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Connection

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By Julie Gorte, Ph.D., and Matthew Wright

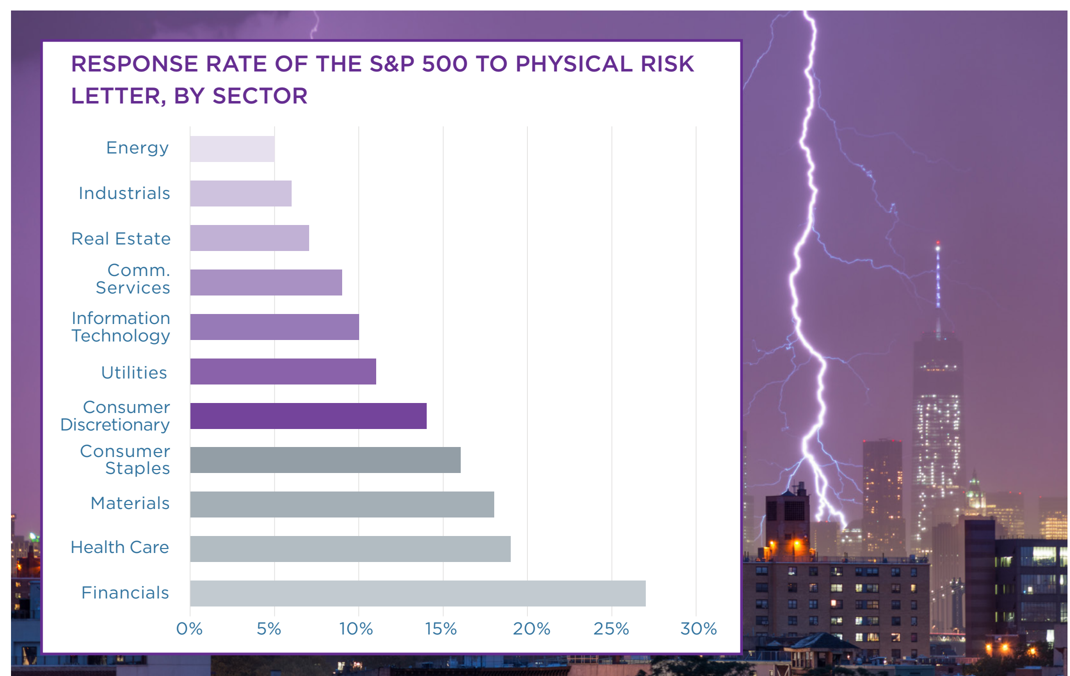
Flooding, droughts, rising sea levels and extreme weather events are posing increased risks not only for companies but for investors, financial markets and the global economy. Two-thirds of large companies around the world have at least one asset at high risk because of the physical hazards created by a warming climate.[1] It is essential that financial markets plan for the physical risks of climate change.

Where a company operates is a major factor in its exposure to physical risks. While companies often provide general geographic information about the locations of their assets, such as states, regions or countries, that is not specific enough. Investors need much more precise physical location data from companies to help make sound long-term financial decisions.

In late 2020, Impax teamed up with the New York State Common Retirement Fund to ask listed US companies in the S&P 500 Index to voluntarily disclose the locations of their significant assets, including facilities, buildings and installations whose loss or impairment would impact financial results.[2]

We received responses from 13% of the companies. Only three demonstrated to us that they had seriously considered their liabilities due to physical climate risk and had plans for adapting to or mitigating those risks.

While it was encouraging to learn that at least a few companies have given physical risk much thought, these responses illustrate



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Proposed DOL Rule a ‘Great Step Forward’

By Joseph Keefe

The Department of Labor has issued a proposed rule that would empower ERISA fiduciaries to consider environmental, social and governance (ESG) factors when making investment decisions on behalf of plan participants and when voting corporate proxy ballots.

The proposal reverses the DOL rule enacted in late 2020, which inexplicably asserted — despite abundant evidence to the contrary — that ESG factors were not material to financial performance, thereby essentially prohibiting fiduciaries from including ESG funds in retirement plans.

A win for retirees

The new rulemaking is a great step forward. The transition to a more sustainable economy will require increased attention to material risks and opportunities, including those related to ESG factors. The DOL’s prior rule effectively prohibited consideration of such material factors, substituting instead the judgement of government bureaucrats for that of experienced investment professionals and fiduciaries. That put today’s workers and tomorrow’s retirees at risk, and it is encouraging to see that the department has reversed course.

The new proposed rule states that “Material climate change and other ESG factors are no different than other ‘traditional’ material risk-return factors.” As Employee Benefits Security Administration (EBSA) Acting Assistant Secretary Ali Khawar underscored, “in that context, fiduciaries should be taking them into account.”

