How to Combine Outperformance, Sustainability And Climate Objectives...

In One Portfolio

Capital Markets Web Conference „ESG Investing“

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Some Myths about Sustainability Investing

It costs performance

Exclusions are easy to implement

?

It is just a fashion trend

„Best-in-class" is the best approach

Our research suggests it is an outperformance opportunity

- ✓ High ESG Scores are a good proxy for better management teams
- ✓ Sustainable Companies will attract more asset flows

AND there are some important implementation challenges:

- ➢ Too strict exclusion lists distort country and sector allocations
- ➢ One-dimensional «Leaders»-approach ignores other performance drivers
- ➢ Investor dilemma of choosing between ESG or Climate objective

It is possible to systematically combine:

1 High fundamental Quality	2 Sustainability	3 Climate Objectives

1. **Apply classical financial analysis criteria on all stocks**:
   - superior growth and growth stability
   - higher profitability
   - robust balance sheet health
   - moderate valuation and P/E-expansion

2. **Sustainability**: Exclude only the most controversial companies and sectors and use a sector and country-adjusted ESG score as a positive selection criterion

3. **Climate Objectives**: Construct portfolios with an explicit **decarbonisation target** and keep the carbon footprint at or below Paris-aligned benchmarks

Get the basics right: Invest in fundamentally good companies

Strong Profitability

Does the company operate efficiently?

Moderate Valuation

Is the market price of the company attractive?

Apply systematically what good financial analysts do on the full stock universe

Is the company successfully expanding its business?

Superior Growth

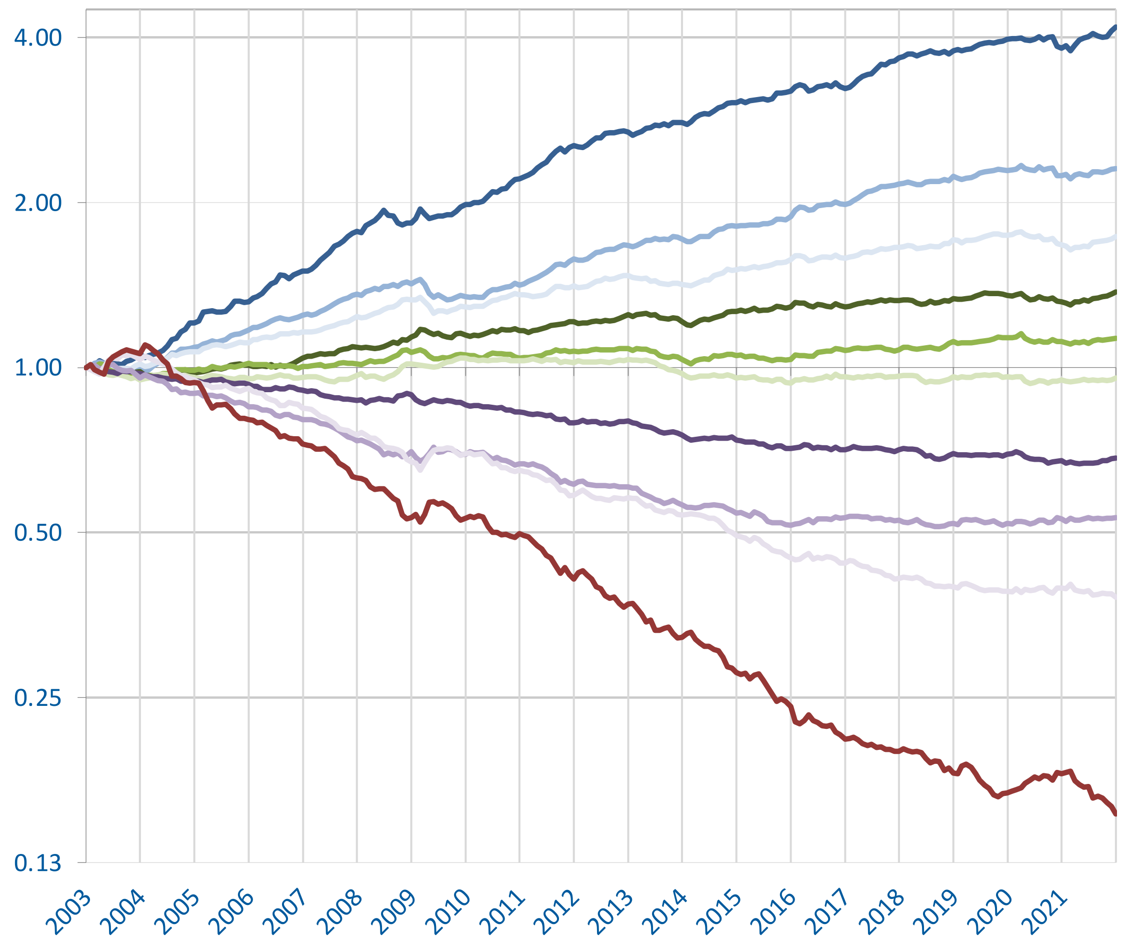
Is the company in good financial condition?

