

Introduction

There has been a plethora of articles and reports about Environmental, Social, and Governance (ESG) investment issues, as well as on Socially Responsible Investing (SRI), during the last three months. Several key trending topics include issues on opioids and private prisons. Additionally, the Principles of Responsible Investing (PRI) released the results of their respondents' annual questionnaires. Overall, it has been a very active quarter in the ESG and SRI space. We believe these issues are likely to get even more attention as politics heats up in the U.S.; the first public debates for the U.S. 2020 elections likely ignited focus on specific ESG/SRI related issues.

Our PRI Assessment

Shenkman became a signatory to the Principles for Responsible Investment (PRI) in August 2017 and, as a result, we are required to submit a report on our responsible investing activities on an annual basis. 2019 (for calendar year 2018) was our first required reporting year, although we reported on a voluntary basis in 2018 (for calendar year 2017). The PRI publishes a public version of our annual questionnaire (Transparency Report), which is available to existing PRI signatories.

The Assessment Report is designed to provide feedback to signatories to support ongoing learning and development. For additional information on our Transparency Report, please visit <https://www.unpri.org/signatories>.

There is no overall score, rather, Shenkman was scored on the following modules: (i) Strategy & Governance; (ii) Fixed Income – Corporate Financial; (iii) Fixed Income – Corporate Non-Financial; and (iv) Fixed Income – Securitized. Scores range from A+ to E and PRI publishes a median score of all responders of each module. Shenkman's score, and the median score, for each module is described below:

Module Name	Shenkman Score	Median Score
Strategy & Governance	A	A
Fixed Income – Corporate Financial	A	B
Fixed Income – Corporate Non-Financial	A	B
Fixed Income – Securitized	A	C

Private Prisons

In our April Newsletter, we highlighted that J.P. Morgan announced that they would no longer finance the private prison industry, in what appeared to be, at least in part, a response to an open letter that called for the bank and Wells Fargo to stop financing companies in the industry. In the past month, Bank of America has announced the same policy with regards to private prison companies.

We believe that the industry has come under additional scrutiny due to well-publicized visits by politicians focused on problems with detention centers near the U.S. borders. This highlights how ESG and SRI risks rarely end with one simple announcement. It is also a great example that it is not always a revenue or legal risk that develops from ESG related factors, but also the risk of higher cost of capital or losing access to capital.

While the industry definitely has ESG and SRI risks that may be higher than others, we found it a bit unusual that banks seemed to use a broad brush approach to the industry in their recent announcements. Private prison operators are effectively contractors for the government and do not set policy. We also believe there are differences in how the companies in the sector operate. GEO Group and Core Civic have been partners with ICE for thirty years and appear to provide the agency with the flexibility they need to manage the U.S.'s border. Each company has stated that it has not and will not house unaccompanied minors. To the best of our knowledge, the facilities that have been reviewed in the media and highlighted by politicians are both government-owned and operated or solely operated by Caliburn International. However, despite the apparent differences in how the various operators in the private prison segment are run, the broad action taken against this industry segment demonstrates that risk assessment at an industry level can lead to a market that does not differentiate operators to the same degree as fundamental, bottom-up and research-driven analysis.

Healthcare and Opioids

Of all the various targets at which campaign rhetoric is firing, it may be most directly hitting the Healthcare industry. Whether the proposals thrown around by Presidential candidates have any merit or realistic chance for success, the debate around them definitely focuses attention on this industry as a political target.

Regardless of any political campaigning, the opioid addiction epidemic in the U.S. has certainly caused this sub-sector of the Pharmaceutical industry to have its own unique and concerning ESG and SRI risks. These factors have migrated rapidly from an issue that could impact sales and revenue for many companies to a much bigger potential financial liability, as various U.S. governmental

entities have brought lawsuits against many industry participants. Companies with exposure to opioids that have less revenue diversity are clearly at a greater risk.

The political environment is increasing the potential economic impact from ESG factors on many segments of the Healthcare industry. However, investors should be careful not to equally weight the risks for all Healthcare companies, and they should conduct careful analysis to understand the different business lines and potential risks from ESG factors. For example, in our opinion, the risks are much lower for a subset of the industry like managed care organizations versus the risks for generic drug manufacturers.

We strive to keep an open dialogue on ESG and SRI factors to constantly improve our process. We look forward to sharing any feedback on these topics.

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