



**AUSTRALIAN  
GOVERNANCE & ETHICAL**  
Index Fund

# **Australian Governance & Ethical Index Fund (ASX: AGM)**

**Investment update**

**April 2019**

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# 1 Introduction

# Investment strategy and objective



## Overview

We aim to provide investors with relatively **lower cost, well diversified** exposure to domestic large capitalisation companies that exhibit **positive governance, social and environmental attributes**.

Primary focus on a corporations;

- Corporate governance frameworks;
- Commitment to overall corporate social responsibility; and
- Sustainability of operating practices including minimisation of environmental harm.

# Why focus on ESG?



## Our philosophy

We believe companies who exhibit superior governance, social and environmental (ESG) practices on average

Have more sustainable business models	Are less exposed to exogenous risk	Command a valuation premium
<ul style="list-style-type: none"><li>• More competitive due to better use of human capital and resources</li></ul>	<ul style="list-style-type: none"><li>• Better risk management and corporate governance</li><li>• Lower regulatory incidents and remediation costs</li></ul>	<ul style="list-style-type: none"><li>• Lower variation in operating performance and less exposure to systemic risk</li><li>• Superior market 'perception'</li></ul>

= **Better cash flow and profitability** + **Lower tail and stock specific risk** + **Higher valuation**

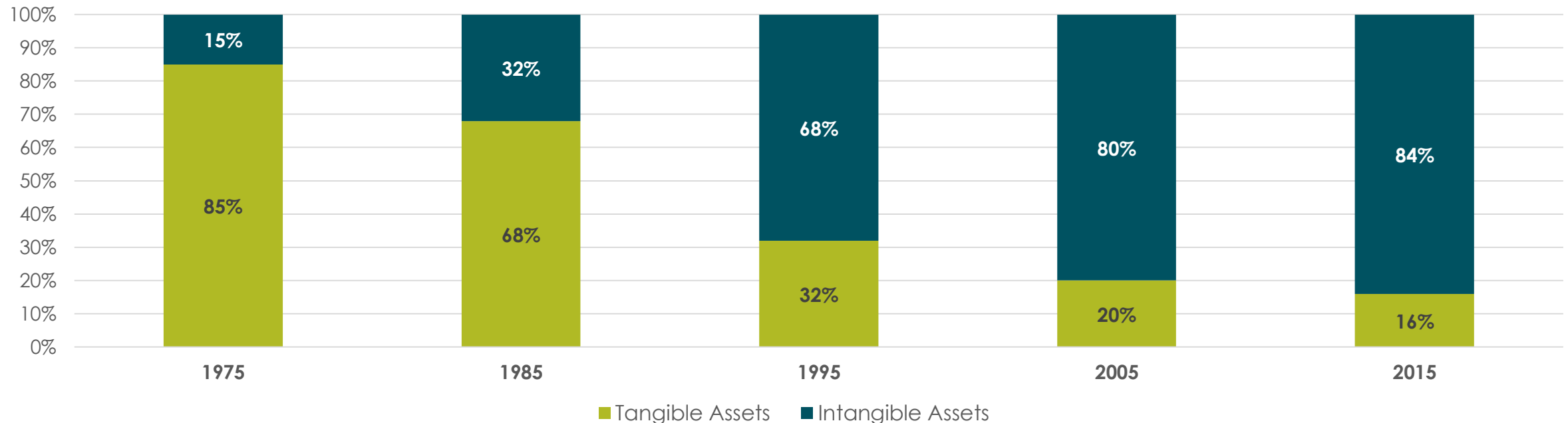
# Why is it important?

## Changing components of corporate value

Components of a corporation's "value" have changed over time. 'Non-financial' factors such as corporate culture and brand value are becoming increasingly important.