Healthy Balance Sheet

The key driver of outperformance is the fundamental quality

“Companies with better fundamentals have a higher probability to outperform”

Published in Wilmott Magazine, July 2015: “Consistent Outperformance based on Published Information – or when reality defies theory” (Herrera/Toivanen)



Best Companies outperformed by over 300%

Worst Companies underperformed by more than -80%

Source: Artico database: Relative Performance of full global investment universe split into 10 sub-portfolios based on company ranking, equally weighted, re-balanced weekly, no trading costs

Exclude only the most controversial companies and sectors

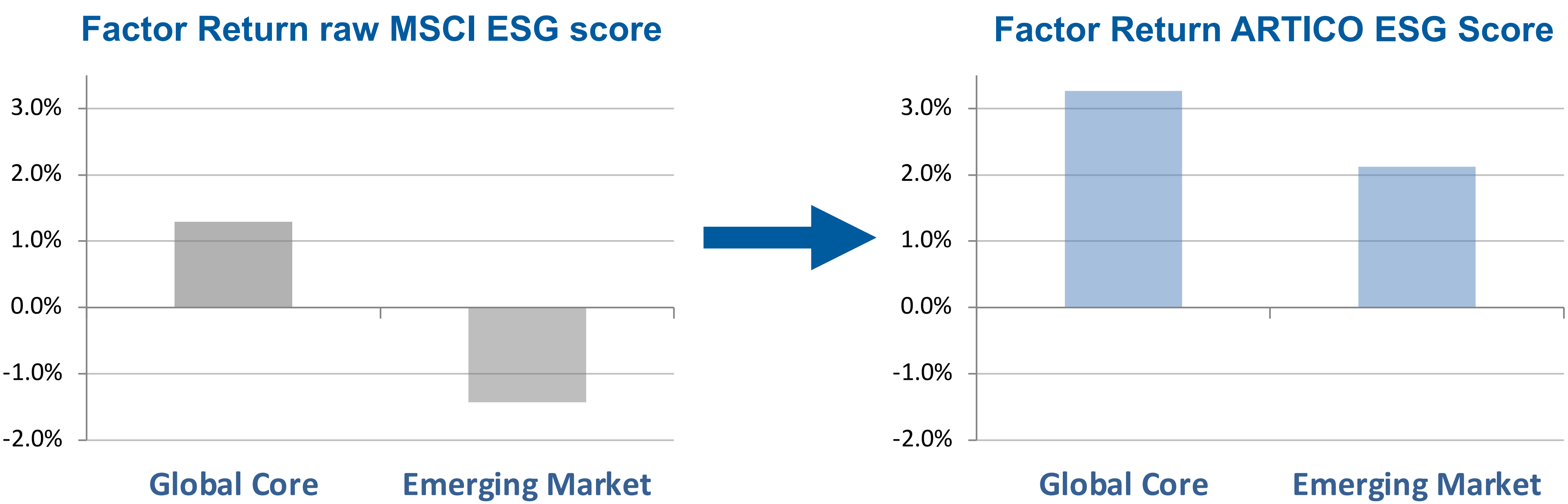
- Because broad exclusions reduce the investable opportunity set and distort the country and sector allocation with undesired effects
- A focused exclusion list can already be very effective