At Impax, we couldn’t agree more. Careful consideration of ESG factors can help spotlight risks — and opportunities — that must be managed so that ERISA fiduciaries can uphold their responsibility to act in the best interests of plan participants. This is particularly the case as we transition to a more sustainable global economy, where environmental issues such as climate change and human capital issues such as diversity and inclusion will have more bearing on how companies and investment portfolios perform.

The evidence underscoring the materiality of ESG factors to business and investment risk is at this point overwhelming. An analysis of more than 2,000 empirical studies concluded that approximately 90% of the studies found a significant relationship between ESG factors and corporate financial performance, and the majority of studies found that the relationship was statistically significant, positive and stable over time.[1]

Under the proposed rule fiduciaries will now have the freedom to choose strategies that benefit participants’ economic interests while also addressing such ESG issues as climate change, gender and racial equality and other critical global challenges that are already influencing financial markets. This is good news for retirement investors.

The role of Congress

While this new rule is necessary, and prudent, it won’t vanquish the chilling effect created by the DOL’s shifting interpretations of ESG materiality from one administration to the next. Even with the new proposed rule in place some fiduciaries may be reluctant to include ESG options in retirement platforms for fear they will have to change course yet again under a new administration.

Congressional action would be welcome. It is high time to end the debate about whether sustainability or ESG factors are material. They clearly are. The market has spoken and now the Department of Labor has as well.

Today there are nearly 400 sustainable mutual funds in the United States.[2] Seventy-two percent of Americans are interested in sustainability-minded investments.”[3] An RBC Wealth Management survey of 1,000 clients conducted in 2021 revealed that 61% want to increase the amount of environmental, social and governance-focused holdings in their portfolios.[4] In fact, ESG funds attracted $51.1 billion from investors in 2020 — the fifth consecutive year of record-breaking growth.[2] Yet fewer than 5% of defined-contribution plans include at least one sustainable fund,[5] despite this growing demand — 69% percent of respondents to a 2021 Schroders study said they would or might increase their contribution amounts if their retirement plans included ESG options.[6] The proposed rule gives plan administrators a green light to add the options that growing numbers of investors clearly want.

The DOL rule is in the best interests of retirement plan participants. Should it be adopted, retirement plan sponsors will gain the additional leverage they need to evaluate a range of risks and opportunities arising as our global economy transitions to a more sustainable model. This will be critical to building resilient investment portfolios for plan participants in the years ahead. Indeed, we believe their retirement security will depend on it. X

[1]Gunnar Friede, Timo Busch and Alexander Bassen, “ESG and Financial Performance: Aggregated Evidence from More Than 2,000 Empirical Studies,” Journal of Sustainable Finance & Investment, Volume 5, 2015.

[2]Jon Hale, “US Sustainable Funds Continued to Break Records in 2020,” Morningstar, Feb. 25, 2021.

[3]Ray Sin, Ryan Murphy, and Sam Lamas, “The True Faces of Sustainable Investing,” Morningstar, May 3, 2021.

[4]Jacqueline Sergeant, “Female Investors Expect Advisors To Be Informed About ESG,” Financial Advisor, April 8, 2021.

[5]Samantha Lamas, Michael Thompson, “Re-Envisioning ESG in 401(k) Retirement Plans,” Morningstar, May 3, 2021.

[6]Schroders, “US Retirement Survey,” 2021.

Pax World Funds News

A High-Yield Bond Fund Says Goodbye to Fossil Fuels

Barron's profiled Portfolio Manager Peter Schwab and the **Pax High Yield Bond Fund** in a recent article.

In it, Peter describes the thinking behind making the Fund the only active high-yield bond mutual fund without traditional energy holdings.

Read more at
www.impaxam.com/barrons

The Fund can invest in "junk bonds" which are considered predominately speculative with respect to the issuer's continuing ability to make principal and interest payments when due. Yield and share price will vary with changes in interest rates and market conditions. Investors should note that if interest rates rise significantly from current levels, bond fund total returns will decline and may even turn negative in the short term. Mortgage related securities tend to become more sensitive to interest rate changes as interest rates rise, increasing their volatility. There is also a chance that some of the fund's holdings may have their credit rating downgraded or may default.

Welcome, Ed Farrington

Ed Farrington joined the Impax team in late September as Head of Distribution for North America, a new role at our growing firm. Ed will lead Impax's North American distribution efforts, working with the leadership of the institutional and intermediary sales and marketing teams and in coordination with the global client services and business development team.

"We are delighted to welcome Ed to the firm," said Impax President Joe Keefe. "He is a seasoned industry veteran, and his strong relationships and deep insights across distribution channels will help us deliver on our next stage of growth."

