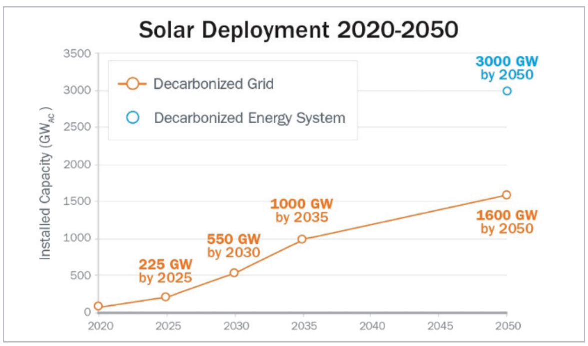
Dividend Growth ESG

Legislating to a Renewable Energy Future

The ongoing progression of renewable power generation is a prominent example where natural market forces have combined with government support, resulting in rapid technological and economic advancements. From punitive regulatory measures to tax incentives, the U.S. government has taken a hands-on approach in pursuit of advancing environmental initiatives. Tax incentives have been particularly critical in the recent evolution in the renewable energy sector. These incentives have de-risked significant capital investment programs, resulting in swift cost improvements to both energy producers and consumers, along with attractive returns for investors.

Recently, the Department of Energy (DOE) laid out its roadmap to increase solar energy's share of electricity production to 45% by 2050, which would reportedly require a quadrupling of capacity between 2025 and 2030 (see chart). To achieve this, corporations and investors look toward legislators to provide a framework for the necessary capital investments. Through tax credit extensions and plans for additional incentives, the Biden Administration has demonstrated its desire to address clean energy with a hands-on approach.



Source: US Department of Energy

Although recent stimulus plans largely ignored environmental initiatives, politicians have begun to re-prioritize ESG issues in an infrastructure spending program and a larger $3.5T budget resolution plan to support ambitious targets. Of course, clean energy is just one factor among the many issues ESG investors now embrace. "S" or social concerns (racial equity, health, education and housing for example) are also being addressed in these government programs. The cost of these programs remains a hurdle in Congress and proposals will likely see significant revisions before a potential passage. Still, the emphasis on ESG issues is clear. If passed, we expect several companies in the Bahl & Gaynor Dividend Growth ESG strategy to benefit from fiscal spending packages. It must be noted, however, our investments are supported by the underlying economics of these businesses… independent of legislation. Notable beneficiaries include certain Utility sector constituents, cellular telephone tower operators, and diversified industrial energy equipment manufacturers.

The B-Corporation and Sustainable IPO

Much of our research to evaluate ESG factors focuses on already-public companies moving toward a more sustainable future. It is our responsibility to maintain awareness of shifts in the markets outside the places where we usually look for opportunities. Enter the recent filing of San Francisco-based shoe manufacturer, Allbirds, to go public as not only a public benefit corporation (B-Corporation), but also a company coming to public markets with an existing Sustainability Principles and Objectives (SPO) Framework. As a B-Corp, the company is required to identify its public benefit and company directors have a duty to balance financial objectives and public benefit, in addition to reporting requirements related to its societal benefit.

To be clear, Allbirds intends to pay no dividend, so this review should not be interpreted as a recommendation or endorsement of Allbirds as a business or investment opportunity. Rather, the significant focus on sustainability throughout the company's regulatory filings strikes us as an interesting convergence between the possible future of capital raising and ESG priorities among investors. With this understanding, let's start by reviewing Allbirds' status as a public benefit corporation.

Allbirds describes themselves as "a global lifestyle brand that innovates with naturally derived materials to make better footwear and apparel products in a better way, while treading lighter on the planet." This mission, vision and purpose are achieved through an SPO Framework. Although not codified in regulation, or tested by a previous company, the SPO Framework is Allbirds' attempt to outline company ESG priorities and methodologies for achieving and reporting on these priorities to the public. The SPO Framework focuses effort on ESG rating, mission and purpose, climate and environment, value chain, people, and governance. Indicators are defined in each category for measurement and eventual regular reporting.

