Sustainable investing: Helping clients navigate the ESG landscape

What is sustainable investing?

Sustainable investing aims to identify companies that offer potential for strong financial returns while also demonstrating a commitment to sustainable business practices and positive impact. Sustainability is often considered through analysis of environmental, social, and governance (ESG) policies, practices, and performance.

Interest in this type of investing has been growing, given increased acceptance that ESG considerations can affect an investment's performance and because of changing investor demographics and preferences.

Increasingly, investors are considering ESG risks and opportunities. Some are motivated to improve investment decisions, while others want to align their portfolios with their values and personal views.

Sustainable investing offers a range of different approaches and products. While there is no standard set of criteria for identifying ESG and sustainable investments, several common approaches are highlighted below:

- Exclusionary approaches focus on avoidance of certain companies or industries
- Integrated approaches seek to combine ESG data and analysis with other investment considerations
- Inclusionary approaches use ESG and sustainability analysis as a significant part of the investment process
- Impact approaches seek explicit goals for both financial return and social or environmental benefits

	Exclusionary	Integrated	Inclusionary	Impact
Investor intentions	"Avoid xyz"	"Sustainability is relevant"	"Sustainability is central"	"Impact is a primary goal"
Investment practice	Screening out	ESG consideration	ESG focus	Impact analysis
	SCREENING AND OPTIMIZING	CORE RESEARCH INTEGRATION	SUSTAINABILITY LEADERSHIP	SUSTAINABILITY SOLUTIONS
Research intensity	Lower	→	→	Higher
Tracking error	Lower	→	→	Increased
Alpha and impact potential	Bounded	→	→	Open-ended

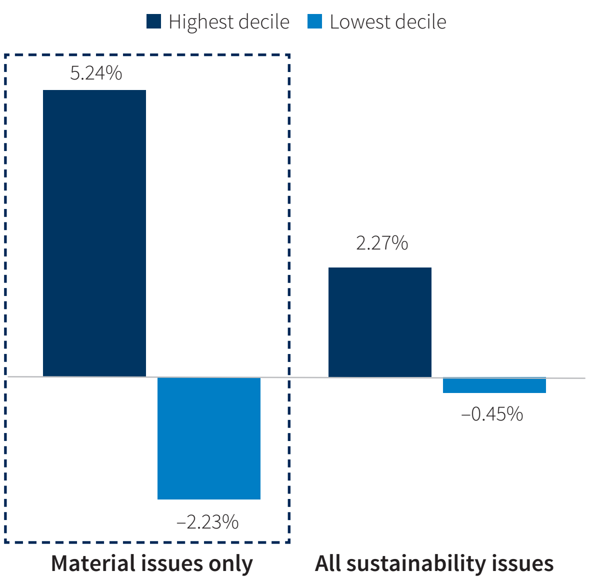
Source: Putnam. For illustrative purposes only.

Potential benefits of sustainable investing

- There is growing evidence within the asset management industry and within academia that ESG factors affect corporate financial performance
- A highly regarded study led by George Serafeim of Harvard Business School found that stocks of companies with strongest performance on material (financially relevant) ESG issues outpaced those with poor ESG performance
- Research also indicates that understanding and quantifying the key ESG issues that a company faces can result in better risk management and more sustainable business practices
- ESG factors can therefore be an effective risk indicator, as companies with poor ESG performance have been more prone to stock market underperformance, volatility, and bankruptcy risk

Focus on material sustainability issues

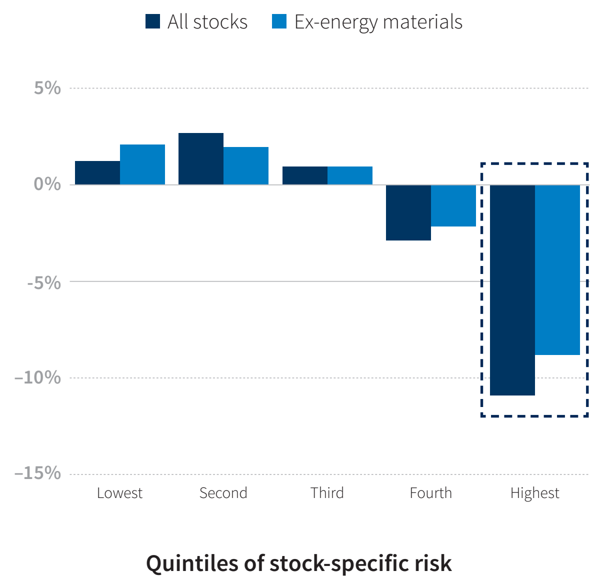
Highest ESG scores on material issues correlate with relative return



