Bahl&Gaynor

3Q 2022 Dividend Growth ESG Update

The Inflation Reduction Act of 2022

Following a sharp and somewhat unexpected reversal from Senator Joe Manchin during 3Q2022, the Biden Administration touted the successful passage of a slimmed-down version of the Build Back Better Bill - *The Inflation Reduction Act* of 2022 (IRA). Although disagreement on its true effect on inflation contributed to unanimous opposition from GOP politicians, the IRA will undoubtedly accelerate the domestic transition to clean energy and contribute to energy diversity and security. Approximately $370B of the bill's spending is tilted toward energy security and climate, primarily funded through new and extended tax credits, rebates and subsidies.

The IRA provides support to a broad array of companies across the clean energy ecosystem. It not only supports the exploration and deployment of emerging clean energy technologies, but also supports continued growth and scaling of existing clean energy technology, including the wind and solar energy industry. Due to the inclusion of carbon-reduction targets, the IRA represents a source of long-term support and may catapult the U.S. into a lasting leadership position in clean energy; in the process, many companies held in Bahl & Gaynor's Dividend Growth ESG portfolio are expected to benefit, including **NextEra Energy (NEE), Air Products (APD), CMS Energy (CMS)** and **Eaton (ETN)**. The IRA serves as a prime example in which financial benefits can be realized for companies within secular ESG trends.

Policy	Cost (-)/Savings (2022-2031)
Energy and Climate	-$391 billion
Clean Electricity Tax Credits	-$161 billion
Air Pollution, Hazardous Materials, Transportation and Infrastructure	-$40 billion
Individual Clean Energy Incentives	-$37 billion
Clean Manufacturing Tax Credits	-$37 billion
Clean Fuel and Vehicle Tax Credits	-$36 billion
Conservation, Rural Development, Forestry	-$35 billion
Building Efficiency, Electrification, Transmission, Industrial, DOE Grants and Loans	-$27 billion
Other Energy and Climate Spending	-$18 billion

Source: Committee for a Responsible Federal Budget, 2022.

ESG Critics Abound in 3Q22 – is the debate explained by shareholder versus stakeholder theory?

Conversations on the merits of ESG abounded in 3Q22. Within the investment community, the essence of the debate seems to be driven from a central discussion in finance – shareholder versus stakeholder theory.

Shareholder theory, as defined by Milton Friedman, states that every corporation should seek solely to increase its profits within the rules of the game. This idea can create pitfalls if a company's management team is too short-sighted, swapping long-term innovation and sustainable growth to maximize profit in a single quarter.

Stakeholder theory espouses a broader view of corporate purpose and includes the interests of many stakeholders, whether it be the community in which a corporation operates, the customer for which a product is made, or the public shareholder. Those who believe in stakeholder theory do not forgo a focus on profits, but instead advocate for a wider view of corporate purpose.

Many of the recent ESG conversations are based on the misperception that corporate directors and management teams must choose between the aforementioned value sets. However, a company's management team is not required to make a mutually exclusive choice between shareholder and stakeholder theory. Instead, shareholder focus on profit maximization is one very important piece of the larger stakeholder theory.

Closing Thoughts

At Bahl & Gaynor, our heritage has focused on holding companies accountable with an emphasis on sustainable growth through a dividend. We believe a strong dividend policy signals earnings power, earnings quality, business stability and financial strength over the long run. In our view there is overlap in what is considered "good ESG policy" and just good policy.

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Strategy Objectives

1. ESG Integration: Significant improvement in ESG rankings relative to benchmark[1]
2. High current and growing income: 2.6% yield; +11.8% growth in trailing-twelve-month income as of 3Q2022
3. Downside protection: Top quartile 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, 2022 [4] Inception: 12/31/2018

Current Quarter Strategy Thoughts Relative to Objectives:

- The Dividend Growth ESG strategy grew trailing-twelve-month income by +11.8%, providing real client purchasing power growth
- 15 strategy holdings announced dividend hikes; average TTM increase was +12.4%, signaling fundamental strength amid a deteriorating economic and market environment.
- Daily downside capture of 83.9%* and 81.7%* across all S&P 500 down days in 3Q2022 and year-to-date, respectively; indicative of investor preference for quality during periods of market volatility.
- The strategy **outperformed**, returning -3.95% gross (-4.04% net) versus the S&P 500's -4.88% return.
- Non-dividend paying market darlings such as Tesla (TSLA), Amazon (AMZN), Netflix (NFLX) and PayPal Holdings (PYPL) bounced in July after large 1H2022 declines, contributing to outperformance of non-dividend paying stocks despite the turbulent quarter.
- Defensive/quality factors such as high-ROIC and shareholder yield underperformed in the July to mid-August low-quality bounce off June lows (Source: Strategas Research, 2022).
  - Defensive and quality characteristics outperformed in the September market washout and will likely remain important as investors navigate current elevated market uncertainty.
- The outlook for active managers with a focus on sustainable dividends and stable fundamentals in this uncertain macro environment remains positive.

3Q2022 Dividend Increases		
Company	% Increase	Current Yield
Accenture (ACN)	+15.5%	1.7%
American Tower (AMT)	+12.2%	2.7%
Broadridge Financial (BR)	+13.3%	2.0%
Cintas (CTAS)	+21.1%	1.2%
Hershey (HSY)	+15.0%	1.9%
Illinois Tool Works (ITW)	+7.4%	2.9%
Keurig Dr Pepper (KDP)	+6.7%	2.2%
Kla Corporation (KLAC)	+23.8%	1.7%
Marsh & McLennan (MMC)	+10.3%	1.6%
Microsoft (MSFT)	+9.7%	1.2%
Mondelez Intl (MDLZ)	+10.0%	2.8%
Regions Financial (RF)	+17.6%	4.0%
Starbucks (SBUX)	+8.2%	2.5%
Texas Instruments (TXN)	+7.8%	3.2%
Truist Financial (TFC)	+8.3%	4.8%

[1]Increases dividend multiple periods per year.
Source: Bahl & Gaynor and Factset, 2022.

