



A Value Manager's Take on Disruption: ESG at Causeway

March 2021

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Signatory of:



The Rising Priority of ESG

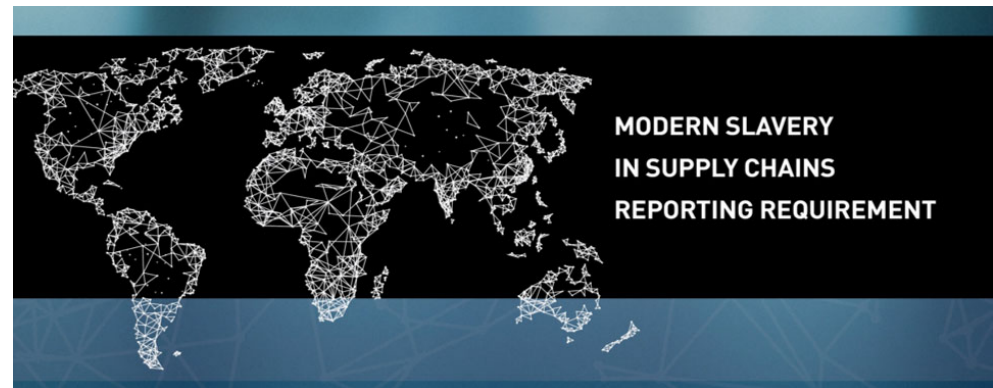
ESG Is Driving Policy, Consumer, and Corporate Priorities...

“By early next year, countries representing more than 65% of global carbon-dioxide emissions...will have made ambitious commitments to carbon neutrality” - UN Secretary General Antonio Guterres, 12/2/2020

A European Green Deal

Striving to be the first climate-neutral continent

The European Green Deal is our plan to **make the EU's economy sustainable**. We can do this by turning climate and environmental challenges into opportunities, and making the transition just and inclusive for all.



Australia Modern Slavery Act 2018

An Act to require some entities to report on the risks of modern slavery in their operations and supply chains and actions to address those risks

Sources: Australia's Federal Register of Legislation, European Commission, UN

Why Should Investors Pay Attention to ESG?

- > Causeway believes material ESG factors have the potential to impact a company's return and risk characteristics

- > This view is supported by
 - Structural drivers of global ESG trends
 - Consumer and investor preference
 - Policy and regulatory attention
 - Potential liability
 - Companies' response to these trends