Source: Mozaffar Khan, George Serafeim, and Aaron Yoon (2016), "Corporate Sustainability: First Evidence on Materiality." Calculated using monthly calendar-time Fama-French regressions. Results shown are for value-weighted material and immaterial factors of firms scoring at the bottom and top deciles of the material index. The regressions are estimated from April 1993 to March 2014. Data set developed to measure firm investments on material sustainability issues by hand-mapping recently available industry-specific guidance on materiality from the Sustainability Accounting Standards Board (SASB) to MSCI KLD that has firm-level ratings on an array of sustainability issues. SASB considers material issues to be those with evidence of wide interest from a variety of user groups and evidence of financial impact. From the merged data, a materiality (immateriality) score for each firm-year that measures performance on material (immaterial) sustainability issues was calculated. Past performance is not a guarantee of future results.

Risk mitigation

High stock-specific risk and weak ESG disclosure can be a warning sign



Large-capitalization stocks in the worst quintile of the ESG score relative returns by quintile of arbitrage risk measured over one-year holding periods 2014 through mid-June 2017.

Source: Empirical Research Partners Analysts, June 2017. Most recent data available.

Third-party research is provided for illustrative purposes only, and no judgment or warranty is made with regard to suitability, accuracy, or timeliness of the content. It is not intended to be relied upon as a forecast, research, or investment advice, and is not a recommendation, offer, or solicitation to buy or sell any securities or to adopt any investment strategy. Consideration of ESG factors is no guarantee of investment success or positive performance. Generally, investments offering the potential for higher returns are accompanied by a higher degree of risk. As with any investment, there is a potential for profit as well as the possibility of loss.

ESG preferences questionnaire

The purpose of this introductory questionnaire is for your financial advisor to learn about you to build a potential portfolio that aligns with your unique preferences concerning environmental, social, and governance (ESG) issues and investing. This questionnaire provides an opportunity to work closely with your financial advisor to identify key areas of importance and highlight potential investment solutions that incorporate relevant ESG issues.

Client name(s):

Summary of investment objectives (return, risk, income & liquidity needs, time horizon):

1. How long have you been interested in ESG/sustainable investing?

- ○ Just starting
- ○ Less than one year
- ○ Several years
- ○ I am not interested

2. Why are you interested in sustainable investing? (Select all that apply.)

- ☐ Potential to add to performance
- ☐ Potential to mitigate risk
- ☐ Care about environmental issues and want my capital aligned
- ☐ Care about social issues and want my capital aligned
- ☐ Other:

For use by financial intermediaries and their clients.

3. Please rate the three broad categories below with a 1 (high importance), a 2 (medium importance), or a 3 (unimportant). Feel free to give the same ratings to different categories.

- ☐ Environmental (climate change; energy efficiency; pollution and waste)
- ☐ Social (gender and diversity; privacy and data security; human rights; labor practices)
- ☐ Governance (corporate behavior; board practices; accounting practices)

4. Which of the following key sustainability issues are you looking to consider incorporating into your investment portfolio? (Select all that apply.)

- ☐ Climate/Clean technology (decarbonization, renewable energy, energy storage)
- ☐ Environmental (sustainable agriculture, water quality and access, recycling)
- ☐ Governance and shareholder alignment (executive compensation, board diversity, accounting practices)
- ☐ Workers' rights (diversity, equal opportunity, inclusionary practices)
- ☐ Privacy and data security (data security, data privacy, data use, infrastructure security)
- ☐ Humanitarian and community investments (urban housing, medical, education)
- ☐ Other:

5. Which approaches to ESG/sustainable investing do you want to apply in your portfolio? (Select all that apply.)

- ☐ Strategies that seek to integrate ESG analysis within their investment process with a goal on understanding each company's sustainability strategy and how this is linked to financial performance
- ☐ Strategies that primarily utilize screens to "screen in" or select companies that score high in key ESG and sustainability concerns
- ☐ Strategies that exclusively apply screens to "screen out" companies that don't align with your key sustainability concerns
- ☐ Strategies that are focused on investing primarily in companies aligned to a specific sustainability theme

6. Are there any specific activities that you would want to minimize (less than 10%) in your investment portfolio (Select all that apply.)