	MSCI World (1492 stocks)	
Exclusion Criteria	**Companies**	**Weight**
Controversial Weapons	20	1.9%
Conventional Weapons	26	1.8%
Nuclear Power	21	1.3%
GMO Agriculture	3	0.4%
Adult Entertainment	0	0.0%
Gambling	16	0.4%
Tobacco	5	0.7%
Coal	3	0.3%
Oil & Gas	62	5.5%
SVVK Exclusion List	1	0.2%
Very Severe Controversies (red flag)	8	0.6%
Severe Environmental Controversies	29	5.8%
CCC ESG Rating	7	1.0%
Worst 2.5% Carbon Emissions & Intensity	84	3.3%
Total	**216**	**16.4%**

Note: Total companies and weight is not the sum of the individual exclusion criteria (due to multiple criteria exclusions). SVVK stands for the Swiss Association of Responsible Investing. UNGC and OECD guidelines are covered in the controversy exclusions.

The challenge of integrating ESG as positive selection criteria

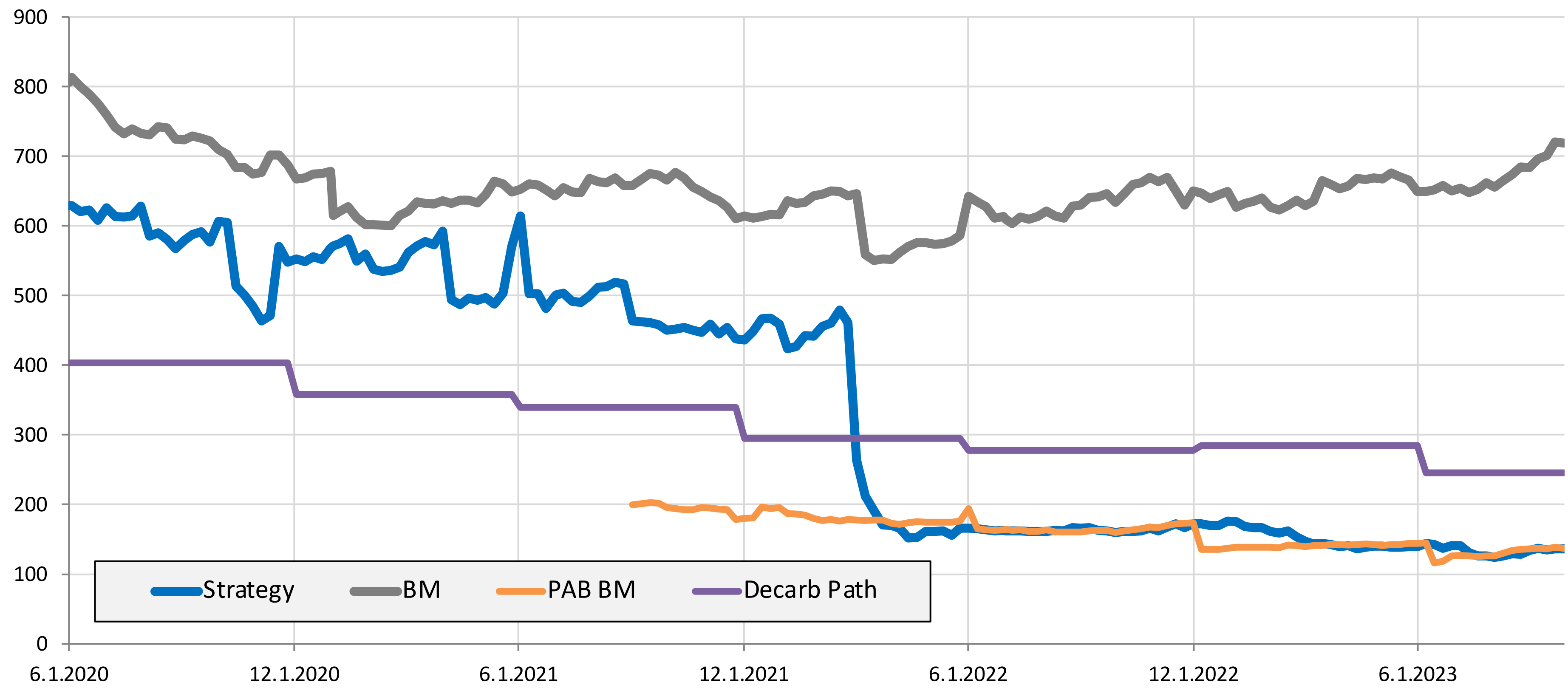
- Available ESG ratings (MSCI, Sustainalytics,..) are surprisingly low correlated. We selected MSCI database due to broad coverage, history, convincing concept and institutional standard
- But: raw MSCI ESG Score has historically no or mixed predictive value
- Artico‘s country- and sector-adjusted ESG score can contribute to outperformance