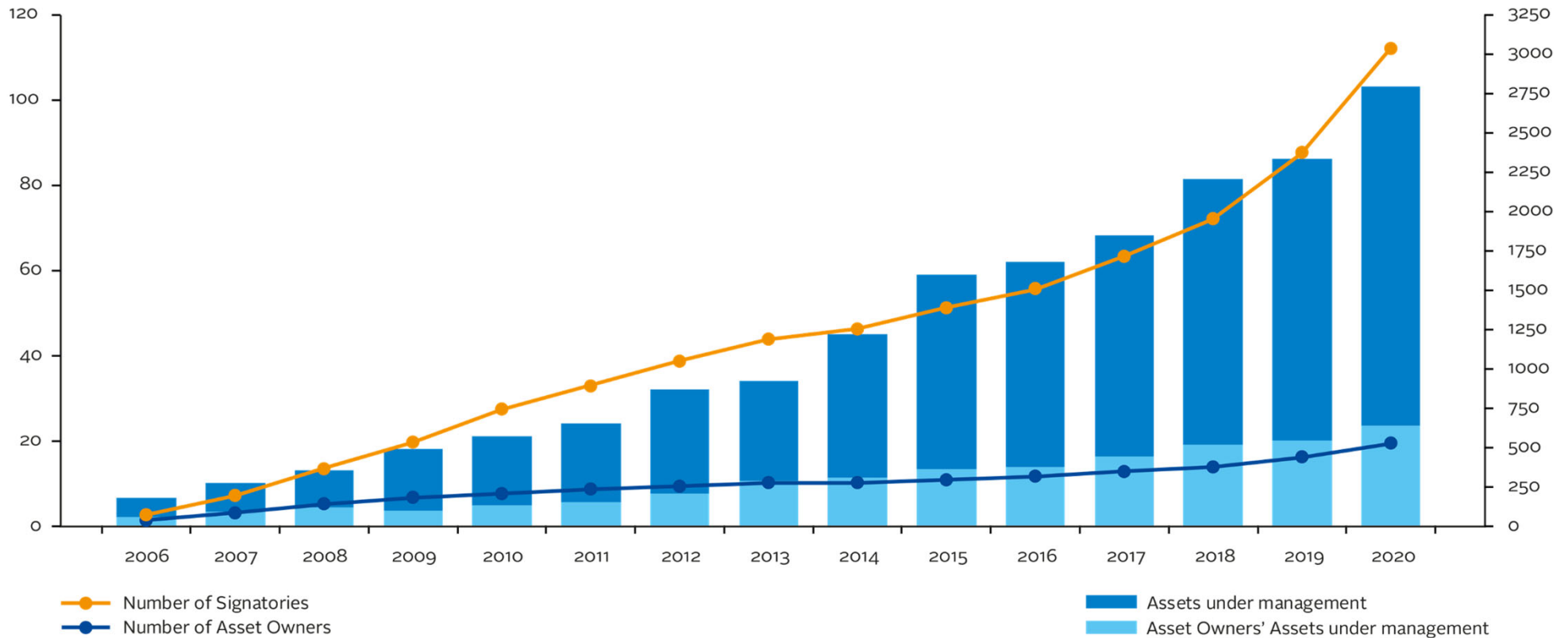
 - Research documenting a positive relation between ESG characteristics and return performance

Many Already Are!

UN PRI SIGNATORIES HAVE OVER \$100 TRILLION IN ASSETS UNDER MANAGEMENT

Assets under management (US\$ trillion)

N° Signatories



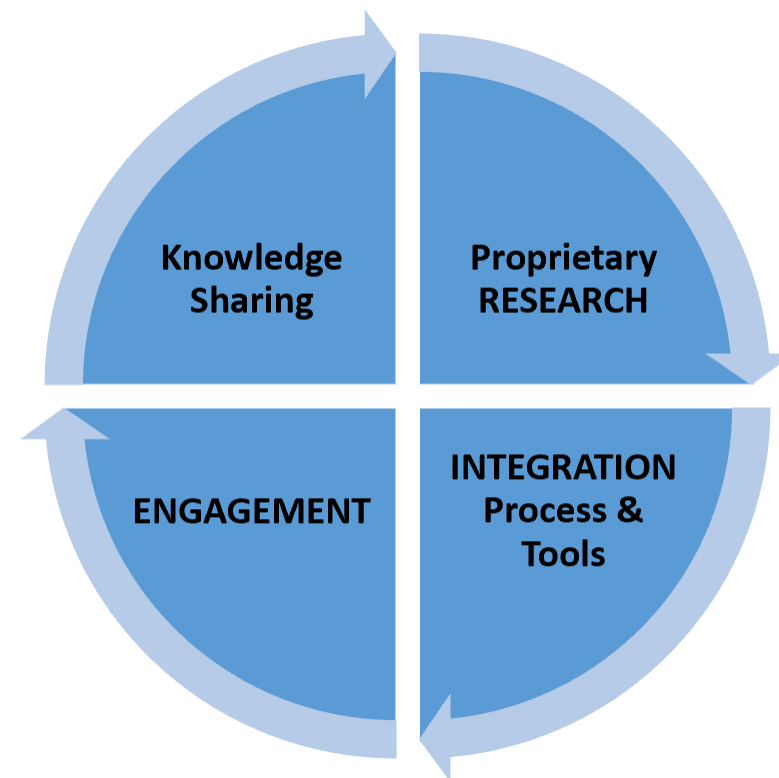
Source: UN PRI

Causeway's Approach to ESG

How Does Causeway Approach ESG?

