

Coho Partners, Ltd.  
**IMPACT REPORT**

July 2018



**COHO PARTNERS, LTD.**

Where protection and participation meet



## CORPORATE ENGAGEMENT

We actively engage with the companies in the Coho ESG 200 universe to better understand their commitment to ESG issues and to advocate for positive change. We actively seek increased transparency through more frequent and robust disclosure and through establishment of tangible goals. Below are several examples of this direct engagement we conducted in the first half of 2018.

### Abbott Labs (ABT)

- Petitioned for additional health care experience on the board as only CEO Miles White and Dan Starks (ex-STJ CEO) have a background in Health Care;
- Encouraged separation of Chairperson/CEO role.

### Aflac (AFL)

- Directed AFL to evaluate and incorporate SASB standards in addition to the GRI standards to which they already adhere;
- Encouraged separation of Chairperson/CEO role.

### Amgen (AMGN)

- Raised awareness of the importance of metrics related to employee turnover and requested the company include related metrics in future disclosures;
- We encouraged the company to consider adding an individual with IT experience to the board.

### ConAgra (CAG)

- Sought a change in the compensation metrics for senior management. It was subsequently confirmed a change will be made to consider sales, EPS growth and returns;
- Encouraged the company to use the SASB standards. Management confirmed it had recent discussions with relevant members of the SASB committee and said it would like to see the relevant standard for the packaged food industry further refined to be more useful for all stakeholders.

### Dollar General (DG)



- Recommended the company formalize its ESG effort, increase disclosure, and publish a corporate sustainability report. The company was actively engaged and sought our input on which standards to consider;
- ESG initiatives will receive more focus going forward. For example, an equal pay survey was conducted to look at gender-based wage gaps. Changes are being implemented as a result of the findings.

### **Grainger (GWW)**

- Participated in a materiality assessment to determine ways in which Grainger could improve its ESG focus. The company already ranks very high on sustainability issues, and we strongly support the proactive effort to improve and incorporate major shareholders' input into its ESG policies and initiatives;
- Encouraged separation of Chairperson/CEO role.

### **Illinois Toolworks (ITW)**

- Discussed the reasons for lack of corporate-wide environmental targets and encouraged the company to adopt clear and time-bound environmental goals;
- Reviewed the skillset of the board members and encouraged addition of new members with more diverse industry experience and backgrounds;
- Requested addition of Environmental and Social metrics as part of the executive compensation package;
- Reiterated our strong support for current CEO but made the case for separation of Chairperson of the board and CEO role.

### **Kroger (KR)**

- Sought to better understand the company's approach to its 84.51 division which sells targeted marketing. While the company indicated that the data is sold at the aggregate rather than individual level, we will continue to monitor this initiative from a data security/privacy perspective;
- Credited the company with setting tangible goals but requested it be more consistent in relaying progress on attaining those targets.



## Omnicom (OMC)

- Conveyed that the company's Corporate Responsibility Report lacks sufficient quantitative metrics and needs to include more tangible targets and goals. Aggregation of data is difficult given 1,500 separate ad agencies under the Omnicom umbrella, but the general counsel indicated this is something upon which they will focus;
- Sought increased structure around data privacy, particularly in light of the implementation of GDPR;
- Encouraged the addition of board members with IT experience given the changing landscape of ad delivery.

## Proctor & Gamble (PG)

- Dissented with Proctor & Gamble's current approach to compensation targets. The goals are not sufficiently challenging and management can be rewarded for delivering below industry performance. We believe this feedback is likely to result in an adjustment to the incentive plan going forward;
- Sought to understand the company's lag relative to its goal to reduce packaging by 20%. A move to smaller pack sizes is the issue, but we view this more as a way to get price/margin and less due to customer demand. We argued for an increased focus on innovation to drive price and reduce waste moving forward.

## Quest Diagnostics (DGX)

- Encouraged the company to set formal quantitative targets, particularly for Environmental metrics. We stated our desire to have those targets be disclosed and transparent so that the company could be held accountable to them;
- The company actively sought our input on what was important to us from an ESG perspective and which standards we deemed relevant and important. Specifically, we encouraged the company to increase its focus on SASB standards;
- Encouraged the company to reconsider its lead independent director as it currently is the longest-tenured board member which we believe has implications as to how independent that board member truly is.



