Today’s Global Quality ESG Strategy

(Publication date 22 March 2021, amended as per 31 October 2023)

Introduction

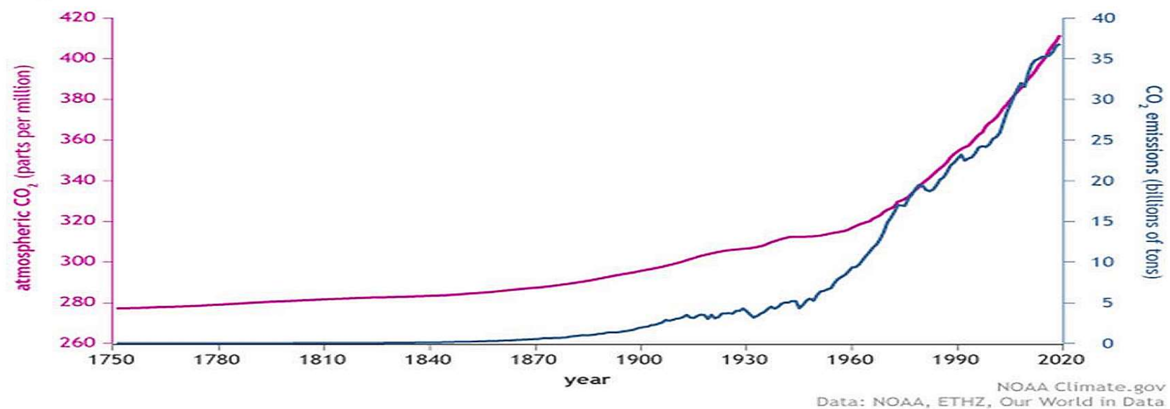
We use various tightly structured models when managing our clients' assets. These models can be roughly divided into technical momentum models and fundamental models. Today's Global Sustainable Equity Strategy is a model in the fundamental category, but also promotes an ESG component. As such, we qualify this model as an “Article 8” model under the SFDR (Sustainable Finance Disclosure Regulation).

Sustainable investments at Today’s Group

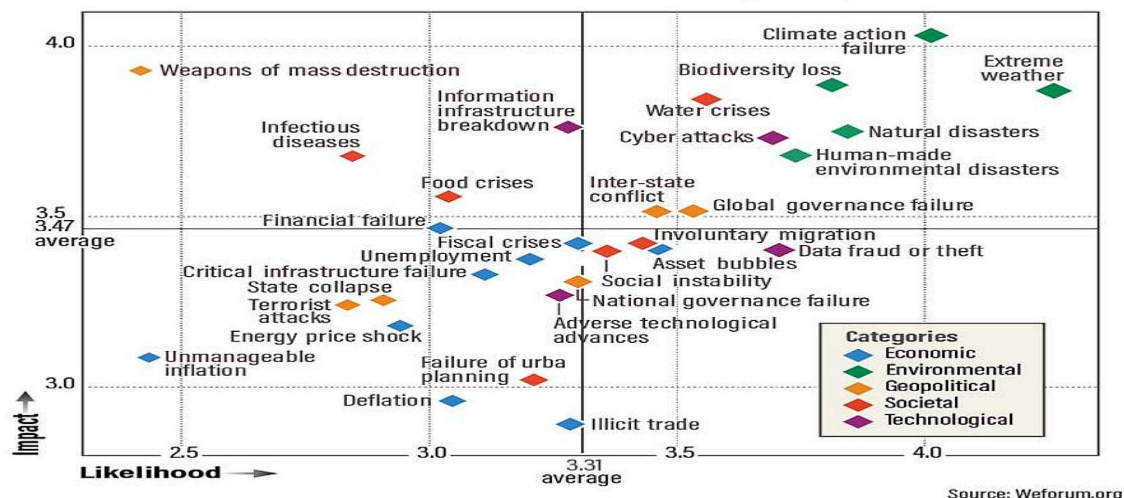
To get to a more sustainable world in 2050, a whole series of measures must be taken. Legislators and regulators have decided that the financial world can also make a significant contribution to this by imposing requirements on the companies in which the financial world invests on behalf of customers. Today's Group BV subsequently setup up its own ESG policy in 2021 and published this on our website. This piece is the final part of a series of articles in which we have explained the laws and regulations in the field of ESG (Environment Social Governance) and investigated how these laws and regulations can be incorporated into our decision models and reports.

