ClearBridge Investments

ESG Investment Program

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Key Takeaways

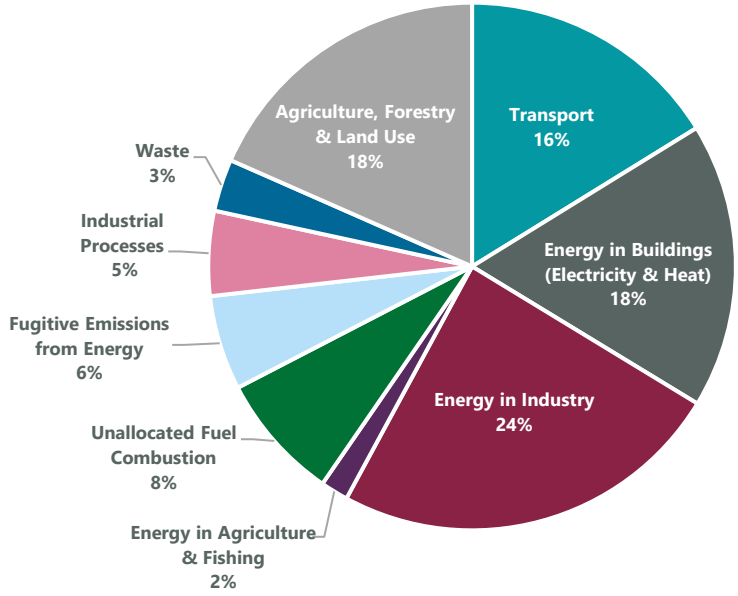
- Public equities are moving the needle on the four goals of COP26 and ClearBridge is spurring and guiding this activity through our role as large shareholder, fiduciary and trusted partner in advising on sustainable business practices.
- Among utilities, early movers in adapting to climate-related threats are better positioned to thrive as their preparedness and resilience protect the community and pave the way for better investor returns.
- Financial services companies ClearBridge owns and engages with, including private equity firms, are bolstering climate-friendly businesses through climate financing and improved sustainability reporting.

COP26 Highlights Climate Opportunities in All Sectors

The conference that brought us the Paris Agreement in 2015 is meeting again in November in Glasgow, where the 26th U.N. Conference of the Parties (COP26) will seek to accelerate action to fight global warming. The four goals of COP26 — 1) speed emissions reductions, 2) protect communities and natural habitats, 3) mobilise climate finance, and 4) build public-private-civil partnerships — intersect in many ways with those of ClearBridge's ESG integration practices. We are excited to see topics ClearBridge regularly addresses with portfolio companies take center stage as governments increase their focus on climate change.

ClearBridge and other investment firms play a crucial role in providing climate financing, one of the main goals of COP26, in ClearBridge's case through our stewardship of capital and our outreach as a large public shareholder. Many companies ClearBridge owns and engages with are playing important roles in meeting the goals of COP26. Importantly, these contributions come from innovative companies working across the economy. We believe contributions to large-scale challenges related to climate change will have to come from all sectors (Exhibit 1). We know renewables cannot do it on their own.

Exhibit 1: Share of Global Greenhouse Gas Emissions



Source: Hannah Ritchie and Max Roser (2020) - "CO_2 and Greenhouse Gas Emissions". Published online at OurWorldInData.org. Retrieved from: 'https://ourworldindata.org/co2-and-other-greenhouse-gas-emissions' [Online Resource]

COP26 Goal 1: Speed Emissions Reductions

The first goal of COP26, to speed emissions reductions through activities such as phasing out coal, accelerating the adoption of electric vehicles (EVs) and encouraging investment in renewables, speaks to investment themes across ClearBridge, where emissions reductions are being enabled by companies across sectors. We have written extensively of our engagements with AES and Vistra Energy, two power companies retiring and disrupting coal power, expanding into renewables and improving their valuations. Similarly, our holdings across the EV value chain, such as TE Connectivity and Aptiv, which make connectors, and even coatings company PPG, which provides thermal, fire and corrosion protection for EV batteries, are helping speed the switch to EVs.

