

# JULEX CAPITAL

## The right way to do ESG . . . and an overall review

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- Started in Europe
- Very well developed over there
  
- Here in U.S.
  - Far behind Europe
  - Very old
  - First called “socially responsible investing”
  - Also touched on “economically targeted investments”
    - Restricted to public pension plans

# Can you have both - superior investment results and ESG/SRI

- Common claim
- You can have it all
  - ESG . . . Socially responsible investing
  - Superior risk-adjusted returns
  
  - Doing good
  - Superior investment returns
- Let's examine this contention

# Is it a rewarded Beta?

If so . . . then it makes sense . . . as a passive or index ETF

## Consider fixed income

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- Checking account
- Money market
- Bank CD
- Ultra short term bond fund
- Short term bond fund
- Intermediate term bond fund
- Long term bond fund
- High yield (junk) bond fund
- Emerging country bonds in local currencies
- Distressed and bankrupt debt

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Low return, low risk



High return, high risk

## Consider the full range of asset categories

- Money market fund
- Treasuries
- Investment grade bonds
- High yield bonds
- Emerging country debt in local currencies
- Physical real estate, bricks & mortar
- Developed country stocks
- Emerging market stocks
- Distressed private debt
- Venture capital

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Low return, low risk



High return, high risk



- You're rewarded for taking risk
- You're penalized for seeking safety
  
- The marketplace is incredibly efficient
  
- It rewards you for taking “non-diversifiable” risk . . . . risk that can't be diversified away
  
- This is why you get the tradeoffs just described . . . 2 prior slides
- This is called “Beta”

- If companies that strongly comply with ESG criteria . . . and
  - As a result, they're inherently and fundamentally more likely to fail or otherwise get into trouble
  - This additional risk . . . can't be diversified away

• Then . . . the market will reward such companies with a HIGHER rate of return

- In such a case . . . ESG becomes a rewarded factor risk . . . a Beta

- **QUESTION** - Are companies that comply with ESG criteria inherently and fundamentally more likely to fail . . . or otherwise get into trouble?
- If YES . . . . they will deliver a higher return
- If instead they have a lower likelihood of failure or trouble . . . . then they must deliver a lower return

## Is ESG a Beta . . . . is it a non-diversifiable source of risk

- ESG . . . . is really easy and incredibly transparent
- It's simple and remarkably straightforward
  - Is following ESG a source of danger and risk
  - Is that additional risk non-diversifiable
  - If so . . . . then the markets must reward (with higher returns) those companies that pursue ESG
- **My perspective on this question**
  - Such a suggestion . . . this is the biggest crock
  - It is remarkably embarrassing to suggest such a thing

## So how do we explain the industry's response to ESG

- One possible explanation
- ESG is not a Beta
- It earns absolutely no inherent reward or penalty . . . the market couldn't care less . . . inherently or fundamentally
  
- BUT . . . it is a temporary source of alpha . . . and you really really need to appreciate that word "temporary"

# Is ESG a possible useful tool for seeking Alpha

Recall . . . . Alpha is only available when the market has mispriced a security

- Alpha . . . . let's ground ourselves with a definition
- The market has screwed up
- The market has mispriced one security relative to another security
- Alpha is the extra performance resulting from
  - Correctly identifying this relative mispricing between securities
  - And . . . successfully harvesting it . . . net of all expenses
- The simple act of harvesting Alpha (a relative mispricing) . . . serves to eliminate the opportunity . . . . closing the relative mispricing . . . eliminating the opportunity

- **Some have suggested that**

- ESG meaningfully affects the ability of a company to succeed or fail . . . it makes a big difference
- The market is not adequately taking this ESG affect into account
- Different securities are therefore temporarily mispriced . . . one relative to another, because security analysts and portfolio managers have not **yet** adequately taken ESG into account

- **If all three of these are true, then**

- Use of ESG analysis may be a **temporary** method for seeking superior risk-adjusted returns
- One would **only** approach ESG using active portfolios . . . and **never passive or index**