Gradual tightening of points of attention: greenhouse gases

As a first point of attention, legislators and regulators have targeted the emission of greenhouse gases in the atmosphere (particularly CO2 and methane). These emissions must be significantly reduced in the coming years. The current emissions of these gases can no longer be absorbed by the natural CO2 absorption of trees, plants and the sea. The CO2 concentration in the air has never been as high as it is now, 416 parts per million (ppm) (data spring 2021). In 2019 the average was 409.8 ppm. Calculations suggest that global temperatures could rise by more than 3 degrees compared to the 1990-average if this increase in concentration continues. This is accompanied by global disruptive environmental risks such as extreme weather, loss of biodiversity, environmental disasters, sea level rise, floods, natural disasters such as (extreme) drought, freshwater shortage, subsidence of buildings and much more.



The amount of CO2 in the atmosphere ppm (pink line) together with CO2 emissions (blue line) have both increased significantly since the Second World War. Due to the industrial revolution from 1800 onwards, emissions due to human activities increased, an acceleration in this can be seen from 1950 onward. CO2 emissions rose from 5 billion tons per year to 35 billion tons per year by the end of the last century. As a result, the CO2 ppm continues to rise worryingly fast.



Research shows time and time again that humans must reduce CO2 emissions.

Following points of attention

It is expected that the next point of attention will be biodiversity on our planet. Lawmakers and regulators are already preparing to require companies to not only report on their sustainability plans regarding greenhouse gas emissions, but also on the impact they have on biodiversity in the environment in which they operate. Ultimately, the intention is for companies visualize what their “PAI” (Product Adverse Impact), or the negative implications that a company and therefore (for financial institutions) the investment products in which investors can participate, have on the 17 UN goals for a better world.

17 UN sustainable development goals

In 2015, the United Nations defined 17 points of attention, 17 goals that should lead to an improvement in the quality of life in our world and society. The idea is that these objectives should all be achieved by 2030 (but whether this will actually be achieved is highly questionable).

VN Sustainable Development Goals

All these objectives will ultimately have to be addressed in reports to investors. In this sense regulators have since introduced three scopes of reporting responsibility in terms of internal ESG assessment for companies:

1.) Scope 1 emissions that originate directly from sources owned or controlled by an organization.

2.) Scope 2 emissions encompass those greenhouse gases resulting from generating the electricity, heat, or steam that an organization purchases and consumes.

3.) Scope 3 encompasses the most comprehensive category of indirect emissions.

So, if Scope 1 and 2 focus on emissions from owned sources and energy purchases, while Scope 3 captures all other indirect emissions occurring throughout a company’s value chain (source: DyDon AI 2023).

The scope 1, 2 and 3 reporting standards for companies are formulated in another regulation called CSRD or Corporate Sustainability Reporting Directive. Ultimately a this type of in depth reporting requirement will be demanded on all 17 UN Sustainability goals.

What can an investor contribute to this?

With these data, financial service providers such as Today's Group can then determine the "Product Adverse Impact (PAI)" of the securities in which our customers invest, whether or not investments are based on our initiative (asset management, asset advice or execution only). As mentioned, the first point of attention is the amount of greenhouse gases emitted by companies in which investments are made. The PAI is then the number of tons of CO2 and the amount of Methane emitted by the company, directly, but ultimately also indirectly. Once this is visualized by all companies in the investor universe, investors can concentrate their investments in companies that are actively reducing their greenhouse gas emissions. And this also applies to companies that have a policy for the sustainable use of freshwater, energy consumption and waste and so on. In addition to the fact that we already test our own universe against specific conditions (see the previously mentioned piece describing our ESG policy), Today's Group has contracted Financiële Diensten Amsterdam (FDA) for its research to create its Global Quality ESG Strategy portfolio.