- > Objective is to develop a differentiated source of alpha
 - Proprietary ESG scores that have the potential to predict return performance

- > There are four elements of our ESG approach:
 1. Research
 2. Integration
 3. Engagement
 4. Knowledge sharing



Causeway Research

> Frameworks

- Develop differentiated frameworks to organize thinking, by studying academic and other literature and engaging with companies
- E.g., new corporate governance framework published in the CFA Institute *Financial Analysts Journal* (Issue 4, 2019)

> Key issues

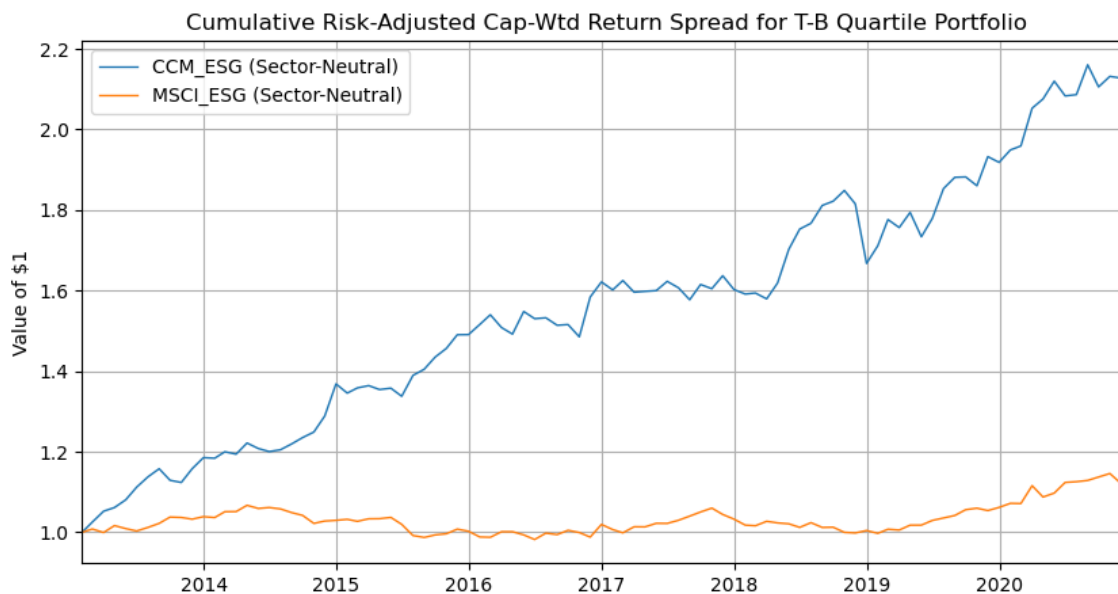
- Identify key issues to focus differentiated measurement efforts. E.g., under S, we identified modern slavery and diversity as key issues
- Capture the breadth of ESG issues by adding comprehensive ESG ratings from external providers

> Alpha signals

- Construct and backtest new alpha signals and factors, by identifying economic implications of ESG issues and developing novel measurement proxies

Causeway Research Offers Potential for Outperformance

- > A hypothetical Portfolio constructed using the Causeway ESG score outperformed that using the MSCI ESG score
- > Cumulative risk-adjusted returns for two portfolios in ACWI ex-CN* are depicted
- > Each portfolio is long the top quartile, and short the bottom quartile, of (sector-neutralized) ESG scores ¹



Graphs sourced from Causeway research; MSCI ESG data from MSCI ESG

¹ See Disclosures for notes. Note that Causeway does not currently manage portfolios based solely on ESG scores.

