ROCQ CAPITAL
MANAGEMENT LIMITED

Introduction to ESG or Responsible Investing

Environmental, Social and Governance ("ESG") investing has become increasingly popular in recent years. This comprises a range of approaches but at its heart the objective is to direct investment only to companies, governments or sectors that meet defined requirements with regard to their activities, impact on society or the environment or other factors that may be deemed socially important, such as corporate governance. For example, investors may choose to exclude oil producers on the basis of concerns over pollution levels, or only include in their portfolios those companies which have demonstrably committed to improving working conditions in their facilities. It is important that we understand each ESG fund's approach to this subjective area so that we can be comfortable that it is investing in an appropriate manner.

Whilst some ESG funds run exclusionary screens (arms or tobacco, for example) we want our investments to do more than that. For example, companies with a mixed record on environmental impact to date might have developed and implemented a clear strategy to improve their practices. By doing so, not only do they foster a more positive impact on society, they may also enhance their own returns. We want our managers to take appropriate exposure to those companies and not just buy the current best in class, which might limit the diversity of sectors and styles that we are seeking. Strict sector exclusions mean that in a different market environment the inability to invest in particular industries can impede a manager's ability to generate returns. Similarly, and somewhat cynically, larger companies have greater resources to manipulate a systematic ESG rating by ensuring certain areas score very highly to compensate for weaker areas; a qualitative, independent assessment by the investment manager can ensure these companies are avoided or scrutinised more closely.

We intend to use a combination of funds that we are familiar with, use in existing portfolios, and that have a consistent track record in their particular field.

In order to generate capital growth, we allocate a proportion of the portfolio to equity investments. Our focus within the equity allocation is to developed markets and particularly towards funds that invest in companies that are considered to be quality orientated, often have paid dividends consistently over time and have the opportunity to grow this income stream into the future. We think this applies to emerging market equities as well. We have focused on funds whose managers have good long term track records and that we expect to outperform their given benchmarks over a market cycle.

An outcome of ESG investing, particularly the Environmental aspect, means that many traditional 'value' sectors, e.g. mining, oil & gas, energy, are excluded from a lot of managers' investments. By investing some of the allocation into funds specifically focusing on environmental opportunities we keep some exposure to those sectors.

We have allocated a portion of the portfolio to funds that are more growth orientated with exposure to small and medium sized companies, looking for opportunities where there are prospects for rapid growth. This latter group of investments are consistent with the longer-term nature of the portfolio. It is important to note that this does not impact the liquidity of the portfolio as we are proposing to invest in instruments that all

offer daily dealing and our analysis has made us comfortable that the liquidity of the underlying securities matches the liquidity made available in the funds.

Within fixed income we allocate to both strategic managers who can invest across the sovereign, credit and geographic universe, as well as pure credit managers with an explicit focus within their investment universe. This provides a regular income, significant total return over a market cycle, as well as diversification to the equity allocation.

We also consider the allocation to alternatives to be much more defensive than equities as the correlation with equity markets is relatively low. There are not a large number of funds in this space which meet ESG requirements, often because they hold large numbers of securities so cannot provide assurance on the degree to which they adhere to particular standards. We hope to expand this allocation over time, as it is designed to provide consistent returns whilst notably reducing the overall volatility of the portfolio and provide a ballast in the case of either equities or bonds suffering a significant drawdown.

We will only pay fund fees where the fee is earnt by the manager. If we do not believe an asset class or sector displays enough inefficiency for a manager to add value, we will use an ETF instead. A consequence of this belief is that most of the equity funds will have 50 or fewer holdings in their portfolio (often considerably less), allowing their ability to pick winning companies to shine.

ESG Balanced portfolio example

The **asset class** breakdown for a Balanced ESG portfolio is shown below, along with typical ranges: