SAGE
INVEST WITH WISDOM™

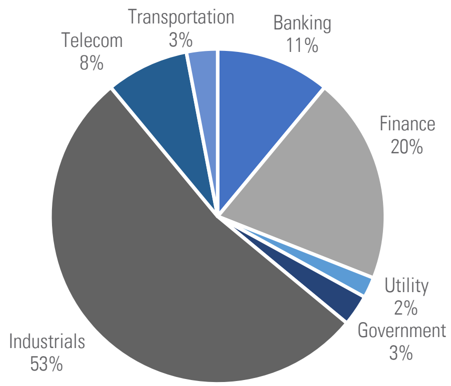
September 2017

ESG PERSPECTIVES

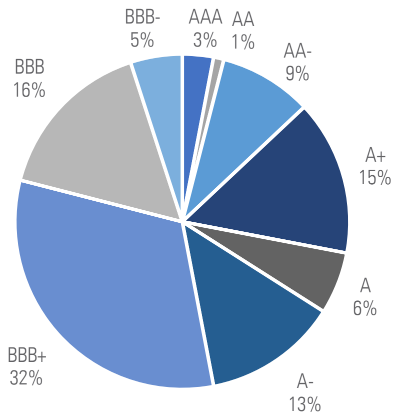
SAGE ESG INTERMEDIATE CREDIT INDEX

Last month we introduced the new Sage ESG Intermediate Credit Index (GUDBESG) powered by Wilshire Associates. The Index is designed to measure a fixed income investment strategy that aims to maximize exposure to positive Environmental, Social and Governance (ESG) characteristics, while maintaining high liquidity and a diversified investment grade profile. The Index uses Sage's proprietary ESG factor analysis framework and rules-based selection process to identify qualified securities from the Bloomberg Barclays US Intermediate Credit Index with optimal ESG ratings, while closely aligning duration and risk characteristics to the Bloomberg Barclays US Intermediate Credit Index. The Index characteristics as of July 31, 2017 are featured below.

SECTOR CLASSIFICATIONS



CREDIT RATINGS



FUNDAMENTALS

Coupon	Yield to Maturity	Effective Duration	Effective Convexity	Years to Maturity	Average Life
3.45%	2.51%	4.28 yrs.	0.26	4.87 yrs.	4.86 yrs.

The rules based methodology behind the Index is straight-forward and supported by the research of Sustainalytics and other ESG information providers. The Index was designed to provide for ease of replication, high liquidity, and optimal trade-ability in all market environments. The portfolio basket is designed around 100-120 individual investment grade security holdings offering high ESG scores with a minimum issue size of $500m. Importantly, none of the holdings exceed 1% of the total index basket and this helps to insure greater liquidity compared to the broader market investment grade credit index.

Fixed income management is largely guided by a variety of market indexes that reflect the core risk characteristics and return attributes of a wide variety of market segments. Until recently ESG metrics were generally unavailable to fixed income investors and advisors seeking to assess various sustainable investment focused fixed income strategies. With the introduction of this Index, market participants will now be able to assess the relative value of both their fundamental and ESG optimization investment management efforts.

ESG INVESTING IN EQUITIES: INHERENT STYLE BIASES?

Responsible investing often comes with the stigma of underperformance – that to align investing with social values means to give up performance relative to conventional market indexes.

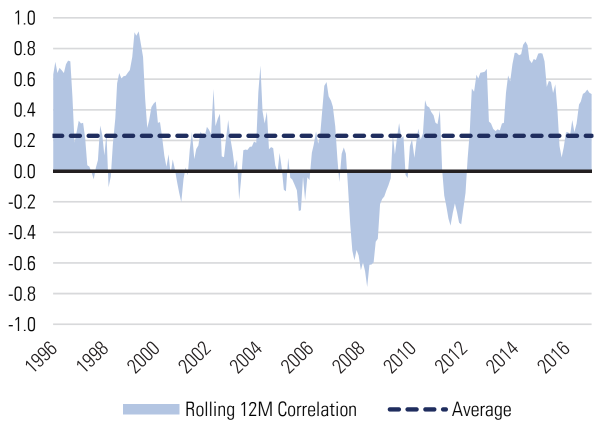
In addition to the studies that have disputed that notion, we do not believe that it is the right question to be asking about responsible investing. The real question regarding responsible investing concerns the difference in its risk profile vs. a conventional index.