## Aggregate components of S&P 500 market value – 1975 - 2015



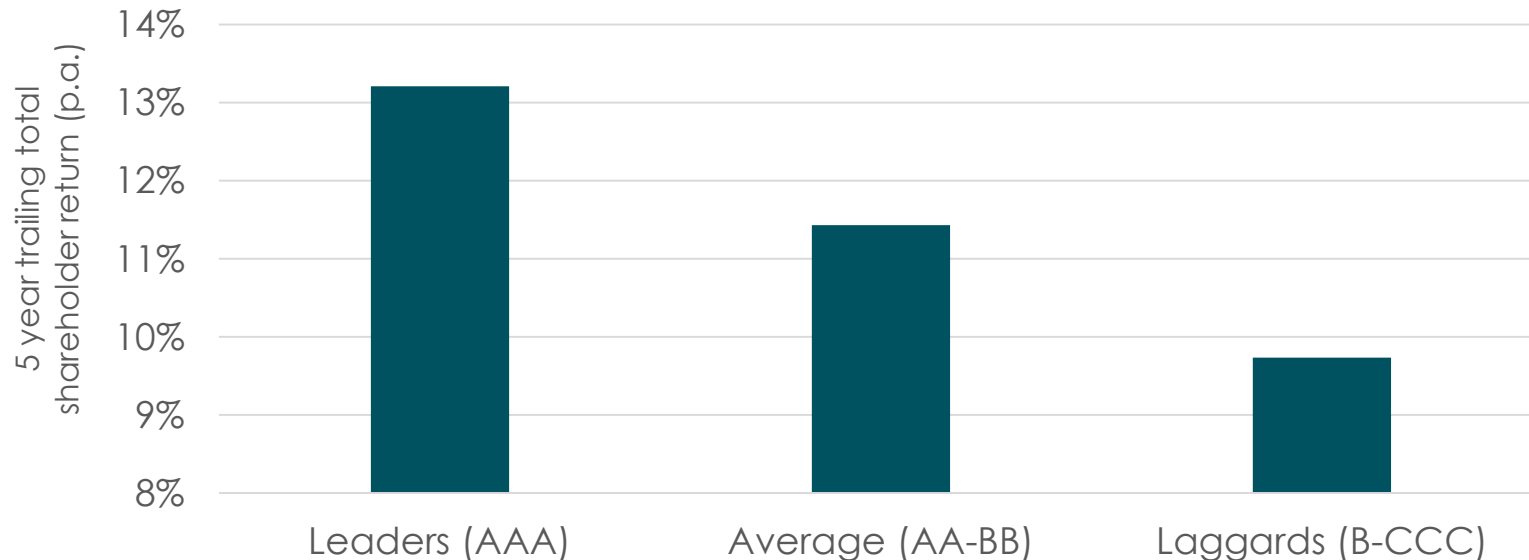
# Philosophy in practice



## Does ESG impact returns?

European markets are well ahead of global peers in terms of ESG integration and prove a practical example; we believe asset pricing domestically will follow a similar pattern.

### Median annualised total shareholder return by MSCI ESG Rating (1 January 2013 – 31 December 2018) – European MSCI ACWI constituents



- In Europe, ESG Leaders (AAA rated) have significantly outperformed peers over the last 5 years
- ESG leaders have **outperformed** ESG laggards over 5 years by:
  - 3.5% p.a. (median return)
  - 4.4% p.a. (average return)



## 2 Investment Process



# Portfolio Construction



## Negative Screen

S&P/ASX 100 Index

Screen investments with very high negative social or environmental impact

## ESG Analysis + Integration

Remaining securities analysed on the basis of +/- corporate governance, social and environmental performance

Apply materiality assessment overlay

## Positive re-weighting

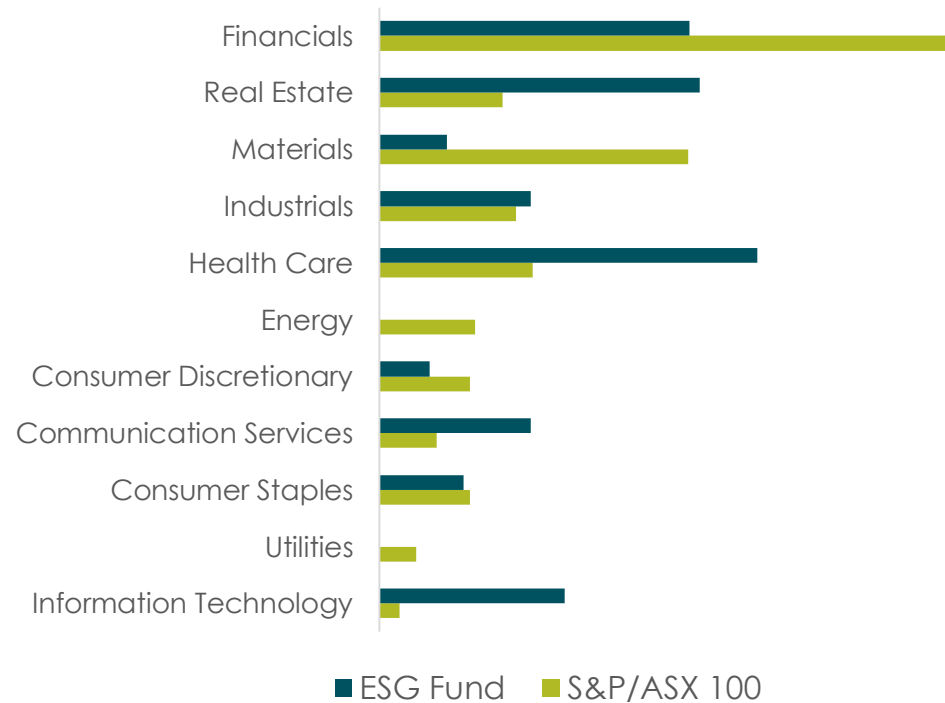
Identify and avoid **industry** laggards