## Rob's view on ESG as an Alpha source

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- I can't say "no"
- Yes . . . . I'm a little skeptical . . . . but I can't say "no"
- If true . . . . then one had better be intensely//incredibly active
- Never never passive or index . . . . . which would prevent the slightest hope of success
- My suspicion . . . and where I come from . . . if you want more of one, then you'll have less of the other

# Our industry's approach to ESG

The good, the bad, and the ugly

OPINION | INSIDE VIEW

# *The Many Reasons ESG Is a Loser*



By [Andy Kessler](#) [Follow](#)

July 10, 2022 11:57 am ET

You'll pay far higher expenses for a fund with similar stocks but worse performance.

A few years ago, a guy with a famous last name who ran a socially responsible investment fund asked me to lunch. I was hesitant because I figured he was planning to yell at me for a column I had recently written: “[Stocks Weren't Made for Social Climbing](#).” I wrote, “Profits are the best measure of a business’s value to consumers—and to society.” Instead, he was quite pleasant, though while I ate, he complained that most other environmental, social and governance funds weren’t all that socially responsible compared with his—“not ESG enough.” I asked him what was in his portfolio, expecting Tesla or some oat-milk company. He answered, “General Motors .” OK then.

These days ESG is big business, with \$2.77 trillion in “global sustainable fund assets.” The average expense ratio is 0.41%. And sure enough, apparently some funds aren’t ESG enough. Police in May [raided](#) the European offices of Deutsche Bank’s DWS unit in an investigation of “greenwashing”—saying its investments were more sustainable than they were. The authorities claim, “We’ve found evidence that could support allegations of prospectus fraud.” In June the Securities and Exchange Commission announced an investigation into Goldman Sachs for claiming some of its funds were sustainable and ESG when they really weren’t. This is a fight over branding. What has the investment world

OPINION | LETTERS

# *The Story Behind the Rise of ESG Investing*

July 14, 2022 11:14 am ET

The industry needed a way to profitably reprise the old fund-management business.

I agree with Andy Kessler that environmental, social and governance investing (ESG) is frequently a branding exercise designed to fatten the profits of investment managers and otherwise underperforming companies (“[The Many Reasons ESG is a Loser](#),” Inside View, July 11). But I don’t think ESG is merely an example of successful marketing. It has grown so quickly in part because it also helps fill a hole left by the recent evolution of the financial markets over the past 30 years. The key elements of that evolution are:

- Greenwashing
- Quality and relevance of the data . . . stocks versus bonds versus other
- ESG . . . . only exists within the context of a specific set of very personal values (person specific)
- Story versus substance
- The ultimate craven despicable story-telling
- Classically . . . crap product
- Genuine well-aimed efforts

- Hypothetical story
- Large and growing roster of clients are demanding ESG . . . reinforced by political dynamics and societal trends
- Sales and reputational opportunity is identified . . . by the investment manager
- Build a new set of ETFs
  - Claiming ESG
  - Promote the proposition that ESG is an inherently rewarded non-diversifiable risk (a Beta)
  - Increase the expense ratio of these new ETFs by 500% to 600% to 700%
  - Stick these new ultra-high-fee ETFs inside all of their model portfolios that they sell/deliver to advisors and financial planners
  - And . . these new “ESG” ETFs aren’t really any different from their non-ESG ETFs
- If such an organization exists . . . there’s only one word to describe them . . . **“Dirty”**

# Julex offers a marvelous ESG offering

I use it with some of my clients

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I use it with some of my clients