- ☐ Fossil fuels ________%
- ☐ Tobacco ________%
- ☐ Gambling ________%
- ☐ Prisons ________%
- ☐ Weapons ________%
- ☐ Alcohol ________%
- ☐ Other ________%

7. What type of investment strategies are you looking to invest in? (Select all that apply.)

- ☐ Strategies that seek to primarily provide similar risk/return exposure as their respective performance benchmarks
- ☐ Diversified strategies that can invest across several key ESG and sustainable themes
- ☐ Thematic strategies dedicated to specific ESG and sustainable themes (water, clean energy, diversity)

8. Do you agree or disagree with the following statement? *I prefer to invest in strategies that integrate sustainability analysis as a key part of the investment process.*

- ○ Strongly agree
- ○ Agree
- ○ Disagree
- ○ Strongly disagree

9. Which best describes your preferred way to engage in ESG/sustainable investing? (Rank in order with 1 being the highest.)

___ ESG issues can impact both the risk and financial performance of a company, and therefore, I prefer to invest in strategies that seek to integrate these factors when they analyze stocks

___ I prefer to invest in strategies that identify growth opportunities among companies that are looking to provide solutions to key sustainability issues

___ Strategies that screen out companies that do not align or that score poorly in key sustainability issues are important to me

10. When considering among the different types of ESG strategies, do you assign a higher priority to returns or the specific ESG objective?

- ○ Return (includes both total and risk-adjusted)
- ○ ESG objective
- ○ Both are important

11. How important is it to you that your investment manager looks to engage with company management teams and corporate boards to address key sustainability issues?

- ○ Very important
- ○ Moderately important
- ○ Little relevance
- ○ No relevance

12. What are some key questions about sustainable investing that you would like to discuss with your financial advisor?

This material is prepared for use by financial intermediaries and their clients and is provided for limited purposes. This material is not personalized investment advice or an investment recommendation from Putnam and are intended for use only by financial professionals, with other information, as a resource to help build a portfolio or as an input in the development of investment advice for its own clients. The implementation of, or reliance on, a sustainable investing strategy is left to the discretion of the financial professional. Such financial professionals are responsible for making their own independent judgment as to how to use sustainable investing strategies. There is no guarantee that any investment strategy will be successful or achieve any particular level of results. The opinions expressed in this material represent the current, good-faith views of the author(s) at the time of publication. The views are provided for informational purposes only and are subject to change. This material does not take into account any investor's particular investment objectives, strategies, tax status, or investment horizon. Investors should consult a financial advisor for advice suited to their individual financial needs. Putnam Investments cannot guarantee the accuracy or completeness of any statements or data contained in the material. Predictions, opinions, and other information contained in this material are subject to change. Any forward-looking statements speak only as of the date they are made, and Putnam assumes no duty to update them. Forward-looking statements are subject to numerous assumptions, risks, and uncertainties. Actual results could differ materially from those anticipated. Past performance is not a guarantee of future results. As with any investment, there is a potential for profit as well as the possibility of loss.

Strategies that select securities based on sustainable investing ("exclusionary," "integrated," inclusionary," "impact") and environmental, social, and governance (ESG) or similar criteria may forgo certain market opportunities available to strategies or products that do not use these criteria. Because a portfolio's ESG investment criteria and/or proprietary framework may exclude securities of certain issuers for non-financial reasons, the portfolio may forgo some market opportunities available to portfolios that do not use these criteria or may be required to sell a security when it might otherwise be disadvantageous to do so. This may cause a portfolio to underperform the relevant market or other portfolios that do not use an sustainable investment strategy. In addition, there is a risk that the companies identified by the portfolio's ESG investment criteria do not operate as expected when addressing ESG issues. A company's ESG performance or investment manager's assessment of a company's ESG performance could vary over time, which could cause the portfolio to be temporarily invested in companies that do not comply with the portfolio's approach towards considering ESG characteristics. There are significant differences in interpretations of what it means for a company to have positive ESG characteristics. In making investment decisions, investment managers may rely on information and data that could be incomplete or erroneous, which could cause an investment manager to incorrectly assess a company's ESG characteristics. The third-party data providers may differ in the data they provide for a given security or between industries, or may only take into account one of many ESG-related components of a company. Furthermore, data availability and reporting with respect to ESG criteria may not always be available or may become unreliable.

A world of investing.®

Putnam Investments

For use by financial intermediaries and their clients.

Putnam Retail Management

Putnam Investments | 100 Federal Street | Boston, MA 02110 | putnam.com

II994_ESG 330976 11/22R1