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## Making a Positive Impact: The State of ESG Advocacy and Engagement

By Julie Gorte, Ph.D., Senior Vice President for Sustainable Investing, Pax World

Shareholder advocacy and engagement comes in many flavors. Most shareholders approach company ownership passively: they buy and sell shares, and they vote their proxies. A few shareowners also engage companies directly, either one-on-one, or through group engagements, and occasionally through the mechanism of a shareholder proposal.

This type of engagement is collectively known as *shareholder activism*, but that term is also used to broadly describe the activities of hedge funds and other so-called activist funds that take large positions in firms with the specific intention of changing their policies or behavior, with a specific and often short-horizon financial return as the objective.

What I'm going to talk about here, and what we do at Pax World, is *not* that kind of activism: sustainability advocacy and engagement is aimed at longer-term outcomes, and specifically targets environmental, social and governance (ESG) factors. The goal is to improve companies' profiles through sustainability.

This type of engagement is gaining prominence. The US Forum for Sustainable and Responsible Investment reports that between 2014 and the first half of 2016, 176 institutional investors and 49 investment manager investors collectively controlling over \$2.5 trillion in assets under management filed or co-filed shareholder resolutions on ESG issues.<sup>1</sup> For the 2016 proxy season,<sup>2</sup> over half of the 370 shareholder proposals

filed concerned two issues: environment (33% of all proposals filed) and political activity (26% of all proposals filed), according to the Sustainable Investments Institute.<sup>3</sup>

Investors who devote time and resources to engagement on sustainability issues likely do it not to be gadflies, but because they believe, as we do at

Pax, that improving companies' sustainability profiles makes them better investments, and helps them perform better in the long run.

There is abundant evidence that companies that do better on sustainability metrics also perform as well as, or better than, their peers financially. It is more difficult to assign a financial outcome to an engagement that, in many cases, may last for years, but

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*"There is abundant evidence that companies that do better on sustainability metrics also perform as well as or better than their peers financially."*

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at least one effort to examine the impact of this kind of ESG engagement shows that activism on material issues is associated with superior financial performance.<sup>4</sup>

More good news: When we look at shareholder proposals, it is clear that support for well-crafted ESG proposals is going up, with vote counts rising from around 14-15% a decade ago to over 20% in recent years. Moreover, the number of proposals that achieve votes in favor of 20% or more has doubled over the past decade.<sup>5</sup>

Shareholders can be a powerful force affecting companies' strategies and performance; however, achieving significant change can be a slow process. Board diversity is an excellent example of this. A few investors, including Pax, have been working

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# How Pax Gives Back

At Pax World, creating positive community and environmental impact isn't limited to our investment approach—it's engrained in our company culture and our business philosophy. With help from the NH Charitable Foundation (NHCF) and a newly formed community impact employee committee, we're making a positive difference in the world through our community involvement and philanthropy.

In 2014, Pax World partnered with the NHCF to establish the Pax World Management Charitable Fund and help administer our corporate donations and sponsorships to a host of organizations.

"Philanthropic money is money that needs to be wisely invested," Pax CEO Joe Keefe said. "NHCF offers abundant knowledge of the non-profit and philanthropic landscape that's now at our fingertips, allowing us to be more impactful."

Understanding Pax's philosophy and interests, the NHCF team brings expertise and funding opportunities to the table and has presented a workshop to Pax employees about charitable giving. Through NHCF, Pax has made grants to support numerous causes, including a group that mentors and empowers teen girls

through the arts, public radio and television, environmental stewardship organizations, homeless shelters and food pantries, women's empowerment organizations, and to groups that battle poverty and oppression.

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*"There's so much need out there and yet we have a finite amount of money. We want to have as much impact with that money as we can."*

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"There's so much need out there and yet we have a finite amount of money," Mr. Keefe said. "We want to have as much impact with that money as we can."