FDA (Financiële Diensten Amsterdam) Consultancy

Financial Services Amsterdam (FDA) specializes in independent, fundamental research and portfolio construction for the professional market. A team of more than 200 analysts takes care of the analyses, selection and optimal portfolio composition. This has been done for more than 25 years based on our own original research.

Sustainability is an integral part of FDA's investment philosophy. All companies in the FDA universe are subject to a proprietary sustainability analysis that is an important part of the company's overall assessment of investment risks and long-term prospects. These analyzes result in sustainability scores for the three ESG dimensions and twenty subcategories.

Companies with the highest ESG scores are eligible for Today's Group's Sustainability portfolio. The explanation of this Sustainability Framework and examples of ESG analyzes are available to you.

FDA ESG Rating system (source: FDA Consultancy)

In addition to a fundamental assessment of the financial quality of a company, its growth prospects, etc. (see below), there are three points in the FDA rating that are directly linked to the sustainability score. Companies receive 1 point for each dimension (E, S and G) for which at least a score of 65% is achieved and provided that the score on all three dimensions is at least 50%.

Shares of companies with a score of less than 50% for one or more of the three dimensions are not eligible for investment. Today's 'Global Quality ESG' portfolio even has a higher limit of at least 65% for all three dimensions.

Within the FDA Sustainability Framework, FDA examines twenty aspects, including the appropriateness of the corporate structure, financial incentives for management, quality of human resource management, exposure to political and regulatory risks, human rights, occupational health and safety, consumer protection and environmental issues.

An individual risk assessment is made for all twenty sub-aspects, which is reflected in a score from 0 to 5, where 0 represents very high risks and 5 represents hardly any risks. The individual scores are also extensively motivated to provide insight into the reasoning for the risk assessment.

The individual scores are added up to a total score, and to a score for the three main dimensions. A score of 100% means the maximum score on all aspects. The 'governance' dimension has a weight of 35% in the total score, the 'social' dimension, with the most sub-aspects, contributes 40% and the 'environmental' dimension has a weight of 25% in the total.

Based on the scores of companies for the individual dimensions and sustainability as a whole, a comparison within the sector (peer group) and the FDA universe is possible.

The selection thus obtained guarantees that there are so-called Article 8 investments, which means that the entire strategy qualifies as an Article 8 Strategy.

Article 8 Strategy

The law recognizes three different categories into which investment products can be divided. The name follows a qualification defined in the SFDR. The SFDR recognizes so-called Article 6, Article 8 and Article 9 investments. Article 9 investments refer to investments that have a demonstrable specific impact in favor of the 17 ESG objectives of the UN. A company must actively contribute to achieving one or more of these objectives in order to be part of an Article 9 portfolio. The Italian company Aquafil (see our analysis on this company) meets this type of impact investment. ESG plays no role at all in an Article 6 investment. It must be classified as such, but investors who invest in Article 6 strategies have not defined sustainability objectives and do not want them incorporated into the strategy. Article 8 investments are investments that pursue a sustainable character, but are passive in this regard.

In the case of Today's Global Quality ESG Strategy, no active impact is sought, but it does require that companies meet relatively high ESG quality standards. For that reason we qualify this as a passive ESG strategy or an Article 8 strategy.

Impact of sustainability criteria on returns

Sustainability is often seen as a cost item. The more a company has to invest to make production more sustainable, the greater its competitive disadvantage becomes due to an ever-increasing cost of the company's product. Counter to this, companies that pay a lot of

attention to “sustainability” generally run a much lower reputation risk. In the example of Aquafil, the company must incur more costs to produce Nylon 6 according to the Econyl label. But with this label it has become the main supplier for plastic coverings for the “completely green” Audi. We assume that companies that achieve a high sustainability score as described above will generally ultimately show a better return than less sustainable competitors. In the present strategy, we therefore also think that the sustainable character has no impact or even a positive impact on the return of the strategy.

