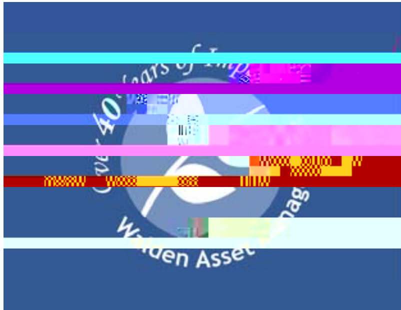
we asked **Emerson Electric** to adopt time-bound, quantitative goals for reducing GHG emissions consistent with the goals of the Paris Agreement. The resolution garnered 39 percent support, up from 34 percent in 2017, sending a strong signal to management of widespread investor support.



ESG Research & Engagement Brief

First Quarter 2018

While the return of volatility is a fitting headline for financial markets in early 2018, we are pleased to report a steady-state of progress in our efforts to advance more sustainable business policiesfranchisees to reduce absolute GHG emissions from its restaurants and offices by 36 percent by 2030 relative to 2015 levels. Additionally, it committed to a 31 percent reduction in emissions intensity (per metric ton of food and packaging) across its supply chain within the same timeframe. These targets were affirmed by the Science-Based Target Initiative, a partnership of CDP, UN Global Compact, World Resources Institute, and World Wildlife Fund, which described this groundbreaking commitment as "charting a course for sustainable growth." McDonald's also joined the "We Are Still In" declaration of businesses, investors, states, cities and other stakeholders who stand by the Paris Agreement despite the announced departure of the United States. Having been involved in formal stakeholder advisory groups as well as private discussions with McDonald's addressing climate change, SBTs, and other issues for many years, we commend the company's extraordinary leadership and encourage other companies to follow suit.

American Water Works recently set a robust GHG emissions reduction target with its commitment to reduce emissions 40 percent by 2025 from a 2007 baseline. This company is included in a collaboration co-led by Walden and the Interfaith Center on Corporate Responsibility (ICCR) that is encouraging more than one hundred companies to adopt science-based targets.

EQUALITY

The wind is at our back with respect to engagement on workplace equality. We are helped by the endurance of the #MeToo movement as well as the proliferation of research, like S&P Global's "The Key to Unlocking U.S. GDP Growth? Women," that articulates a strong business case for making full use of our country's diverse human capital. This work takes several forms at Walden: advocating for greater board diversity; seeking disclosure of workforce composition data to hold companies more accountable for hiring, retaining, and promoting women and people of color; and assuring strong workplace protections for lesbian, gay, bisexual, and transgender (LGBT) employees. In each area, Walden has seen meaningful progress.

Board Diversity: The Nominating Committee Chair at **Valmont Industries** wrote to us to report on its January appointment of two new directors, one of whom is a woman. The Committee Chair also reported that another woman director will be added in April following the retirement of the lead director. In addition, Valmont expanded proxy disclosure on board diversity to affirmatively state that gender, race, and ethnicity of director candidates are considered in the nominating process. **Amdocs** elected a woman and a Hispanic man to its board of directors in January, and **Dentsply Sirona** recently added a woman director as well. **Tanger Factory Outlet Centers** updated its corporate governance policies to explicitly reference gender, race, and ethnicity as factors considered in director nominations.

Workforce Data Disclosure: Walden withdrew our resolution requesting disclosure of workforce composition statistics at **Dollar General**. The company agreed to report annually

OUR PORTFOLIO CARBON FOOTPRINTS

For the fifth consecutive year, we are pleased to disclose carbon footprint metrics of representative client portfolios. Our disclosure has expanded over time to include additional strategies and the majority of assets under management. This year we introduce a new metric—the weighted average carbon intensity—and analyze the carbon reduction commitments of companies in the Large Cap portfolio.

