

# Sustainable equity investment strategies

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## Sustainable investment philosophy and integration

Over the last decade, demand for sustainable investing has risen as clients and practitioners evaluate the impact of energy conservation, carbon usage, boardroom diversity, workplace safety, and human rights on a company's valuation. Assets domiciled in some form of sustainable, responsible, or impact investing strategy have nearly quadrupled from roughly \$3T in 2010 to \$12T in 2018.<sup>1</sup>

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At Mesirow Financial Equity Management ("MFEM"), our comprehensive framework integrates fundamental and Environmental, Social and Governance (ESG) analysis along with aspects of responsible investing and company engagement to provide our clients an opportunity to do well and do good (i.e., influence positive behavior while delivering favorable performance).

We believe that excess returns can be produced by investing in attractively valued stocks that are poised to appreciate due to catalyst driven earnings and cash flow growth. We also believe that ESG factors are interconnected with our fundamental assessment of macro, sector and company specific trends and can have a material impact on investment performance during our investment time horizon. As a result, we consider ESG factors in conjunction with

other material risk and fundamental factors that, in aggregate, influence our decision to invest in an individual company.

**"We actively incorporate sustainable investment criteria such as environmental, social, and governance factors with our fundamental assessment of macro, sector and company specific trends to derive favorable performance and risk characteristics for our portfolios."**

In addition, we seek to make a positive impact on the environment and society as well as encourage incremental improvements through active engagement with companies in which we invest.

We believe that companies that incorporate sustainability assessments into their strategic plans have an opportunity to enhance firm value and/or reduce overall levels of risk.

**Carefully consider the Funds' investment objective, risk factors, charges and expenses before investing. This and additional information can be found in the Funds' full & summary prospectus, which may be obtained at [mesirowfinancial.com/mutual-funds](https://www.mesirowfinancial.com/mutual-funds) or by calling 1.833.MESIROW. Read the prospectus before investing.**

1. U.S. SIF Foundation, Report on U.S. Sustainable, Responsible, and Impact Investing Trends 2018. Mesirow Financial Equity Management ("MFEM") is a division of Mesirow Financial Investment Management, Inc., ("MFIM") an SEC-registered investment advisor. Past performance is not necessarily indicative of future results.

## Our Sustainable Investing Framework

We actively incorporate environmental, social, and governance factors into our investment decisions to derive favorable performance and risk characteristics for our portfolios.

**Environment** It is often economically logical for a company to take actions that benefit themselves but harm the environment. By investing in companies that think carefully about their environmental impact, we help incentivize long-term, environmentally-friendly decisions.

**Social** Caring for those in need and protecting the vulnerable are foundational human ethics. We believe it is incumbent on corporations to contribute to these human ethics. By investing in companies that help fulfill this social responsibility, we help enable those companies who seek to become stronger corporate citizens.

**Governance** As a fiduciary for our clients, we have long sought investment opportunities at companies with good governance policies. At its core, good governance protects the interests of minority shareholders, reduces the probability of fraud, and aligns the goals of companies with investors.

## Alignment and Sustainable Development Goals

Corporate responsibility has been a core value at our firm since its founding in 1937. Today, Mesirow's enduring and diverse set of commitments forms the foundation for how we embrace and align our actions across the firm with the United Nations Sustainable Development Goals.

### Mesirow Corporate Responsibility



#### SUSTAINABLE INVESTING

Strategies that seek to help investors prosper while doing good

- Signatory, Principles for Responsible Investment (PRI)
- Signatory, FX Global Code of Conduct
- Offerings across the capital structure and investment vehicles: Equity, Income and Alternatives



#### COMMUNITY ENGAGEMENT

Investment of time, talent and financial support

- Neighborhoods: Family services, education
- Social justice: Tolerance, anti-gun violence
- Opportunity & inclusion: Supporting persons with disabilities



#### WORKPLACE ENRICHMENT

Within one of the industry's most inclusive work cultures

- Firm focus on diversity and inclusion
- Perfect score of 100 on Human Rights Campaign Corporate Equity Index<sup>3</sup>
- WomenConnect, PeerConnect, PrideConnect Employee Resource Groups
- Top workplace awards from Investment News, Chicago Tribune, Crain's
- LEED certified headquarters; environmental improvement initiatives