Note: Factor Return defined as performance difference between top and bottom decile of ESG-rated companies, average of multiperiod annualized returns from 2012 to 2019

Portfolio Construction with a clear Decarbonisation Target

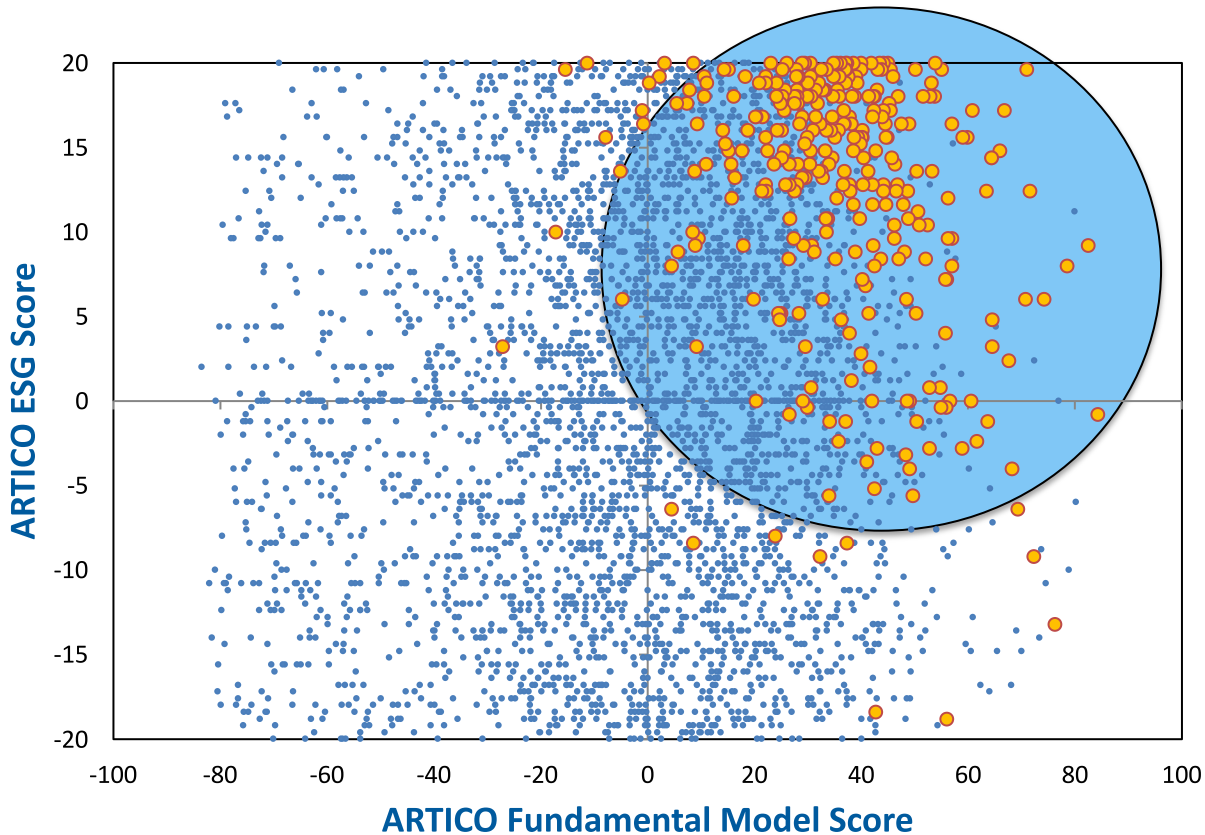
Carbon Intensity is used as a restriction for ARTICO Sustainable Emerging Market Strategy



Source: ARTICO database; Decarbonisation path starts with a 50% reduced carbon intensity as of 1/6/2020 and a 7% annual decarbonization rate thereafter. Chart shows weighted Avg EVIC Scope 123 carbon intensity (tons of CO_2 / m of Enterprise Value). Decarbonization path is adjusted by changes in enterprise value to compensate for pure market movements which can lead to short term fluctuations of the decarbonisation path in both directions

How is it possible to combine all these dimensions in one portfolio?