**This is a concentrated portfolio**

**The version I use is**

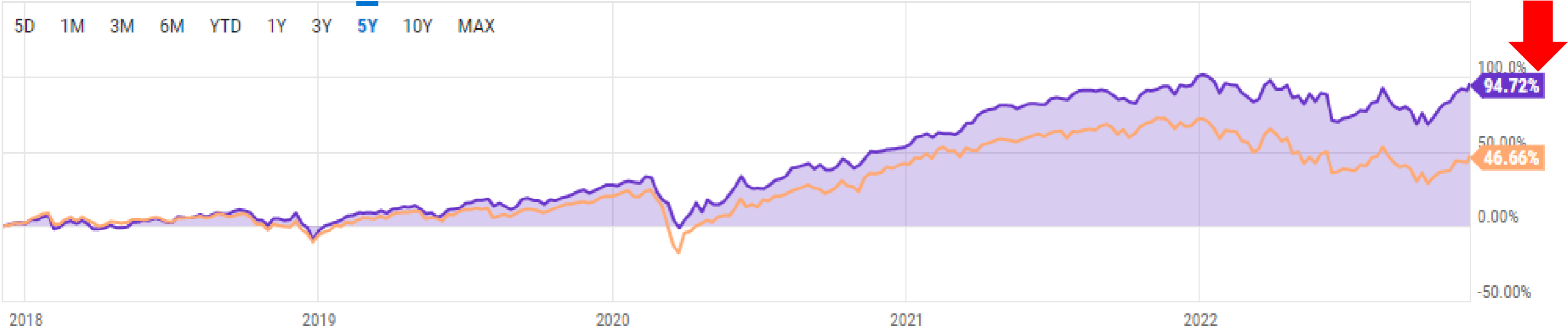
- **25 stocks**
- **Equal-weighted**



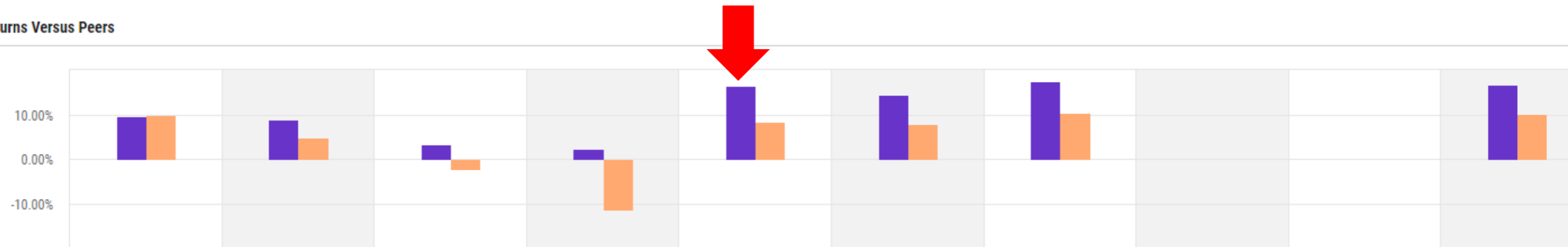
Level Chart

Show Benchmark Comparison | LEVEL RETURNS | VIEW FULL CHART

- CONCENTRATED ESG YEARS 21 AND GREATER (P:548605) LEVEL % CHANGE
- 99/1 U.S. BIASED (70.9% ALL-CAP U.S. STKS, 14.1% DEVELOPED COUNTRY INT'L, 14.1% EM STKS, 0.9% T-BILLS) (P:564562) LEVEL % CHANGE