Re-allocate capital to **industry** leaders

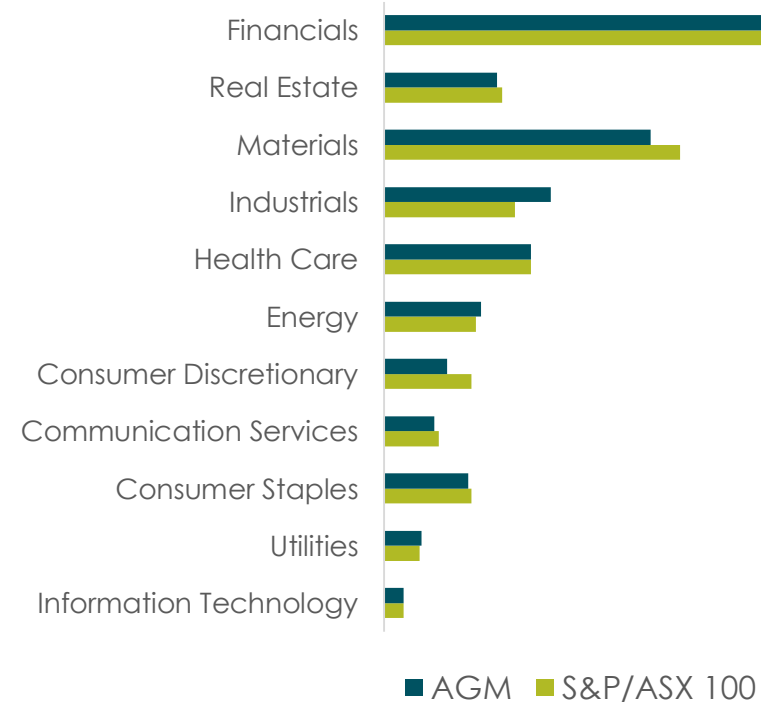
# Industry approach reduces sector bias



## Largest domestic ASX-listed ESG focused fund<sup>1</sup>



## Australian Governance & Ethical Index Fund



# Company measurement



Governance measurement driven by bottom up analysis.

- Governance analysis primarily based upon in-depth company and financial analysis through internal evaluation, industry consultants and investment network
- Process built through 8 years of experience and data from Australian Governance Masters Index Fund Limited (AQF)<sup>1</sup>
- Companies are analysed according to fundamental analysis of:
  - **Stewardship**; board quality, independence and diversity
  - **Accountability**; pay structure and materiality
  - **Ownership**; related parties and alignment
  - **Transparency**; reliability, timeliness, transparency and accuracy of financial accounts

# Company measurement



Social & Environmental analysis driven by industry based approach.

- Companies analysed according to key exposures within specific industry and business model
- Key **Social** considerations (among others)
  - Corporate culture
  - Operational health and safety, supply chain standards
  - Privacy & data security
  - Opportunities in nutrition & health
- Key **Environmental** considerations (among others)
  - Carbon emissions or carbon footprint
  - Environmental safeguards and remediation practices
  - Impact on natural capital (water efficiency, biodiversity and land use)
  - Evaluation of toxic emissions, waste creation and disposal practices



# 3 Portfolio positioning

# Portfolio positioning



## Largest active positions

### Top 10 (overweight)

A2 Milk Company

Rio Tinto

Cleanaway Waste  
Management

Sydney Airport

CSL

Unibail-Rodamco-  
Westfield

Macquarie Group

Woodside Petroleum

OZ Minerals

Worleyparsons

### Bottom 10 (underweight)

AGL Energy

Origin Energy

Amcor

Santos

Aristocrat Leisure

Sonic Healthcare

BHP Group

South32

Goodman Group

Treasury Wine Estates

# Corporate governance still key

Stewardship and accountability remain key tenants of our investment approach and we believe these are becoming increasingly reflected in share prices.



## IOOF board faces ASIC action

Three more AMP directors leave in wake of bank royal commission scandal

## Knives out for IOOF board

DECEMBER 07, 2018

**Source:** Australian Financial Review, The Australian, Australian Broadcasting Corporation Walsh & Company Asset Management, Factset, as at 31 March 2019  
*Historical Performance is not a reliable indicator of future performance*