Learn more about Ed at
www.impaxam.com/ed

All About Climate

Few global challenges loom as large as climate change; thus, we were honored to be an active participant in COP26, joining global public policymakers and other solution-seekers in Glasgow for the annual Conference of Parties in November.

Impax CEO Ian Simm and Head of Policy and Advocacy Chris Dodwell shared our firm's climate change thinking — and actions — during week two of the event. Find out more about their contributions on our dedicated COP26 page. **www.impaxam.com/COP26**

Conversation Pieces

"We are interested in semiconductor companies because of the profound energy efficiency from using chips to monitor performance data."

David Winborne, Senior Portfolio Manager, Managing Director
MarketWatch

"A lot of young people want to invest in companies that are part of the solution rather than part of the problem. Whether it comes to climate change or diversity and equality issues, they want to invest in companies whose values are aligned with theirs. That's moving the marketplace, and we're seeing that movement."

Joseph Keefe, President
InvestmentNews

"We have an unequal society that has been reinforced by decades of discrimination and policies, and we need to remedy it."

Julie Gorte, Senior Vice President for Sustainable Investing
Roll Call

IRA Contributions

It's January, you can make a 2022 IRA contribution! And, if you haven't yet, you can still make a 2021 contribution until April 15, 2022.

Contribution limits didn't change this year. If you are under the age of 50, typically you can contribute the smaller of $6,000 or your taxable compensation for the year. If you are 50 years of age or older, you can contribute the smaller of $7,000 or your taxable compensation for the year.

Subject to deduction limits, Traditional IRA contributions are generally made on a tax-deferred basis, which means that you may be able to deduct some or all of your contribution from your taxable income. Taxes are typically paid when funds are withdrawn, presumably during retirement, when you may be in a lower tax bracket. As a reminder, with the passage of the SECURE Act in 2019, there is no longer a maximum age for being able to contribute to a Traditional IRA.

Subject to income limits, contributions to Roth IRAs are not tax deductible. Since these funds were already subject to income tax, after holding a Roth IRA for five years, certain types of withdrawals, including those taken in retirement, can be made on a tax-free basis.

For more information about your eligibility or the differences between Traditional and Roth IRAs, please see IRS Publication 590-A, "Contributions to Individual Retirement Arrangements (IRAs)" at **www.irs.gov**, or call the IRS at 800.829.3676 to order a copy.

You can open a new Traditional IRA or Roth IRA, or you can make a contribution to an existing account through the Pax Portal at

www.impaxam.com/account. For assistance, or for other options, please call Investor Services at 800.372.7827. **X**

Please note that the information above does not constitute tax advice and, as of the time written, can change with the passage of legislation currently before Congress. State tax regulations may differ from federal tax regulations. Always consult your tax advisor before making any tax-related investment decision.

SEEKING COORDINATES: A UNIQUE ENGAGEMENT ON PHYSICAL CLIMATE RISK, CONTINUED from FRONT PAGE

how unprepared most companies are for the effects of climate change. We believe that our engagements will help put this topic on the agenda for boards and executives.

In our report "Physical Climate Risk and the S&P 500," we explain our engagement and detail the responses by sector, how executive suites are thinking about physical climate risk, and what we've concluded about companies' preparedness for the physical risks of climate change. **X**

View the report on our website:
www.impaxam.com/SP-500

The authors would like to acknowledge Eri Yamaguchi, ESG Investment Officer at New York State Common Retirement Fund, whose insights have been essential to this engagement.

[1]S&P Global, "Physical Risks," www.spglobal.com/esg/education/essential-sustainability/climate/physical-risks?gclid=CjwKCAjwr56IBhAvEiwA1fuqGiu-wj6EseQ3n-k4VGkGyNA2oyLUmhEROMk3eZJge1jyD1gCKrtnXBoCs8cQAvD_BwE. Accessed Sept. 15, 2021.

[2]Impax does not own shares in all the companies in the S&P 500 Index.

The S&P 500 Index is an unmanaged index of large capitalization common stocks.

You should consider a fund's investment objectives, risks, and charges and expenses carefully before investing. For this and other important information, please obtain a fund prospectus by calling 800.767.1729 or visiting www.impaxam.com. Please read it carefully before investing.

An investment in Pax World Funds involves risk, including loss of principal. Past performance does not guarantee future results.

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ESG Strategy Risk - The investment techniques and decisions of the investment adviser and the Fund's portfolio manager(s), including the investment adviser's assessment of a company's ESG (Environmental, Social and Governance) profile when selecting investments for the Fund, may not produce the desired results and may adversely impact the Fund's performance, including relative to other Funds that do not consider ESG factors or come to different conclusions regarding such factors.

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