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Though Allbirds is not likely a viable opportunity for our strategies in the foreseeable future, we watch with great interest to see how the investing public receives the concepts of a B-Corporation, SPO Framework and the results (both societal and financial) Allbirds delivers. We believe choosing a direction, following it, and refining the approach with incremental learnings are important first steps for any organization pursing focus on ESG factors. In a still loosely defined landscape with respect to ESG reporting and analysis, we believe it benefits the ESG investing community to have increasingly visible and thoughtfully considered examples of ESG prioritization.

Strategy Objectives

1. ESG Integration: Significant improvement in ESG rankings relative to benchmark[1]
2. Income Growth: 2.0% yield; +9.6% growth in trailing-twelve-month income as of 3Q2021
3. Downside protection: Top quintile downside capture vs large core peers (S/I) [2, 3, 4]
4. Price appreciation: Competitive risk-adjusted returns through a full-market cycle

1 Source: Sustainalytics 2 Measured against the S&P 500 index 3 Source: PSN, Bahl & Gaynor, 2021 4 Inception: 12/31/2005

Market Recap

Investors enter 4Q2021 with equity returns well into positive territory for the year (S&P 500 +15.92% YTD), yet with a feeling of unease. Investor sentiment measured by the American Association of Individual Investors is near the low levels last seen in mid-2020 amid the depths of the pandemic. Waning fiscal and monetary support, rising inflation pressures, legislative wrangling, and moving past peak GDP growth in 2Q2021 are likely all contributing factors to the dour investor outlook. Markets have shown cracks too, most obviously with small and mid-cap equities rolling over toward negative return territory in 3Q2021 while larger cap indices continued their upward march. Volatility in September did push the S&P 500 below a critical 50-day moving average support level; a level that had served as a floor to occasional market downdrafts coming out of the pandemic…until now.

Bahl & Gaynor remains extremely optimistic about our balanced and diversified high-quality exposure during this time of investor unease. We believe the high-quality orientation of our approach remains well suited to address risks on investors' minds. We further believe the lower valuations assigned to high-quality dividend growth equities today is undeserved, out of step with forthcoming reality and indicative of an almost numbing indifference to risk at this point in the market cycle. We continue to execute on our core competency of delivering growing cash flow streams and protection from permanent capital impairment to our clients through our time-tested approach.

3Q2021 Dividend Increases		
Company	% Increase	Current Yield
Accenture PLC (ACN)	10.2%	1.2%
American Tower (AMT)[1]	3.1%	2.0%
Bank America (BAC)	16.7%	2.0%
Broadridge Financial (BR)	11.3%	1.5%
Hershey Company (HSY)	12.1%	2.1%
Illinois Tool Works (ITW)	7.0%	2.4%
JPMorgan Chase (JPM)	11.1%	2.4%
KLA Corporation (KLAC)	16.7%	1.3%
Marsh & McLennan (MMC)	15.1%	1.4%
Microsoft (MSFT)	10.7%	0.9%
Mondelez Intl (MDLZ)	11.1%	2.4%
PNC Financial Services (PNC)	8.7%	2.6%
Starbucks (SBUX)	8.9%	1.8%
Truist Financial (TFC)	6.7%	3.3%
Verizon Communications (VZ)	2.0%	4.7%

3Q2021 Income Growth Trades Executed	
Initiations	Eliminations
TJX Companies (TJX)	Amgen (AMGN)
Increases	Reductions
AbbVie (ABBV)	Comcast (CMCSA)
Air Products (APD)	Microsoft (MSFT)
Merck (MRK)	
Old Dominion Freight (ODFL)	
UnitedHealth Group (UNH)	
Waste Management (WM)	

Source: Bahl & Gaynor and Factset, 2021.
[1]Increases dividend multiple periods per year.

Current Quarter Performance Breakdown

- ESG Dividend Growth strategy income grew +9.6% in trailing 12 month income as of 3Q2021.
- 15 strategy holdings announced dividend hikes with an average increase of +10.1%.
- The strategy **outperformed**, returning +0.75% gross (+0.66% net) versus the S&P 500's +0.58% return.

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Positive drivers of current quarter performance

– Ownership of large and regional banks as credit trends, loan growth and execution remain positive for strategy holdings. Rising treasury yields in late 3Q2021 also benefitted.

– Stock selection within Industrials and Information Technology sectors due to exposure within consulting and environmental services industries while being underweight in industries such as financial processors and shipping.