Australian Governance & Ethical Index Fund Investment update

**AMP Limited (ASX:AMP) and IOOF Limited (ASX:IFL) 1 year total shareholder return (period ended 31 March 2019)**

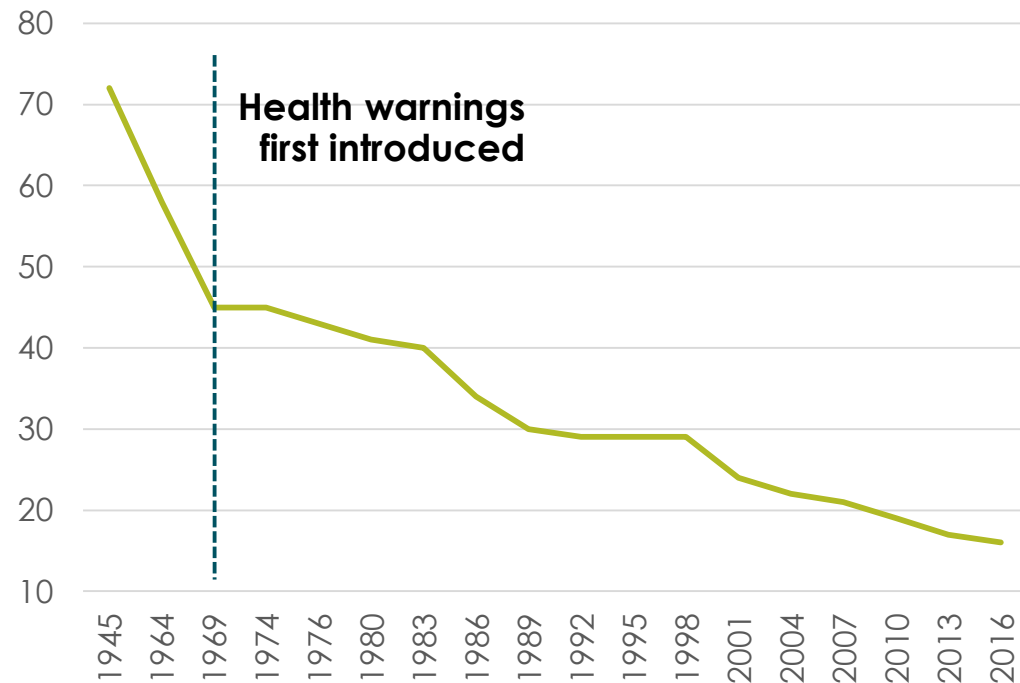


# Social impact changing behaviour

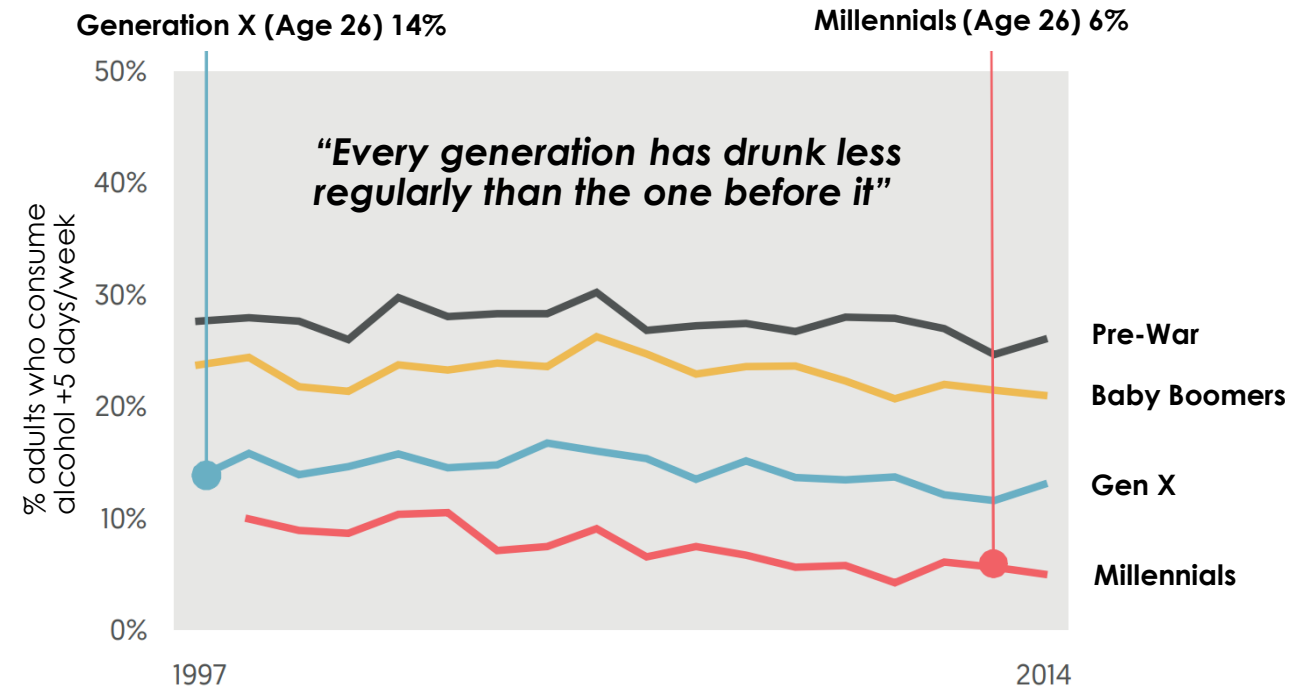
Generational change and social considerations are impacting consumer choices.



Percentage of current Australian smokers (male) (1945 – 2016)



Frequency of alcohol consumption by generation (1997 – 2014)



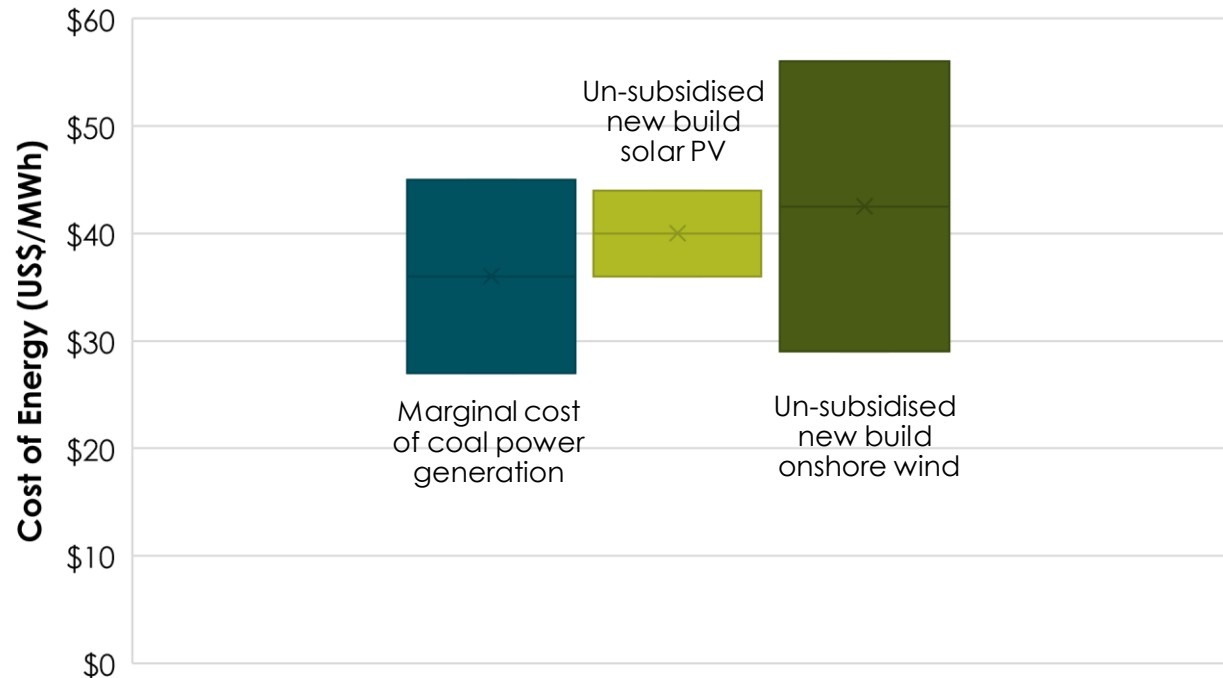


# The economics of power generation

Economics are rapidly changing, while the environmental impact of energy generation is becoming increasingly important.



