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Guide to Parametric Responsible Investing Strategies

Parametric offers a series of index-based responsible investing strategies: ESG, Fossil Free, Catholic Values, and Shariah Compliant. These strategies are designed as an expedient way to access commonly requested responsible investing themes, and complement our full suite of customization tools. In this brief we describe each strategy in turn, as well as some alternative options.

General Approach

Parametric has been offering client-driven, index-based portfolios that incorporate ESG criteria for more than fifteen years now. Our robust and continually evolving menu of ESG screens and licensed indexes gives investors a wide range of portfolio design choices. In many cases, however, investors are well-served by a standardized portfolio with minimal modifications. With this in mind, we have designed a series of risk-controlled, index-like exposures that can be used as a core equity portfolio allocation while aligning with common responsible investing themes. These strategies represent our best thinking with regard to implementing each theme and are supported by quarterly marketing materials in order to help clients make more informed decisions.

The Fossil Free, Catholic Values and Shariah Compliant strategies are screen-based and utilize screens that are also available separately. Our ESG Strategy involves building a portfolio which tilts in favor of companies with above average environmental, social and governance (ESG) characteristics¹. Each strategy comes with either domestic or international exposure, based on the S&P[®] 500 or MSCI EAFE Indexes, respectively, and is optimized to reduce tracking error relative to the these indexes. The strategies are reconstituted on a fixed schedule and strive to incorporate changes in ESG data and index constituents in a timely manner without generating excessive turnover.

These strategies can be implemented within a separately managed account, allowing investors to take advantage of customization options, such as Parametric's well-established tax-management capabilities, or to apply additional screens.

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¹ A screen essentially reconfigures the eligible investment universe such that companies with objectionable business involvement or behaviors are excluded and only those with acceptable characteristics remain. The construction of the final portfolio depends on the chosen investment style and maybe driven by additional ESG considerations. A tilt refers to a process in which company-level ESG characteristics are used to directly select and weight the portfolio constituents, subject to constraints designed to maintain a diversified exposure. This process strives to overweight companies with better ESG scores, and underweight the others, but may not necessarily exclude any securities outright, as a screen does. For more information please see our brief, Understanding ESG Screens and Tilts.

Catholic Values Investing

Parametric-FFV Catholic Values Strategy

The Parametric-FFV Catholic Values strategies aim to provide large-cap U.S. or large- and mid-cap international equity exposure in accordance with the United States Conference of Catholic Bishops' (USCCB) socially responsible investment guidelines (the Guidelines). The strategy contains constituents of the S&P 500 or MSCI EAFE Indexes, which meet specific moral and ethical standards, as determined by IWP Capital's Faith and Family Values FFV Scorecard®. The strategy is rebalanced twice a year, in conjunction with an updated screen.

The FFV Scorecard consists of securities that are restricted based on an explicit USCCB divestment policy as well as those that are determined to be in violation of Catholic teachings based on IWP Capital's qualitative interpretation of the Guidelines and norms within the Catholic community. Divestment areas include abortion, contraceptives, embryonic stem cell research, racial and gender discrimination, curbing pornography, and the production and sale of weapons and antipersonnel landmines. Companies may also be restricted based on a consideration of behavior with regard to the protection of human rights and the environment, the pursuit of economic justice, and corporate responsibility. Although not explicitly recommended as divestment areas in the Guidelines, companies engaged in the production of tobacco, alcohol and gambling products tend to be excluded by the FFV Scorecard based on their negative impact on the community.

Alternative Catholic Values Approaches

Alternatives for Catholic investors at Parametric include tracking the MSCI USA Catholic Values Index, applying the FFV Catholic Values screen, or selecting a mix of individual business involvement screens on any available index in order to create an investable portfolio. These options can differ from the Parametric-FFV Catholic Values strategies in the securities restricted, the underlying index exposure, or both. In particular, the MSCI USA Catholic Values Index (the Index) is based exclusively on MSCI's own research. This index embeds restrictions from MSCI's interpretation of the Guidelines and an ESG tilt. Currently, it is only available with U.S. equity exposure, which includes small-cap representation. Clients who identify individual screens to create their own package should be aware that there may be notable differences in the companies that are restricted compared to portfolios utilizing the FFV Catholic Values screen or tracking the MSCI USA Catholic Values Index.

The table below summarizes these options.