*Based on Causeway analysis, China has a unique blend of policy intervention and free markets that has seen unprecedented stock market performance with generally lower ESG scores on average

Causeway Research Led to Development of Proprietary ESG Metrics

- > Environmental score considers, for example, climate change transition, circular economy, and adaptive capacity
- > Social score considers, for example, modern slavery risks in the supply chain and operations
- > Governance framework considers, for example, top-down factors such as the strength of institutions and shareholder protection, and bottom-up factors such as auditor and board characteristics, executive compensation alignment, and minority investor protection

Integrating ESG Research at Causeway

From Research to Integration: ESG Navigator

- > Based on our research, we developed ESG scoring frameworks, and identified potential alpha signals
- > That research led to the development of proprietary ESG scoring applications used by all Causeway fundamental analysts
 - A snapshot of the Corporate Governance Navigator is shown
 - Includes top-down and bottom-up components
 - Enables quantitative and fundamental analyst inputs
- > The governance score is saved to our security rank sheet
 - The score is part of fundamental investment memos, and is an input into building a holistic picture
 - Governance scores are monitored exposures for all holdings

Causeway Corporate Governance Assessment Model

Ticker: [] Total Score (0-10): **7.4** Portfolio Score: [] Sector / Region Avgs: []

Buttons: Load Data, Get Score, Publish Score, Last Published Score, Help, Quit

Top Down/Country Factors

Effective HQ Country: Japan Top Down Score (0-3): **2.62**

Shareholder Orientation: 3

Bottom Up Factors

Ownership Concentration: Low Bottom Up Score (0-7): **4.81**

Category	Score	Factor	Questions	Answers
Audit		Quality	The auditor is one of, or affiliated with, Deloitte, PwC, EY, KPMG	True
		Independence (A)	The company pays its auditor less for non-audit than for audit services	True
Board		Independence (B)	The company has a separate CEO and Board Chair	True
		Competence	The audit committee does NOT include any current or former company executives	True
		Presence	The audit committee has a financial expert The audit committee has an industry expert	True
Compensation		Pay for Performance	The board has NO directors that serve on four or more corporate boards total All board members attended at least 75% of board and committee meetings	True
		Skin in the Game	I do NOT have concerns about CEO pay-for-performance In FY2018 (March 2019) CEO earned 1.758B JPY, of which 269M JPY was base compensation, 638M JPY was bonus and 851M JPY was related to long-term incentives. Goals are based on revenue, operating free cash flow, earnings per share and targeted R&D goals	False
Shareholder Rights		Director Selection	I do NOT have concerns about CEO equity ownership (i.e. Inadequate ownership; excessive selling) CEO owns 293.6K shares, of which 145.4K are shares scheduled to be issued pursuant to equity-settled share-based compensation plans; ownership appears insignificant relative to other pharmaceutical CEOs	True
		Voting	The board is NOT staggered Cumulative voting is allowed	False
Integrity Multiplier		Company Integrity	Shareholders have the right to call a special meeting or to action by written consent	True
			My concerns about forward impact of realized or potential leadership lapses are: Following [], company remains focused on de-levering have taken net leverage down from >5x to <4x in FY2Q:19; committed to stable dividend, would entertain opportunistic buybacks; still reliant on external activity to enhance R&D efforts	Moderate

Additional Comments (Optional): []

From Research to Integration: ESG Navigator

- > In the last year we have developed, and just launched, Environmental and Social scoring applications used by fundamental analysts
 - A snapshot of the Environmental Navigator is shown
 - Includes top-down and bottom-up components
 - Enables quantitative and fundamental analyst inputs

