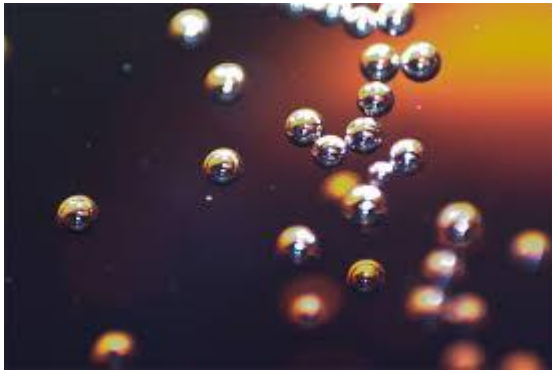


Unintended outcomes of low carbon investment – turning a blind eye to waste and water?

Lowering emissions is a key component in the transition to a more sustainable future but it's not what differentiates the real winners.



In a world of growing constraint, characterised by rising demand from population growth and improving living standards, objectively analysing corporate sustainability data allows us to identify companies that have addressed the issues of resource constraint and executed a sustainability program that has delivered to the bottom line.

However, despite the numerous data agencies offering insights into a company's sustainability practices, the market is still largely dominated by 'off the shelf' investment products that focus solely on carbon reduction exposure, or a broad-brush approach incorporating the plethora of ESG factors, targeting a one size fits all approach. How often do we now hear the term, we fully integrate ESG?

The overriding issue with sustainability lies in the definition. From an environmental perspective, is focusing on carbon reduction potentially compromising investment portfolios? Could you inadvertently be increasing your exposure to companies that are mis-managing their water and waste? Whilst carbon may well be the (well earned) nemesis that is currently making headline news, and consequentially rising up the investor, political and social agendas, Osmosis have always advocated that carbon emissions should not be the sole indicator of environmental efficiency. Indeed, it is hard to justify that because a company's CO₂e emissions are lower than their sector peers that they have the most significant environmental impact. We affirm that when assessing a company's environmental metrics, it is imperative to take a broader and deeper approach with a full analysis of a company's use of natural resources.

By lifting the lid on some of the companies that are included in the low carbon indices, the MoRE approach reveals that there's more to sustainability than their low carbon label suggests. Many of the low carbon companies in the MSCI ACWI Low Carbon Target Index fail to make it into our models as the broader environmental balance sheet highlights inefficiencies in water or waste management

compared to their sector peers. The MoRE model identifies those companies who may win on one environmental issue while ignoring or performing badly on the others. Consistent performance on all three metrics is necessary for inclusion in our investment universe.

To illustrate the point, we have identified two companies from our investment universe that fall short of reaching our investment portfolios but are included in many low carbon indices.

Honda: Talking Rubbish?

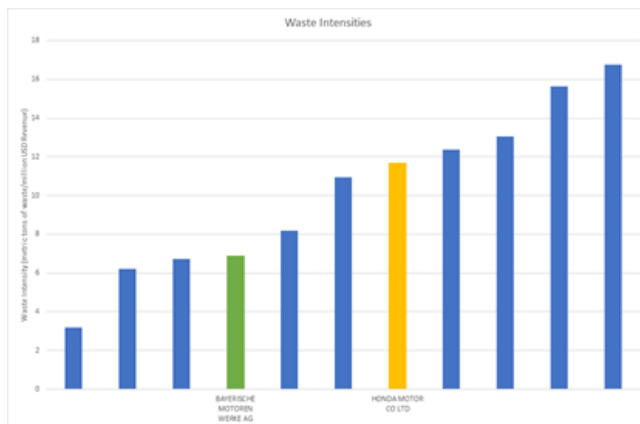
Honda Motor Co, the Japanese car and motorbike manufacturer, is an example of a company included in Low Carbon Indices. While Osmosis' MoRE shows they are indeed performing in line with their industry on carbon and water use, their waste figures exclude them from our portfolios.

Recycling and resource conservation are key business principles according to the latest sustainability report, however, comparing their performance to industry peers shows there is more to be done in this area. In the car manufacturing industry, a segment of the economy that has endured decades of process optimisation and margin compressions, the waste produced per product is a good proxy for how fine-tuned the sourcing and assembly lines are, and how efficient a company is at creating economic value. In 2018, Honda produced over 1,620 thousand tons of waste, mainly in Asia and North America. While the company's carbon emissions, energy use and water use has been stable in the last four years, its waste generated has risen by 15%.

