

An Approach to Incorporating Sustainable Investing within your Bond Portfolio

September 2016



Introduction

Community Capital Management (CCM) is a pioneer in managing fixed income impact investing and fossil fuel free portfolios. We incorporate the “environmental” and “social” aspects of ESG investing in our investment philosophy by proactively screening market-rate bonds that positively contribute to economic and sustainable impact.

One of the main developments seen so far in the sustainable bond space has been driven by green bonds. We are seeing growing progression towards sustainable bonds with a wider focus on environmental and/or social positive impact.¹ In fact, as noted below, the Green Bond Principles (GBP) released an update to its use of bond proceeds earlier this summer to include themes with social objectives.

CCM continues to focus upon the ultimate use of proceeds for all impact investments, green bonds included. For us, a threshold declaration of green intent by an issuer is a starting point. We need to be able to identify, record, and track the underlying environmental and social activity that the transaction supports. In this regard, we use a combination of proprietary research augmented by the use of third-party standards to screen our portfolios ensuring bonds purchased support one or more environmental initiatives.

Our analysis follows the guidelines of the GBP which focuses on four core components: Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds, and Reporting. In June 2016, an update to the GBP was released which included an update to the bond concept “use of proceeds” to themes beyond the environment, such as bonds financing projects with social objectives, or with a combination of social and environmental objectives.² The GBP are voluntary process guidelines that recommend transparency and disclosure and promote integrity in the development of the green bond market by clarifying the approach for issuance of a green bond.

Fixed Income

Fixed income is an ideal place to start making sustainable investments for two primary reasons:

First, it is typically a lower-risk asset class with lower volatility and greater liquidity than other sustainable asset classes.

Second, there are tangible positive environmental outcomes that can be measured quantitatively and monitored qualitatively. The additional research associated with sustainable fixed income investments provides an added layer of transparency by detailing the use of bond proceeds to analyze the investment’s sustainable benefit.

By incorporating positive social and sustainable outcomes into fixed income investment decisions, investors can align these assets with their beliefs or missions.

At CCM, we incorporate the “environmental” and “social” aspects of ESG investing in our investment philosophy by proactively screening market-rate bonds that positively contribute to economic and sustainable impact.

¹ <http://business.nasdaq.com/list/listing-options/European-Markets/nordic-fixed-income/sustainable-bonds>

² <http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/green-bonds/green-bond-principles/>

Types of Investments

CCM invests in three main sectors of the bond market where we can conduct a use of proceeds analysis and track the positive environmental and social outcomes of an investment. Some of the investments listed as examples in this report have a “green” label by the state and/or issuer and some do not. Regardless of the label, the examples all have significant positive sustainable outcomes. They have been classified by CCM as sustainable or green investments as a result of our meticulous due diligence on the use of bond proceeds and our ability to track and document the underlying impact.

Taxable Municipal Bonds

Taxable municipal bonds, like their counterparts in the tax-exempt market, are backed by state and local governments.³

Taxable municipals may be used to finance a variety of sustainable initiatives such as:

- Energy efficiency
- Wind turbines
- Solar panels
- Water conservation
- Recycling
- Habitat preservation
- Neighborhood revitalization
- Brownfield redevelopment
- Adaptive reuse

Many of the issues listed above and discussed throughout this report are positively impacted through our investments but most of these bonds do not necessarily have a “green” label.

Examples:

CCM’s Taxable Municipal Bonds

The following are examples of taxable municipal bonds purchased on behalf of CCM portfolios that are financing a variety of environmental and social initiatives.

Hawaii’s Green Energy Market Securitization Program (GEMS)

The Green Energy Market Securitization Program (GEMS) is an innovative, sustainable green financing initiative designed by the Hawaii State Energy Office to make clean energy improvements more affordable and accessible for Hawaii consumers.⁴

The program provides low-cost capital to finance solar photovoltaic systems and other clean energy improvements for those who may otherwise have difficulty obtaining financing for these projects. Low-credit homeowners and renters, as well as nonprofits, are among those who will qualify for project financing through GEMS.⁵

Loan benefits to residential homeowners include:⁶

- Owning their own solar system
- Immediate bill savings
- Loan payments beginning after the installation is complete and the system being connected to the grid via a utility net energy meter

Tuolumne Wind Project

The Tuolumne Wind Project is located in Klickitat county, Washington, along the Columbia River. The site has been recognized as one of the most productive wind resource areas in the Western United States. The Project is a wind farm comprised of 62 wind turbines that are three-bladed, upwind, horizontal-axis wind turbines.