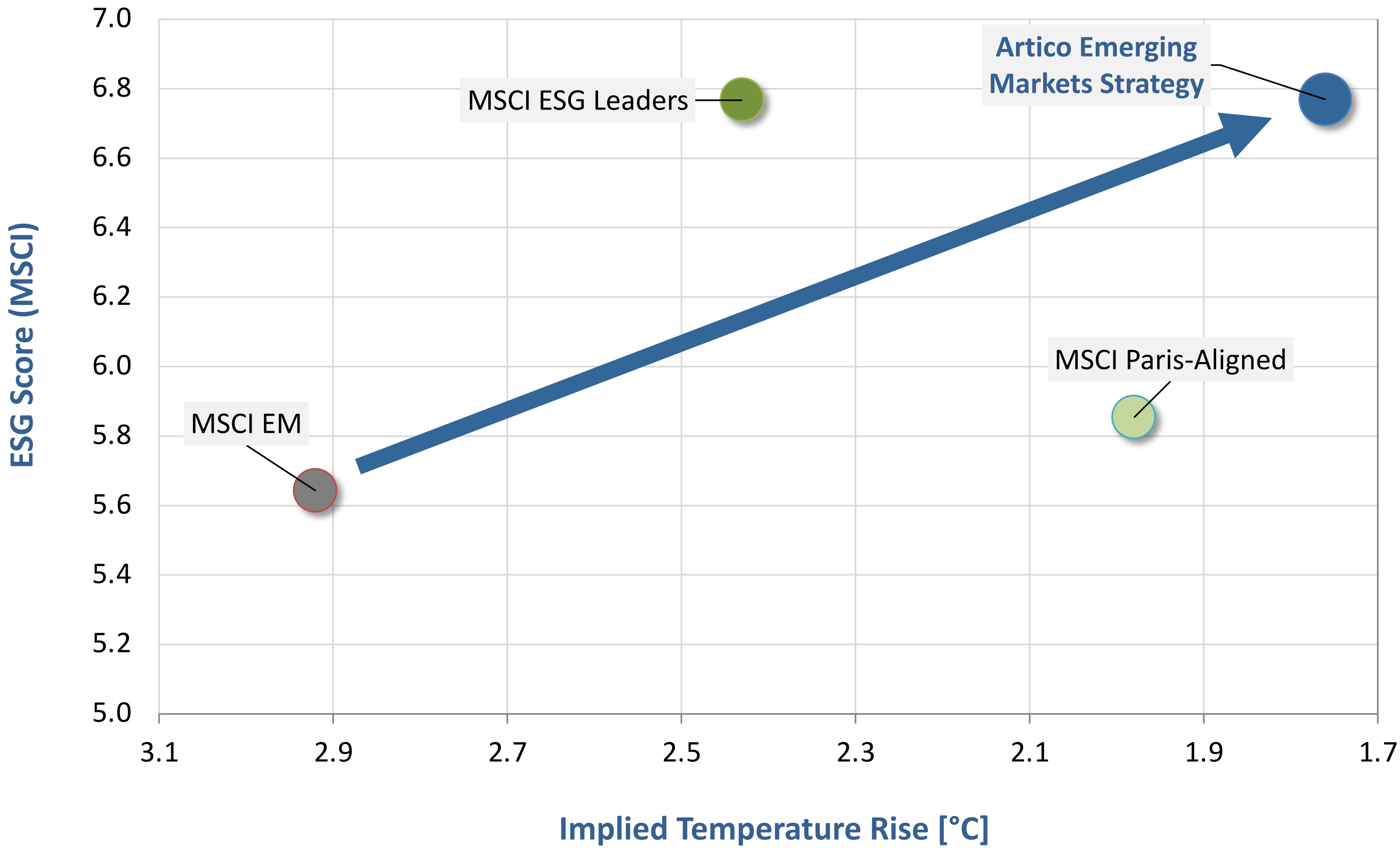
- The key is to start with a large enough investment universe
- Portfolio holdings (yellow dots) target high scores in all dimensions
- There are enough companies with the right characteristics to choose from