**2018 Levelized cost of Energy Analysis version 12.0 (unsubsidised)**



**Mean unsubsidised levelised cost of energy (new build) and CO2 equivalent emissions**

	Estimated Cost (US\$/MWh)			CO2 Emissions	
	2009	2018	% Change	Tons/MWh	% Reduction (vs. Coal)
Coal	\$111	\$102	-8%	0.92	-
Gas (combined cycle)	\$83	\$58	-30%	0.51	-45%
Nuclear	\$123	\$151	+23%	-	-100%
Onshore Wind	\$135	\$42	-69%	-	-100%
Solar PV	\$359	\$43	-88%	-	-100%

# Stranded assets

Understanding both physical and transition risks.



IEEFA | March 26, 2019

Switzerland's UBS says it no longer will finance new coal-fired plants

— — — Exclusive

**QBE to abandon thermal coal by 2030**

**Glencore moves to cap global coal output after investor pressure on climate change**

**BNP Paribas fund arm plans €1bn coal divestment**

French asset manager is latest company to reduce fossil fuel exposure

## Selected Australian coal fired power stations

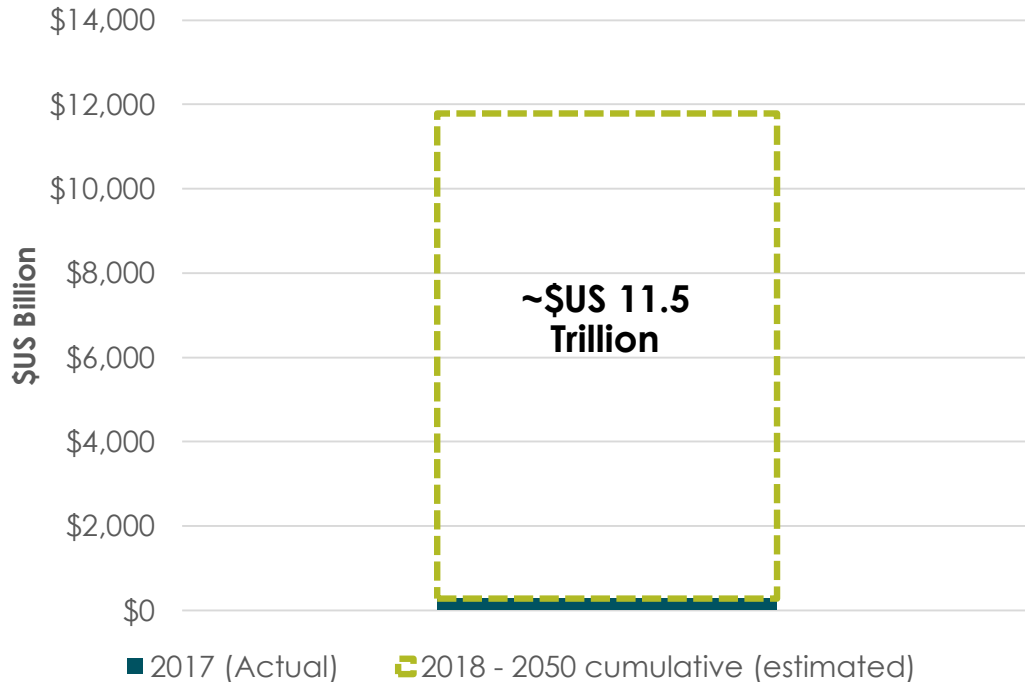
Station	Output (TWh)	Scope 1 Emissions (t CO <sub>2</sub> -e)	% of total sector emissions	Estimated useful life (years)	Owner
Liddell	8.5	7.8m	5%	3	AGL
Yallourn	10.2	13.7m	8%	5-9	Energy Australia
Gladstone	9.0	8.5m	5%	10	Consortium
Vales Point	8.1	7.0m	4%	10	Sunset Power
<b>Eraring</b>	<b>17.2</b>	<b>14.8m</b>	<b>9%</b>	<b>13</b>	<b>Origin</b>
Tarong	12.1	10.4m	6%	16	QLD Gov't
Stanwell	8.8	7.6m	5%	24	QLD Gov't
<b>Bayswater</b>	<b>15.5</b>	<b>13.7m</b>	<b>8%</b>	<b>16-26</b>	<b>AGL</b>
Loy Yang B	8.9	10.1m	6%	28	Chow Tai/Mitsui
<b>Loy Yang A</b>	<b>17.0</b>	<b>19.8m</b>	<b>12%</b>	<b>29</b>	<b>AGL</b>