Last year, Pax established a 10-person committee consisting of employees from a cross section of the firm's departments to advise on the Pax World Management Charitable Fund. "Giving employees another avenue for community engagement is the perfect answer for us," Mr. Keefe said, "For a firm our size,

it's just a great way to be more involved in the community."

In 2017, the employee committee set goals to target charitable contributions in three categories: empowerment of women; environmental protection and conservation; and general needs in the Greater New Hampshire Seacoast area, such as help with substance abuse and addiction, or food and fuel assistance. The committee's goal is to balance a mix of strategic, longer-term focused grants with those focused on more urgent needs.

In addition to offering financial support to various community organizations through the Pax World Management Charitable Fund, Pax matches employee contributions to non-profit organizations (up to \$250 for each of our 52 employees). In 2016, Pax World donated \$12,250 as part of the Employee Match Program. Pax also gives back through our employee volunteer program, United Way Day of Caring projects, and organized donation opportunities.

"We want happy, engaged employees," said Mr. Keefe. "Part of that happiness and engagement is knowing we make a positive impact on the community." 

## MAKING A POSITIVE IMPACT: THE STATE OF ESG ADVOCACY AND ENGAGEMENT CONTINUED from FRONT PAGE

to achieve greater diversity on boards of directors for decades, and those efforts have begun to achieve notable success.

A recent article on the Harvard Law School Forum on Corporate Governance and Financial Regulation website noted that 2016 was a "breakout year" for gender diversity in the U.S., and noted that "momentum toward gender parity on boards is building, particularly in the top tier of public corporations."<sup>6</sup>

At Pax, we have voted against or withheld proxy votes from all board slates with fewer than two women for several years, and each time, we have written to the companies explaining the reason for our votes. This has resulted in several productive dialogues with companies, as have the shareholder proposals

we have filed urging companies to assure in their Nominating Committee Charters that every board search include diverse candidates. We have been able to successfully withdraw every shareholder proposal we have filed on board diversity, and several of the companies have subsequently added women to their boards.

Would progress have happened without investor engagement? It's impossible to know; we can't test a counterfactual argument. But what we do know is that investor efforts to advance board diversity have coincided with a period of progress, albeit slow, in the gender diversity of boards. That is the way advocacy and engagement works.

And that is why we continue to move forward with these efforts—it is making a difference. 

<sup>1</sup>The Forum of Sustainable and Responsible Investment, "Report on US Sustainable, Responsible and Impact Investing Trends 2016," November 2016.

<sup>2</sup>A proxy season is the term applied to the season in which most publicly traded companies hold their annual shareholder meetings. Over half of these meetings occur in spring, which is loosely referred to as "proxy season" in the United States.

<sup>3</sup>Heidi Welsh, "Proxy Season Forecast: Social and Environmental Proposals in 2016," Sustainable Investments Institute, February 16, 2016.

<sup>4</sup>George Serafeim, "Shareholder Activism on Sustainability Issues," Harvard Business School, July 25, 2016.

<sup>5</sup>Heidi Welsh, "Proxy Season Mid-Year Review: Social, Environmental & Sustainable Governance Shareholder Proposals in 2016," Sustainable Investments Institute, August 15, 2016.

<sup>6</sup>David A. Katz and Laura A. McIntosh, Wachtell, Lipton, Rosen & Katz, "Corporate Governance Update: Prioritizing Board Diversity," Harvard Law School Forum on Corporate Governance and Financial Regulation, January 30, 2017.

## Pax CIO Elected to US SIF Board



Congratulations to Steve Falci, Pax World Chief Investment Officer, who was elected to the US SIF (The Forum for Sustainable and Responsible Investment) board of directors.

“It is a privilege to serve on the US SIF Board of Directors and I welcome the opportunity to work with US SIF members to further the adoption, growth and impact of sustainable, responsible and impact investing,” said Steve Falci.

The US SIF board provides strategic guidance to advance sustainable, responsible and impact investing.