## PROXY VOTING

2018	% of Holdings	Companies
CEO/Chairman separation	8%	KR, ABT
Sustainability initiatives	15%	KR, RDS, MMM, ITW
Shareholder rights	31%	DGX, KO, OMC, ITW, MMM, MRK, LOW, CVS
Director overboarding	23%	KO, ABT, OMC, GWW, DG, LOW
Improved execution compensation metrics	8%	MMM, JNJ

We vote our proxies with consideration to ESG factors across all of our portfolios, not just our Coho Relative Value ESG portfolio. We consider the Broadridge-Proxy Edge and Glass Lewis ESG recommendations but do not adhere to those recommendations by default. One example where we often differ is on board diversity. Whereas Glass Lewis and other proxy voting services consider only gender diversity, our proprietary research allows us to look more deeply at gender, ethnic, cultural, industry, and academic experience. Below are several recent examples where we voted against management recommendations on a variety of issues. Although these shareholder proposals did not pass, we feel that the momentum for management to take action is building as indicated by the increasing number of votes in favor of these resolutions.

### Abbott Labs (ABT)

- Voted our proxy in support of a shareholder resolution for separation of CEO and Chair of the board role. The proposal was defeated with 31% of votes in favor.

### Illinois Toolworks (ITW)

- Voted our proxy in support of a shareholder resolution to set company-wide greenhouse gas emissions targets. The proposal was defeated with 25% of votes in favor.

### Johnson & Johnson (JNJ)

- Voted for a shareholder resolution to incorporate litigation and compliance charges in executive compensation performance measures. The proposal failed with 18% of votes in favor.



## Kroger (KR)

- Voted for a shareholder resolution to publish a report assessing environmental impacts of using unrecyclable packaging for private label brands. Proposal failed with 30% of votes in favor up from 23% in favor the prior year.
- Voted for a shareholder resolution to publish a report assessing climate benefits and feasibility of adopting enterprise-wide targets for increasing renewable energy sourcing. Proposal failed with 31% of votes in favor up from 24% in favor the prior year.

## SUSTAINABLE DEVELOPMENT GOALS (SDGs)

The Sustainable Development Goals (SDGs) set forth by the United Nations are a “universal call to action to end poverty, protect the planet, and ensure that all people enjoy peace and prosperity”. Although we do not explicitly target any single or series of SDGs within our ESG investment framework, we seek to drive positive change that touch on a majority of the 17 goals. Our core investment philosophy and longer-term investment horizon focuses on identifying and engaging with companies with long-term sustainable business models. We believe that responsible stewardship of all stakeholders including the shareholders, society, communities, and environment are vital components of a long-term competitive advantage. Through our direct engagement with company management teams and our proxy voting decisions, we have encouraged our portfolio companies to take action to address these important goals.

1 NO POVERTY



Many of our portfolio companies have reinvested the benefits of U.S. corporate tax reform back into their employees. This has come in the form of enhanced benefits, one-time bonus payments, and hourly employee salary increases. Ross Stores (ROST), for example, improved its paid leave benefits for new parents and issued a one-time bonus to hourly employees. Outside of tax reform, it has also raised its minimum starting wage across its entire employee base in each of the last two years. Our companies are engaging in a variety of initiatives to help reduce global poverty. Proctor & Gamble (PG), for instance, has an initiative to train and certify independent small, palm oil farmers to ensure they can meet the certification requirements of the palm oil industry and maintain their livelihood and land rights.



2 ZERO HUNGER

In 2017, Kroger (KR) launched a Zero Hunger, Zero Waste campaign. Through this initiative, the company plans to accelerate food donations and provide three billion meals by 2025. Kroger also gets high marks for making organic and natural food more affordable through its private label brands. Additionally, the company has set an audacious goal to end hunger in the communities they serve and eliminate waste in the company by 2025. It will also advocate for public policy solutions and join forces with nonprofits focused on the same initiatives.