# Renewables origination and financing

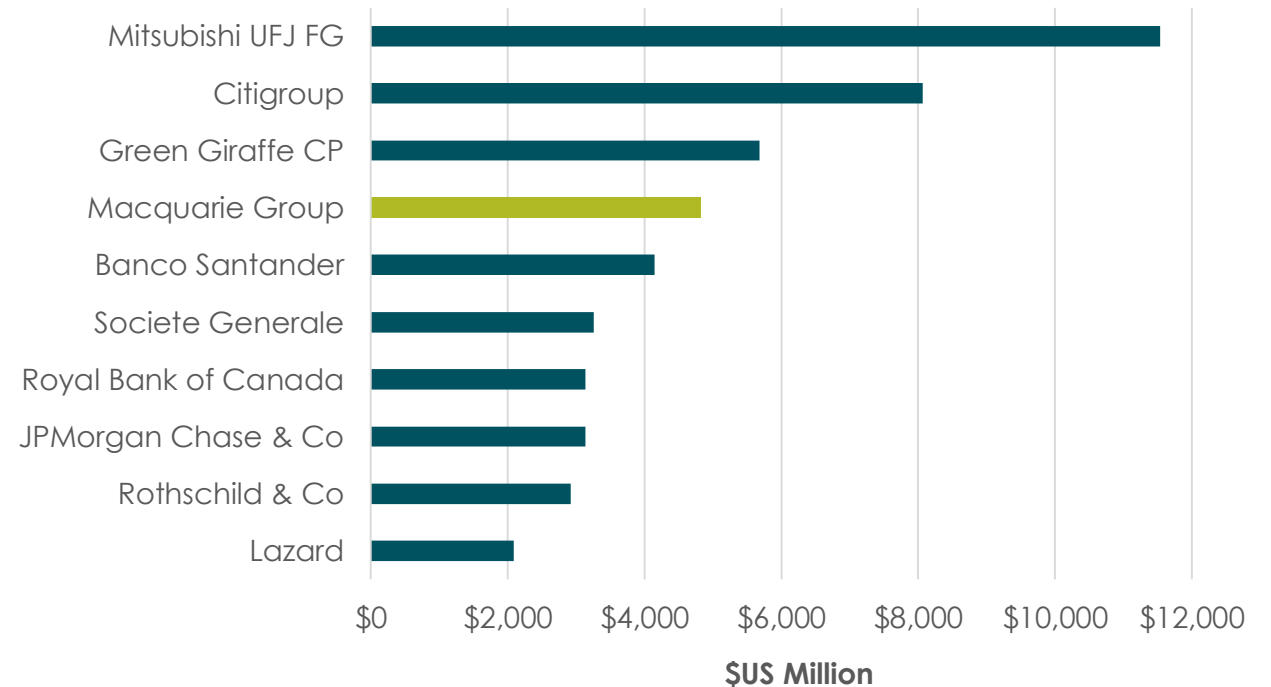


With a change in economics green energy investment is expected to grow exponentially; where are the opportunities?

