Environmental/Social Asset Management

ES Asset Management

Identification of Market Inefficiency/ problem

As the country's vast natural gas and oil reserves are extracted more aggressively, largely due to advances in hydraulic fracturing (fracking), the risk profile of the companies along the supply chain supported by fracking and of the environment around shale formations increases. With every new well, new opportunities arise for accidents to occur that can ruin a company's reputation and destroy the ecosystem and community around it. A major factor contributing to these risks is the lack of transparency into the environmental and social responsibility standards that these companies set. As long as this lack of transparency continues it will be difficult for both shareholders and other stakeholders to drive positive changes in these companies to reduce their risk profile. However, this also presents an opportunity for companies willing to embrace transparency and improve their operations by reducing their risk levels and opening up doors for new revenue sources, driving abnormal positive returns for their investors and improving the environmental impacts of these companies.

Our Solution

ES Asset Management will use activist investment tactics to take significant positions in small growth companies in the Oil/Gas Extraction and Equipment and Services industries to increase their transparency on their environmental and social impact in order to drive improvements in their operations and reduce the companies' risk profiles over time.

By taking an equity position in the range of 2 -15% of a company, depending on its size, ES Asset Management will work with the management team to drive these changes at the lowest possible cost to the company. Our goal is not to be seen as a corporate raider; but rather as a partner of the current management team, who we will work with to drive the changes that are necessary to improve the company's overall performance and to reduce its exposure to the following issues: government fines, spills, workplace accidents, GHG emissions and water usage and safety. As a result, our work with the company can also act as a catalyst to unlock the true market value of the company.

Investment Criteria

ES Asset Management realizes that it will be difficult to take such positions in larger companies prior to proving our concept, which is why we will begin by targeting smaller companies within the industry to prove our concept and develop a positive reputation within the industry.

Financial Screening

- Proven Operational Efficiency
  - Strong asset turnover ratio's
  - Strong Free Cash Flows and Revenue Growth
- Large Proven Reserves (Oil/Gas Extraction Companies)
- Low P/E and Cash Flow Multiples Compared to Peers

Environmental and Social Screening

- Low ESG Transparency historically
- History of Violations
- Recent violations
- Signs of management buy-in

Due Diligence Process

The due diligence process will be a key factor in our success due to the concentrated nature of our portfolio. We will be conducting a thorough analysis of all publically available data, both financial reporting and government agency reporting, as well as using third party Social Responsible Investment research (i.e. Bloomberg, Capital IQ and Sustainalytics).

Financially, we will focus on positive trends that affect the free cash flow and asset quality and for indicators that the management team will be able to continue to run the company effectively going forward. For Oil/Gas extraction companies we will focus on their proven reserves, modeling the value of these reserves based on market prices as well as the ability of the company to turn these reserves into cash flows; while also testing the effects of large price shocks in the oil/gas markets. Our main goal will be to test our thesis as to why the company is undervalued and to identify any potential catalysts, besides our own work, that could unlock the value of the company.

Our environmental due diligence process will use reports available through the EPA, OHSA and MMS to conduct research on the company's history of violations and accidents. We will also visit as many sites as possible to evaluate their safety records, or use reports by third parties who have access to those sites. We will also research recent statements by management, in the media or in financial statements, which might indicate a willingness to embrace change. Our main goal will be to identify if the company will embrace transparency in ESG reporting, and how large of an impact it will have on its operational efficiency.

Deal Selection Process

Our final deal selection process will be completed through a committee of the fund's partners, focusing on the deal selection criteria below and information uncovered during the due diligence process.

Decision Criteria

Liquidity of the Stock
Ability to build a position without affecting the price drastically
Valuation
Confirmation of undervaluation thesis
Identification of catalysts
Expected return compared to alternatives

Strong Assets Base
Ability to turn assets into cash flows
Management Quality
Operational ability
Indications that Management is embracing change
Firms Overall ESG Transparency