### ALIGNMENT WITH UNITED NATIONS CAUSE PILLARS<sup>2</sup>



ENVIRONMENT



EDUCATION & INNOVATION



COMMUNITY IMPROVEMENT



HUMAN RIGHTS & EQUALITY

2. For more information on the United Nations Sustainable Development Goals underlying these cause pillars, please visit <https://www.un.org/sustainabledevelopment/sustainable-development-goals/>.  
 3. Human Rights Campaign Foundation's 2020 Corporate Equality Index (CEI) 4. Fride, Busch, Bassen – Journal of Sustainable Finance & Investment, Vol 5, Issue 4, ESG and Financial Performance... Past performance is not necessarily indicative of future results.

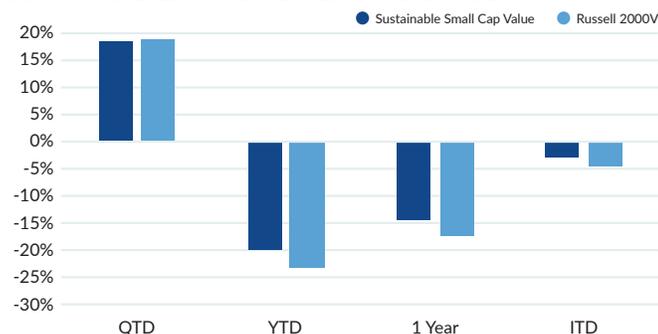
## Performance

The cornerstone of any investment strategy is the ability to deliver desired performance and outcomes for clients. Conventional wisdom asserts that maximization of firm value drives investment returns. As such, it has been believed that companies primarily focused on “non-fundamental issues” cannot meet desired performance goals. However, sustainable investing and competitive returns are not mutually exclusive concepts. More than 2200 unique studies analyzing ESG criteria in relationship to corporate financial performance show that companies with high ESG profiles or ESG orientation are 4-7x more likely to have positive relative performance.<sup>4</sup>

The same holds true for our own Sustainable Equity Strategies.

Our strategies have outperformed – with lower downside capture – over time

**Chart 1: MESIROW SMALL CAP VALUE SUSTAINABILITY FUND PERFORMANCE**



Source: MFEM and Russell. As of June 30, 2020. Inception Date is December 19, 2018.

The performance date quoted represents past performance. Past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost and current performance may be lower or higher than the performance quoted. Performance current to the most-recent month-end may be obtained at [mesirowfinancial.com/mutual-funds](http://mesirowfinancial.com/mutual-funds) or by calling 1.833.MESIROW. There is a 1% redemption fee applicable if shares are redeemed within 90 days of purchase. Investment performance does not reflect the redemption fee; if it was reflected, the total return would be lower than shown. Expenses for the institutional share class are 1.40% (gross) and 0.98% (net). Expenses for the investor share class are 1.65% (gross) and 1.23% (net).

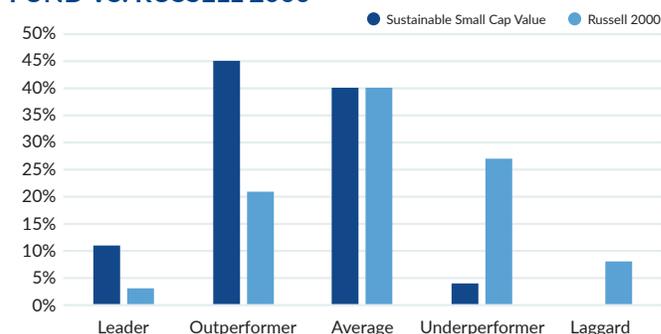
## Sustainability Scores and Profile

Along with traditional fundamental metrics, our analysts make broad assessments of a company's ESG profile and sustainability framework. MFEM obtains ESG profile scores and sustainability rankings from third-party vendors and aggregates them into a composite score based on our proprietary methodology. Based on the composite scoring process described above, as well as incremental due diligence with individual companies, we then generate a list of companies that we believe possess favorable ESG profiles.

