



Value  
income

 **Federated Hermes  
ESG integration in  
Value Income strategies**



- For the Federated Hermes Value Income team, assessing material Environmental, Social and Governance (ESG) issues when evaluating company fundamentals is an integral component of the investment process and assists us in identifying companies that are exhibiting catalysts for internal and external change.
- We believe direct engagement with company boards and senior executives on material ESG-related issues can provide an important information advantage and is an essential component of sound stewardship.
- We believe ESG integration can help identify undervalued investment opportunities and serve as the basis for prudent risk management.

At Federated Hermes, we believe that incorporating ESG factors into our research across asset classes provides greater insight into investment risks and opportunities. While the assessment of ESG factors can help reveal important information about a company's practices and leadership, the ability to extract value from ESG factors within a portfolio can depend on how these factors are incorporated into the investment process.

To this end, Federated Hermes' global team of engagement and responsible-investing specialists provides proprietary ESG data and analytics, which our investment teams use to manage risk and identify opportunities. A key input of our data comes from our experienced engagement and stewardship division, EOS. EOS's direct engagement with companies is not only important to obtain insights into a company's ESG practices, but it can also advocate for improvement in an issuer's ESG profile that may help to reduce the issuer's risks over the longer term. Through our engagement, in addition to proprietary and select third-party ESG data, we generate custom "materiality" assessments focused on the long-term ESG considerations that are financially relevant to each industry. Our investment teams use this ESG data analytics, materiality assessments and engagement in ways that are appropriate to their specific strategies in order to seek better outcomes for our clients.

## ESG: The future of value investing at Federated Hermes

There are many reasons to consider ESG issues when making investment decisions. For some it's the ability to align their values with their investment dollars. From an investment manager's perspective, there is another powerful rationale: the ability to assess an investment's risk-reward potential. We believe enhancing existing investment processes through the integration of ESG considerations can help mitigate portfolio risks and unlock opportunities. For the Federated Hermes Value Income team, ESG integration can contribute to the team's capital allocation process to pursue alpha throughout an economic cycle.

The Federated Hermes Value Income team seeks to identify companies with the catalysts for internal and external change—including ESG change—that can improve portfolio risk characteristics and prospects for long-term alpha generation and/or an income stream. Consideration of material ESG factors provides an additional tool to help identify change, as well as pockets of risk, that are potential indicators of an issuer's long-term success.

We have long considered environmental and governance factors, in particular, as part of our investment process. Today, our ability to access direct engagement resources and robust, proprietary ESG data analytics enables us to incorporate and focus on ESG drivers more formally. Engagements, through our dedicated engagement and stewardship division, EOS at Federated Hermes, enhance our investment team's fundamental research with unique, real-time insights based on continuing dialogue with company boards and executive management. We now actively integrate ESG insights and scores into our bottom-up fundamental analysis along with quantitative reports.

Our strategies are diversified across all market sectors, and we evaluate ESG factors in an attempt to identify those companies that are either showing positive fundamental ESG momentum for potential investment or ESG deterioration and increased risk. Our risk management philosophy seeks to maximize our stock-specific alpha and minimize unintended bets by allocating capital to our highest-conviction ideas. Incorporating ESG early in the investment process, helps us build conviction in companies and industries that are improving their ESG footprint—those that are exhibiting positive environmental, social or governance change.

## Our differentiated ESG approach

We believe incorporating ESG into our proprietary approach to fundamental and quantitative research—complemented by proactive risk management and an experienced team of analysts—allows us to pursue consistent alpha throughout an economic cycle. Importantly, we believe the best stocks over time are issued from strong franchises that are driving positive fundamental change, including ESG change, and providing a growing cash flow stream for investors while presenting an attractive relative valuation. Our ESG integration framework seeks to:

- **Identify the relevant ESG factors** using external and internal proprietary Federated Hermes research. These factors will help us develop our investment thesis and will be incorporated into our discussions with management as well as our overall risk evaluations.
- **Incorporate proprietary ESG research** consisting of data analytics and corporate engagement. The Federated Hermes Value Income team uses these findings to help identify mispriced securities undergoing positive fundamental change at the company and sector level.
- **Engage**—Direct fundamental and ESG engagement with corporate issuers helps us to formulate a more comprehensive picture of the risks a company must navigate in order to sustain positive cash flows over a business cycle. During the security review process, our analysts regularly interact with our in-house stewardship experts at EOS.
- **Measure progress**—Advanced Federated Hermes portfolio analytics assess engagement progress based on quantifiable milestones, providing a measurement of forward-looking and intentional ESG integration.

# EOS: The engagement advantage

Federated Hermes is one of the largest active managers with a dedicated engagement and stewardship division. EOS at Federated Hermes is a pioneer in the engagement space with a 18-year proprietary database that we believe can provide a competitive advantage for Value Income strategies and our firm. Engagers are ESG subject-matter experts on topics such as climate change, human capital management, sustainable supply chains and corporate governance, and are uniquely positioned to assess the ESG progress and momentum of a corporate issuer.