ES Asset Management

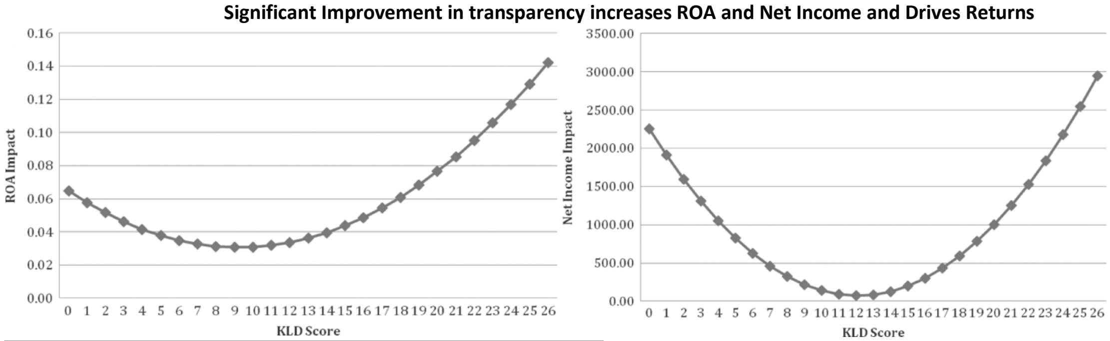
Returns

The funds goal is focusing on generating financial returns in the form of positive stock performance over the long term and generating a positive Environmental and Social Impact by improving transparency and driving operational improvements through our chosen Environmental and Social indicators. ES Asset Management also hopes to gain a competitive advantage as we demonstrate that we are able to work effectively with management to improve these issues and lower the company's risk exposure.

Financial Returns will be driven by the realization of value within our portfolio companies through increased transparency, operational efficiency and financial performance over the long term. These cash flow improvements will combine with an increase in the firm's multiples valuation, due to a reversion to the industry average, to create an abnormally positive return for us as investors. As a result of our unique portfolio composition, ES Asset Management will have a flat return goal of 10% instead of a relative return compared to an index.

Environmental and Social Impacts will come from increased transparency within our portfolio companies. The companies will be under increased pressure from third parties to improve their Environmental and Social impacts as their transparency increases. As this pressure increases the firm will come under some negative pressure; however as long term investors our goal is to support management through this phase until their transparency scores improve and we can begin to see the benefits of these improvements, which have been shown to come once companies reach high levels of transparency, as seen below.

Significant Improvement in transparency increases ROA and Net Income and Drives Returns



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http://onlinelibrary.wiley.com/doi/10.1002/smj.1980/full#fig1

Improvement in Bloomberg ESG Disclosure Score

After analyzing over 2,000 U.S. companies in the Bloomberg ESG Disclosure database we found that an improvement in this score is correlated with a higher total return over the same time period with a 95% confidence level. This illustrates that increasing transparency in ESG indicators can lead to higher returns and lower volatility. The chart has improvement in Bloomberg ESG Disclosure score over the past 3 years on the X Axis and 3 year Total Return on the Y Axis.

Risks & Risk Management

ES Asset Management will be a risk adverse fund, seeking to manage risk by purchasing companies at a margin of safety to our valuation. Risks include, but are not limited to, the risk of a major accident in one of the portfolio companies, the fluctuation of oil and natural gas prices and the risk that company management will not be receptive to our goals. We will minimize these risks by reducing our downside risk by adhering to our margin of safety principles, with the goal of minimizing losses in holdings over three to five year periods.

Monitoring the Portfolio

ES Asset Management will need to aggressively monitor the portfolio companies to ensure that they are improving their Environmental and Social transparency. We will also monitor our companies' financial performances, however ES Asset Management realizes there is an inherent J-Curve in financial returns associated with increased reporting. As a result we will focus mainly on environmental and social reporting, as long as companies maintain base line performance levels that will allow the firm to take advantage of the long term improvements in environmental and social performance.

Institutional Investor Interest

Due to the long term nature of the fund, investor selection will be critical. It is critical to ensure all investors share our environmental and social goals and understand the long term time horizon of our investments. Qualified investors should expect to invest in companies in inherently risky industries, like Oil & Gas, at a lower risk profile than the rest of the industry as a result of reduced operational risks from improved ESG performance and the risk adverse nature of the fund.

Management Team

Tim Barbis, CFA: Financial analysis and valuation expert, with the ability to drive the financial results of the firm.
Luke Wilkinson: SRI Research Manager, with the ability to create value through environmental and social best practices.