**Estimated new renewable energy capacity investment (2018-2050)**



**Global renewable energy investment – Asset finance financial advisory by total deal flows (2017 - current)**

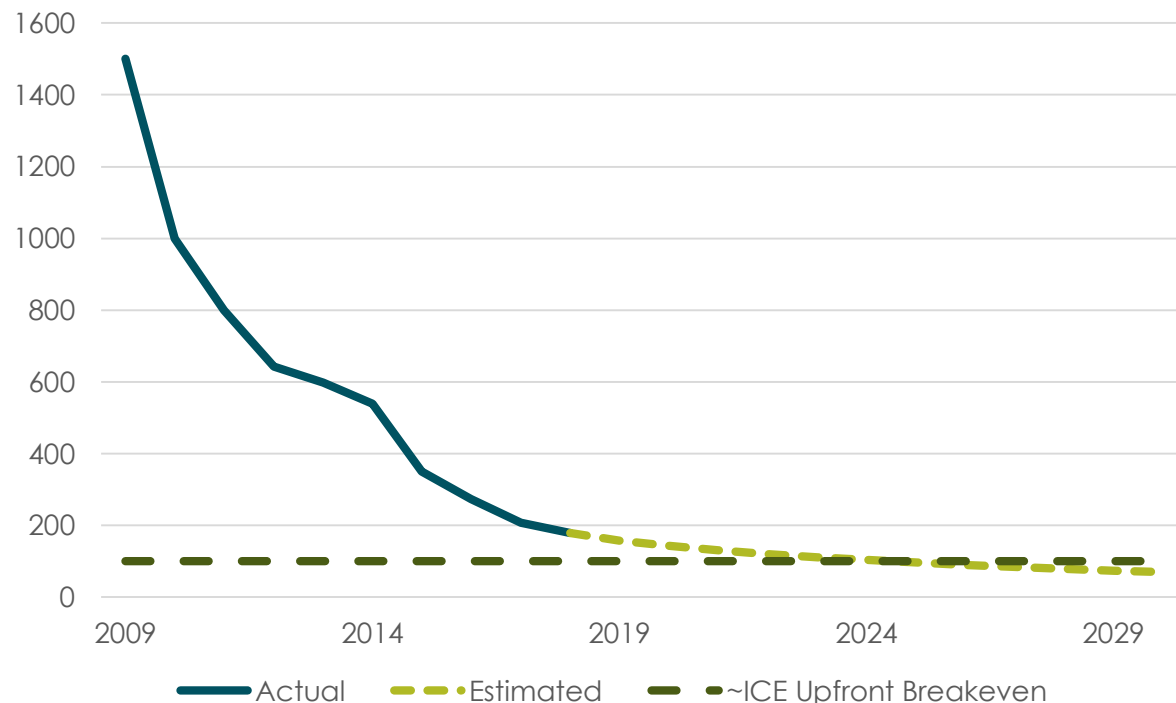


# Electrification of the transport industry

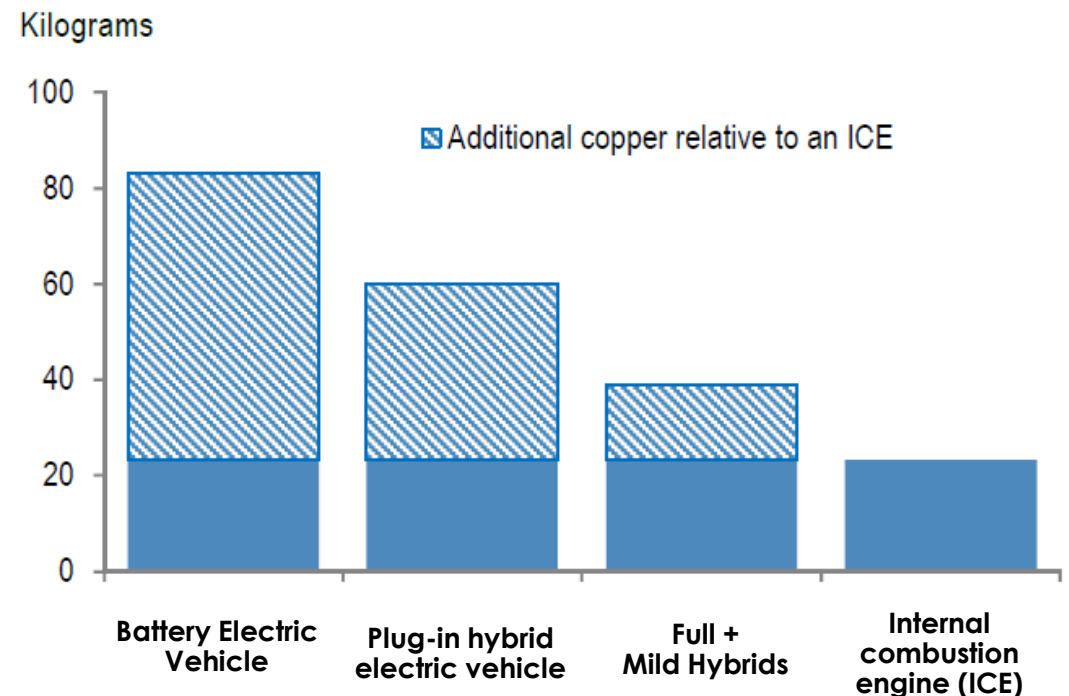


Declining battery prices are expected to drive electric vehicle adoption. We are cognisant of changing material demands.

## Average price of lithium ion batteries (US\$/kWh)



## Copper contained in light vehicles by powertrain

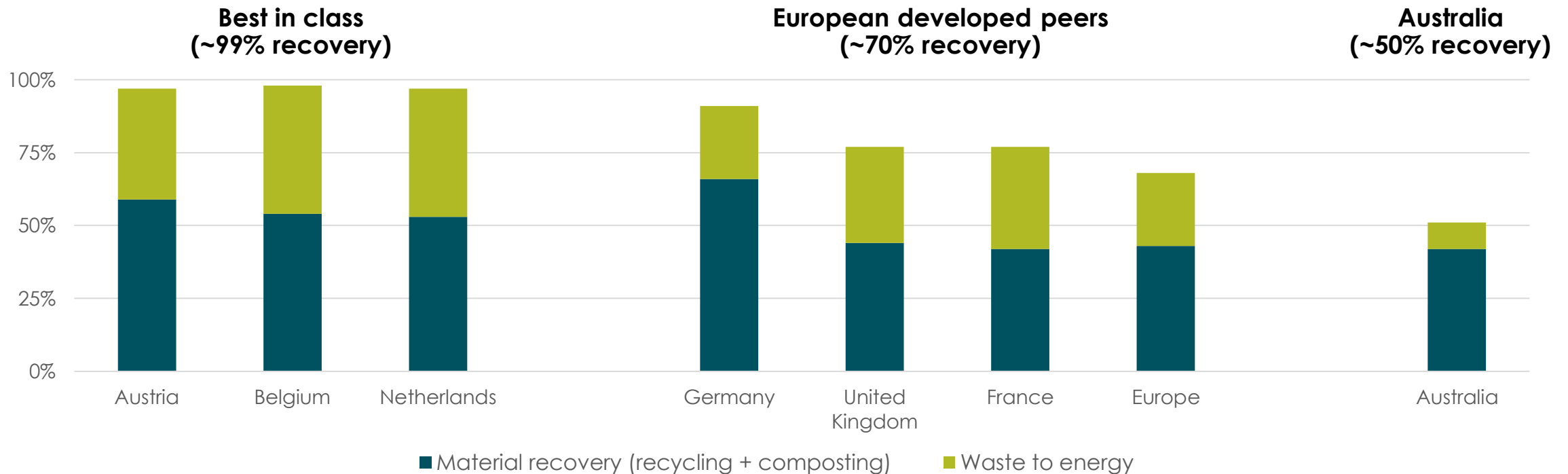


# Recycling and waste management

Opportunity for incumbent players; domestic recovery rates well behind peers.