3Q2022 Dividend Growth ESG Trades Executed	
Initiations	Eliminations
CMS Energy (CMS)	Bank of America (BAC)
Regions Financial (RF)	Comcast (CMCSA)
Williams (WMB)	JPMorgan Chase (JPM)
	Visa (V)
	Verizon (VZ)
	WEC Energy (WEC)
Increases	Reductions
Booz Allen (BAH)	Best Buy (BBY)
Broadridge Financial (BR)	Cisco Systems (CSCO)
Cintas (CTAS)	Microsoft (MSFT)
Fidelity National (FIS)	
Regions Financial (RF)	
UnitedHealth (UNH)	
Williams (WMB)	
Zoetis (ZTS)	

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Positive drivers of current quarter performance

- Ownership of stable growth companies in the waste management, support services and building products industries within the Industrials sector.
- No exposure to high-growth, non-dividend paying internet and direct marketing companies or levered, slow growth telecommunication services companies in the Communication Services sector.
- Stock selection within the semiconductors and communications equipment industries within the Information Technology sector.
- High-quality positioning towards regulated utilities amid both investor preference for stability and the passage of the Inflation Reduction Act (IRA).
- Ownership of companies in the Materials sector with reduced cyclicality and less commoditized earnings streams.

Negative drivers of current quarter performance

- No exposure to mega-cap, non-dividend payers that rebounded, including Amazon (AMZN) and Tesla (TSLA).
- An underweight allocation to the Energy sector which continues to show unique stability due to elevated commodity prices.

Largest Portfolio Contributors

1. Waste Management (WM) As the largest solid waste company, WM has seen volumes return to pre-pandemic levels while also demonstrating its robust pricing power. WM has also improved its ESG profile via increased organic investments in advanced recycling facilities and building renewable natural gas plants.

2. Starbucks (SBUX) SBUX is set to drive sales growth through loyalty enhancements and expand margins through beverage innovation and digital/delivery options. Store reinvention plans by new leadership aims to grow SBUX's global store portfolio and boost efficiency at existing locations.

3. NextEra Energy (NEE) NEE outperformed due to the Inflation Reduction Act (IRA) passage which supports its renewables portfolio as well as investors' flight to safety stocks amid volatility. NEE's best-in-class regulated and renewable assets should continue to drive industry-leading earnings and dividend growth.

Largest Portfolio Detractors

1. Fidelity National (FIS) FIS is emerging from a phase marked by investment in its cloud-based SaaS offerings and its acquisition of Payrix but has now successfully decreased its leverage and is set to be rewarded with healthy cash flow and dividend growth.

2. American Tower (AMT) Rising interest rates pressured the Real Estate sector during 3Q2022. AMT remains structurally positioned to growth FFO and dividends from its globally scaled infrastructure of wireless tower and emerging 5G assets leased by carriers.

3. AbbVie (ABBV) Concerns over 2023 sales erosion of its blockbuster Humira drug and near-term sales from its more-discretionary aesthetics business pressured shares. Longer-term, ABBV is positioned to re-rate and grow earnings and dividends beyond Humira at a peer-high rate.

Strategy Characteristics			
Qualified Dividend Income (% of Total)	93.5%	Number of Holdings	53
Median ESG Percentile Rank (Universe / Sub-Industry)[1]	19.2 | 13.2	Weighted/Median Market Capitalization	$173.5 B / $69.4 B
QTD / YTD Turnover	7.5% / 14.2%	A-or better S&P Ranking	43.9%

Source: [1]Sustainalytics. Please refer to Disclosures for additional information on third-party data.

PERFORMANCE	3Q2022	YTD	1 Year	2 Years[1]	3 Years[1]	S/I[1,3]
Dividend Growth ESG (Gross)	-3.95%	-20.82%	-9.57%	+6.15%	+6.33%	+10.72%
Sharpe Ratio	-	-	*-0.55*	*0.33*	*0.32*	*0.58*
Dividend Growth ESG (Net)[2]	-4.04%	-21.04%	-9.89%	+5.79%	+6.09%	+10.52%
Sharpe Ratio	-	-	*-0.57*	*0.31*	*0.30*	*0.56*
S&P 500[†‡]	-4.88%	-23.87%	-15.47%	+4.83%	+8.16%	+11.93%
Sharpe Ratio	-	-	*-0.80*	*0.23*	*0.38*	*0.58*

Source: Bahl & Gaynor and PSN, 2022. [1]Annualized. [2]B&G net-of-fee figure is after management, trading and applicable bundled fees. [3]Inception: 12/31/2018

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Thanks

Your continued support and interest are much appreciated.

Everyone at Bahl & Gaynor would like to thank you for the opportunity to serve your investment needs.

Important Disclosures

Legal Stuff

*Bahl & Gaynor and FactSet; historical downside (upside) capture is the sum of strategy returns on all S&P 500 down (up) days divided by the sum of index returns on all respective down (up) days. Down (Up) days are defined as any trading day the index posts a negative (positive) total return. Strategy performance is derived from the internal rate of return (IRR) of a single non-fee paying representative/model account.

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