Honda's latest sustainability report doesn't make for bad reading. The report highlights the importance of packaging waste in the logistics area, including disposable transport packaging. Switching to reusable containers and eliminating using steel cases has led to a significant drop in packaging materials used, over 70% reduction since the start of the century. However, if we dig deeper into the figures it becomes clear that the impact on total waste generated is minimal. Honda's waste generation per unit of production has risen in the last five years and is only 7% lower than what it was a decade ago.

In comparison, according to the BMW Sustainability Report, BMW has reduced waste per vehicle produced by 33% in the last five years, bringing it down to less than 4kg per car produced.

Comparing Honda's total waste generation per unit of revenue to some of its sector peers (see graph below), it is clear they are within the bottom half of the industry.



Source: Osmosis proprietary Model of Resource Efficiency

MGM Resorts International: Saving water in the Mojave Desert

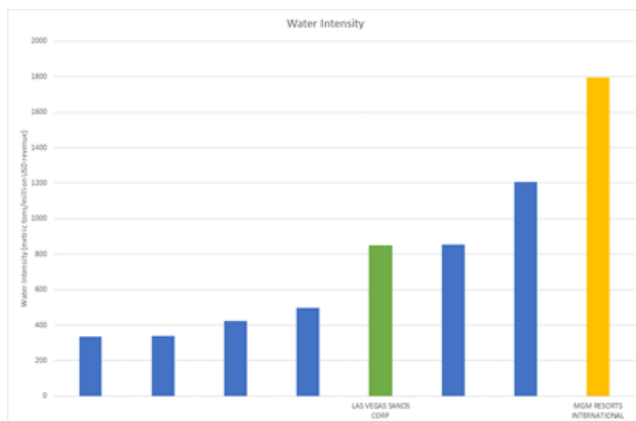
Another company included in the Low Carbon Index is MGM Resorts International, a hospitality and entertainment company operating mainly in the desert city of Las Vegas. Given its location it is key that the company not only invests in carbon reduction initiatives, but also makes sure its reliance on water is optimally managed. While long-term water conservation targets are in place, and many water efficiency technologies are being implemented both in existing and new developments, the company still compares poorly to its direct peers in terms of water consumption within its economic framework, as per the figure below.

In the same sector, our model shows that the Las Vegas Sands Company, which owns the Venetian, Palazzo and Sands Expo, is twice as efficient with its water use according to our model. When it comes to Sands properties on the Strip, the Palazzo is particularly water-efficient because of its nano water filtration system, whereby water is collected from a well below the hotel-casino. This allows the resort's entire horticulture system to operate outside the Valley's water grid.

Water collected from the aquifer is also used for the hotel's cooling system, cleaning and for one of the largest fountains on the property. It's then filtered and reused on-site. In addition, Sands has invested in pool-cleaning equipment that uses glass filters instead of traditional sand filters to further reduce water use.

For any company operating in the Mojave Desert, water security is key to success and if not done properly could have a significant impact on its performance.

The graph below demonstrates the water intensity per unit of revenue of MGM Resorts and Las Vegas Sands Company versus their sector peers.



Source: Osmosis proprietary Model of Resource Efficiency

For more information please visit www.osmosisim.com

© Osmosis Investment Research Solutions Limited

IMPORTANT INFORMATION

This document was prepared and issued by Osmosis Investment Research Solutions Limited (“OIRS”). OIRS is an affiliate of Osmosis Investment Management US LLC (regulated in the US by the SEC) and Osmosis Investment Management UK Limited (regulated in the UK by the FCA). OIRS and these affiliated companies are wholly owned by Osmosis (Holdings) Limited (“Osmosis”), a UK based financial services group. Osmosis has been operating its Model of Resource Efficiency since 2011.

The examples of specific investments described herein should not be considered a recommendation to buy or sell any specific securities. There can be no assurance that such investments will be purchased in a client’s portfolio. It should not be assumed that any of the investments identified in these case studies will be profitable in the future. Whilst the information contained herein is believed to be accurate, no representation or warranty, express or implied, is or will be made, and no responsibility or liability is or will be accepted by Osmosis, or by any of its officers, employees or agents, in relation to the accuracy or completeness of this document or of any information contained within it.