Weighted Average Carbon Intensity (tCO_2e/$million sales)
as of 12/31/17

average carbon intensity that is about 80 percent less than their benchmarks. In both cases, stock selection, in contrast to sector allocation, accounts for most of the outperformance. The SMID and Mid Cap benchmarks are replete with carbon intensive utilities and energy companies. In contrast the top two contributors to the Mid Cap portfolio's emission intensity, **Consolidated Edison** and **Eversource**, are highly carbon efficient relative to most utilities because they do not produce electricity, but rather focus on transmission and distribution. Similarly, **Helmerich & Payne** is far more carbon efficient than many companies in its sector, which includes oil and gas producers that have more carbon-intensive business models.

Air Products, **Praxair**, and **Union Pacific** are among the largest contributors to the Large Cap and Fossil Fuel Free (FFF) Large Cap portfolios' carbon intensity. Both Praxair and Air Products are carbon intensive industrial gas companies but their products enable customers to be more carbon efficient—a factor that is not reflected in the metric.[1] While carbon intensive, railways are a relatively carbon efficient method of transportation. According to the Rocky Mountain Institute, the average freight train has an efficiency of 400 ton-miles per gallon whereas trucks average about 130 ton-miles per gallon.

Readers might be surprised that the carbon intensity of the FFF Large Cap portfolio is slightly higher than the unrestricted Large Cap portfolio. This result reflects another shortcoming of the intensity metric: namely, the measure does not capture emissions associated with the use of products. The FFF strategy would appear superior if the metric included the emissions associated with the use of the oil produced by **ConocoPhillips** and **Apache**, holdings in the Large Cap portfolio. Our analysis indicates that the carbon intensity of the Large Cap portfolio would increase to 221 metric tons of CO_2 equivalent per million dollars of revenue, compared to 126 for the FFF portfolio, if emissions associated with burning the oil brought to market by these fossil fuel companies were included.

Company Carbon Reduction Commitments

In addition to not accounting for emissions associated with the use of products, carbon footprint metrics typically capture the carbon intensity of a company at a past moment in time, but do not indicate a company's intention (or lack thereof) to reduce its greenhouse gas (GHG) footprint in the future. To address the backward-looking nature of the metrics, we researched the companies in our Large Cap portfolio for public commitments to reduce GHG emissions. This research complements and informs our climate advocacy work asking all companies to set emissions reduction targets that limit warming to 2 degrees Celsius above preindustrial levels. We focused on large cap companies since their emissions tend to be significantly larger than smaller cap companies.

As part of our climate advocacy work, we ask companies to set emissions reduction targets. If the companies meet their stated reduction targets, the climate-related risk implied by the weighted average carbon intensity metric may be less than it appears.

Forty-seven of sixty-six companies in the portfolio as of December 31, 2017 have either an absolute or intensity-based (emissions normalized by sales, production volume, or something similar) GHG emissions reduction target. The varied degree of ambition among these targets is as varied as the companies themselves. Among companies with emissions exceeding one million tons per year, **3M** committed to reduce emissions by 50%, **Johnson & Johnson** by 80%, **PepsiCo** by 20% (inclusive of its value chain), and **Google** and **Microsoft** set goals of carbon neutrality. The heaviest emitters in our portfolio have also committed to reductions, albeit on a more modest scale. **ConocoPhillips** announced a new emissions reduction target in 2017, and **Praxair**, **Union Pacific**, and **United Parcel Service** have all committed to improve the carbon intensity of their operations. If the companies meet their stated reduction targets, the portfolio climate-related risk may be less than it appears based on the weighted average carbon intensity metric alone.

In addition to the recommended use of a weighted average carbon intensity metric, the TCFD provided a comprehensive climate risk disclosure framework, including specific guidance for asset managers. Stay tuned for a publication aligned with the TCFD framework.

[1] For a more detailed discussion of the challenges associated with carbon footprint metrics see: http://waldenassetmgmt.com/wp-content/uploads/2017/10/CarbonFootprinting-Feb2016.pdf.