluation of ESG factors can be an excellent risk management tool. In general, companies that have effective environmental policies and procedures in place;

- are thoughtful, safe and equitable employers;
- respect human rights; and
- are responsible corporate citizens overall

May be less vulnerable to

- costly accidents,
- litigation and fines, and may be
- less apt to suffer irreparable reputational damage.

Through these efforts, they may also enjoy lower operating costs as well as lower cost of capital.

Opportunities

Beyond the benefits of sound risk management, companies that are providing solutions to address climate change or gender inequality or any one of the 17 UN Sustainable Development Goals (SDGs) along with prudent financial management may be better positioned for growth and long-term value creation. Finally, companies that are responsible corporate citizens are more likely to be considered employers of choice, which can provide a distinct competitive advantage.

More Opportunities

With respect to market demand for sustainable and responsible investment strategies, there appears to be real opportunity. Younger investors, namely Millennials and Gen Z, as well as European investors and U.S. institutional investors, have signaled a preference for investments that have positive social and environmental impact. These are areas of potentially strong future growth.

Myth

“There’s no real discipline behind it.”

When done well, there is a great deal of discipline required, including fundamental analysis, sifting through relevant data, and consistent application of process. There can be a shortage of reliable data for analysis because to date much of this reporting is voluntary in the U.S., but there is progress.

Approaches

Just as there are many terms for sustainable and responsible investing, there are many ways to incorporate ESG factors in the investment process. Here are the approaches most commonly in use:

Incorporation Strategy	Description
Positive Screening/Best-in-Class	Select investments based on positive ESG performance relative to industry peers and avoid investments that do not meet the ESG performance thresholds
Negative/Exclusionary Screening	Exclude investments in sectors or companies operating in business areas deemed to be controversial
ESG Integration	Systematically and explicitly include ESG risks and opportunities into the financial analysis process
Impact Investing	Invest in companies, organizations, or funds with the explicit intention to generate positive social and environmental impact along with financial returns, regardless of whether they are below market
Sustainability Thematic	Construct portfolios thematically around specific ESG areas, such as gender-lens investing, clean technology, sustainable food and agriculture, or renewable energy
Index Based	Construct a portfolio to replicate established indices of ESG companies: Bloomberg SASB US Large Cap ESG Select Total Return Index
Direct Corporate Engagement and Activism	Work directly with corporations to promote adoption of ESG practices

Source: US SIF, “Report on US Sustainable, and Impact Investing Trends, 2018”; Eagle Asset Management research

It is not unusual to find multiple approaches used in combination. For example, ESG integration can be easily incorporated with some element of screening, such as norms-based, exclusionary, or best-in-class.

Myth

“It’s a marketing gimmick.”

As the idea of sustainable and responsible investing gains wider acceptance, it does lead to spin. So this does have some truth because there are those out there touting sustainable investment practices which are nothing more than window dressing. There is actually a term for this: “greenwashing.” Therefore, it is important to find an investment manager who is truly dedicated to sustainable investing principles and can show how they are put in practice.

While myths may exist about what ESG investing really is, more information is becoming available every day to assist investors in understanding these concepts, and help them incorporate sustainable investing principles into their portfolios. You can learn more about how Carillon Tower Advisers and our affiliates approach sustainable investing or how to partner with us at www.carillontower.com.

About Carillon Tower Advisers

Carillon Tower Advisers is a global asset management company that combines the exceptional insight and agility of individual investment teams with the strength and stability of a full-service firm. Together with our partner affiliates — ClariVest Asset Management, Cougar Global Investments, Eagle Asset Management, Reams Asset Management (a division of Scout Investments), and Scout Investments – we offer a range of investment strategies and asset classes, each with a focus on risk-adjusted returns and alpha generation. Carillon Tower believes providing a lineup of institutional-class portfolio managers, spanning a wide range of disciplines and investing vehicles, is the best way to help investors seek their long-term financial goals.

Sustainable Investing at Carillon Tower Advisers

At Carillon Tower Advisers, we believe investor interests are best served by allocating capital to organizations that generate long-term value for all constituents. While each of the Carillon affiliated asset management firms is unique in its investment approach, they all share a commitment to investing for the long-term. Incorporating environmental, social, and governance ("ESG") considerations in investment decisions, consistent with each firm's philosophy and process, is at the heart of the Carillon approach to sustainable investing.

Disclosures / Disclaimers

All investments are subject to risk. Asset allocation and diversification do not ensure a profit or protect against a loss. There is no assurance that any investment strategy will be successful or that any securities transaction, holdings, sectors, or allocations discussed will be profitable.

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Indices are unmanaged, and one cannot invest directly in an index.

Bloomberg SASB US Large Cap ESG Select TR Index is an ESG-weighted index derived from the Bloomberg US Large Cap Index (B500). The Index is optimized to maximize exposure to the ESG score, (R-Factor).

ESG refers to Environmental, Social, and Governance factors used in measuring the sustainability and societal impact of an investment in a company or business. An ESG investment strategy will include only holdings deemed consistent with the applicable ESG guidelines. As a result, the universe of investments available to the strategy will be more limited than strategies not applying such guidelines, which may cause it to perform differently than similar portfolios that do not have such a policy.

Impact investing and/or Environmental, Social and Governance (ESG) managers may take into consideration factors beyond traditional financial information to select securities, which could result in relative investment performance deviating from other strategies or broad market benchmarks, depending on whether such sectors or investments are in or out of favor in the market. Further, ESG strategies may rely on certain values based criteria to eliminate exposures found in similar strategies or broad market benchmarks, which could also result in relative investment performance deviating.

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