## Recovery rates of municipal waste (selected countries)





# 4 Overview

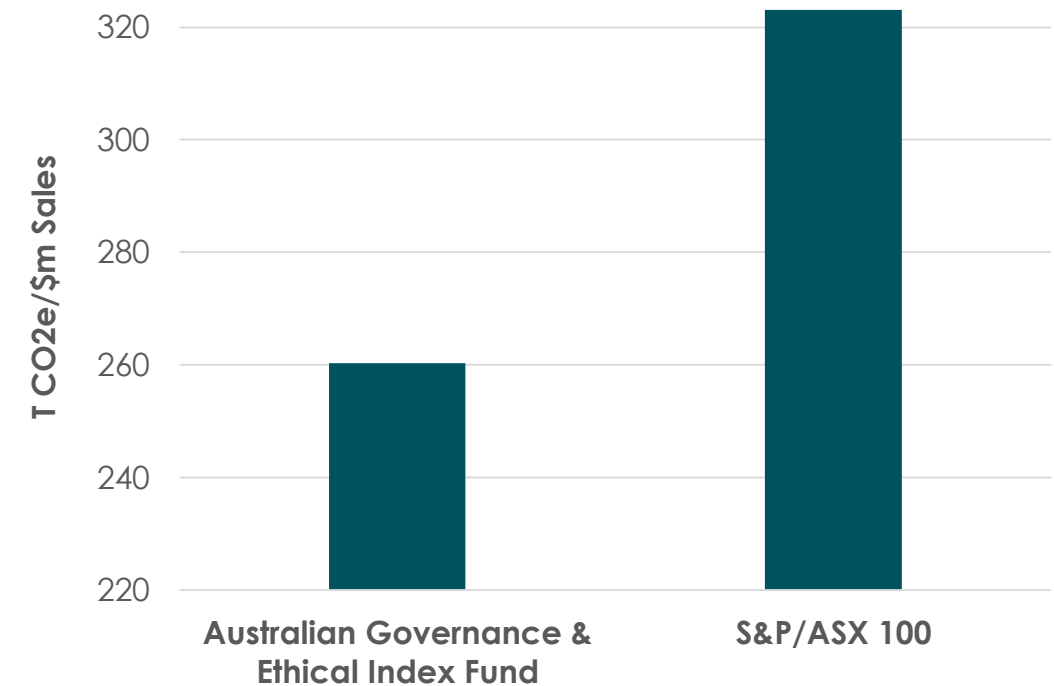
# Portfolio characteristics

## Australian Governance & Ethical Index Fund vs S&P/ASX100 Index

As at 31 March 2019

	AGM	S&P/ASX 100
Holdings	77	100
Dividend Yield	4.5%	4.5%
Price/Earnings	15.7x	16.3x
Price/Book	2.0x	2.0x
ROA	7.1%	6.3%
3-5 Year EPS Growth	5.4%	5.5%

## Weighted Average Carbon Intensity (t CO2e/\$m Sales)



# Competitive fee structure



## ASX-listed Australian equity focused responsible investment products

Code	Name	Management	Market capitalisation	Total Ongoing Fees
FAIR	BetaShares Australian Sustainability Leaders ETF	Passive	\$255 million	0.49%
RARI	Russell Investments Australian Responsible Investment ETF	Passive	\$113 million	0.45%
UBA	UBS IQ MSCI Australia Ethical ETF	Passive	\$192 million	0.17%
<b>AGM</b>	<b>Australian Governance &amp; Ethical Index Fund</b>	<b>Active</b>	<b>\$45 million</b>	<b>0.19%</b>

**Source:** Walsh & Company Asset Management, Company reports, as at 15 April 2019

**Notes:** Ongoing fees include management fees and estimated other costs



# Investment performance



## Australian Governance & Ethical Index Fund (AGM) – 31 March 2019

	1 Months	3 Months	6 Months	1 Year	3 Year (p.a.)	Since Inception (p.a.)
AGM	0.9%	10.8%	2.3%	-	-	3.4%
S&P/ASX 100 Accumulation Index	0.8%	10.7%	2.2%	-	-	2.1%
<b>Excess Return</b>	<b>+0.1%</b>	<b>+0.1%</b>	<b>+0.2%</b>	-	-	<b>+1.3%</b>

**Source:** Walsh & Company Asset Management, Bloomberg  
Historical performance is not a reliable indicator of the future performance. AGM Inception date 10 July 2018  
AGM performance numbers are total returns based on Net Tangible Asset values, inclusive of distributions and net of fees and costs.

# Our team



**Ian Watt, AC**

Advisory committee member

Former Secretary of the Department of the Prime Minister and Cabinet, Department of Finance and Administration

Citigroup Australia and Grattan Institute Board Member



**Josephine Tan**

Advisory committee member

UK based founder, CFO and COO, Sandown Bay Resource Capital

Previously Senior Investment Banker at UBS AG



**Nerida Cole**

Advisory committee member

Managing Director, Head of Advice at Dixon Advisory

Member of the Financial Services Council Advice Board Committee



**Will Hart**

Portfolio Manager

Prior roles across Evans Dixon in research and capital markets

BComm (Melb), MAppFin (Macq)



**Matt Baillie, CFA**

Senior Performance Analyst

Prior roles at CFSGAM and in small cap broking as an analyst/dealer

BEng, BComm (Syd), CFA