

RIVER ROAD ASSET MANAGEMENT, LLC

# ENVIRONMENTAL, SOCIAL, & GOVERNANCE (ESG) POLICY

DECEMBER 31, 2022

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## INTRODUCTION

River Road recognizes that environmental, social, and governance (ESG) issues can impact the investment risk and return profiles of the companies in which we invest. Many ESG factors have long been embedded in River Road's Absolute Value® research process as scrutinizing sustainability and corporate governance are key aspects of our critical investment criteria. This includes our assessment of a firm's business model (including its sustainability and risks), financial strength, shareholder orientation, and the accuracy of our valuation assumptions. Yet, we believe a more robust ESG integration into our Absolute Value® research process helps us better appreciate risks and opportunities increasingly being recognized and valued by investors.

River Road's ESG integration process began in 2019 and was completed in June 2022; it is an example of how we continually strive to improve our Absolute Value® research process. As with any initiative to improve our investment processes, such as our proprietary conviction framework and position sizing models, we expect to learn, refine, and improve ESG integration. Indeed, our research process has evolved since the team's inception, from an outline on a single piece of type-written paper to a well-defined, data-driven discipline of how River Road goes about generating investment ideas, valuing securities, assigning conviction ratings to a set of critical investment criteria, constructing portfolios including a framework for position sizing determined by discount and conviction, and finally selling securities based on a discipline that compels us to act if a stock exceeds our assessed valuation, violates our investment thesis, or accumulates unrealized losses counter to our thesis.

## RIVER ROAD ESG: PAST, PRESENT, & FUTURE

River Road began managing socially responsible investing (SRI) mandates in 2007. This experience laid the groundwork for our awareness not only of SRI issues as they evolved, but also provided valuable insights into how integrating ESG into our Absolute Value® approach could further refine and improve our investment process. We formally began exploring the idea of more fully integrating ESG in 2018 and by early 2019 had deemed ESG a mission-critical priority for River Road. A committee was formed to build our institutional knowledge of ESG, lay the groundwork for its integration, and explore becoming a United Nations-supported Principles for Responsible Investment (PRI) signatory.

We ultimately determined becoming a signatory to the principles of the world's most widely accepted and respected proponent of responsible investment, the PRI, was a critical step in demonstrating our commitment to responsible investing. Commitment to these principles, following much intense internal debate (including whether ESG is a fad), is viewed as a means of strengthening our Absolute Value® research process with little to no downside. Investors are increasingly placing value on environmental, social, and governance issues that are not readily captured through a more traditional fundamental analysis of financial statements, regulatory filings, company presentations, and the like. Although incremental time and resources are required to capture and analyze more data, and more *intangible* data, we believe the benefit of considering a more comprehensive set of material risks and opportunities in our research improves investment outcomes. A further benefit to ESG integration is our ability to meet increasing client demand for responsibly invested portfolios that consider how a company interacts with all stakeholders, including its community, environment, employees, suppliers, customers, and shareholders.

In October 2019, we became a PRI signatory and quickly immersed ourselves in the process of gathering necessary resources, which included extensive due diligence on third-party ratings providers. In Q2 2020 we formed a focused ESG group, comprised of investment team members led by Director of Research & Associate Portfolio Manager Jeffrey B. Hoskins, CFA. The selection of Sustainalytics as River Road's third-party ESG ratings provider was among the first actions undertaken by the ESG group, closely followed by the formation of a phased ESG integration framework and a series of educational meetings to explain ESG-related roles and responsibilities for every River Road associate. River Road formally began collecting ESG data and performing analysis for all River Road held securities in the final quarters of 2020 and completed the process in early 2022.

The next milestones were the formalization of the ESG integration framework and full implementation of River Road's proprietary ESG ratings into the firm's Absolute Value® investment process, which was completed as of June 30, 2022. Looking ahead, we believe offering ESG-considerate strategies with the ability to add ESG tilts and SRI overlays by request will provide clients with a set of solutions to meet a wide range of responsible investing needs while remaining true to the core principles of Absolute Value® investing.

