Dividend Growth ESG

Leadership Changes in Washington Bolster ESG Momentum

Following the transition of power in Washington D.C., the Biden Administration facilitated the passage of the American Rescue Plan Act of 2021. With a wide variety of benefits and provisions, the administration touted the roughly $1.9T stimulus package as a plan aimed at fighting the COVID-19 pandemic through testing and vaccination programs, delivering immediate relief to families and supporting communities and small businesses struggling in the wake of the pandemic. Related to the increasing fiscal and ongoing monetary support, inflationary concerns are mounting among investors causing an upward shift in long term interest rates. Despite this concern, the S&P 500 managed to edge +6.18% higher during the quarter as nationwide COVID-19 cases continue to decline amid vaccine administration. In an effort to convey the more qualitative nature of the Dividend Growth ESG's primary objective, ESG integration, below we highlight noteworthy market developments and updates across a range of portfolio holdings. It is important to note that this review is not a recommendation to buy or sell, but rather an inventory of examples that illustrate the focus on ESG issues the strategy seeks to emphasize.

> Merger and acquisition activity has rapidly accelerated through year-end into 1Q21. This represents a unique opportunity for management to evaluate company performance and to carry forward ESG principles.

Despite various calls for climate change progress and environmental initiatives, the American Rescue Plan Act primarily focused on delivering immediate relief of pandemic-related challenges. While the bill did not include extensive environmental provisions, the Biden Administration continues to advocate for an infrastructure plan which is expected to include spending and provisions aimed at combating climate change through net carbon emission reduction. Surprisingly, the American Petroleum Institute (API) – the largest U.S. trade association for the oil and natural gas industry – endorsed some form of a price on carbon emissions. Having historically opposed such a policy, the shift in the API's stance seems to encapsulate a broader shift in sentiment. While the structure of a carbon pricing system is far from finalized, the endorsement removes a key hurdle in establishing mechanisms to more effectively regulate emissions and potentially transform the economy's approach toward addressing climate change.

While lofty goals and targets have been established regarding climate change, including emission reductions and "net-zero" targets, a significant hurdle in the transition to clean energy was highlighted in Texas by Winter Storm Uri. During the extreme weather, power generation, grid reliability and grid management (i.e. ERCOT) issues occurred across Texas, resulting in energy blackouts and extreme pricing. Although issues also occurred across renewable energy systems, the natural gas system failure played a significant role in the crisis given the heightened reliance on this infrastructure during colder winter months. This was exaggerated by failures and inefficiencies associated with Texas' deregulated, independent grid. Although analysis is still ongoing, the natural gas failure has been largely attributed to underinvestment in grid modernization, storm hardening, and natural gas pipeline replacements and upgrades.

Winter Storm Uri underscored an important reality to be considered in the ongoing and accelerating transition to clean energy: it cannot occur overnight. Meanwhile, significant investments in infrastructure and resiliency cannot be neglected. With a focus on maintaining reliability and affordability, technological limitations inhibit the ability to transition too rapidly. Further, this process can be effectively managed through a regulatory construct in which Bahl & Gaynor continues to find attractive dividend growth investment opportunities. We recognize the vital role the Utility sector plays in the transition to cleaner energy sources, despite its significant carbon footprint. Certain utility companies aim to achieve carbon neutrality targets in ways beyond renewable generation, such as the transition away from coal, technological advancements (e.g. RNG-blending initiatives and piloting hydrogen projects) and transmission and distribution efficiency improvements. As an example, recently initiated strategy position, **Eversource Energy (ES)**, has detailed its

continued >

industry-leading carbon neutrality target date of 2030 through offshore wind power generation, equipment and fleet replacements, and efficiency improvements in its gas and electric system.

Despite the uncertainty caused by the COVID-19 pandemic, which sharply reduced M&A transactions across the marketplace, activity has rapidly accelerated through year-end into 1Q21. This represents a unique opportunity for management to evaluate company performance across various ESG-related objectives and to carry forward ESG principles into the newly constructed entity. This process may consist of emphasizing higher ESG standards in smaller acquired companies, targeting ESG synergies, or simply establishing and/or reinforcing ESG principles in the structure of the new entity. During 1Q2021, the Dividend Growth ESG strategy initiated a position in **Truist Financial (TFC)** in recognition of its amplified commitment and continued progress in its ESG mission. While both predecessor entities BB&T and SunTrust were leaders in their respective communities, management of the merged company amplified its focus on ESG principles by specifically including a section on diversity, equity and inclusion in the actual merger agreement. TFC's ESG strategy and its keen focus on its predominantly southeastern US communities, teammates, and clients stood out among peers during 2020 while the public grappled with the impact of COVID-19 and social unrest. For example, the company deepened its support for underrepresented communities while also launching several philanthropic programs including Truist Cares, which has committed significant capital to meeting the needs of the bank's stakeholders.

As highlighted, Bahl & Gaynor initiated the following positions in the Dividend Growth ESG portfolio during 1Q2021:

Truist Financial (TFC)

TFC provides banking and trust services for small and mid-sized businesses, public agencies, local governments, corporations, and individuals in the Southeastern and Mid-Atlantic United States. TFC continues to exhibit best-in-class and still-improving ESG characteristics. This is evidenced through its strong business ethics practices, focus on diversity across all levels of the company with 45% of the board representing diverse backgrounds, and strong compliance programs including a dedicated anti-money laundering program. We are initiating a position in TFC due to significant tailwinds related to loan loss reserve releases as well as a positive outlook regarding their loan pipeline. These tailwinds, when combined with their quality fundamentals, attractive valuation, and dividend focused management, provide confidence in the dividend growth and downside protection moving forward.

Eversource Energy (ES)

ES is the largest New England Utility with 3.22 million electric customers, 880,000 natural gas customers, and 220,000 water customers. Eversource Energy is well positioned to benefit from the Northeast's transition to a larger mix of natural gas and renewable energy sources. Through efficiency improvements, system upgrades and increased use of renewable energy, ES is the only US Energy Utility System targeting carbon neutrality by 2030. We believe offshore wind will be an incremental driver of future earnings growth and will help ES deliver on regional energy and environmental goals. The company has a low 62% payout ratio and stated visibility of both earnings and dividend growth of 5-7% off a 2019 base through 2024. Near-term capital expenditure will focus primarily on upgrades and reliability investment into transmission, electric distribution, and Massachusetts Solar.

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.