## Pax CEO Joe Keefe Honored



*Joe Keefe, Pax World President and CEO, receives the 2016 Social Innovator of the Year Award from Fiona Wilson, D.B.A., Executive Director of UNH's Center for Social Innovation and Enterprise. Photo by Perry Smith Photography.*

Pax World's President and CEO, Joe Keefe, was honored as the 2016 Social Innovator of the Year by the University of New Hampshire's Center for Social Innovation and Enterprise (CSIE).

Each year CSIE selects a New England leader with a demonstrated commitment to social innovation. CSIE said Mr. Keefe's voice “has helped change the field to champion both sustainable investing and women's empowerment, and his influence has been felt

across the globe.”

When asked, what does the Social Innovator of the Year honor mean to you, Mr. Keefe responded “I believe this honor recognizes the work that Pax World employees and shareholders do to engage companies through dialogues and resolutions. We've focused on gender diversity because we have seen from experience and compelling research that companies with more women in leadership positions simply perform better.”

## Kathleen McQuiggan Receives Award



*On February 15, 2017 business people from across New Hampshire gathered to celebrate the 2016 Outstanding Women in Business. Kathleen McQuiggan speaks to the crowd after receiving her award. Photo by Jodie Andruskevich.*

Pax World is pleased to announce that Kathleen McQuiggan, Pax World Senior Vice President of Global Women's Strategies and Managing Director of Pax Ellevest, was among the winners of the 2016 Outstanding Women in Business Award.

Each year New Hampshire Business Review bestows this award to six women who have truly excelled, not only in their professional lives, but as community leaders and role models.

At Pax World and Pax Ellevest, Ms. McQuiggan is responsible for initiatives related to gender diversity and women's empowerment, including its efforts to advance gender equality as an investment concept.

## CONVERSATION PIECES



“Investor interest in sustainable investing strategies is growing rapidly, and we've expanded our lineup with a total of five new funds in the last year to meet this increased demand.”

*Pax World adds Smart Beta, Bond, Large-Cap Funds  
Financial Advisor, February 1, 2017  
Joe Keefe, President & CEO*

“Companies thoroughly understand the business case [for gender diversity]. I don't see the topic going away any time soon.”

*Goldman, Citigroup Targeted by Diversity Activists  
in 2017*

*Bloomberg, December 6, 2016*

**Heather Smith, Lead Sustainability Research Analyst, Portfolio Manager, Pax Ellevest Global Women's Index Fund**

“Proposals are getting enough votes that make it hard to ignore.”

*Environmental Proxy Proposals Are Making  
More Demands*

*Wall Street Journal, November 28, 2016*

**Julie Gorte, Senior Vice President for Sustainable Investing**

“All the research demonstrates that investing in women is a smart investment.”

*The business of women*

*Financial Times, December 2, 2016*

**Joe Keefe, President & CEO**



# Three Questions on Sustainable Fixed Income Investing

## Q&A with the Portfolio Manager of the Pax Core Bond Fund

Pax World recently launched the **Pax Core Bond Fund (PAXBX)**, joining the Pax High Yield Bond Fund as our second fixed income strategy. This investment-grade bond fund invests across multiple fixed income sectors and allocates a portion of the portfolio to impact bonds promoting positive community and environmental outcomes.

In this Q&A, Portfolio Manager Tony Trzcinka shares his views on the value of fixed income ESG integration and growth in the impact bond market. Learn more about the Pax Core Bond Fund at [paxworld.com/corebond](http://paxworld.com/corebond).

### Q: How does environmental, social and governance (ESG) research integration support fixed income portfolio management?

In managing an investment-grade bond fund, a big focus is minimizing downside risk. Credit risk, or the risk that a borrower's credit rating deteriorates, is one of the primary risks that we seek to manage, particularly within our corporate bond allocation. ESG research serves an important role alongside our financial research as we vet each issuer. We feel that by incorporating ESG considerations into credit selection we are able to identify better-managed companies that are less likely to run into credit issues.