Option	Screen	Exposure	Marketing Material
Parametric-FFV Catholic Values Strategies	FFV Scorecard® provided by IWP Capital, interpreting USCCB Guidelines	<ul style="list-style-type: none"> S&P 500 MSCI EAFE (ADR only) Controls security, sector and fundamental factor deviations relative to index in order to minimize tracking error 	Quarterly Parametric provided fact sheets with performance, overviews, and presentation. White papers.
MSCI USA Catholic Values Index	Package determined by MSCI based on internal ESG and business involvement research, interpreting USCCB Guidelines	<ul style="list-style-type: none"> MSCI USA IMI Index Overweights companies with high ESG scores with some sector control No tracking error consideration 	Monthly MSCI provided fact sheets
FFV Catholic Values screen	FFV Scorecard® provided by IWP Capital, interpreting USCCB Guidelines	Any Parametric strategy or available licensed index	White papers
Custom combination of screening areas	Determined by client based on Parametric guidance and third party ESG research data	Any Parametric strategy or available licensed index	None

Shariah Compliant Investing

Parametric Shariah Compliant Strategy

The Parametric Shariah Compliant strategies aim to provide large-cap U.S. or large- and mid-cap international equity exposure while avoiding companies that do not comply with generally accepted Shariah investment principles. The strategy contains constituents of the S&P 500 or MSCI EAFE Indexes, respectively, that do not receive more than 5% of revenue from prohibited business activity, derive significant income from interest, or have excessive leverage, as determined by MSCI's ESG Research. The strategy is rebalanced quarterly, in conjunction with an updated screen.

Although Islamic law (Shariah) is open to interpretation, the MSCI screen follows a widely used approach of restricting securities based on business involvement and a reliance on interest, either borrowing or lending. Prohibited business activity includes adult entertainment, alcohol, cinemas, conventional financial services, gambling, music, pork, tobacco, and weapons. A company's reliance on interest is determined by examining accounts receivables, cash and interest bearing securities, and total debt, relative to total assets.

Alternative Shariah Compliant Approaches

Alternatives for Shariah compliant investors at Parametric include tracking the Russell-IdealRatings Islamic series, applying MSCI's Shariah Compliant screen, or selecting a mix of individual business involvement screens on any available index in order to create an investable portfolio. These options will differ from the Parametric Shariah Compliant strategies in either the restricted securities or underlying index exposure, or both. In particular, the Russell-IdealRatings Index series is based on IdealRatings ESG research and Russell defined geographic and size exposure. Clients selecting individual screening areas to create their own package should be aware that there may be notable differences in the companies that are restricted compared to a portfolio utilizing the MSCI Shariah Compliant screen or tracking a Russell-IdealRatings Index. In particular, a screen based only on business involvement will generally be significantly less restrictive than one that includes a financial ratio screen.

The table below summarizes these options.

Option	Screen	Exposure	Marketing Material
Parametric Shariah Compliant Strategies	Package determined by MSCI based on business involvement research and financial ratios	<ul style="list-style-type: none"> • S&P 500 • MSCI EAFE (ADR only) • Controls security, sector and fundamental factor deviations relative to index in order to minimize tracking error 	Quarterly Parametric provided fact sheets with performance, overviews, and presentation. White papers.
Russell-IdealRatings Islamic series	Package relying on IdealRatings research based on business involvement and financial ratios	<ul style="list-style-type: none"> • Russell Developed • Russell U.S. Large Cap • Russell Global • No tracking error consideration 	Monthly Russell provided fact sheets
MSCI Shariah Compliant screen	Package determined by MSCI based on business involvement research and financial ratios	Any Parametric strategy or available licensed index	White papers
Custom combination of screening areas	Determined by client based on Parametric guidance and third party ESG research data	Any Parametric strategy or available licensed index	None

Fossil Free Investing

Parametric Fossil Free Strategy

The Parametric Fossil Free strategies aim to provide large-cap U.S. or large- and mid-cap international exposure while avoiding companies that own fossil fuel reserves. The strategy permits only those constituents of the S&P 500 or MSCI EAFE Indexes, respectively, for which there is no evidence of any ownership of oil, natural gas, or coal reserves, as determined by MSCI's ESG Research. The strategy is rebalanced quarterly, in conjunction with an updated screen.