## SCOPE

River Road considers ESG risks and opportunities as part of our proprietary Absolute Value® investment approach, which applies to all the firm's strategies. As of June 2022, proprietary ESG conviction ratings were fully integrated into the firm's Absolute Value® investment approach and existing River Road strategies, which we define as ESG-considerate portfolios. Objectives for River Road's ESG-considerate portfolios are consistent with historical objectives. Generally speaking, these objectives are returns in excess of, and lower volatility than, the respective benchmark. Additional objectives determined at the strategy level (e.g., a yield objective for the Dividend All-Cap Value Strategy). The consideration of ESG risks and opportunities is merely an enhancement to River Road's Absolute Value® investment approach. We believe consideration of a wider range of issues than previously contemplated, leads to better investment outcomes through improved returns or reduced risk, thus enhancing our opportunities to achieve long-standing objectives.

We continue to offer clients with more stringent ESG mandates an option to overlay SRI constraints (exclusionary screening) or ESG tilts (e.g., low carbon, diversity, and UN Sustainable Development Goals) as a bespoke solution for responsible investing needs.

## FIDUCIARY RESPONSIBILITIES

River Road has a fiduciary duty to act in clients' best interests. We believe ESG integration helps River Road consider a much wider range of risks and opportunities than typically considered in a more traditional fundamental analysis, logically leading, we believe, to better investment outcome potential. Accordingly, in acting in the best financial interests of clients, we consider ESG issues in making our investment decisions.

## ESG TEAMS & COMMITTEES

River Road does not have associate(s) whose responsibilities are solely focused on ESG (the 'standalone' approach). Our investment professionals are responsible for incorporating all relevant factors into investment analysis and decision making, including ESG risks and opportunities (the 'integrated' approach). We prefer the integrated approach because we believe it is critical for ESG issues to be considered equally with more traditional fundamental analysis (and other proprietary approaches within River Road's Absolute Value® investing) and view this as best accomplished by placing ESG considerations as close to the Absolute Value® process as possible, which includes idea generation, security analysis, and portfolio construction.

For the purpose of establishing, implementing, and maintaining ESG policies, River Road has a focused ESG investment group led by Director of Research & Associate Portfolio Manager Jeffrey B. Hoskins, CFA. Each of the other members of the ESG group are members of the investment team.

## IMPLEMENTATION

We incorporate analysis of what we consider to be relevant ESG factors into our fundamental research, which is conducted in house. If applicable, ESG matters are included in the proprietary investment summaries written on our portfolio holdings. These summaries are uploaded to FactSet for both broader communication and permanent record keeping.

Our primary sources of fundamental data are the regulatory and corporate filings of our companies. We seek to understand the business model, financial strength, and shareholder orientation through a thorough review of current and past 10-K, 10-Q, 20-F, 8-K, proxy filings, as well company transcripts and corporate presentations, including corporate social responsibility and sustainability reports. Our analysis provides an understanding of the key drivers of the business so we can develop financial models for estimating future operating cash flow and financial strength, including leverage trends and available liquidity. We also evaluate how management utilized discretionary cash flow in the past and develop insights into how we believe it will be deployed in the future. Sustainability risks are assessed both quantitatively and qualitatively and may have an impact on our assessed valuation and/or conviction.

While the majority of our research is fundamental analysis of a company's financial statements and other publicly available sources, we do utilize specialized outside services (such as ISI Group and Ned Davis) for industry and macro level research to help provide context to our bottom-up analysis of a company. We also use data aggregators (such as FactSet and Bloomberg) to help bring efficiencies to our process. We utilize Sustainalytics for third-party ESG ratings; additionally, we have access to ESG information via ISS's DataDesk platform and Bloomberg as well as public data sources such as CDP and The Transition Pathway Initiative.

A portfolio manager is never prohibited from purchasing or holding a position due to an ESG issue, but consideration of material ESG issues is part of the investment decision and the stock's sizing in the portfolio. River Road typically does not systematically exclude entire industry groups due to ESG concerns. However, River Road has historically avoided investment in industries such as tobacco and adult entertainment due, in part, to ESG-related concerns. From our perspective, industries subject to intense regulation, large liability exposure, political scrutiny, and declining consumer/fundamental trends make poor investments. Thus, we often avoid groups that raise broad ESG issues based solely on our fundamental approach.

