**SKY HARBOR** CAPITAL MANAGEMENT

# Staying the Course on Sustainability

## People Planet Purpose Profits & Politics

## Our Purpose

To grow our clients’ assets by investing in sustainable high yield companies that have committed to benefit all their stakeholders and society as a whole.

## How We Do It

By compounding interest over time, protecting principal and giving our clients the returns they expect and the information they need.

## Why We Do It

We believe that companies that meet their ethical obligations to employees, customers, suppliers, communities, shareholders, government, the environment, and society as a whole will prosper over the long term, attract lower cost capital, and generate superior returns to their investors.

Sustainability Newsletter
October 2020

Covid-19: testing the “S” in ESG

Sustainability Spotlight:

KeHE Food Distributors

## Human Capital: a company's most strategic asset

Pre-pandemic it was often said that a company's most important assets walked out at the end of every working day. For most of 2020 even with significant numbers of employees working remotely, the notion that a company's workforce is its most strategic asset rings truer than ever.

In acknowledging the notion that proper management of human capital is essential to a sustainable business, the SEC in late August announced reforms that, among other things, will require public companies to include as a disclosure topic, a description of its human capital resources to the extent such disclosures would be material to an understanding of a company's business. Investors will likely press for further transparency with respect a company's treatment of all its essential stakeholders. In response, corporations recognize the importance of how they are treating or, perhaps just as importantly, how they are perceived by the public to be treating their essential stakeholders.

## The People part of Sustainability – talking the talk and walking the walk

In one sense, COVID-19 can be viewed as a test of how well or poorly companies have responded in their treatment of essential stakeholders. The actions taken by a company in response to the pandemic may be viewed as a manifestation of a company's commitment to a sustainable business model, which depending on how it is perceived could positively or negatively affect its ability to attract capital and achieve lasting profitability.

A recent review conducted by SKY Harbor based on public disclosures and media sources found that companies' responses to COVID-19 usually include safety precautions like working from home and social distancing, but not necessarily support for employees, customers, or communities. Many, but not all, companies provide supports to their employees such as paid sick days and an employee assistance fund, although most companies do not provide any pay or benefits to furloughed employees. Donations of money, product, and time to individuals and organizations dealing with COVID-19 are somewhat common, as are salary reductions for top executives to prevent or at least spread out decreases in pay or hours for employees lower down.

Several companies, however, have been reported in the news media as not fulfilling their promises. One example is a healthcare company that received negative press coverage after four nurses at one hospital alleged that they were fired for speaking out about inadequate care and staffing during the COVID-19 patient surge. Some companies that received government stimulus are, nevertheless, significantly reducing the size, pay and benefits of their workforce (one healthcare company received hundreds of millions in aid and tax deferrals and reported a profit of almost $100 million, yet it still cut 10% of its staff and suspended an employee retirement benefit).

An industry that has been especially affected by COVID-19 is the meatpacking industry, which has been plagued with outbreaks in meatpacking plants. While this is partially due to the difficulty of automation in the processing animal meat other than chickens, poor management undoubtedly also plays a major role. One meatpacking company was accused by whistleblowers of allowing symptomatic employees to work, charging employees for COVID-19 tests, and other allegedly negligent practices.

## Meeting the COVID Challenge

On the other side of the ledger we also found companies that did walk the walk as well as talk the talk. One in particular, which we highlight in this month's column, is **KeHE Food Distributors Inc. ("KFD")**, a high yield debt issuer.[1]

**KFD** is a leading natural and organic, specialty and fresh products food distributor in North America specializing in simplifying the complex supply chain for its customers by managing thousands of SKUs and vendor relationships across multiple product categories, while reducing costs by leveraging its purchasing scale and efficient distribution network. Its network allows for distribution of +72.5k food and non-food SKUs from over 4.3k vendors to ~7.7k customers and 25.5k customer locations.

### KFD's COVID-19 Response

**Proactive Measures** – Monitoring and following state-by-state mandated laws with face masks and social distancing; providing PPE, increased sanitation and offering health and wellness checks to employees

**Supporting Frontline Workers** – Temporary essential service bonus to employees in above normal COVID states

**WFH** – Advising staff in corporate offices to work remotely and providing support to remote employees

**Sick Employees** – Employees feeling ill are relieved from work and provided sick pay and other benefits. Employees testing positive for COVID are quarantined for 14 days.

**Specific Processes involving Drivers and Deliveries** – increased sanitation on trucks, disinfectant wipes and hand sanitizers have been provided to keep drivers' work areas clean; drivers are required to wear face coverings.

- *Founded in 1952 as a regional, family-owned business incorporated in 1961 and as of 2000 an employee owned enterprise*
- *As a Certified B Corporation, KFD is committed to environmental, social and governance standards and responsible business practices*
- *Core Purpose: "We SERVE to make lives better® for our customers, our suppliers, our employees and our communities."*
- *Believes that its business conduct should be a force for good in society, for the planet, and for those less fortunate around the world.*
- *Employs 5,467 people*
- *Contributes 10% of its profits to KeHE Cares™ run by company employees, which serves local soup kitchens, creates meal kits for the hungry, builds and repairs homes, collects relief supplies, and engages in multiple ways to advance its core values*
- *COVID Risk Mitigation Strategy: Keep those with symptoms at home; Keep people separated & safe at work; Ensure a clean environment; and Reduce risk of droplet spread*

[1] KeHE Food Distributers is an issuer of high yield debt, which is included in portfolios managed by SKY Harbor, but its inclusion in this column is for educational and illustrative purposes with respect to the topic of this column and is not intended as an investment recommendation to buy, sell or hold the issuer's securities. SKY Harbor's investment in the company's debt securities is subject to change without notice.

## Why is all this Important?

Environmental, Social, and Governance ("ESG") factors are part of SKY Harbor's integrated sustainability research process as summarized by FASST, an acronym that stands for Fundamentals, Asset valuation, Sentiment, Sustainability, and Technicals.

We believe that companies, particularly in the high yield space, that have pivoted to or are in transition to a sustainable business model as evidenced by a company's commitment to Sustainability — embodying the notion of stakeholder primacy — will have a much greater likelihood of growing top-line revenue, attracting capital, generating lasting long-term profitability, and avoiding default while at the same time contributing to the good of society as a whole.

Our FASST process is a holistic approach and seeks to identify those companies that are suitable for inclusion in the portfolios we manage for the benefit of our clients. The Sustainability factor, which can be more qualitative than quantitative, is in our view essential to understanding the full range of risk and opportunities in evaluating an issuer's creditworthiness over the long term.




For more information, contact SKY Harbor Capital Management, LLC at +1 203 769 8800 or email info@skyhcm.com