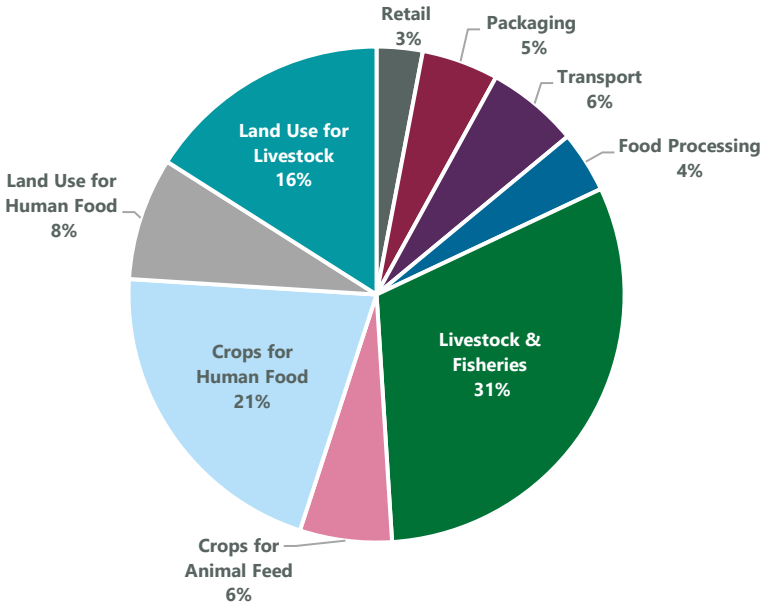
While renewable energy from utilities or solar and wind equipment makers in ClearBridge portfolios is having an impact, many innovations outside of renewable energy are combating climate change and its effects. Resideo Technologies is enabling greater sustainability in the home with “behind the wall” products that enable energy and water conservation. With motors consuming 45% of global electricity production, electric motor and control maker Regal Beloit’s focus on improving efficiency can have a meaningful impact on greenhouse gas (GHG) emissions among its customers. Digital infrastructure company Equinix, in the real estate sector, serves hyperscale cloud companies; it is a leader in renewable energy sourcing and

supporting co-location computing efficiency and data security provision. Recyclable aluminum beverage can company Ball has introduced an infinitely recyclable stadium cup and continues to raise the goals for worldwide aluminum recycling from 69% today to 90% in the future. Recycled aluminum only uses 5% of the energy needed compared to that for virgin aluminum.

A diversified mega cap company like Amazon.com could also be a large contributor, given its reliance on and involvement in heavy transport. The company is creating a fleet of 100,000 electric delivery vehicles to help reach a goal of at least 50% of all shipments being net-zero by 2030, and it has a clear opportunity, given its volume and reach, to implement climate-friendly changes to delivery infrastructure, including air and rail, that would benefit all e-commerce and society at large.

In addition, food is an often-overlooked industry for thinking about emissions (Exhibit 2). Since food is a necessity, it can't take second place to more discretionary spending as a focus for climate. But agriculture is a large contributor to global emissions and an area where consumers and investors can be proactive through advancing plant-based alternatives to meat and dairy products.

Exhibit 2: Food-Related GHG Emissions (26% of Total GHG Emissions)



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COP26 Goal 2: Protect Communities and Natural Habitats with Resilient Infrastructure and Agriculture

While we work to reduce emissions, managing the effects of climate change will require protecting communities through weather resilience, part of the second goal of COP26. Across U.S. states facing extreme weather events, one lesson seems to be that early movers in adapting to climate-related threats are better positioned to thrive; their preparedness and resilience protect the community and pave the way for better investor returns.

In the U.S., we're seeing significant impact of climate change on the West Coast. Wildfire season, which used to generally run for four months, now lasts six to eight months due to earlier snow melts and delayed rain seasons. The extent of wildfire damage has been increasing. According to the California Department of Forestry and Fire Protection, which has looked at the largest wildfires in the state since 1932, 9 of the 20 largest fires happened in 2020 and 2021. The average acreage burned by wildfire over the course of the 2020–2021 wildfire season exceeds the five-year average by almost 3x.

We spoke to Edison International recently, who observed that the majority of fires so far this year were from dry lightning and not caused by utilities. This lack of utility-related fires reflects the better operational preparedness of the companies and the state's increased focus on the issue. With the passage of California's sweep of wildfire prevention, mitigation and response bills in 2019, the state has sizably increased its funding for wildfire prevention and suppression efforts and vegetation management. The wildfire bill requires utilities to pass annual wildfire safety certification and allocate significant spending to wildfire mitigation measures.

In addition to legislative changes, utilities in the state are making operational improvements, directing spending to resilience measures such as better insulation or undergrounding of transmission lines, regular line inspections, vegetation management, weather condition monitoring and focusing on circuit-specific mitigation plans. Both the state and companies have also invested in firefighting abilities through expanding firefighting crews.

California utilities are adapting to climate change realities, and we notice a trend of early movers thriving while better protecting the community. Following wildfires in San Diego Gas & Electric's territory in 2007 and 2008, Sempra Energy (SDG&E's parent) began what is now a decade of enhancements to infrastructure and technology to limit the risk of utility-related wildfires, and, with a state-of-the-art wildfire monitoring system among other resources, the company is now a recognised industry leader in this regard.