Does responsible investing - specifically ESG integration - have inherent style biases? Answering this question allows us to better understand potential untended risks in the portfolio and account for them in our portfolio construction process.

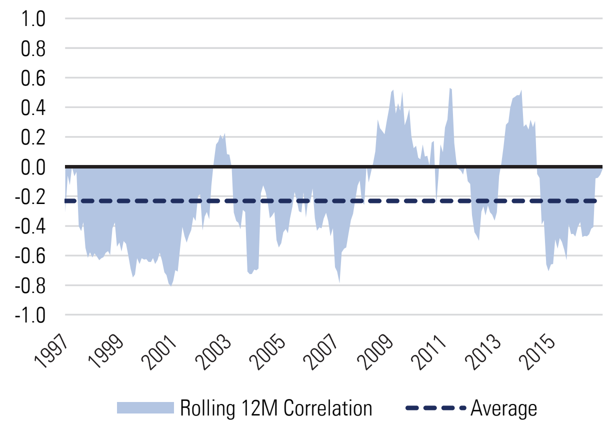
In this study, we conduct an analysis of the alpha (relative return to the S&P 500) of a long-standing ESG equity index, the KLD 400, vs. the relative return of common "smart beta" factors that have been ubiquitous over the past 5 years: Value, Growth, Size, Low Volatility, and Quality.

We find that the ESG returns are generally positively correlated with Growth and Quality, although correlations vary over time. We use this information during our portfolio construction process to account for potential unintended biases. The following charts show ESG rolling correlations vs. Value and Growth. Over the past 20 years, ESG excess returns have been on average negatively correlated to Value and positively correlated to Growth. ESG excess returns do not seem to have much of a relationship with the size factor, and interestingly its relationship with Low Volatility has flipped since the financial crisis.

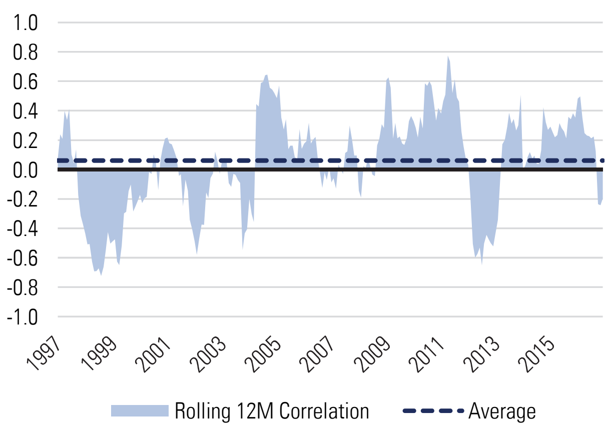
Rolling 12M Correlation of Excess Return: ESG vs. Growth



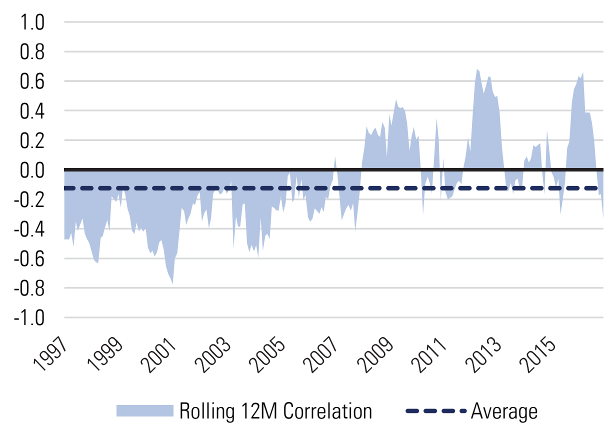
Rolling 12M Correlation of Excess Return: ESG vs. Value