In fact, recent research<sup>1</sup> backs this up by showing that companies with higher ESG factors are less likely to declare bankruptcy and a separate study<sup>2</sup> shows that bonds of companies with stronger ESG ratings perform better. We also seek to invest in corporate bonds of companies whose products, services and technologies are proactively confronting global sustainability challenges.

So ideally, we are trying to capture the risk mitigation benefits from this sustainability lens and potentially improve performance



**Tony Trzcinka, CFA®**  
Vice President, Portfolio  
Manager, Pax Balanced Fund  
and Pax Core Bond Fund

through a portfolio bias toward companies with ESG strength.

### Q: What is driving growth in the green bond market?

The green bond market has experienced tremendous growth over the last few years. Issuance has gone from \$42 billion in 2015 to \$81 billion in 2016 to an estimated \$150 billion in 2017.<sup>3</sup> Green bonds are aimed specifically at environmental impact, focusing on climate change mitigation, energy efficiency and clean energy.

In speaking with green bond issuers, they frequently cite two drivers of the growth in the market. First, there is tremendous demand from the growing number of investors seeking more than financial return. Second, green bonds attract a diverse group of investors which helps expand the issuing company's investor base. One treasurer actually referred to them as a "treasurer's dream."

### Q: Can you provide examples of bonds in the Fund that help improve community and environmental outcomes?

The Fund holds a number of investments that specifically target positive impact in areas such as energy and environment, community development, and sustainable infrastructure. The Fund owns 16 different green bonds that finance environmentally beneficial projects. For example, Bank of America Green Bonds are aimed at initiatives that address climate change, reduce demands on natural resources and advance lower-carbon economic solutions.

On the community development end of the impact investment spectrum, Envest Microfinance is an example of a Fund investment that supports microfinance entrepreneurs in developing countries, such as Nicaragua, Kyrgyzstan, Peru, and Tajikistan. The organization targets the world's economically marginalized populations by lending primarily to small microfinance institutions. 🌱

As of 12/31/16, Bank of America Green Bonds was 0.83% and Envest Microfinance was 0.02% of the Pax Core Bond Fund. Holdings are subject to change.

<sup>1</sup>Source: Equity Strategy Focus Point, Bank of America Merrill Lynch, December 18, 2016.

<sup>2</sup>Source: Sustainable Investing and Bond Returns, Barclays Research Quantitative Portfolio Strategy Group, 2016.

<sup>3</sup>Source: Climate Bonds Initiative.



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**You should consider a fund's investment objectives, risks, and charges and expenses carefully before investing. For this and other important information, please obtain a fund prospectus by calling 800.767.1729 or visiting [www.paxworld.com](http://www.paxworld.com). Please read it carefully before investing.**

**An investment in the Pax World Funds involves risk, including loss of principal. Past performance does not guarantee future results.**

**RISKS:** Equity investments are subject to market fluctuations, a fund's share price can fall because of weakness in the broad market, a particular industry, or specific holdings. Emerging market and international investments involve risk of capital loss from unfavorable fluctuations in currency values, differences in generally accepted accounting principles, economic or political instability in other nations or increased volatility and lower trading volume. Investments in high yield bonds generally are subjected to greater price volatility based on fluctuations in issuer and credit quality. When investing in bonds, you are subject, but not limited to, the same interest rate, inflation and credit risks associated with the underlying bonds owned by the Fund. Mortgage related securities tend to become more sensitive to interest

rate changes as interest rates rise, increasing their volatility. Funds that emphasize investments in mid-size and smaller companies generally will experience greater price volatility. Investing in non-diversified funds generally will be more volatile and loss of principal could be greater than investing in more diversified funds. The Pax Mid Cap Fund, Large Cap Fund, Core Bond Fund and the ESG Beta® Dividend Fund are new and have a limited operating history.

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