3 GOOD HEALTH AND WELL-BEING



Improving access to health care is an important objective of the health care holdings within our portfolio. Merck (MRK) and Amgen (AMGN) are both working to introduce new biosimilar therapeutics to help reduce the cost of these expensive specialty pharmaceuticals. We believe United Healthcare (UNH) is the leading company in the industry with regards to effectively bending the cost curve in the U.S. while moving deliberately to do the same globally. All of our pharmaceutical and biotechnology holdings distribute millions of doses of free drugs and vaccines annually.

4 QUALITY EDUCATION



Many of our portfolio companies seek to improve access to education globally. Coca-Cola (KO) founded its Coca-Cola Scholars Foundation in 1986, one of the largest corporate-sponsored achievement-based scholarship programs in the country. It provides scholarships to individuals who achieve high academic success and demonstrate leadership in service to their communities. Dollar General (DG) established the Dollar General Literacy Foundation in 1993 and has provided nearly \$150 million in grants that have helped more than nine million individuals learn to read, prepare for their high school equivalency degree, or learn English. The drive to enable others to achieve this most basic skill is ingrained in the company's culture as DG's founder, J.L. Turner, himself, was illiterate.

5 GENDER EQUALITY



When engaging with corporate management teams we seek to understand the company's culture and its commitment to gender equality. This can include board representation, overall workforce makeup, pay gaps, and the number of women in leadership positions. Quest Diagnostics (DGX) excels in this area with nearly 70% of the workforce comprised of women. The company has a dedicated support effort and mentoring program to develop and nurture their talent. This has resulted in nearly 50% of leadership positions within the company being held by women. Women also represent 40% of board seats at the company.

## 6 CLEAN WATER AND SANITATION



Access to clean water and sanitation is imperative to life and health. Within our portfolio, 3M Company (MMM) is at the forefront of water purification. In 2013, it was the first company to achieve the Water Quality Association (WQA) Sustainability Certification. The standards assess the “cradle-to-grave” qualities of the products including raw material sourcing, manufacturing, packaging, and disposal management. 3M has engaged in many efforts around the globe to help bring clean water to the world. In China, it established the 3M China Purification Residential Water Team that developed products to filter specific local contaminants. This initiative has successfully brought clean water into the homes of hundreds of thousands of Chinese citizens.

## 7 AFFORDABLE AND CLEAN ENERGY



We choose not to eliminate integrated energy companies from our ESG universe or portfolio. Rather, we seek to identify, engage with, and encourage those firms that are seeking solutions to the affordable and clean energy needs of future generations. Royal Dutch Shell (RDSA) established its New Energies division in 2016 and has committed to spending \$1-\$2 billion annually on the pursuit of green energy initiatives - more than any other major oil and gas company. Despite being one of the largest oil and gas companies in the world, Royal Dutch models a future without fossil fuels and is driven to be part of the solution. Recent acquisitions of a smart-home and energy management company, along with purchases of solar, wind, and fuel cell companies and an electric-car charging network, demonstrate the company’s commitment to a clean energy future.

## 8 DECENT WORK AND ECONOMIC GROWTH



Our portfolio consists of some of the largest employers in the world. We have been encouraged by the recent commitment of many of our companies to improve wages, benefits and training for their employees. Dollar General (DG), for example, increased the salary levels of its store managers in early 2017. While this was met with some concern among investors due to the material impact to labor costs, we at Coho viewed it as the right thing to do from both a social benefit perspective and a financial return perspective. Our focus on the long-term allowed us to identify the business opportunity in taking care of employees and, indeed, DG’s manager turnover has moved to historic lows. A more stable store management team has led to improvements in assistant manager and hourly employee turnover, an uptick in same store sales, lower levels of shrink (i.e. product theft), and higher customer satisfaction scores. DG is also committed to providing one of the fastest paths to promotion and career advancement within the retail industry. It was recently recognized by Training Magazine as one of the top five companies in the United States when it comes to employee training and development.



**9** INDUSTRY, INNOVATION  
AND INFRASTRUCTURE



Innovation is the lifeblood of sustainability. We seek to invest in companies that thrive on a culture of innovation and efficiency. Illinois Tool Works (ITW) sold much of its commodity businesses a few years ago to focus on products that are developed from customer led innovation. ITW serves businesses and industries with complex needs and seeks to partner with its customers to develop novel solutions to difficult problems. This allows ITW to contribute to the resilient and sustainable industrialization espoused by this goal. In 2017, 22% or \$3.1 billion of ITW's sales came from products that help with water conservation, renewable energy use, and emissions reductions. Importantly the company seeks to foster this culture across its entire impact continuum by requiring its suppliers to invest in collaborative innovation efforts as well.

