



## **Environmental, Social, and Governance Factors for the Jensen Quality Growth Strategy**

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Over the last thirty years Jensen Investment Management's long-term investment philosophy has naturally led to a universe of companies that have durable competitive advantages, growth in operating cash flows, and the ability to reinvest those cash flows in a meaningful way to support margins and protect market share against competitors. This is the result of Jensen's disciplined requirement that a business generate at least a 15% return on equity (as defined by the advisor) for ten consecutive years before qualifying for investment consideration. Out of the 225+ names in the Jensen Quality Growth Universe™, the Investment Committee is extremely selective and chooses 25-30 companies that it believes possess the most durable competitive advantages, are attractively valued, and typically have the ability to allocate a portion of excess cash flows towards business risk mitigation.

Utilizing Environmental, Social, and Governance (ESG) criteria in the Jensen Quality Growth investing process is not new. Since inception, Jensen has explicitly focused on governance issues. As long-term investors, the Investment Committee is keenly attuned to shareholders' rights and ensuring that companies are structured such that management interests are aligned with those of shareholders. Historically, Jensen has implicitly analyzed environmental and social issues as they relate to the fundamentals of a business, whether they enhance a company's value creation opportunities and/or mitigate risk. For example, under environmental factors, we take into consideration explicit targets for reductions in greenhouse gas emissions (GHGs), improvements to energy efficiency through the use of renewable sources, waste recycling (zero landfill), and water conservation efforts. Jensen recognizes there may be differences in the degree of adoption by management teams as well as industry factors that may limit the scope of environmental initiatives.

In 2014, Jensen developed its own proprietary ESG metrics based on data from IW Financial, which was subsequently acquired by Institutional Shareholder Services (ISS) in 2017. When the firm initially explored incorporating ESG criteria into our investment process, we found that ESG lacks a common industry definition and that ESG factors varied greatly in their materiality depending on which ESG data resource was used. By building our own metrics, we believe that our ESG values and viewpoints are reflected in the analytics. These custom metrics allow us to first evaluate each company's ESG factors in the Jensen Quality Growth Universe™ and subsequently rank all the companies. We then incorporate the ESG scores in the portfolio management dashboard to aid the Investment Committee in identifying potential ESG-related risks, including ongoing regulatory issues as well as reputational concerns.

In 2019, Jensen contracted with Sustainalytics, a global leader in sustainability research and ESG data, in order to consider their ratings alongside our own fundamental analysis. We believe that Sustainalytics' insights into ESG integration and risk management may help augment our understanding of long-term risk. Although the firm does not invest based on any explicit top-down or thematic drivers across sectors or industries, the Investment Committee members evaluate and incorporate ESG information into their initial and ongoing assessment of portfolio companies and candidates. The firm recently published its first in a series of white papers that are intended to help investors understand how Jensen evaluates the internal rankings in the top third versus the middle and bottom thirds of the Jensen Quality Growth Universe™ for our portfolio companies.

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