In Florida, it is not fire but hurricanes and flooding that are the concern. The long history of severe weather events in Florida has engendered a forward thinking and a preparedness in that state that has benefited both the people and the early adopters of protective measures for infrastructure resilience. Florida Power & Light (FPL), a regulated utility and subsidiary of NextEra Energy, has been investing heavily in reinforcing its vital infrastructure from weather impact. The utility has been replacing wooden transmission poles, undergrounding lines and focusing on smartening the overall grid to improve problem diagnostics and prevent flow interruption. The state regulators have been receptive to the utility's capital allocation, allowing regulatory mechanisms to track investments and earn above-industry returns.

Comparing the grid's performance in Florida between two extreme weather events highlights the success of FPL's investment program. Between Hurricane Wilma (2005) and Hurricane Irma (2017), FPL saw an eight-day reduction in total number of days to restore power, a 60% reduction in utility poles lost and an 80% improvement in time to energise all substations.

These results are consistent with NextEra Energy's leadership role as an early mover in shifting its generation fleet away from coal toward a mix of efficient gas generation and solar. The better generation fleet has brought down the company's fuel cost and operational expenses, while reducing the level of GHG emissions. Today, FPL's residential customer bills remain well below the national average while FPL leads its utility peers on safety and reliability metrics. Investors have recognised the company's leadership, awarding the shares premium earnings multiples and driving NextEra shares' consistent relative outperformance.

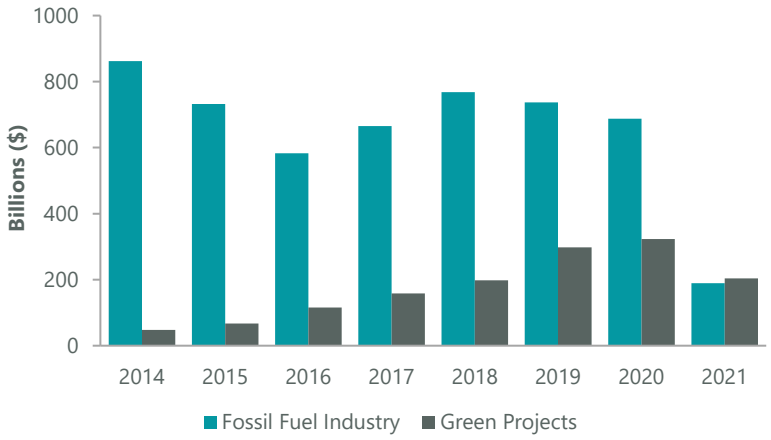
COP26 Goal 3: Mobilise Climate Finance

Financial services companies ClearBridge owns and engages with are also doing their part, making big commitments to support climate-friendly businesses through climate financing, the third goal of COP26, as well as through their own operations. Bank of America, for example, recently announced a goal of deploying and mobilising $1 trillion by 2030 in its Environmental Business Initiative in order to accelerate the transition to a low-carbon, sustainable economy. JPMorgan Chase has pledged to facilitate over $2.5 trillion over 10 years to address climate change and contribute to sustainable development. It has also developed a method for measuring GHG emissions of its financing clients in order to set Paris-aligned targets for carbon reductions. These involve a goal of a 41% reduction in carbon intensity for new autos, including tailpipe emissions, a 69% reduction from electric power generation and a 35% reduction in operational carbon intensity from oil and gas. Morgan Stanley has pledged to

mobilise at least $750 billion of low-carbon solutions; its institutional securities business also issues a wide variety of green bonds that may include financial advisory and underwriting services designed to improve the environmental impact of borrowers.

Large financial institutions are looking to help companies they invest in change their businesses to be better for the environment, and we view these commitments as ambitious, realistic and appropriate to the size of these institutions. They come against an encouraging backdrop of growing green debt issuance, which, while historically trailing finance related to fossil fuel, is closing the gap and in 2021 looks poised to overtake it (Exhibit 3).

Exhibit 3: Green Project Financing Near a Milestone



As of May 14, 2021. Source: Bloomberg Finance L.P. Data covers almost 140 financial services institutions worldwide and compares oil, gas and coal-related finance with bonds and loans to renewable projects and other climate-friendly ventures.

Another recent positive development, sustainability-linked bonds (SLBs), offered by JPMorgan, Bank of America and others, are making climate financing easier in a broader range of sectors. Whereas green bonds tend to finance strictly green businesses such as renewable energy, SLBs can finance environmental goals at any company and incentivise environmental gains by tying pricing to specific targets. A 2019 SLB for Royal Dutch Shell via a consortium including Bank of America, JPMorgan Chase and others, for example, links interest and fees on a $10 billion revolving credit facility to Shell's progress against a target for net-carbon footprint intensity. Reflecting the growing impact across sectors of SLBs, issuance has grown to $350 billion in the first half of 2021, from $197 billion in all of 2020, according to research by Bank of America.