The screenshot displays the ESG Navigator interface. At the top, there is a search bar for the company name and a button for the 'MSCI ESG Ratings Report'. To the right, a summary of scores is provided: Total Environmental Score: 5.58, Total Social Score: 8.1, Total Governance Score: —, and Total ESG Score: —. Each score has a 'Print' and 'Publish' button. Below this, there are tabs for 'ENVIRONMENTAL SCORE', 'SOCIAL SCORE', and 'GOVERNANCE SCORE', with 'ENVIRONMENTAL SCORE' selected. There are buttons for 'Load Defaults' and 'Load Published Score'. The main section is divided into 'Top Down / Country Key Issues' (score 7.07) and 'Bottom Up Key Issues' (score 4.55). Under 'Country Adaptive Capacity', the 'Effective HQ Country' is set to 'United States' and the 'Human Development Index' score is 9.2. The 'Bottom Up Key Issues' section includes input fields for 'Carbon Intensity' (0.19), 'Water Intensity' (1183.18), and 'Waste Intensity' (0.07), each with a 'Comments' field. A 'Sector-relative score' of 2.79 is also shown. A large 'PROPRIETARY' watermark is overlaid on the right side of the interface.

Integration

> Training

- Build analyst awareness of frameworks and key issues developed in research
- We have designed and conducted several ESG training sessions for all fundamental analysts

> Tools

- We have built E, S, and G desktop scoring applications to facilitate integration of issues in fundamental investment analysis

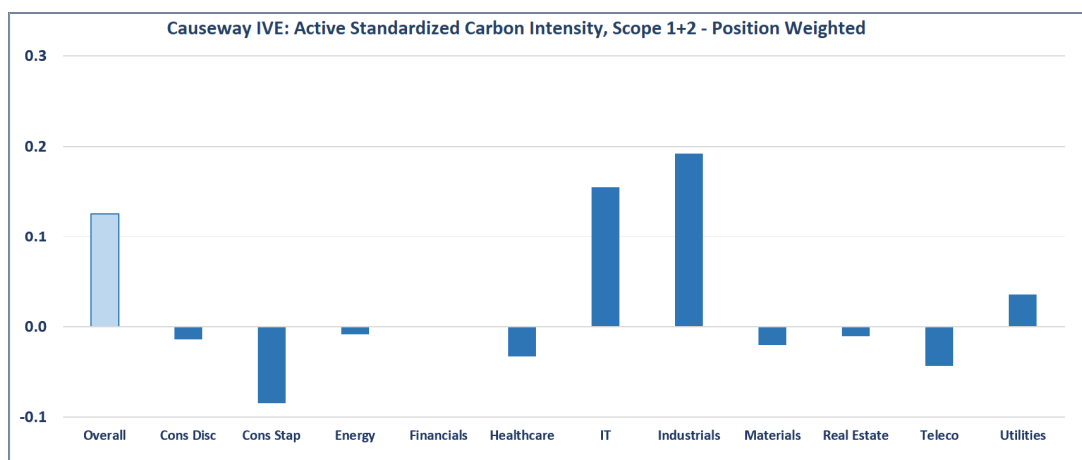
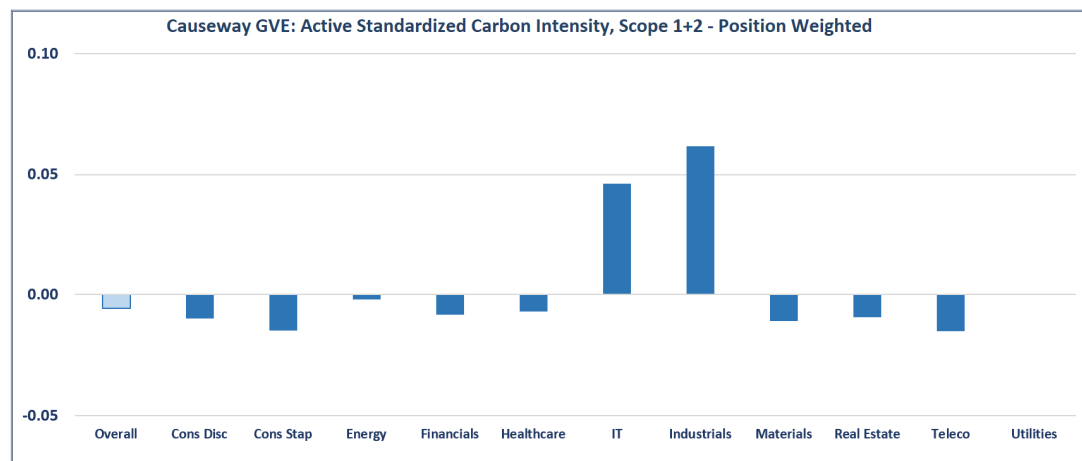
> Accountability