Specific exposure to sustainability risks

The companies whose stocks are chosen in this strategy are all exposed to various sustainability risks. But the high ESG score (for both the three individual dimensions and the combined score, which must be more than 65%) means that they are less exposed to those risks than many of their competitors. That said, much is still unclear in the sense that complete data sets up to scope 3 on all 17 UN goals are not yet available for all companies. For example, a lot of attention is currently being paid to the odious character of fossil fuels. The result is that many IT service providers are included in these types of models precisely because they are not involved with fossil fuels at all. But the biggest energy guzzlers at the moment are AI-related, cloud-operating large IT companies such as Alphabet, Microsoft, Meta and Amazon. The enormous energy consumption that these companies are responsible for is not yet reflected in many ESG analysis models. So this is clearly a sliding scale. What can be characterized as sustainable one moment may no longer be so the next. Unclear and often slow-to-availability legislation and regulations also do not contribute to consistency and predictability in this area. But our strategy is flexible enough to adapt to this sliding scale over the years. In the reports that we make available to our clients, we make the actual exposure to sustainability risks visible as much as possible. For comparison, we also include the sustainability risks associated with the benchmark of this strategy, the MSCI World Sustainability Index in €.

Fundamental assessment

In addition to the fact that companies in this model must meet specific sustainability criteria (at least a 65% score on all three ESG dimensions), companies are also tested against a number of fundamental criteria that form the basis for the FDA's research effort and which we as asset manager in collaboration with the FDA also use within the Today's Global Quality ESG Strategy.

The FDA bases its findings on its own in-house original research. Consistent application of these principles reduces risk and increases returns (a principle that applies to Today's Group in all its facets). Portfolios are composed of a relatively limited universe of internationally operating companies. The limitation of the fund universe ensures a strong focus on the companies followed. This ensures portfolio choices with high conviction, relatively few changes and therefore an attractive return in the long term.

Risk assessment is the essence of the investment process. Risks are limited by understanding what is being invested in. The special attention to risk in this strategy is manifested in an in-house (FDA) developed risk concept. This is fundamentally different from common risk concepts that can be traced back to a mathematical/statistical description of historical price movements. The risk concept used by FDA reflects an evaluation of a number of more or less objective and a number of subjective fundamental criteria, including the financial strength of the company, the quality of management, the degree of competitive advantage, and the sustainability of the business model.

Quantitative criteria

Roughly speaking, it can be stated that the basic quantitative criteria for fundamental screening are:

- the universe is defined by all the stocks included in the MSCI Europe Index and the MSCI USA Index;
- the market capitalization is at least US$10 billion;
- the company's ROIC (Return On Invested Capital) must be at least 7.5% (average);
- the PEG ratio should be between 0.5 and 5;
- EBITA margin must be greater than 8%;
- the total debt to equity ratio should not exceed 100%.

Moment of evaluation and number of positions

The fundamental analysis of companies takes place continuously, but new data in fact only become available when valuations are adjusted (usually after each quarterly report) and when annual figures are published.

A maximum of 30 shares are held in the portfolio.

Use of ETF / Trackers

In the past, a number of ETFs (Exchange Traded Funds, also called Trackers) have been used for up to 10% of the portfolio. This often involved trackers that followed a specific ESG Index. This part of the strategy is now being phased out; in accordance with our own and the FDA's principles, the Strategy now focuses exclusively on individual shares.