A wind turbine is a type of energy system that transforms the kinetic energy of the wind into electrical energy that can be harnessed for practical use. Power generated by the turbines is transferred to a transformer which raises the voltage to that of the level of electrical collection system. Cables carry the electricity from and within groups of wind turbines and transmit it to a collection substation.⁷

³ <http://www.msrb.org/msrb1/pdfs/About-Taxable-Municipal-Bonds.pdf>

⁴ <http://gems.hawaii.gov/learn-more/>

⁵ Ibid.

⁶ <http://www.energyfinancesolutions.com/forhomeowners-hawaii-gems-financing-for-solar-project>.

⁷ http://www.tid.org/sites/default/files/documents/news-resources/Tuolumne%20Wind%20Fact%20Sheet_Web.pdf

The Project went into commercial operation in 2009 and adds a significant amount of renewable energy to the Turlock Irrigation District's portfolio, taking it to 28 percent qualified renewable energy, eight years ahead of the Board of Director's adopted goal of 20 percent by 2017.⁸

Renewable energy provides substantial benefits for our climate, health, and economy:⁹

- Little to no global warming emissions
- Improved public health and environmental quality
- A vast and inexhaustible energy supply
- Jobs and other economic benefits
- Stable energy prices
- A more reliable and resilient energy system



⁸ Ibid.

⁹ http://www.ucsusa.org/clean_energy/our-energy-choices/renewable-energy/public-benefits-of-renewable.html#V9l2CfkrJph

¹⁰ <http://news.semo.edu/regents-approve-58-2-million-budget-to-fund-renovations-to-academic-magill-halls-deferred-maintenance-power-plant-upgrades/>

Southeastern Missouri State University

Southeastern Missouri State University is a public, accredited university located in Cape Girardeau, Missouri, near the banks of the Mississippi River.

Proceeds are being used to finance various improvements of educational facilities on the University's campus including: the renovation of Academic Hall, the main administration building on campus (including replacing the roof and HVAC system, upgrading the plumbing, and installing a new elevator); the renovation of the Magill Hall of Science (plus building an addition to house a new HVAC system for the building); the transition of a current coal-burning power plant to natural gas; and other miscellaneous capital improvements to academic facilities on the campus.¹⁰

The following are examples of improvements and the current and/or expected environmental benefit:

- Exterior improvements, combined with the installation of energy efficient mechanical systems, are estimated to save the university approximately one million dollars a year on utility bills.
- The power plant conversion to natural gas has reduced overall university emissions by 25 percent.
- Car pool tags and additional bike racks are helping to lower emissions.

Agency CMBS

Agency CMBS are securities backed by mortgages on a multifamily residential property such as:

- Low- and moderate-income multifamily housing
- Nursing homes and assisted living facilities
- Health care centers
- Multifamily rental housing and rural developments

Agency CMBS are issued by Ginnie Mae and Fannie Mae. At CCM, we invest in Fannie Mae's Delegated Underwriting and Servicing (DUS) Program. We also invest in Ginnie Mae Project and Construction Loans and Real Estate Investment Mortgage Conduits (REMICs). A typical REMIC deal can include multiple loans.

Although many of these issues have multiple sustainable benefits, none of them have a "green" label.

Examples: CCM's Agency CMBS

The following are examples of agency CMBS purchased on behalf of CCM portfolios that are financing a variety of environmental and social initiatives.

Flats 170 at Academy Yard¹¹

Flats 170 at Academy Yard is a green community built to achieve LEED Silver certification. The property is located in Odenton, Maryland. The project was built with over 75% recycled and regionally sourced materials, both stimulating the local economy and minimizing energy required for transportation. Over 90% of the construction waste during the project's development was recycled and diverted from landfills. The property continues its commitment to recycling with its resident recycling program providing easily accessible recycling containers to ensure maximum resident participation.

The property is a 100% smoke-free community and used low VOC paints, adhesives, and carpet during construction for a healthy living environment. An indoor air quality management program was maintained throughout construction to ensure building interiors provide a high level of air quality for residents. This process ensures apartment doors are air-sealed to the outside and neighboring homes have natural ventilation from the outside, bringing controlled fresh air inside. Additional insulation and caulking were used to better seal the building for energy efficiency and sound.

Residential units and common areas at Flats 170 are equipped with ENERGY STAR certified appliances, low-energy lighting, high-efficiency dual-flush toilets, and faucets that reduce approximately 40% of water consumption. A high efficient HVAC system was installed to cut down utility usage by greater than 15%.