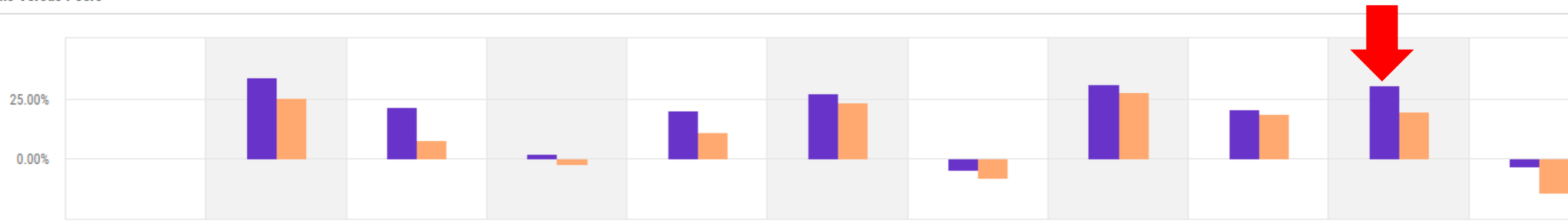
Periodic Total Returns Versus Peers



Name	1M	3M	6M	1Y	3Y	5Y	10Y	15Y	20Y	AT
● <a href="#">Concentrated ESG Years 21 and Greater</a>	9.74%	8.90%	3.33%	2.26%	16.50%	14.38%	17.39%	-	-	16.75%
● <a href="#">99/1 U.S. Biased (70.9% All-Cap U.S. stks, 14.1% Developed Country Int'l, 14.1% EM stks, 0.9% T-Bills)</a>	9.84%	4.76%	-2.29%	-11.44%	8.32%	7.94%	10.35%	-	-	10.06%

As of December 02, 2022. Returns for periods of 1 year and above are annualized.

### Annual Total Returns Versus Peers



Name	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	YTD
● <u>Concentrated ESG Years 21 and Greater</u>	--	33.64%	21.63%	2.26%	20.02%	27.29%	-4.42%	31.16%	20.72%	30.32%	-2.98%
● <u>99/1 U.S. Biased (70.9% All-Cap U.S. stks, 14.1% Developed Country Int'l, 14.1% EM stks, 0.9% T-Bills)</u>	--	25.47%	7.91%	-2.08%	11.27%	23.18%	-7.80%	27.86%	18.53%	19.78%	-14.09%

As of December 02, 2022.

## Stock Style Exposure (?)



As of December 04, 2022

# Stock Style Exposure

Data as of: Dec. 4, 2022



	Co...ater	Bmark		Co...ater	Bmark		Co...ater	Bmark
● <b>Lg Cap Value</b>	28.25%	17.35%	● <b>Mid Cap Value</b>	24.15%	5.43%	● <b>Sm Cap Value</b>	0.00%	2.35%
● <b>Lg Cap Blend</b>	8.00%	31.86%	● <b>Mid Cap Blend</b>	23.56%	8.96%	● <b>Sm Cap Blend</b>	0.00%	3.24%
● <b>Lg Cap Growth</b>	11.99%	24.55%	● <b>Mid Cap Growth</b>	4.05%	4.63%	● <b>Sm Cap Growth</b>	0.00%	1.61%