Fossil free investing typically focuses on eliminating companies that own sources of potential future pollution, rather than companies that are sources of current pollution. (The term low carbon is typically used to refer to the latter.) Owners of fossil fuel reserves are concentrated in the energy sector but can also include vertically integrated utility and industrial companies that own their own fuel sources. Additionally, the energy sector contains service companies whose business relies on the production of fossil fuels, but do not own reserves, and therefore are not excluded from a fossil free portfolio.

Alternative Fossil Free Approaches

Alternatives for fossil free investors at Parametric include tracking the Fossil Free Indexes US Index (FFI US Index), applying the MSCI Fossil Fuel Reserves screen, or selecting sector or industry based screens on any available index in order to create an investable portfolio. These options differ from the Parametric Fossil Free strategies in either the restricted securities or underlying index exposure, or both. In particular, the FFI US Index incorporates the Carbon Underground 200 restriction list, utilizes a modified market cap methodology, and maintains the energy sector underweight. Clients should be aware that an industry or sector based screen can have notable differences from the MSCI Fossil Fuel Reserves screen.

The table below summarizes these options.

Option	Screen	Exposure	Marketing Material
Parametric Fossil Free Strategies	All companies with any evidence of owning coal, natural gas, or oil reserves, as determined by MSCI	<ul style="list-style-type: none"> S&P 500 MSCI EAFE (ADR only) Controls security, sector and fundamental factor deviations relative to index in order to minimize tracking error 	Quarterly Parametric provided fact sheets with performance, overviews, and presentation. White papers.
FFI US Index	Largest global 100 coal and 100 oil and gas companies, ranked by potential carbon emissions content from fossil fuel reserves	<ul style="list-style-type: none"> S&P 500 Max weight of 1.25% at quarterly reconstitution No tracking error consideration, maintains underweight to energy sector 	Quarterly FFI provided fact sheets
MSCI Fossil Fuel Reserves screen	All companies with any evidence of owning coal, natural gas, or oil reserves, as determined by MSCI	Any Parametric strategy or available licensed index	White papers
Sector or industry screen	Based on Barra USSLOW or GEM3 sector or industry groups	Any Parametric strategy or available licensed index	None

ESG Tilt Investing

Parametric ESG Strategy

The Parametric ESG strategies aim to provide large-cap U.S. or large- and mid-cap international equity exposure while overweighting companies with high environmental, social and governance (ESG) scores and moderating tracking error relative to a standard index. The strategy contains constituents of the S&P 500 or MSCI EAFE Indexes, respectively, that are ranked highly on a holistic consideration of ESG metrics, as determined by Sustainalytics, a third party research provider. The strategy is rebalanced annually, in conjunction with updated ESG scores, and controls for security, sector, and factor biases, as well as industry and country biases, as applicable.

Sustainalytics' robust analytical framework addresses a broad range of macro-level ESG issues and trends that have a significant impact on each industry and company. Using the Barra risk model and Sustainalytics ESG research as inputs, the strategy is constructed in a manner that results in predicted tracking error of approximately 1.0% relative to the Index. ADR implementation for the International version results in total predicted tracking error of about 1.5%.

Alternative ESG Tilt Approaches

Alternatives for investors seeking an ESG tilt at Parametric include tracking any of MSCI's ESG Indexes (the Sustainability series). This series differs from the Parametric ESG Core strategies in the underlying ESG ratings, the index construction, and the final exposure. In particular, MSCI's Indexes rely on overweighting securities according to their in-house scoring system, controlling primarily for sector biases, and are based on MSCI "parent" indexes. This means that a portfolio tracking the MSCI USA ESG Index will have greater small cap representation than the Parametric ESG Core Domestic strategy and notably higher tracking error relative to the S&P 500.

The table below summarizes these options.

Option	Tilt	Exposure	Marketing Material
Parametric ESG Core Strategies	Maximize the portfolio's ESG score, as determined by Sustainalytics, subject to security, sector, and factor bias constraints. Additional bounds are placed on industry, for domestic, and country, for international.	<ul style="list-style-type: none"> • S&P 500 • MSCI EAFE (ADR only) • Controls security, sector and fundamental factor deviations relative to index in order to minimize tracking error 	Quarterly Parametric provided fact sheets with performance, overviews, and presentation. White papers.
MSCI Sustainability Index series	Overweights the constituents with higher ESG scores, as determined by MSCI, subject to sector constraints	<ul style="list-style-type: none"> • Any MSCI regional or country index • Relatively sector neutral, but no explicit tracking error consideration 	Monthly MSCI provided fact sheets

Disclosure

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