The site was planned to provide easy access to public transportation. The use of eco-friendly transportation is promoted by ample bike storage and preferred parking spaces for low-emission and fuel-efficient vehicles. Green spaces throughout the property were landscaped in an ecologically balanced manner to limit irrigation and reduce potable water use. Additionally, Flats 170 has installed a green cleaning program that uses only eco-friendly products to clean all common areas and amenity spaces.

¹¹ <http://www.flats170.com/wp-content/uploads/2013/11/GreenFlyer.pdf>; <http://www.flats170.com/green-living/>

Solabella Apartments

A loan to Solabella Apartments financed the substantial rehabilitation of an affordable rental property in Miami Gardens, Florida that incorporates environmentally friendly features. The development, a Low Income Housing Tax Credit Property, consists of 92 townhouse apartments with 100% restricted to residents with incomes at or below 60% of area median income.

Energy conservation features include wall and attic insulation, efficient windows, and ENERGY STAR certified appliances. The following Green Building options were included in the development: programmable thermostats, toilets with dual flush options, ENERGY STAR qualified lighting, and Carpet and Rug Institute Green Label certified carpet and pad.¹²

In addition to its sustainable features, the following applicant programs are offered to residents: Welfare to Work, homeownership opportunities, first-time homebuyer seminars, literacy training, health and nutrition classes, resident activities, and financial counseling.¹³

Prescott Place

Prescott Place is an affordable rental property in Portland, Oregon where 19 of the 20 units receive Section 8 assistance. Residents have access to a vegetable and flower garden, community patio, community room, and a computer lab with free internet access. The property is located on a public transportation bus line and next to a grocery store.

Prescott Place is a REACH Community Development property. REACH is a non-profit affordable housing development and property management company. REACH offers residents access to several economic empowerment programs and services allowing residents to increase their financial knowledge and skills, overcome short-term cash flow problems, build credit, and save money toward achieving long-term goals.

Sustainable features at Prescott Place include:¹⁴

- Low flow faucets/toilets
- Ventilation fans
- Front loading washing machines
- On-site recycling
- Raised garden beds
- Fluorescent light bulbs



¹² <http://www.olcdc.org/news/docs/20130313175048.pdf>

¹³ http://www.floridahousing.org/FH-ImageWebDocs/AboutUs/BoardOfDirectors/BoardPackages/Exhibits/2011/03-March%2018/Consent/MFB_Ex_A.pdf

¹⁴ http://reachcdc.org/properties/docs/prescott_final.pdf

Asset-Backed Securities

Asset-backed securities (ABS) are securities backed by one or more of the following:

- Loans
- Leases
- Receivables against assets other than real estate and mortgage-backed securities

We invest in Small Business Administration (SBA)¹⁵ loans issued and guaranteed by the U.S. Government. Loans issued through the SBA may finance sustainable businesses or organizations incorporating sustainable business practices.

In the last few years, we have seen more issuance of more innovative financing in the sustainable ABS space such as our first solar asset backed notes deal sponsored by Tesla, following its acquisition of SolarCity Corporation. Some ABS have a “green” label. Other types, such as SBA loans, do not have the label even though they have a variety of environmental benefits.

Examples:

CCM’s Asset-Backed Securities

The following are examples of ABS purchased on behalf of CCM portfolios that are financing a variety of environmental and social initiatives.

SolarCity Corporation d/b/a Tesla Energy¹⁶

SolarCity Corporation, d/b/a Tesla Energy, was acquired by Tesla, Inc. in November 2016 to create the world’s only integrated sustainable energy company, from energy generation to storage and transportation. Tesla’s mission is to accelerate the world’s transition to sustainable energy for a better future. The Notes are collateralized by cash flows related to Tesla Energy’s interest in the Managing Members of four partnerships that own portfolios of solar energy systems and related Host Customer Leases/Power Purchase Agreements originated by Tesla Energy. The collateral pool is made up of 33,499 solar assets comprised of residential (98%) and commercial/government (2%) host customers across 19 states and 97 utility districts. The primary states include California, Maryland, Arizona, New York and Massachusetts.

Tesla Energy customers purchase electricity, solar energy systems and other energy-related products and services from Tesla Energy that typically lower their overall energy costs. Products include solar panels to produce clean energy, powerwalls to store energy and allow households to become 100% self-powered, solar roof’s and large scale solar and storage projects. The majority of Tesla Energy’s solar energy sales are in the form of long-term leases or power purchase agreements which provide households with green energy typically at a discount to utility rates.