River Road applies negative screens when specific guidelines are provided by a client. For clients with ESG and/or SRI restrictions, River Road utilizes ISS data to create a customized screening on a pre- and post-trade basis. River Road's process is designed to ensure that the practices of the company being considered for investment do not conflict with the client guidelines provided to River Road. Typically, River Road only performs negative screenings, but ISS can accommodate positive screenings as well. The screening system is highly customizable and examples of corporate practices that may be screened for include:

- Adult entertainment
- Alcohol
- Animal welfare
- Bioethics
- Diversity
- Environment
- Gambling
- Human rights
- Medical ethics
- Military and weapons
- Nuclear power
- Tobacco
- Workforce

Full integration of River Road's proprietary ESG conviction ratings was completed in June 2022. A proprietary conviction rating system is, in our view, an important component of full ESG integration, since we do not want to rely on third-party ratings for two primary reasons: (1) we may disagree with how a third-party rating is determined, be it the nature of a specific issue or its weighting/materiality in the overall score, and (2) we may determine management teams are making more rapid progress for managing ESG risks than third-party ratings providers indicate.

A fully integrated proprietary ESG conviction rating provides for a consistent approach across River Road investment strategies just as the firm's Absolute Value<sup>®</sup> investment approach provides a 'common language' through which the investment team discusses and shares investment ideas and constructive criticism.

## MONITORING

River Road regularly monitors portfolios, portfolio holdings, and watchlist names for ESG risk through a combination of third-party research (Sustainalytics) and proprietary internal research notes documented by portfolio managers and research analysts. Relevant monitored data includes ESG risk ratings and ratings changes, new controversies, and ESG policy and practice updates we believe are not yet reflected in periodic third-party ratings updates. This data is reviewed regularly but no less frequently than quarterly.

For clients with SRI guidelines, River Road utilizes ISS data to create a customized SRI screening on a pre- and post-trade basis. River Road's SRI process is designed to ensure that the practices of the company being considered for investment do not conflict with the SRI guidelines that the client has provided to River Road. For a specific list of restricted stocks, River Road encodes the restrictions into its pre-trade compliance system, Eze Compliance, preventing portfolio managers from inadvertently executing trades that would violate them.

Consistent with our bottom-up investment approach, the investment team focuses on risks, which may include ESG, of individual positions as well as aggregate portfolio. The Chief Investment Risk & Analytics Officer independently monitors adherence to our

philosophy and process with metrics based on the historical characteristics of our portfolios. Risk is monitored and managed with a multi-faceted, multi-layered approach rather than a single risk measurement model.

## CLIMATE CHANGE

River Road recognizes that climate change presents risks, as well as opportunities, that can impact the value of our investments. All River Road strategies assess climate risks and opportunities as part of our proprietary Absolute Value<sup>®</sup> investment process. Key elements of our assessment include:

- Carbon intensity metrics (scope 1 and scope 2, and scope 3 where appropriate) and carbon intensity trends
- Transition risk (policy, technology, market, and reputation)
- Physical risk (acute and chronic)
- Opportunities (e.g., renewable energy, battery storage, and carbon capture)

We expect companies with high carbon intensity (tCO<sub>2</sub>e/Mil USD) to receive a lower conviction rating as will companies with deteriorating carbon intensity metrics. Similarly, we expect lower conviction companies might also have high exposure to climate transition and/or physical risks. Higher conviction companies will likely have lower carbon intensity, improving carbon intensity trends, and comparatively little climate transition or physical risk. Higher conviction also may be achieved by showing progress toward GHG reduction goals (e.g., Paris Agreement alignment) or by offering a climate solution product or service (e.g., carbon capture technology and renewable energy). The assessed conviction rating (1.0 = highest conviction, 5.0 = lowest conviction) for these issues rolls up into an ESG conviction rating, which, in turn, rolls up into an overall conviction rating for a stock. The combination of River Road's overall conviction rating and assessed valuation for a stock helps guide buy/sell and portfolio sizing decisions.

River Road is a public supporter of the Task Force on Climate-related Financial Disclosures (TCFD). Our commitment to the TCFD includes promoting disclosure of climate-related risks by the companies in which we invest. The commitment to promote better disclosure as well as cases where we believe climate change issues could have an impact on the value of our investments lead us to engage with boards and management teams when appropriate. These considerations also help inform our proxy voting.