Accordingly, our methodology shows a significantly positive skew toward companies we would classify as leaders or outperformers based on their sustainability profiles with diminished exposure to those considered underperformers or laggards.

Our strategies emphasize investment in sustainability “leaders” or “outperformers”

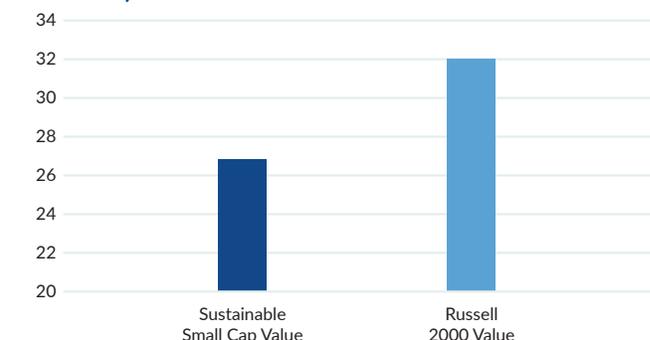
**Chart 2: MESIROW SMALL CAP VALUE SUSTAINABILITY FUND VS. RUSSELL 2000**



Source: MFEM, ISS Datasdesk As of June 30, 2020. Sustainability scores are based on a custom weighted average of ESG factors.

... and are meaningfully underexposed to sustainability risks relative to major benchmarks

**Chart 3: MEDIAN SUSTAINALYTICS RISK SCORE (LOWER IS BETTER)**



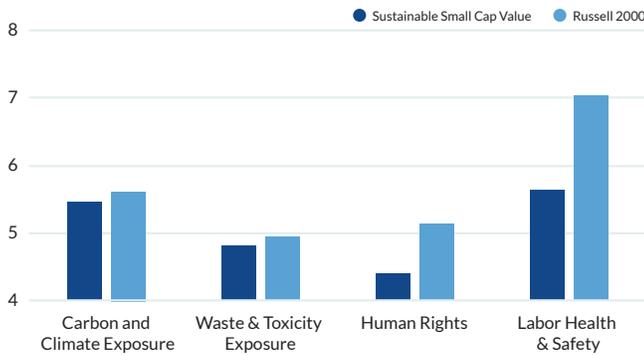
Source: MFEM, Morningstar Direct, Sustainalytics As of March 31, 2020. Sustainalytics risk score as published in Morningstar Direct based on Sustainalytics risk scoring methodology. Lower scores indicate good relative governance, disclosure and/or transparency.

## Responsible Impact

While we employ ESG analysis to evaluate how corporate governance issues such as staggered boards of directors, board independency and executive compensation can affect firm volatility, credit spreads and cost of capital, **we also evaluate the impact of environmental and social factors on firm value.**

We believe that, by investing in companies that carefully consider their environmental impact, we help incentivize long-term, environmentally-friendly decisions that can also **help improve company profitability.** In addition, we believe that by investing in companies that help fulfill social responsibilities and reduce negative impacts on communities, we enable those companies to become stronger corporate citizens and reduce levels of fundamental risk.

Chart 4: **AVERAGE QUALITY SCORES (LOWER IS BETTER)**



Source: MFEM, ISS Datadesk As of March 31, 2020. Equal-weighted average of all companies in the index and portfolio for those various categories.

## Social and Community Responsibility

We are also mindful of how our investments can impact our society and communities, and believe it is important that this impact be measurable.



NO EXPOSURE TO TOBACCO



NO EXPOSURE TO PAY-DAY LOANS



NO EXPOSURE TO FOR-PROFIT PRISONS



NO EXPOSURE TO NUCLEAR WEAPONS AND FIREARMS



NO EXPOSURE TO GAMBLING AND GAMING



NO EXPOSURE TO OIL, GAS, AND CONSUMABLE FUEL PRODUCTION

Source: MFEM, Bloomberg, FTSE Russell

## Materiality

Fundamental research is the primary driver of excess performance through stock selection. We combine fundamental and ESG analysis along with other factors in our investment selection process to identify specific opportunities. A valuable part of this analysis is the broad qualitative consideration of material factors which may have more influence on financial performance. Material factors are given more consideration within the overall evaluation of an investment opportunity. The chart on the following page is an example of select ESG issues and the degree of consideration given within certain sectors.