Source: Artico Database, ESG and fundamental model scores as of September 2021 for Global Core Universe

The resolved dilemma: ESG and Paris-alignment both achieved

ARTICO Emerging Market Strategy with High ESG Score and Low Portfolio Temperature



Note: ESG Score and Implied Temperature Rise on strategy/ETF holdings as of 30.09.2023

A systematic approach allows to achieve top marks in all criteria

The Emerging Markets Strategy scores high in all dimensions

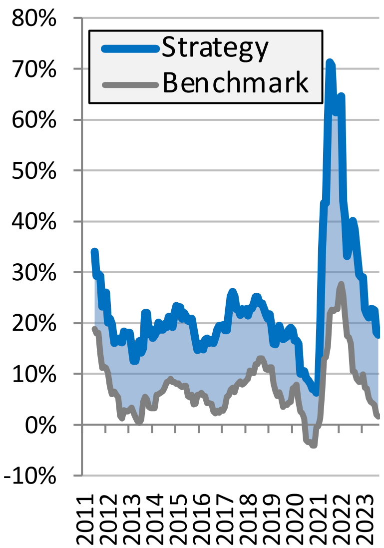
	Standard MSCI EM ETF	MSCI EM ESG Leaders ETF	MSCI EM Paris Aligned ETF	ARTICO Emerging Markets Strategy
No of Companies	1'151	474	436	185
ESG Quality Score (MSCI)	5.64	**6.77**	5.85	**6.77**
Carbon Footprint	530	178	**53**	**31**
Implied Temperature Rise	2.92	2.43	**1.98**	**1.76**
PE Ratio	17.0	16.6	**20.2**	**15.2**
ROE	11.0%	11.2%	12.2%	**19.0%**
Net Income Growth	1.7%	4.3%	10.8%	**17.7%**

Source: Data as of 29.09.2023; Artico Database. Carbon Footprint includes Scope 1 & 2 Carbon Emissions. ESG Scores and Implied Temperature Rise based on MSCI single company values; PE ratio, Return on Equity and Net Income Growth are Median Values.

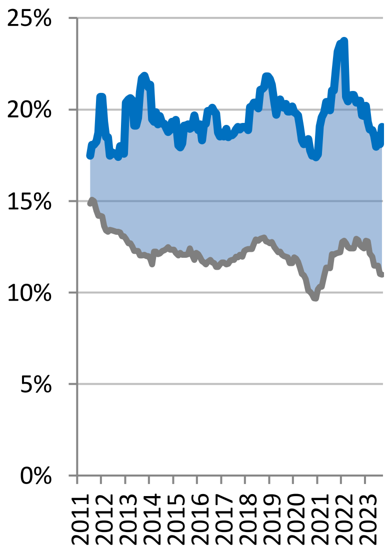
Unique strategy characteristics are stable over time

FASTER Growth and **HIGHER Profitability** at **LOWER Valuation** with **BETTER ESG Score** and **LOWER Carbon Footprint**