## ENGAGEMENT & VOTING

River Road engages with companies as part of its Absolute Value<sup>®</sup> investment approach, which includes seeking clarification on ESG risks and opportunities. If appropriate, our portfolio managers and research analysts will urge boards and management teams to strengthen ESG practices, policies, and disclosure. River Road will also engage with companies on proxy issues, especially when Glass Lewis & Co. (River Road's proxy voting agent) disagrees with a management team recommendation (River Road's proxy voting policy is available on request).

In our view, engagement with small firms represents a particularly attractive opportunity to drive change, as we have found smaller firms with fewer resources or less pressure to adopt and disclose ESG practices rate more poorly than larger firms with greater resources and generally more intense investor focus on ESG risks. This opportunity to engage with smaller firms is attractive to River Road given our firm was founded with our Small Cap Value Strategy and smaller cap stocks continue to be a focus for River Road.

River Road does not maintain an explicit measurement of engagement success or voting outcomes but instead measures and tracks progress under our critical criteria, which capture important notes around key votes or issues we deem significant to our investment thesis or the progress of important investment issues we have discussed with management.

## REPORTING

River Road's research analysts and portfolio managers document investment research with internal research reports and research notes kept in FactSet. Research reports and notes cover a range of investment considerations, including a stock's valuation, business model, shareholder orientation, and financial strength. Material ESG risks and opportunities are embedded in these investment considerations.

In terms of external reporting, we provide, upon request, ESG data comparing portfolio ratings versus relevant benchmarks as measured by Sustainalytics data. We believe this standardized score means clients may more quickly and easily evaluate River Road portfolios versus other investment managers' portfolios without reconciling a variety of differing proprietary ESG ratings.

Lastly, River Road reports its ESG activities annually through the PRI reporting framework as part of our commitment as a PRI Signatory. River Road's transparency report and assessment is available on request.

## TRAINING

River Road is committed to continuing education on ESG topics. We frequently refer to materials available from the CFA Institute, which include white papers, journals, and seminars covering relevant ESG topics.

River Road has a long history of supporting educational and continuing education activities for its associates. Although some of these activities are required (e.g., annual compliance training), River Road regularly organizes and sponsors activities for associate enrichment and development. Examples of such programs and activities include full sponsorship for associates wishing to pursue professional designations (e.g., CFA, CIPM) and professional development goals. River Road also encourages associates to take time for professional development activities such as pursuing continuing education credits.

## REVIEW

River Road is committed to continually improving its Absolute Value<sup>®</sup> approach to investing. Examples of such improvements to our process include the thorough review and expansion of our proprietary conviction rating framework (2014, 2016, and 2020) and our proprietary position sizing models (beginning 2014).

We expect our process will continue to evolve, including our integrated ESG practices and policies. We monitor our investment process on a continuous/ad-hoc basis but no less frequently than annually.

## **APPENDIX: ORGANIZATIONS & INITIATIVES**

### **United Nations-supported Principles for Responsible Investment (“PRI”)**

River Road is a signatory to the United Nations-supported PRI. The PRI Initiative is an international network of investors working together to put the six principles for responsible investment (the “Principles”) into practice. As such, River Road is committed to the following:

- **Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.**
- **Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.**
- **Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.**
- **Principle 4: We will promote acceptance and implementation of the Principles within the investment industry.**
- **Principle 5: We will work together to enhance our effectiveness in implementing the Principles.**
- **Principle 6: We will each report on our activities and progress towards implementing the Principles.**

*Source: [www.unpri.org](http://www.unpri.org)*

### **Task Force on Climate-Related Financial Disclosures (“TCFD”)**

River Road supports the TCFD. The Financial Stability Board (FSB) formed the TCFD in 2015 to develop recommendations for more effective climate-related disclosures that “enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system’s exposures to climate-related risks.” In 2017, the TCFD published climate-related financial disclosure recommendations that today are widely recognized and accepted as a framework for reporting entities to follow.

*Source: [www.fsb-tcfid.org](http://www.fsb-tcfid.org)*

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