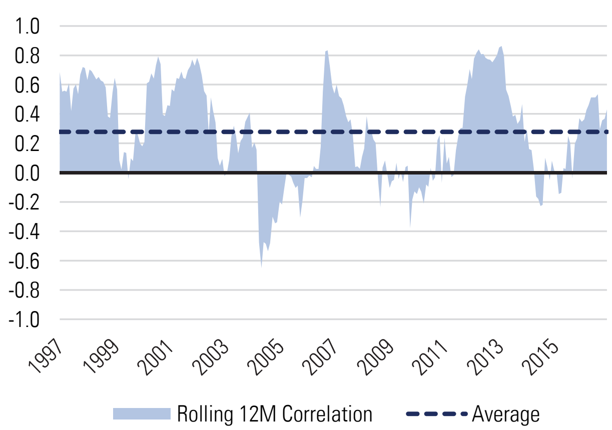
Rolling 12M Correlation of Excess Return: ESG vs. Size



Rolling 12M Correlation of Excess Return: ESG vs. Low Vol



Rolling 12M Correlation of Excess Return: ESG vs. Quality



List of Indexes

Index	Style
S&P 500	Core
KLD 400	ESG
S&P 500 Pure Value	Value
S&P 500 Pure Growth	Growth
Russell 2000	Size
MSCI USA Minimum Volatility	Low Volatility
MSCI USA Quality	Quality

Lastly, ESG has a positive relationship to the Quality factor with a positive correlation for the majority of the past 20 years.

Sage's approach to ESG investing involves both ESG integration as well as traditional portfolio construction and risk management. In the Global Equity ESG strategy, we leverage the tools that we use in our flagship equity ETF strategy to construct a portfolio of best-in-class ESG ETFs with a balanced, diversified, and intentional risk profile.

EVALUATING GENERAL OBLIGATION DEBT FOR ESG COMPLIANCE: FOLLOW THE MONEY

At Sage, when it comes to evaluating municipal issues from an ESG standpoint, stated use of proceeds reigns supreme. A clear, concise stated use of proceeds gives an end investor peace of mind that his investment dollars are going to be used as intended, and not diverted elsewhere if the issuer determines a better use. When it comes to general obligation debt under the governance framework, use of proceeds becomes even more important.

A general obligation bond is a common type of municipal bond in the United States that is secured by a state or local government's pledge to use legally available resources, including tax revenues, to repay bond holders. Proceeds from this type of debt issuance can be used in a multitude of ways: funds can be deposited into a general fund to be used for a myriad of expenses, they can be used to fund a large swath of projects or they can be used to fund very specific projects. How the proceeds are going to be used is laid out in the offering statements. From an ESG perspective, since use of proceeds can't be determined to be ESG compliant when proceeds are deposited into a general fund, these issues are excluded from consideration. When proceeds are expected to be used to fund a large swath of projects, it can be hard to determine whether the overall issue is ESG compliant if there is a mix of projects that would qualify along with projects that wouldn't qualify. If the proceeds are going to be used for a very specific project, then the evaluation of that project should provide a clear yes or no regarding compliance.

An example of a non-compliant and a compliant general obligation issue is laid out below with their actual stated use of proceeds.

- ***New York City General Obligation Issue, 5.00% of 3/1/33 – Use of proceeds: The proceeds of the bonds will be used for capital purposes.***
- ***California State General Obligation Issue, 6.20% of 10/1/19 – Use of proceeds: to fund various projects under certain of the Bond Acts (listed). California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Act of 2002. California Reading and Literacy Improvement and Public Library Construction and Renovation Bond Act of 2000. Disaster Preparedness and Flood Prevention Bond Act.***

And so on. As you can see, there are two very different stated use of proceeds. One is very general, the other covers a large number of projects, all of which would be considered ESG compliant, therefore that California issuance would be considered for inclusion within our investable universe. The second factor to consider would be an assurance that proceeds will be used as intended.

In the news, recently there was an article reviewing New Jersey Transit and their raiding of project funds to pay day-to-day operating expenses. Granted, they are diverting funds from their federally funded project budget, but this should give investors pause as to whether they would divert funds from their municipal bond funded project budget. Their offering statements might state a use of proceeds, but their actions indicate that they might not follow it. On the other side, the State of California has added language to certain offering statements that the proceeds ***cannot*** be diverted away from the intended projects.

With ESG compliant General Obligation debt, knowing how the proceeds are going to be used, and being assured that they are going to be used as intended is a big part of the evaluation process. Taking the time to thoroughly review the offering statements, and the past actions of the issuer are all part of the ESG evaluation process within the Governance framework.

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