SELECT MATERIAL ESG ISSUES		CONSUMER PRODUCTS	FINANCIALS	HEALTH CARE	TECHNOLOGY	TRANSPORTATION
Environment	Energy Management	High	Low	Medium	High	High
	Water & Wastewater Management	High	Low	Low	Low	Low
	Waste & Hazardous Materials Management	Low	Low	Medium	Low	Low
Social	Human Rights & Community Relations	High	High	Medium	Low	Low
	Employee Health & Safety	Low	Low	Medium	Low	High
	Employee Engagement, Diversity & Inclusion	High	Medium	Medium	High	Low
	Product Quality & Safety	High	Low	High	Low	Medium
Governance	Business Ethics	Medium	High	High	Medium	Medium
	Board Structure and Diversity	High	Medium	Medium	High	Medium
	Management of the Legal & Regulatory Environment	Low	High	High	Medium	Medium

Materiality Consideration ● High ● Medium ● Low

## Engagement

We have deep experience collaborating with management teams about ways to maximize firm value. This **ongoing, active dialogue is vital in the small-cap universe** where our access to management is more direct and can lead to faster implementation of solutions.

Evaluating the relative capabilities of management, both qualitatively and quantitatively, plays a critical role in our investment decision-making process and internal research effort. Company management teams are expected to have a **demonstrated record of delivering shareholder value** and/or an identifiable strategy, with benchmarks and milestones, designed to deliver shareholder value over our investment time horizon.

We proactively communicate with management teams to **build awareness of ESG factors** and encourage management teams to make positive incremental changes to support ESG initiatives. These conversations happen on an ongoing basis and include ways that the company and its management can initiate improvements to their sustainable profile while stressing the importance of building an infrastructure for engagement and disclosure of material sustainable risks.

MFEM tracks a company’s sustainability profile and changes over time, a process which informs our stock selection process and leads to investment in companies with stronger

governance and positive community impact as well as an **improvement in our overall high-quality emphasis.**

### Case Study 1: The Curious Case of QTS – QTS Realty Trust Premise

QTS Realty Trust is a data center REIT that was originally excluded from our investible universe due to an unfavorable sustainability profile with no interim plan to address or rectify material issues. While significant progress had been made on governance issues in 2018, the company’s lack of meaningful disclosure on environmental issues suggested a continued lack of concern as it related to social and environmental issues.

#### ENGAGEMENT

As part of our due diligence, we investigated several ESG topics that we deemed material, including the presence of super-voting shares for the Chairman and CEO, related party transactions and renewable energy usage. In addition, we used our conversations with management to advocate for more diversity on the board and management team and reiterate our support for specific environmental goals.

#### COMPANY ACTION

While the two governance issues were not ideal, we concluded that the arrangements were acceptable given the level of review and the underlying economic ownership.

The case studies contained herein have been included to illustrate the investment process utilized by MFEM in the selection of investment opportunities. The inclusion of these case studies is not designed to convey that a past specific investment selection by MFEM would have been profitable to any person. It should not be assumed that investment selections made in the future will be profitable or will equal the performance of any selections described herein.

On the environmental front, we were encouraged to discover that the company was taking the topic more seriously than we believed.

- QTS was completing their GRESB<sup>5</sup> study and was about to issue their first Sustainability Report
- QTS Implemented specific environmental goals to be achieved by 2025, including 100% renewable energy
- Ongoing discussion related to board and management diversity

## RESULT

Our research suggested that their ability to report granular sustainability data to their clients afforded a material ESG opportunity for sustainability-minded corporate clients. While QTS still has more room for improvement, their sustainability profile improved considerably, and we are confident that the company is making incremental improvements. As such, they became eligible for our Sustainable Equity strategies in 2020.