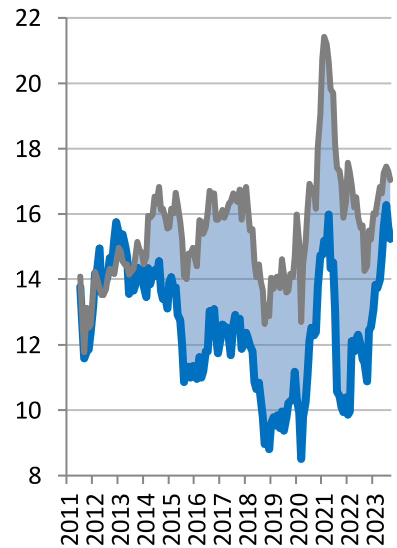
Income Growth Premium



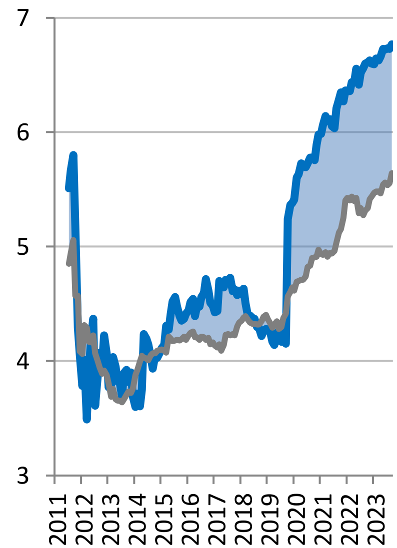
RoE Premium



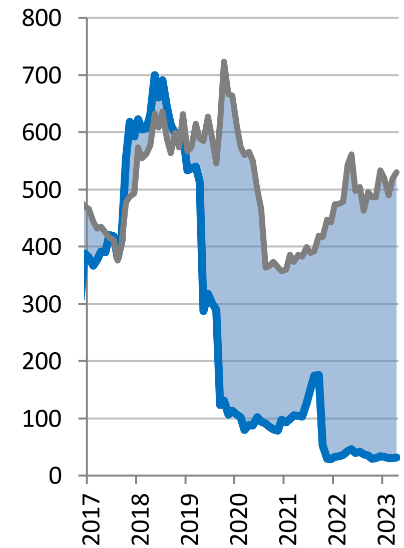
Price/Earnings Discount



ESG Quality Score



Carbon Footprint

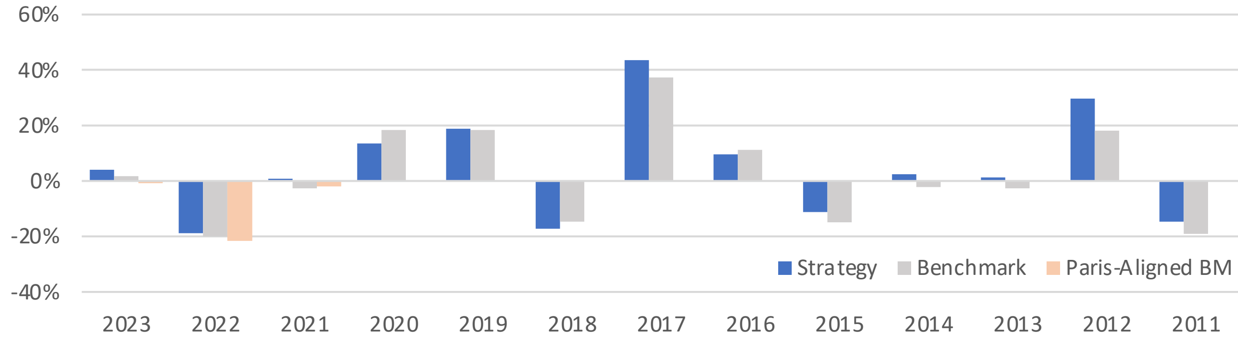


Source: September 2023; Artico Emerging Markets strategy versus benchmark; median growth, profitability and valuation characteristics and ESG Score since June 2011. Carbon footprint since June 2017.