¹⁵ <https://www.sba.gov/>

¹⁶ Tesla Energy is the largest distributed generation solar power provider in the U.S., with over 3.1 GWs of installed capacity across over 360,000 residential and commercial customers as of June 30, 2017. <https://www.tesla.com/blog/tesla-and-solarcity>

Craters & Freighters

Craters & Freighters is a specialty freight handling company with 13 employees in Garland, Texas. The company was founded in 1990 and aids both customers and businesses in all sectors with their specialty freight handling needs, including pick-up, crating, shipping, packaging, tracking, insuring and delivering of shipments that are too heavy/oversized, or too valuable and time-sensitive.

Recognizing the opportunity for the radical improvement of environmental conservation in the packing and transportation industry, Craters & Freighters launched a sustainable initiative in June of 2015 to help reduce climate change and create environmental solutions that benefit people and communities. By partnering with Arbor Day Foundation and Trees for the Future, the company has committed to planting a tree for every crate they build. Their goal with this initiative is to give back to the communities in which they operate and do their part to help replenish national forestry and drive sustainability.¹⁷

Craters & Freighters prides themselves on being deeply involved in the research and development of new and innovative eco-friendly packaging and shipping methods. Many of their locations use the latest technology in eco-friendly cushioning products including recycled cardboard materials.

The loan to Craters & Freighters was authorized under the SBA's 7(a) program which was established to serve small business borrowers that cannot otherwise obtain private sector financing under suitable terms and conditions. The program is the SBA's primary vehicle for providing small businesses with access to credit.

Corporate Bonds

Corporate bonds are debt obligations issued by companies to finance capital investment and operating cash flow.

As a pioneer in analyzing use of proceeds for fixed income impact investments, we believe this space presents a challenge from a due diligence perspective. There is typically not enough information for us to identify, record, and track the underlying environmental and social activity. As a result, we typically do not invest in corporate bonds; however, we recently came across a sustainable issue by Starbucks, the first U.S. company to issue a corporate sustainability bond. We bought this particular issue as a result of its clear intended use of proceeds, environmental and social benefits, and ongoing impact reporting of the bonds' proceeds.

Example: CCM's Corporate Bonds

The following is an example of a recent corporate bond purchased on behalf of CCM portfolios that is financing a variety of environmental and social initiatives.

Starbucks Corporation

The \$500 million bond supports the company's multiple sustainable projects, including ethical sourcing of coffee supplies, climate change mitigation, and financing support for farmers. Proceeds also will go toward maintaining crop stability and sustainable-farming practices. The bond gets Starbucks closer to its goal of making coffee the first sustainable agricultural commodity. Starbucks will publish annual updates on the use of the sustainability bonds' proceeds until they have been fully allocated to projects.¹⁸



¹⁷ <https://www.cratersandfreighters.com/news/blog/detail/craters-freighters-celebrates-25-year-anniversary-by-launching-plant-a-tree-sustainability-initiative-see-more-at-http://www.cratersandfreighters.com/about/blogsthashjfc1r8qddpuf/13/>

¹⁸ <https://news.starbucks.com/news/starbucks-issues-the-first-u.s.-corporate-sustainability-bond>

Conclusion

We are excited to be a part of the growing momentum in sustainable investing and the new and innovative ways that investments and finance play a role in benefiting our environment. The various case studies described in this paper demonstrate CCM's and our client's ongoing commitment to making positive environmental and social impacts. Collaboration among local communities, issuers, investors, and advisors has the potential to create a tremendous amount of impact.

Increased investor demand for sustainable fixed income investments will lead to greater issuance along with the ability for more innovative financing in the space.

As a pioneer in fixed income impact investments, we are extremely pleased to see a growing progression towards sustainable bonds with a wider focus on the environment and social objectives. This expansion will further increase the size of the sustainable fixed income market allowing advisers like us, at the forefront of environmental and social innovation, the opportunity to put even more money to good use.

About CCM

CCM's mission is to deliver superior risk-adjusted returns through investment strategies that contribute to positive environmental and social outcomes.

CCM is a privately-held registered investment advisor registered with the Securities and Exchange Commission. Headquartered in Ft. Lauderdale, FL with offices in Charlotte, NC and Boston, MA, the firm was founded in 1998 and began managing assets in 1999. CCM currently manages over \$2.3 billion for foundations, religious organizations, pension funds, high net worth investors, registered and unregistered funds, financial advisers and their clients, non-profits and healthcare organizations. CCM's intermediate fixed income impact investing strategy can be customized based on specific impact themes or geographies. It is available as a separate account or via a mutual fund (CRA Qualified Investment Fund). CCM also integrates impact investing analysis into its liquid alternative income strategy (CCM Alternative Income Fund) and within customized portfolios. For more information, please visit www.ccminvests.com or call 877-272-1977.

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