1D

5D

1M

3M

6M

YTD

1Y

3Y

5Y

10Y

MAX

DATE RANGE ▾

12/03/2021

MM/DD/YYYY

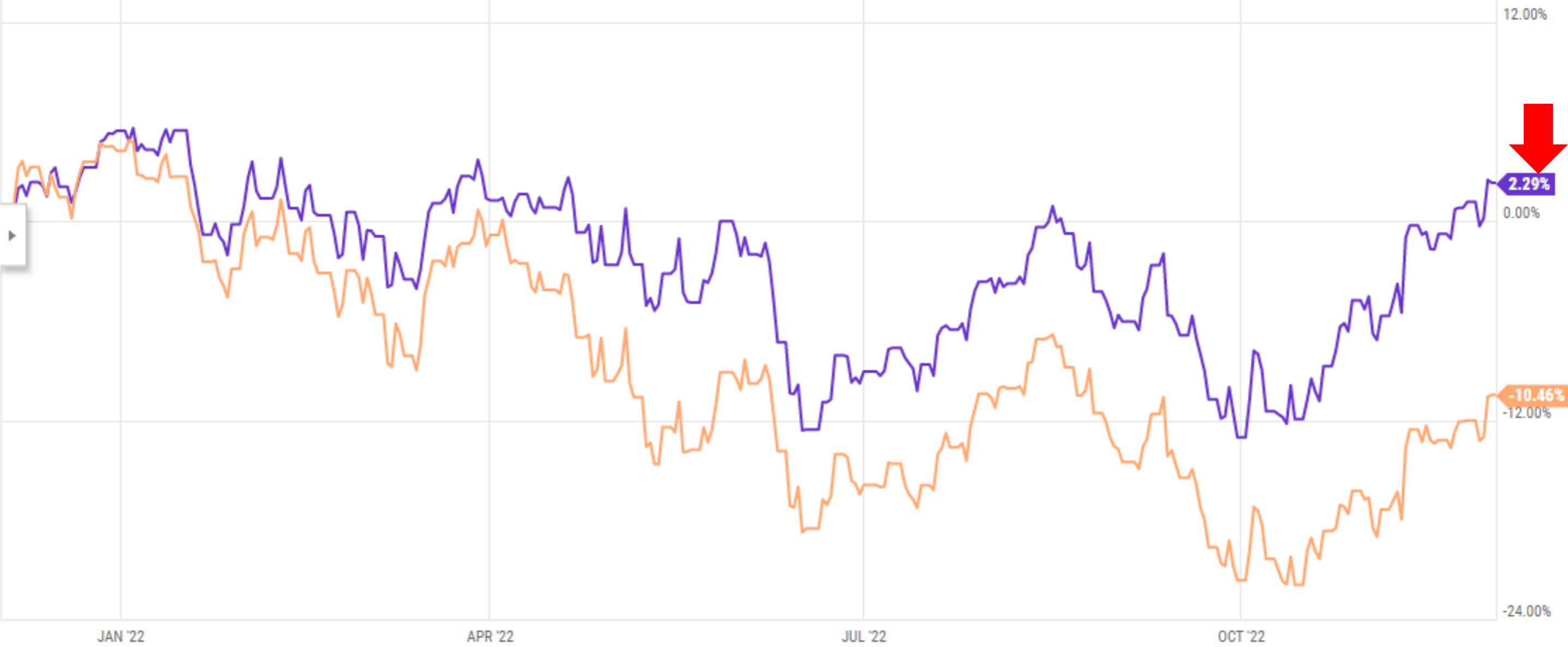
- Concentrated ESG Years 21 and Greater (P:548605) Level % Change
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Dec 2 '22

2.29%

Dec 2 '22

-10.46%



## Risk Info

Data as of Nov. 30, 2022

		3 Yr.	5 Yr.	10 Yr.
<b>Alpha</b>	<b>Concentrated ESG Years 2..ater</b>	9.054	6.785	7.545
	<b>Benchmark</b>	-2.317	-2.615	-2.437
<b>Beta</b>	<b>Concentrated ESG Years 2..ater</b>	0.9064	0.9658	0.9505
	<b>Benchmark</b>	0.9451	0.947	0.9557
<b>Standard Deviation</b>	<b>Concentrated ESG Years 2..ater</b>	20.78%	18.47%	15.05%
	<b>Benchmark</b>	22.16%	18.98%	15.37%
<b>Historical Sharpe</b>	<b>Concentrated ESG Years 2..ater</b>	0.8597	0.8188	1.193
	<b>Benchmark</b>	0.4321	0.4414	0.699

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## Disclosure

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**Portfolio Rebalance:** Each portfolio listed on this report contains a rebalance frequency. This can be selected when you create the portfolio on YCharts. The Portfolios are rebalanced to the proper target weights at each target rebalance point. For monthly rebalancing, the portfolio will rebalance to the target weight at the end of each calendar month. For quarterly rebalancing, the portfolio will rebalance to the target weight at the end of each calendar quarter (March 31st, June 30th, September 30th, December 31st). For annual rebalancing, the portfolio will rebalance to the target weight at the end of each calendar year. Lastly, if the portfolio never rebalances, the target weights are implemented at the portfolio inception date, but will not change after that.