- Fundamental analysts' annual performance review includes an assessment of their observance of ESG integration procedures

Corporate Engagement Process

From Integration to Engagement: Carbon Footprint

- > By monitoring portfolio-level ESG characteristics, such as carbon footprint, we can identify the biggest contributors
 - E.g., Causeway's representative GVE (IVE) portfolio had lower (higher) Scope 1+2** carbon intensity than its MSCI ACWI (EAFE) benchmark at year-end 2020
 - The portfolio emissions intensity is the sum of company-level intensities weighted by portfolio weights (weighted average)
 - Active (portfolio - index) emissions intensity z-score is shown
- > The biggest contributors to the portfolio carbon footprint are identified as candidates for engagement by fundamental research teams



*Representative accounts in Causeway's Global Value Equity (GVE) and International Value Equity (IVE) strategies. Holdings can and do change over time.

** Scope 1 and 2 are defined by the Greenhouse Gas Protocol

Engagement by Causeway's Fundamental Analysts

> Constructive

- We prefer constructive engagement rather than negative screening (unless exclusion is mandated by a client for its portfolio)

> Selective

- We engage with selected companies in fundamental portfolios on the most material ESG issues
 - E.g., during a recent investor consultation with a large global food service company, we queried their policies, metrics, and executive accountability on modern slavery risk mitigation and water and waste efficiency

> More structured (in 2021)

- Prioritization tools
- Engagement templates

Knowledge Sharing

We Contribute to the ESG Ecosystem through Knowledge Sharing

> Shared journey

- Sharing ideas at conferences and other investor forums helps the development of the ESG ecosystem at this stage
- We have published our research in academic journals and white papers, and presented at several conferences globally

> Client resource

- We act as a resource for clients on relevant issues based on our research

Q & A

Disclosures

This presentation is solely for information purposes. It may not be re-distributed without Causeway's consent. It should not be relied on as research or investment advice regarding any investment. These views and any portfolio holdings and characteristics are subject to change, and there is no guarantee that any forecasts made will come to pass. Forecasts are subject to numerous assumptions, risks and uncertainties, which change over time, and Causeway undertakes no duty to update any such forecasts. Information and data presented has been developed internally and/or obtained from sources believed to be reliable; however, Causeway does not guarantee the accuracy, adequacy or completeness of such information.

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Alpha refers to performance exceeding a benchmark.

Information about, and characteristics of, Causeway's ESG score and the MSCI score are derived from back-tested data using a simulated investment process. Causeway does not currently manage assets using this process. There are numerous inherent limitations in the use of simulated information, including that it may not reflect the impact that material economic and market factors might have had on the portfolio managers' decision making if they were actually managing accounts using that process. The simulated returns do not reflect contemporaneous trading or any transaction costs. Simulated returns may not be indicative of the future returns of any portfolio.

¹ Each month, the cross-section of stocks is sorted into quartiles of the CCM ESG score, or the MSCI ESG score. The one month forward capitalization-weighted USD return of each hypothetical quartile portfolio is calculated, to obtain a return time series for each portfolio. The bar chart on the left (right) shows the average return, and volatility of the return stream, for each of the CCM ESG (MSCI ESG) score quartile portfolios from January 2013 to December 2020.

² Returns are risk-adjusted for exposures to size, value, growth, momentum, cyclicity, and volatility factors.