Investment horizon

The approach within Today's Quality ESG Strategy does not typically support a short-term trading strategy. Shares once purchased can remain in the portfolio for years. After all, if the company continues to meet the growth criteria and never really becomes too expensive, its future value will increase every year and the share price can continue to rise annually without ever having to be sold. This is also called a “buy-and-hold” strategy. This strategy, as mentioned above, has a very big disadvantage. If stock markets as a whole panic, cheap

stocks will become even cheaper. There is no point in selling, but this does result in a sometimes significant price loss. Eventually this will be caught up, but that can take a long time and sometimes requires a lot of patience and nerves of steel. This strategy is therefore not without risk!

Statistics

There are many statistics that can be calculated on the results of this method. Legally required quantities such as realized net return (Net R), Total Cost of Ownership (TCO), Risk as measured by the standard deviation of results (StDev). We actively apply this methodology in practice. All numbers published here are based on the model portfolio that we have administered for years, the portfolio that is actually and fully invested on the basis of Today's Quality ESG Strategy.

Year	2018	2019	2020	2021	2022	2023 until 27/10
Net Return	-/- 2,9%	35,6%	10,6%	27,4%	-/- 19,7%	7,1%
StDev	Nvt	27,2%	19,5%	17,2%	22,4%	8,1%
TCO	1,4%	1,4%	1,4%	1,4%	1,4%	1,4%

For a detailed explanation of the concept of TCO, please refer to the special explanation on our website. We suffice here to indicate that this percentage is the total cost percentage, which includes our own management costs (incl. VAT), all transaction costs, but also all costs charged by any funds we invest in themselves. The results shown are inclusive, i.e. after deduction of all costs (the TCO). What is not included here is the difference between the bid and ask prices, which more often than not exist on stock exchanges. This is especially important for highly illiquid investments, but in this model only liquid investments are chosen and this part of the TCO is negligibly small. In addition, actual traded prices are used and these costs, to the extent they occur, are thus also fully included in the Net Return.

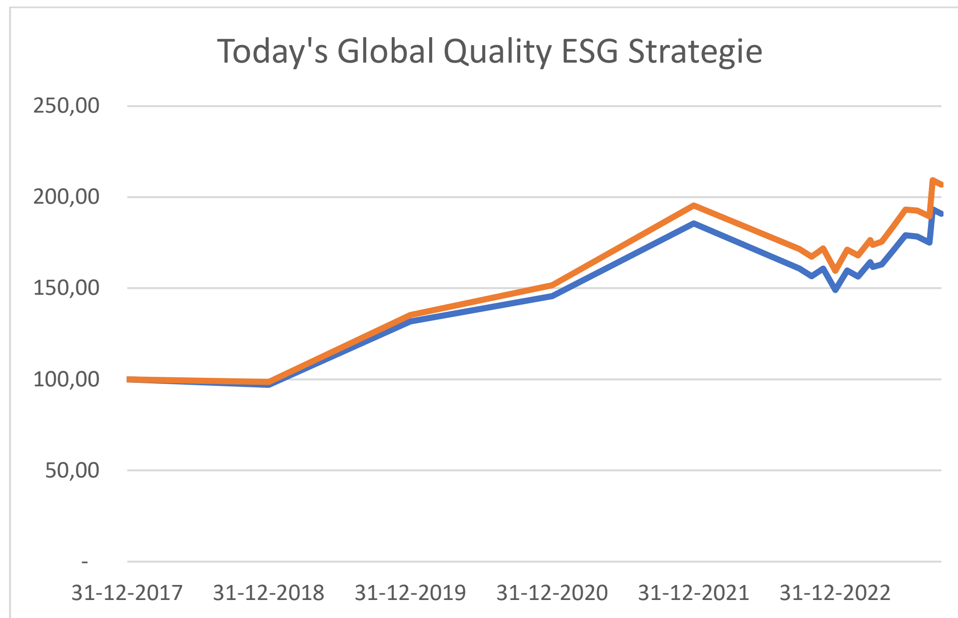
Supervisors make a distinction between an expected TCO (TCO ex-ante) and a realized TCO (TCO ex-post). The TCO in the table is an ex-post TCO. We estimate the ex-ante TCO at approximately 1.5% per year. The actual percentage will usually not deviate significantly.