### Case Study 2 From Good to Great – Wyndham Hotels and Resorts

#### PREMISE

Wyndham is the world's largest hotel franchisor. When we purchased Wyndham in our Sustainable Equity strategies in August 2019, the company had an adequate sustainability profile driven by general strength in governance despite some shareholder rights issues. Overall, we saw significant room for improvement on the environmental and social fronts, particularly related to disclosures.

#### ENGAGEMENT

As part of our due diligence and engagement process, we sent a letter to management in October 2019 advocating for more deliberate consideration of environmental, social and governance issues, as well as creating an infrastructure for more disclosure of material issues. We received a response the following month indicating that management was taking these issues seriously.

## COMPANY ACTION

In the interim, Wyndham dramatically improved their disclosures on environmental and social topics and demonstrated real positive change.

- Increased their partnership with Polaris to provide short term housing for victims of human trafficking
- Eliminated the super-majority requirement to remove directors
- Achieved 100% gender pay equity at the executive level and 95% for the rest of the firm.
- Instituted 5 levels of environmental training certifications for associates which focuses on energy and water conservation, reducing waste and CO<sup>2</sup> emission reduction
- 25% female representation on Board of Directors
- Perfect score of 100 for LGBTQ equality in HRC Best Places to Work

## RESULT

As one of the few companies in the small-cap universe that publishes a full Corporate Sustainability Report, we expect Wyndham to have substantial disclosures when the second report is released in June/July 2020. We are pleased with their effort to run an economically successful business while also improving disclosure and becoming a better corporate citizen.

## Conclusion

Mesirow has long history focusing on important environmental, social and governance factors, both in the way we do business, and in how we evaluate investments within our equity portfolios. In striving to constantly deliver for our investors, we continue to prioritize companies that share similar sustainability goals, and believe the result is enhanced value for the portfolio with reduced overall levels of risk.

5. GRESB is a global ESG benchmark for real estate and infrastructure investments. The case studies contained herein have been included to illustrate the investment process utilized by MFEM in the selection of investment opportunities. The inclusion of these case studies is not designed to convey that a past specific investment selection by MFEM would have been profitable to any person. It should not be assumed that investment selections made in the future will be profitable or will equal the performance of any selections described herein. Past performance is not necessarily indicative of future results.

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The Mesirow Funds are distributed by SEI Investments Distribution Co. (SIDCO). The Funds are managed by Mesirow Financial Investment Management, Inc. SIDCO is not affiliated with Mesirow Financial Investment Management, Inc. or Mesirow Financial, Inc.

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**Benchmark Definition:** The S&P 500® is widely regarded as the best single gauge of large-cap U.S. equities. There is over USD 9.9 trillion indexed or benchmarked to the index, with indexed assets comprising approximately USD 3.4 trillion of this total. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

The Russell 2000 Index® offers investors access to the small-cap segment of the U.S. equity universe. The Russell 2000 is constructed to provide a comprehensive and unbiased small-cap barometer and is completely reconstituted annually to ensure larger stocks do not distort the performance and characteristics of the true small-cap opportunity set. The Russell 2000 includes the smallest 2000 securities in the Russell 3000. The Russell 2000 Value Index® offers investors access to the small-cap value segment of the U.S. equity universe. The Russell 2000 Value is constructed to provide a comprehensive and unbiased barometer of the small-cap value market. Based on ongoing empirical research of investment manager behavior, the methodology used to determine value probability approximates the aggregate small-cap value manager's opportunity set.

Environmental, social and governance (ESG) guidelines may cause a manager to make or avoid certain investment decisions when it may be disadvantageous to do so. This means that these investments may underperform other similar investments that do not consider ESG guidelines when making investment decisions.

## About Mesirow Financial

Mesirow is an independent, employee-owned financial services firm founded in 1937. Headquartered in Chicago, with offices in 21 cities, we serve clients through a personal, custom approach to reaching financial goals and acting as a force for social good. With capabilities spanning Global Investment Management, Capital Markets & Investment Banking, and Advisory Services, we invest in what matters: our clients, our communities and our workplace culture. To learn more, visit [mesirow.com](https://www.mesirow.com) and follow us on LinkedIn.