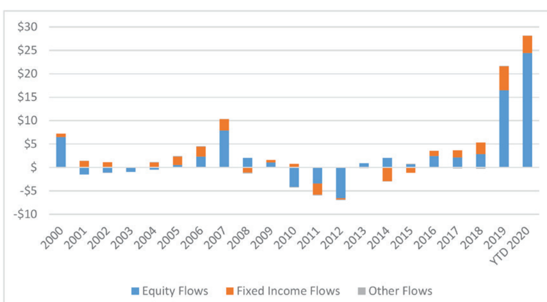
Dividend Growth ESG

Embracing ESG: The Pandemic Amplifies the Value In ESG Investing

Despite the market-cap weighted S&P 500 index setting an all-time high during 3Q2020, the performance of the average stock suggests a more divided economic recovery. A number of companies, most notably bellwether technology firms, appear to be managing the impact of COVID-19 with minimal financial strain. In fact, some companies find themselves uniquely positioned to benefit from the virus' impact. However, various economic data points and anecdotal evidence suggest the economic strain remains severe for the majority of global companies. In these difficult times, companies can be pressured to make business decisions impacting various stakeholders in vastly different, and often conflicting, ways. In an effort to maximize near-term profitability or maintain solvency, companies may execute cost cutting strategies that frequently result in headcount and/or employee benefit reductions. This has been the case in 2020 as 20 million individuals remain unemployed due to the economic disruption caused by COVID-19. **For Environmental, Social and Governance (ESG) funds, including Bahl & Gaynor's Dividend Growth ESG strategy, investments should be selected not only for their profit-maximization potential, but also for the way in which they conduct business according to ESG core values.**

Figure 1: U.S. Sustainable Flows ($bn) - By Asset Class



Source : Morningstar Direct, Deutsche Bank
Note: YTD thru Aug 2020

In traditional business environments, poor treatment of stakeholders may take years to materialize in the form of financial impact. However, as a result of COVID-19, companies that have prioritized human and social capital management enjoyed more rapid and tangible benefits from these socially motivated investments. For example, companies which invested in its technological infrastructure and embraced workforce flexibility find themselves more resilient and productive throughout global shutdowns than their peers. Beyond workforce flexibility, Bahl & Gaynor has observed many companies' steadfast commitment to other key "Social" issues. Despite needing to shut its doors and operate a curbside-only operating model, Best Buy (BBY) maintained its commitment to employees with a recently elevated pay structure featuring a $15 minimum hourly wage and enhanced benefits. BBY also prioritized community investments with its commitment to create 100+ Teen Tech Centers focused on bridging the opportunity gap for teens in underinvested communities and signing on as a founding member of the ParityPledge in support of people of color. We believe actions such as these increase long-term shareholder value through enhanced brand equity, improved customer loyalty and higher workforce productivity.

Socially influenced business decisions are welcomed not only by their direct beneficiaries, but also by a growing base of ESG-motivated investors. **In a recent report, Deutsche Bank noted that despite the significant COVID-related drawdown of the S&P 500 earlier this year, flows into ESG-oriented funds remained robust (See Figure 1). Further, Bahl & Gaynor notes an increasing demand for "social bonds" and "sustainability bonds" in the global market-place. In fact, aggregate ESG-labeled bonds issued in September doubled the previous record set earlier this year.** These debt instruments provide a unique method for companies to raise funds to target specific ESG-related projects. During 3Q2020, Bank of America (BAC) issued a $2B sustainability bond designed to advance racial equality, economic opportunity and environmental sustainability. This was the first bond issued by a US bank dedicated to financial empowerment of people of color as well as BAC's eighth ESG-themed bond. Similarly, Verizon (VZ) issued its second $1B bond explicitly focused on carbon neutrality by 2035 while Visa (V) also issued its inaugural green bond intended to advance environmental and payment ecosystem sustainability.

While the focus during 3Q2020 has primarily centered upon social factors, there was no shortage of excitement surrounding renewable and alternative energy sources, including the viability and application of "green hydrogen."

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Currently, hydrogen is a common source of energy almost entirely generated from steam reforming of fossil fuels feedstock. However, significant investment in recent years has focused on creating equipment and procedures to enable the cleaner production of hydrogen via renewable powered sources. **During 3Q2020, Air Products (APD) announced its involvement in the largest project of its kind focused on enabling the efficient production and delivery of carbon-free hydrogen energy for broad consumption.** This investment could represent a significant step toward the future of clean energy. APD has further illustrated its expertise in the area through its recent decision to join the European Clean Hydrogen Alliance (ECH2A) in the EU. While many pure-play investments in this potentially revolutionary technology come with significant risks conflicting with B&G's core approach, APD represents a high-quality avenue to gain exposure to a significant area of renewable energy focus.

During 3Q2020, Bahl & Gaynor initiated the following positions in the Dividend Growth ESG portfolio:

Alexandria Real Estate Equities (ARE)

ARE is an urban office REIT focusing on high-quality life science and technology properties which generally demonstrate resiliency during periods of consumer demand shock. The company exhibits strong environmental awareness with 48% of annual revenues coming from LEEDS recognized projects and robust water, carbon, and energy reduction efforts. Additionally, ARE significantly impacts the communities where it invests through supporting various rehabilitation centers, as well as community service and engagement efforts.

Crown Castle International (CCI)

CCI is a REIT that operates and leases domestic wireless tower and fiber infrastructure to carrier companies. The company's recently announced board structure focused on tenure and diversity should result in better overall company governance. CCI has a "Connected by Good" program which serves as the overarching social impact initiative, including volunteerism, philanthropy, and three sub-initiatives: improving public spaces, creating safer communities, and advancing access to education & technology.

Qualcomm (QCOM)

QCOM is a leading developer and provider of digital communication technology, most notably chipsets primarily used in 3G/4G/5G cellular networks. The company recently heightened its strategic focus on its long-term ESG vision while more clearly documenting and disseminating its progress toward these goals. These goals exist in four key areas: Purposeful Innovation, STEM Education, Responsible Business and People. QCOM has been recognized for its diversity and talent retention efforts as well as security management initiatives.

Zoetis (ZTS)

ZTS is a leader in animal safety and wellbeing, providing products to protect animals from disease and illness. Animal health and safety is a fast-growing area within healthcare as a result of increased companion animal ownership and higher protein consumption. To ensure ethical testing of its products, the company commits itself to principles known as the "3R's of animal research": **Replacement** of animal testing with simulations and models when possible; **Reduction** of the number of animals used in studies where animals must be used; and **Refinement** of procedures involving animals.

Despite the ongoing economic and social challenges presented by COVID-19, the current environment highlights the relevance of ESG investment efforts and the impact in supporting faster and more equitable recovery from this unique societal challenge.

Please contact your Bahl & Gaynor Portfolio Manager if you are interested in learning more about our Dividend Growth ESG strategy.