– Stock selection to utilities with visible forward earnings and dividend growth supported by expanding demand for renewable energy.

Negative drivers of current quarter performance

– Stock selection within Health Care due to exposure to pharmaceutical companies which were subject to political scrutiny during the quarter.

– No exposure to non-dividend paying FAANG names NFLX and GOOG/L which rallied during 3Q2021.

Top 3 Companies Contributing to Relative Performance

1. Marsh & McLennan (MMC) MMC is one of the largest brokers in a fragmented, growing industry with opportunity to gain market share. The company is benefitting from both a strong insurance pricing market and a recovery in the economy, which led to above consensus 2Q2021 results in Brokerage and Consulting business lines. A history of consistent, predictable growth in a capital-light business supports continued dividend growth potential.

2. JPMorgan Chase & Co. (JPM) JPM remains one of the most dominant players with leading investment bank, commercial bank, credit card, retail bank and asset management businesses. Additionally, the company continues to invest in organic expansion efforts to steadily expand its competitive advantage. Optimism regarding an improving loan growth environment, strong fee related results and rising interest rates benefitted shares in 3Q2021.

3. NextEra Energy (NEE) NEE is one of the most dominant players in the generation and distribution of renewable energy through unregulated operations, with best-in-class regulated Utility operations in the Southeast. After underperforming the market during 1H2021, shares outperformed in 3Q2021 partially due to a favorable settlement announcement in its ongoing Florida rate case. NEE's high quality regulated operations combined with its leading renewable energy profile should continue to drive industry-leading earnings and dividend growth.

Top 3 Companies Detracting from Relative Performance

1. Air Products & Chemicals (APD) APD is one of the largest global suppliers of industrial gases to a wide range of industries with a focus around energy, environment, and emerging markets. Shares underperformed in 3Q2021 due to reduced contribution and delays in project closures spanning from the Lu'An and Jazan joint ventures. Air Products is well positioned to benefit from expanding gasification market opportunities, which should fuel attractive future earnings and dividend growth.

2. Qualcomm (QCOM) While QCOM remains the undisputed leader in cellular connectivity and is delivering operational strength across its markets, short-term concerns remain that supply chain issues are constraining growth. Longer term, QCOM should see robust growth away from pure mobile in other 5G applications, leading to earnings and dividend growth.

3. Illinois Tool Works (ITW) ITW is a highly diversified manufacturer of industrial products and equipment with a strong track record of margin expansion. The company is experiencing strong demand, but supply chain issues and cost inflation negatively impacted sentiment on the stock during 3Q. The company's expertise in cost management and ability to increase pricing should allow it to offset weakness in certain end-markets and grow earnings through supply chain issues, ultimately supporting continued dividend growth.

Strategy Characteristics			
Qualified Dividend Income (% of Total)	93.4%	Number of Holdings	53
Median ESG Percentile Rank (Universe / Sub-Industry)[1]	20.0 / 9.9	Weighted/Median Market Capitalization	$280.7 B / $131.7 B
QTD / YTD Turnover	3.0% / 6.3%	A-or better S&P Ranking	44.0%

[1]*Source: Sustainalytics*

PERFORMANCE	3Q2021	YTD	1 Year	2 Years[1]	S/I[1,3]
Dividend Growth ESG (Gross)	+0.75%	+13.09%	+24.60%	+15.31%	+19.18%
Sharpe Ratio	-	-	*1.98*	*0.88*	*1.18*
Dividend Growth ESG (Net)[2]	+0.66%	+12.82%	+24.19%	+15.12%	+19.04%
Sharpe Ratio	-	-	*1.95*	*0.87*	*1.17*
S&P 500†‡	+0.58%	+15.92%	+30.00%	+22.35%	+23.97%
Sharpe Ratio	-	-	*2.25*	*1.18*	*1.32*

Source: Bahl & Gaynor and PSN, 2021. [1]Annualized. [2]B&G net-of-fee figure is after management, trading and applicable bundled fees. [3]Inception: 12/31/2018

Thanks

Your continued support and interest is much appreciated.

Everyone at Bahl & Gaynor would like to thank you for the opportunity to serve your investment needs. Please feel free to contact any member of the Institutional Client Service Team through the information provided below if you have questions.

Sincerely,

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Legal Stuff

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