The approach led to robust outperformance in all 3 strategies

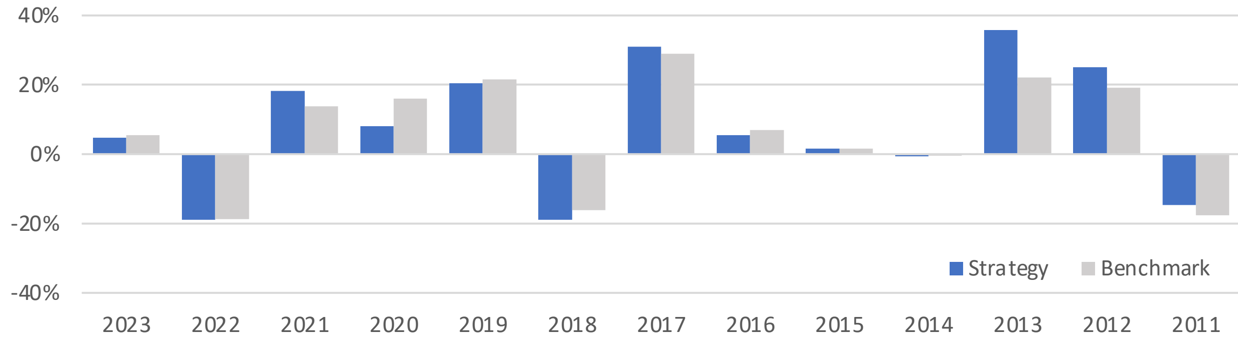
ARTICO Emerging Markets Strategy

Return %	YTD	Start
Strategy	4.1	53.2
Benchmark	1.8	12.3
PA Benchmark	-0.8	



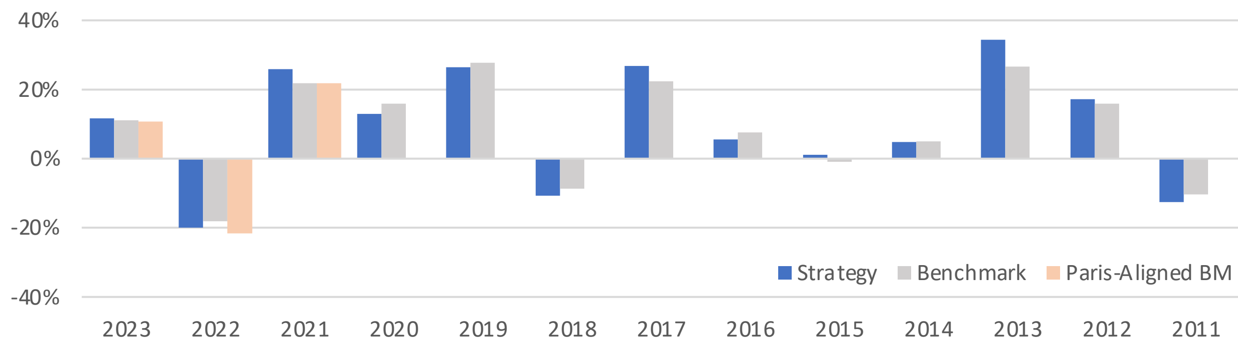
ARTICO Global Small Cap Strategy

Return %	YTD	Start
Strategy	4.8	114.4
Benchmark	5.4	91.9



ARTICO Global Equities Strategy

Return %	YTD	Start
Strategy	11.6	180.0
Benchmark	11.1	169.7
PA Benchmark	10.8	



Source: Data for ARTICO strategy from 30.06.2011 to 30.09.2023. “Benchmark” refers to **market-cap** weighted MSCI Indices, “PA Benchmark” refers to the **Paris-Aligned** benchmarks. Global Small Cap BM is a composite of 4 Regional MSCI SC Indices (each 25%). All benchmarks are total net return.

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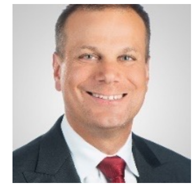

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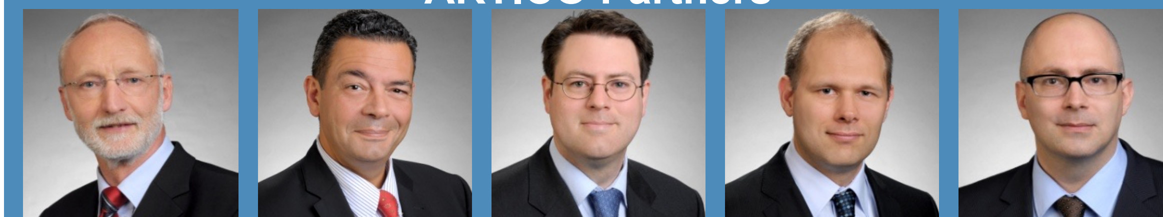

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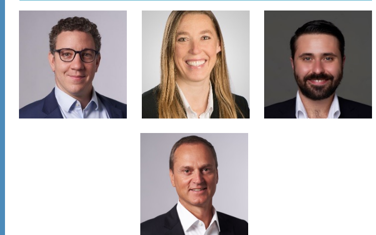

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