**10** REDUCED  
INEQUALITIES



Many of the broad goals of this SDG relating to immigration policies and financial assistance to developing countries are beyond the purview of our companies. Companies like State Street Corporation (STT), however, are engaged in helping developing and emerging market countries facilitate financial flows, access capital, and comply with global regulations. When it comes to inclusion and equal opportunity, nearly all of our companies are actively engaged in ensuring a welcoming and diverse workplace. Johnson & Johnson (JNJ) was named the top company for diversity by Diversity Inc in 2018. Portfolio companies such as Automatic Data Processing (ADP), Abbot Labs (ABT), Proctor & Gamble (PG), and CVS Health Corporation (CVS) were also recognized in the list of Top 50 Companies for diversity this year.

**11** SUSTAINABLE CITIES  
AND COMMUNITIES



Several of our portfolio companies are committed to protecting the cultural heritage of the communities in which they operate and source materials. For J.M. Smucker (SJM), smallholder support is integral to its green coffee sustainability strategy. The company provides technical expertise, training, and resources to help indigenous farmers increase production and improve individual economic development. It has partnered with numerous foundations to expand these initiatives, increase the percent of green coffee sourced from smallholders, and change lives within the communities in which it operates.

**12** RESPONSIBLE  
CONSUMPTION  
AND PRODUCTION



ConAgra Brands (CAG) is a great example of doing well by doing good. The company has reinvigorated its frozen food business through innovation that is resonating with its customers. This includes the development of a novel, plant-based microwaveable bowl. The bowl is completely compostable and recyclable and eliminates the use of plastic packaging for its Power Bowl line of entrees. This

packaging change has helped drive acceptance of this 30 year old brand among millennial consumers and accelerated revenue growth for the company.

### 13 CLIMATE ACTION



All of our portfolio holdings are seeking to reduce energy use and reduce waste within their companies and supply chains. One of the most interesting initiatives, however, relates to one of our energy holdings, Occidental Petroleum (OXY). OXY has developed a carbon dioxide (CO<sub>2</sub>) sequestration process that allows it to permanently store approximately 40% of the CO<sub>2</sub> it uses in its production process in the reservoirs from which it extracts oil. The remaining 60% is recycled for reuse leading to <0.1% of CO<sub>2</sub> being emitted into the atmosphere and a meaningful portion being permanently isolated underground. It is working to develop this technology further with the goal of being able to sequester not only its CO<sub>2</sub> but also the CO<sub>2</sub> produced by other energy and industrial companies. The carbon capture technology could play a meaningful role in reducing global carbon emissions.

### 14 LIFE BELOW WATER



As the second largest grocer in the United States, Kroger (KR) has made a commitment to sustainable seafood procurement. The company partnered with the World Wildlife Fund in 2009 to help guide its sustainable sourcing initiative. Since that time the company has achieved 87% sourcing of wild-caught seafood from Marine Stewardship Council (MSC) certified fisheries. More than 90% if its farm-raised seafood is sourced from programs certified by the Global Seafood Sustainability Initiative (GSSI). It has set goals to reach 100% sustainable sourcing for both wild- and farm-raised seafood by 2020. Kroger is also supporting numerous fishery improvement projects to ensure more fisheries achieve the MSC standard. This will not only help improve the health of the oceans, but it is also key to sustaining the livelihood of fisherman and their communities around the world.

### 15 LIFE ON LAND



Proctor & Gamble (PG) and J.M. Smucker (SJM) have both pledged to source their direct palm oil exclusively from Roundtable on Sustainable Palm Oil (RSPO) certified sources. SJM updated its palm oil policy in 2017 to commit to ensuring its purchased palm oil can be traced back to plantations not linked to tropical deforestation which includes no development of high conservation value areas, no burning to clear land for new planting, and no development on peat lands.

SDGs 16 (Peace, Justice and Strong Institutions) and 17 (Partnerships for the Goals) are generally beyond the scope of our portfolio companies.