In addition, the transaction frequency can influence the ex-ante TCO.

Graphical representation of returns with and without costs

Some time ago, the regulator added an obligation to the publication of returns. This concerns the graphical representation of a net return development, which must then be compared with the same value development of the portfolio, but without costs (i.e. with a TCO of 0%). This completely ignores the added value of the manager and assumes that the return of a model can also be obtained by any investor without the cooperation of an asset manager. It also ignores the fact that this not only by definition leads to a graph that is above

the net return, but the longer a model is used, the greater that difference becomes. We have included an opinion on this in our TCO publication.



The graph shows how the Global Quality ESG Strategy portfolio has developed since January 1, 2018. The blue line is the actual return of the portfolio, net, including costs, the orange line is the same development, but without all costs . Both graphs are shown based on the actual purchase and sale prices and the graphs are not indexed but based on a portfolio that was worth € 130,000 on January 1, 2018. By definition, the orange line will increase faster than the blue line, but you will also see that the deviation is developing quite stably. And that has to do with the cost structure, which has been the same for years.

Risks of the Today's Global Quality ESG Strategy

But in principle the model is always fully invested in shares, so it does not engage in "market timing". This is therefore one of the most important risks of the model. When stock markets enter a "bear market", stock prices fall across the board. A strategy that is fully invested in shares will do the same and will therefore move downwards during general market declines. By introducing nuances, the risk can be mitigated somewhat, but not much. There is a real chance that the value of the portfolio will halve in such a phase. In the period 2001 – 2003 and again in 2008, many fundamentally driven strategies that remained fully invested in shares lost more than 40% to sometimes even 60% of the value of the portfolio. The models also recover afterwards, but one must have nerves of steel to cope with this risk.

Other risks are the concentration risk and the liquidity risk of the portfolio. Investments are made in a maximum of 30 individual shares. Individual stocks can experience significant price movements from one day to the next. For example, Adyen's price halved within a few days in August 2023. With an exposure of more than 3% of the portfolio at that time, this price drop alone resulted in a loss of 1.5% on the total portfolio.

The liquidity risk is formed by the question of whether or not a share can be traded at any time. That risk is smaller within this strategy because larger, established companies are generally chosen, whose tradability on stock exchanges can actually be considered good under almost all circumstances. But it is always possible that trading in a specific share will be stopped at some point and investors will no longer be able to get rid of their position, or only at relatively high costs.

Currency risk

Shares are chosen that are quoted in €, in $'s (often the largest group), CHF, DKK, SEK and GBP. Thus a currency risk may be associated with the shares. But shares are compared in terms of valuations, so currency fluctuations ultimately lead to purchases or sales in favor of the total return because falling currencies lead to falling prices and therefore cheaper shares.

Risk of delay's in information

The analysis methodology is based on historical figures. Annual accounts are usually only published a few months after the end of a year. The methodology therefore inherently has a delay of many months on the current developments of a company. Moreover, a good foundation does not protect a portfolio against general price falls.

Investors are therefore advised not to invest all their assets using this system, but to make a diversification within their assets themselves. As a building block in the overal portfolio, this can be an excellent addition to the total.

Other information

Participation in Today's Global Quality ESG Strategy is possible from € 100,000 per account. Management costs are 1.0% per year excl. VAT to be calculated in three monthly installments at the start of the period (every quarter in advance).

The value of your investments may fluctuate. Past performance is no guarantee for future results.

The Hague, 22 March 2021 (amended 31 October 2023)
Today's Group BV
Gijsbrecht K. van Dommelen

www.todaysgroup.nl

Used url's:

https://todaysgroup.nl/nieuws/esg-en-de-keuzecriteria-7-van-today-s-group-als-vermogensbeheerder/

http://www.fdaconsultancy.nl

https://www.vladeracken.nl/aquafil-spa-circulariteit-to-the-max/

https://www.vladeracken.nl/11310-2/