The third goal of COP26 specifies public and private sector financing for net-zero, and it is clear climate financing will need to be a public-private partnership. Governments alone can't raise enough capital through taxes to solve climate challenges, while

Private equity is helping meet the third goal of COP26 through sustainability-linked financing and pushing operational improvements at portfolio companies.

the private sector can't be effective without widely acknowledged goals and data reporting standards. Reporting standards, such as those sought by Bank of America CEO Brian Moynihan at the World Economic Forum, help financial institutions measure their contribution to fighting global warming. In effect, they enable transparency and thus the efficacy of climate financing by banks.

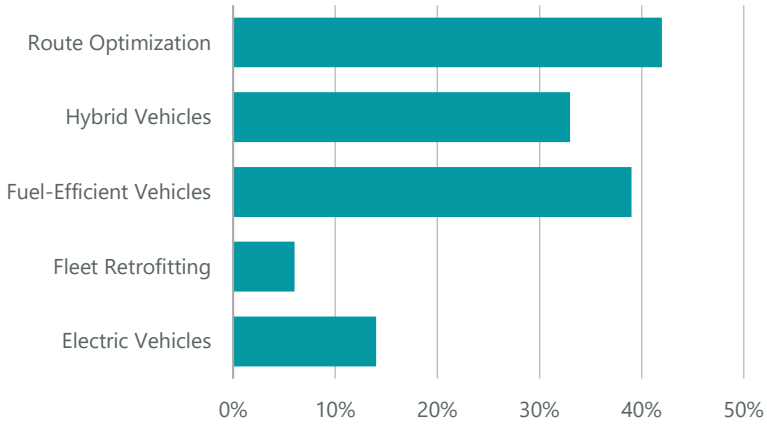
Private Equity Also a Source of Climate Financing

On the private equity side, alternative asset managers are also helping meet the third goal of COP26. Blackstone has set a goal of reducing carbon emissions by 15% within the first three years of buying any asset or company across its portfolio. The goal, equating to 5% in reductions each year for three years, is scientifically aligned with an overall goal of getting halfway to net-zero by 2030. Blackstone also invests in climate solutions and has spent $11 billion over the past three years on companies and projects supporting the energy transition. Projects include the Champlain Hudson Power Express, which will deliver a 24/7 firm supply of renewable energy to New York City, and 10 million square feet of solar panels all together on the rooftops of Blackstone's large portfolio of U.S. logistics warehouses and on Stuyvesant Town, a residential development in New York City.

Meanwhile, Apollo Global Management invests in and lends to many companies in the renewable energy space, and it has over $1.6 billion in capital committed or invested in renewable investments. It has also participated in debt syndication with sustainability-linked covenants, where companies can lower the price of their debt by cutting carbon emissions. The company is working to introduce similar covenants to deals it originates privately.

In an ESG program in place now for 13 years, Apollo asks its companies to measure upwards of 156 environmental, social and governance metrics. Through the program, Apollo transforms the operations of portfolio companies, improving transparency around emissions and instilling efficiency-boosting best practices that reduce emissions (Exhibit 4). In a recent ClearBridge engagement with Apollo Global Management, the company discussed its success in implementing lasting sustainability changes in operations of portfolio companies even after Apollo had exited its ownership position.

Exhibit 4: Apollo Reporting Companies with Fuel Reduction Initiatives



Source: Apollo ESG Report Volume 12.

COP26 Goal 4: Build Public-Private-Civil Partnerships

The fourth COP26 goal, to work together to deliver on the Paris Agreement, affirms ClearBridge's partnership approach and throws into relief the value of ClearBridge's participation in investor-led initiatives and climate-focused organisations. We believe investors working together is crucial in terms of articulating expectations on behalf of the investment industry to government. For example, ahead of COP26, ClearBridge has signed the 2021 Global Investor Statement to Governments on the Climate Crisis, which unites 587 investors representing over $46 trillion in assets and aims to deliver on the Paris Agreement by raising climate ambitions and implementing meaningful practices. We also maintain active relationships with many organisations that support climate-related ESG goals, such as CDP, Ceres Investor Network on Climate Risk, Net Zero Asset Managers Initiative, Climate Action 100+ and the Task Force on Climate-Related Financial Disclosures (TCFD).

Public equities are moving the needle on the goals of COP26 and ClearBridge is proud to be spurring and guiding this activity through our role as a large shareholder, fiduciary, and trusted partner in advising on sustainable business practices. We are encouraged by the wealth of potential, both realised and yet to be realised, for companies across sectors to advance on climate-related challenges as we work to keep 1.5 degrees of global warming attainable.