**Portfolio Weights :** All stated portfolio weights are based on allocation choices input by the creator of this report. These weights represent the values used at rebalance periods and not necessarily the implied weights at the time this report was generated. All weightings ignore the concept of whole shares and instead uses the exact percentage chosen when setting up the portfolio.

**Rebalancing:** Rebalancing is conducted on either a quarterly or monthly basis, as selected by the creator of this report. Weights may drift away from the target allocations between rebalance periods

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- I have a small set of clients
- An even smaller slice expects ESG sensitivity
- I'm unusually forthright with them about
  - The industry's misleading story-telling
  - How difficult it is to measure
  - It's even more difficult to execute
  - They and I need to engage on . . . what's important to them . . . how do they define ESG
  - That I will present honest viable opportunities . . . as they arise, but they are few and far between

- **A label**

- Use one or more of the ESG models being offered by segments of the industry
- Don't expect it to work . . . . other than the label, and being ultra-easy to use

- **Custom build**

- This is seriously time consuming
- It tailors the solution (which you have to build) to how your client defines (and evolves) their own personal definition of ESG

- **Honest forthright industry products**

- Julex ESG
- Others . . . Real estate, private debt, electrification . . . all limited partnership structures
- Use the Custom Series

- **A label**

- Use one or more of the ESG models being offered by segments of the industry
- Don't expect it to work . . . . other than the label, and being ultra-easy to use

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- **Honest forthright industry products**

- Julex ESG
- Others . . . who follow a similar approach to Julex

- Custom
- What I'm doing
  - Engaging with the client
  - Build a stock portfolio from scratch . . . . one stock at a time . . . based on their criteria
  - But I set and maintain their expectations as to what is actually doable
  - I'm always hunting for potentially viable solutions
  - Interesting possibilities that I've run across have appeared in
    - Bricks & mortar physical real estate
    - Private credit . . . . that is ultra sensitive to ESG concerns
    - Unique alternatives that address the client's ESG concerns
      - Physical reinsurance on wind farms . . . et al

un film di  
**SERGIO LEONE**



**IL BUONO**      **IL BRUTTO**      **IL CATTIVO**

di SERGIO LEONE  
CLINT EASTWOOD • ELI WALLACH • LEE VAN CLEEF

IL BUONO IL BRUTTO IL CATTIVO

di ALDO GIUFFRÈ  
LA MUSICA È DI ENZO ANGILERI  
LA MONTAGNA È DI ENZO ANGILERI  
LA DISTRIBUZIONE È DI ENZO ANGILERI  
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Attractive, ESG solutions do exist. But they're rare. It's critical to draw a distinction between "doing good" and "outperformance"



un film di  
**SERGIO LEONE**



Attractive, ESG solutions do exist. But they're rare. It's critical to draw a distinction between "doing good" and "outperformance"

It's not easy. You've got to ask and adequately answer "Why does it exist?" and "Why does it work?" Very few can afford the required calorie burn

**IL BUONO** **IL BRUTTO** **IL CATTIVO**

...di SERGIO LEONE  
 CLINT EASTWOOD + ELI WALLACH + LEE VAN CLEEF  
 IL BUONO IL BRUTTO IL CATTIVO  
 - ALDO GIUFFRÈ -

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**SERGIO LEONE**



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A record level of bad product is appearing. This will undermine ESG's reputation . . . and its appropriate application

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# TAA when you've only got a couple of years to invest

Friday

December 16<sup>th</sup>

11:00 a.m. EASTERN

All data and statistics were provided by Global Financial Data, Inc. and NDR, Inc. (unless otherwise indicated in the exhibit)

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The composition of a benchmark index may not reflect the manner in which a Julex portfolio is constructed in relation to expected or achieved returns, investment holdings, portfolio guidelines, restrictions, sectors, correlations, concentrations, volatility, or tracking error targets, all of which are subject to change over time.

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