EOS specialists have deep industry-specific knowledge, with extensive experience in particular sectors and on the select companies they cover. EOS engages on material ESG objectives along with key environmental, social, governance and strategic themes which comprise 36 unique sub-themes. Engagers provide meaningful insight into a company’s willingness and ability to manage ESG risks. By integrating engagers’ deep understanding of financially relevant ESG factors, our portfolio managers are better equipped to assess the quality of current and potential holdings. [Learn more about EOS at Federated Hermes here.](#)

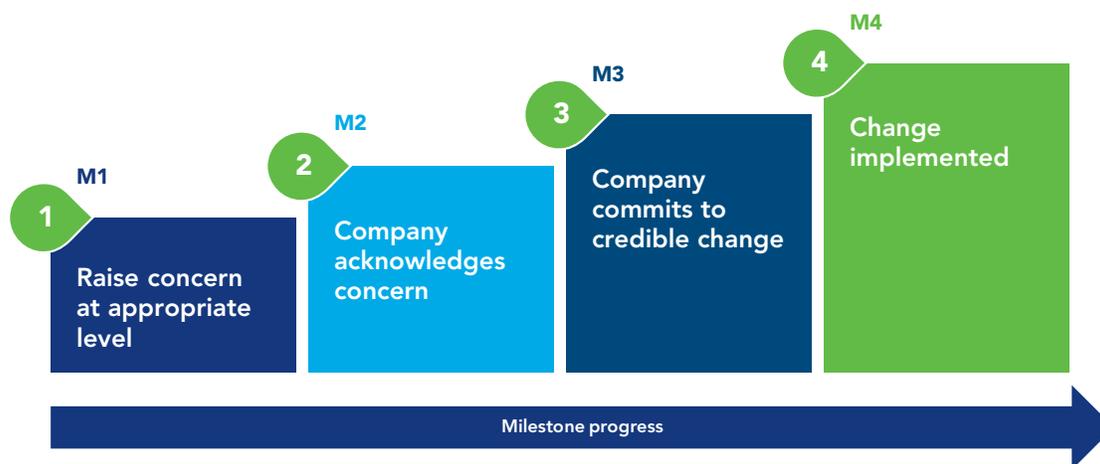
## Material engagement objectives



## Engagement milestones

Engagements are an important component in understanding long-term ESG risk, providing us with unique ESG intelligence. These resources, in aggregate, serve as part of the Federated Hermes Value Income team’s fundamental investment mosaic. Through our investment process we seek to identify companies with catalysts for internal and external change (including ESG change) to improve portfolio risk characteristics, and prospects for long-term capital appreciation and/or an income stream, depending on the investment strategy.

The Federated Hermes Value Income team’s ESG momentum ranking is based on a proprietary milestone system used by EOS engagers. Engagers track progress in their engagements relative to the objectives set at the beginning of their company interactions. The specific milestones used to measure progress in an engagement vary depending on each concern—environmental, social or governance—and its related objective. They can broadly be defined as follows:



## The value of ESG integration

For the Federated Hermes Value Income team, corporate or industry change drives investment opportunity, whether that change is related to internal company developments, innovation, an upgrade in a company’s competitive position or continuous improvement in its response to material ESG issues.

By incorporating ESG considerations into the investment process, the Federated Hermes Value Income team can take advantage of emerging ESG matters that may be key to a company’s or an industry’s prospects. Understanding ESG information that may not be well documented and recognized, but increasing in investment materiality, provides us with an additional lens to help identify mispriced opportunities over the long term.

### A word about risk

Terminology such as “ESG integrated”, “sustainable”, “engagement” or “impact” among other terms, is not uniformly defined across the industry. Investment managers may understand and apply ESG factors in different ways, and that the role those factors play in investment decisions also varies. Therefore, we recommend investors understand the role of ESG factors in a strategy to ensure that approach is consistent with their investment objectives. Like any aspect of investment analysis, there is no guarantee that an investment strategy that considers ESG factors will result in performance better than or equal to products that do not consider such factors. Investing and making buy and sell decisions that emphasize ESG factors carries the risk that, under certain market conditions, the fund or strategy may underperform those that do not incorporate such factors explicitly into the decision-making process. The application of ESG criteria may affect exposure to certain sectors or securities and may impact relative investment performance depending on whether such sectors or securities are generally in or out of favor in the market.

There is no guarantee any investment approach will be successful.

Past performance is no guarantee of future results.

Diversification does not assure a profit nor protect against loss.

Value stocks may lag growth stocks in performance, particularly in late stages of a market advance.

Alpha is a measure of risk-adjusted performance.