

SRI: small caps are now major league players

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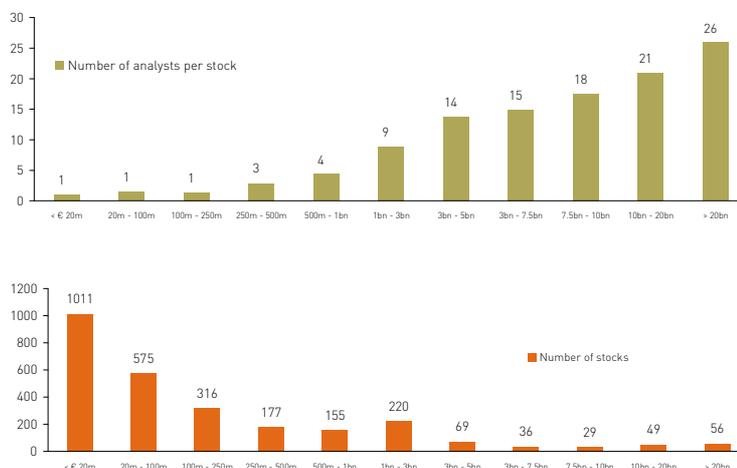
On the third anniversary of the Sycomore Sélection Responsable* fund launch, Léa Dunand-Châtellat, who runs the fund and heads up ESG research at Sycomore AM, says it makes sense to include small and mid cap stocks in a conviction-driven approach to SRI equity management.

Diversifying a conviction-driven SRI portfolio now requires giving a major role to small and mid-cap stocks. Specialised rating agencies and brokers devote less time to covering them so they do not have the place they deserve in socially responsible funds which are too often benchmarked.

WHY?

Analyst coverage of stocks capitalising less than EUR 1bn is practically inexistent. There are, on average, six analysts covering stocks capitalising between EUR 500m and 1bn. And coverage of stocks with market caps below EUR 3bn is still very limited with only nine analysts covering the EUR 1-3bn segment. Deprived of in-house research and relevant information on these stocks, SRI fund managers tend to avoid them, preferring to focus on blue chips which benefit from in-depth financial and extra-financial analyst studies.

SMALL & MIDCAP STOCKS: A BROAD UNIVERSE BUT ONLY MARGINAL ANALYST COVERAGE



Source: Sycomore Asset Management, Factset

AND YET SMES HAVE MANY POSITIVE QUALITIES

We believe that SME environmental, social and governance standards are just as high as in larger groups. But arguably midcaps have simply not spent enough time publicising the fact. Far too often, ESG reports have hitherto been the preserve of large groups as they know how to provide analysts and investors with the information they are looking for. But this handicap is diminishing due to the favourable impact of provisions in the Grenelle Act of July 12 2010 and, more specifically, article 225. Company reports published in 2013 for the financial year 2012 must now include an extra-financial report which will therefore also be audited. The article requires all listed companies to provide a standardised profile of their social and environmental policies (governance is already covered in the company report). This standardisation will make comparisons easier and, of course, help investors to realise that SMEs can be quite proud of their procedures. It will also make it easier to identify the best performing stocks.

TREATING SMALL CAPS LIKE LARGE CAPS

These observations should logically mean a single analytical grid for all companies whatever their size. It makes sense to adapt ESG criteria to a company's sector as the issues at stake can vary depending on a company's business but it is equally sensible to put small and large players within the same sector on an equal footing. It is essential to be just as rigorous in assessing how smaller listed companies roll out social, environmental and governance policies, asking them the same questions and applying the same criteria. In fact, such a rigorous approach is precisely what will help showcase their excellent performance in this field. Some of this performance can be attributed to the importance of reputational issues for smaller companies which are growing fast and run by a handful of people. They need to be capable of attracting and keeping talented people and so have to be irreproachable.

AN OPPORTUNISTIC APPROACH

Building a portfolio of small and midcap companies which lead the field in social and environmental responsibility must not be restricted to a thematic or sector approach. Stock market history teaches us that focusing exclusively on start-ups with strong positioning in a trendy sector is often dangerous and can lead to bubbles. Extra-financial analysis must necessarily be completed by financial analysis with a focus on valuation criteria.

Europe has a very broad universe of small and midcap stocks with 250 stocks in the EUR 1-3bn market cap bracket and 450 stocks in the EUR 250m-1bn segment. This helps us build a diversified portfolio with no country or sector bias.

This favourable development occurs at a time when investors are returning to mid cap stocks amid several important initiatives in France: Euronext's creation of the dedicated EnterNext market, a big increase in RFPs for midcap equities from large French institutionals and the launch of a *PEA* (French equity savings scheme) targeting SMEs. Moreover, this favourable environment has already resulted in market outperformance: France's CAC 40 gained 18% in 2013 while the CAC Mid & Small index jumped by close to 27%.

**Since its launch on January 24 2011, Sycomore Sélection Responsable has returned +34.9% vs. +20.0% for the EURO STOXX index, dividends reinvested and with reduced volatility of 11.8% over 1 year vs. 14.5%. The fund is an opportunistic selection of European stocks (including small, mid and large companies) based on proprietary ESG analysis that complies with sustainability principles. Data as of 10/01/2014.*

ABOUT SYCOMORE ASSET MANAGEMENT:

Founded in 2001, Sycomore Asset Management is one of the first equity-focused independent investment management companies in France. The Paris-based firm is majority-owned by its founding partners and its employees. Rated « High Standards » by Fitch Ratings since 2008, Sycomore Asset Management is managing \$2.75 billion through open-ended UCITS vehicles and institutional dedicated mandates. The firm's investor base includes pensions, banks, insurance companies, foundations & endowments, family offices, private banks and multi-managers. A signatory to the UN's Principles for Responsible Investment (UNPRI) and the Carbon Disclosure Project (CDP), it has gone one step further by rolling out Sycaway, its own corporate responsibility policy. This entails publishing a CSR report each year. "Our goal is to extend the responsibility approach used in our investment process and to structure a company initiative to match the efforts we expect from companies in which we invest," says Laurent Deltour, Chairman of Sycomore Asset Management.

CONTACT

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