



Annual  
ESG Report  
2021

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## 2021 in Hindsight

I was pleased when my colleagues asked me to write an introduction to AQR's ESG Annual Report.

This year-in-review sums up what I see as our firm's long-standing role in the increasingly crowded and complicated world of ESG investing — contributing to research, striving to bring clarity to new and complex issues, and, ultimately, helping investors to make more informed decisions.

This effort is not new to us. Our oldest ESG investment signal (i.e., a factor in our multi-factor process) dates back to our launch in 1998 and we've been publishing research on the topic of responsible investing since 2009, becoming more prolific as time has gone on and the discourse has become more active. Today over 80% of our AUM now integrates ESG-related alpha or risk signals, and we manage approximately \$30 billion in dedicated ESG solutions.<sup>1, 2</sup>

Along the way, we've started engaging with the management teams of select portfolio holdings, pushing them to provide more transparency through their ESG disclosures. For our efforts, we were recognized recently by the CDP for our effectiveness in influencing companies to enhance their carbon-related disclosures. While this is a recognition in and of itself, it's also a start in disproving the false narrative that quants can't be responsible owners (it is still the case that we are horrible dancers).

This past year, I wrote a blog post on my colleague's research on the role of shorting in ESG investing, why it was important, and why AQR cares. And the answer is: We care because it matters to our clients and because we think we have a better mousetrap. Many of our clients are looking to effect change through their portfolios and, well, our research shows that shorting can help them reach that goal. Allowing a relatively small amount of shorting both creates more impact and we believe offers a better risk/return trade-off. Once again, for the record, shorting counts.

Our advocacy for shorting and ESG is emblematic of our commitment to share ideas that help investors achieve their ESG goals, even (and especially) if they challenge the status quo. Arguing for something we believe is better, even if it's uphill on occasion, is what makes me most proud of AQR.

In the pages that follow, I hope you'll see the progress we've made to date, but more than that, I hope you'll see our commitment to keep doing more.

We'll continue to search for alpha and to improve our stewardship practices because responsible investing matters — to our clients and to our firm.

### Cliff Asness

Managing and Founding Principal

<sup>1</sup> ~80% of AQR's assets under management integrated ESG-related alpha or risk signals. We include ESG-related signals in our multi-factor security selection models as standard, and have since AQR's inception; in all portfolios, we will incorporate ESG to the extent that we believe it improves the risk/return profile, consistent with our research on the ESG-efficient frontier.

<sup>2</sup> As of 12/31/2021, AQR managed ~\$30 billion in dedicated ESG solutions, designed in service of our clients' ESG-related objectives. These include ~\$27 billion in carbon-aware portfolios (which actively manage carbon intensity and other metrics for significant carbon reductions in long-only accounts and zero carbon exposure where shorting is allowed) and ~\$9 billion in our Sustainable strategies, two processes which may also be combined. The Sustainable process seeks to avoid companies with the largest ESG risk exposures by imposing static and dynamic exclusions, while targeting an improvement in portfolio ESG profile; in relaxed constraint and alternatives portfolios, we may actively short the worst ESG offenders.

# About AQR

AQR is a global investment management firm dedicated to delivering results for our clients. At the nexus of economics, behavioral finance, data and technology, AQR's evolution over two decades has been a continuous exploration of what drives markets and how it can be applied to client portfolios. Our culture of intellectual curiosity compels us to challenge the status quo, disrupt long-held beliefs and uncover new insights - we view the pursuit of truth and research excellence as our fundamental responsibility to ensure we remain at the forefront of systematic investing. AQR is committed to its fiduciary duty and to serving as a responsible investor. We offer diversified strategies across long-only and relaxed constraint equity, total and absolute return alternatives, and dedicated ESG solutions within each asset class.<sup>3</sup>

1998

AQR - Applied Quantitative Research - is founded

~60%

of our researchers hold advanced degrees and ~40 employees hold PhDs

~\$124B<sup>4</sup>

in AUM and ~25% of firmwide AUM in dedicated ESG portfolios<sup>5</sup>

63

Awards received for our academic research since firm's inception

4

Consecutive years as a Best Place to Work for LGBTQ Equality with a perfect score in the Human Rights Campaign's Corporate Equality Index

5

Consecutive years as one of Pensions & Investments' Best Places to Work and ranked first in our category in 2021

<sup>3</sup> Source: AQR. Information as of December 31, 2021. Diversification does not eliminate the risk of experiencing investment losses.

<sup>4</sup> AUM data includes assets managed by AQR and advisory affiliates.

<sup>5</sup> As of 12/31/2021, AQR managed ~\$30 billion in dedicated ESG solutions, designed in service of our clients' ESG-related objectives. These include ~\$27 billion in carbon-aware portfolios (which actively manage carbon intensity and other metrics for significant carbon reductions in long-only accounts and zero carbon exposure where shorting is allowed) and ~\$9 billion in our Sustainable strategies, two processes which may also be combined. The Sustainable process seeks to avoid companies with the largest ESG risk exposures by imposing static and dynamic exclusions, while targeting an improvement in portfolio ESG profile; in relaxed constraint and alternatives portfolios, we may actively short the worst ESG offenders.

# ESG Philosophy

AQR is committed to helping our clients achieve their ESG goals. We seek to integrate ESG in both our asset selection and our ownership practices.

## AQR will:

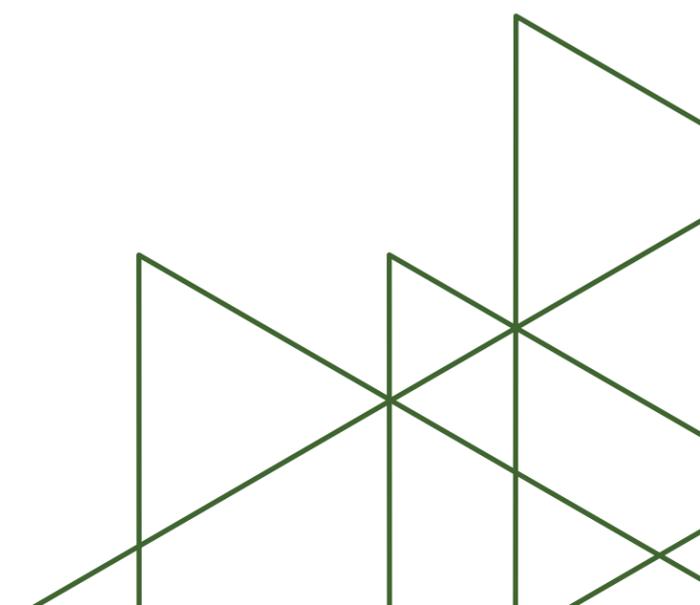
**Embrace research and education** on ESG criteria in pursuit of continuous improvement to our understanding of the risk and opportunities to our clients, our investment strategies, and our business.

**Consider incorporating ESG** investment ideas **on an equal footing** with other investment ideas. In all mandates, ESG investment ideas will be implemented to the extent they are driven by improvement to risk and portfolio return characteristics.

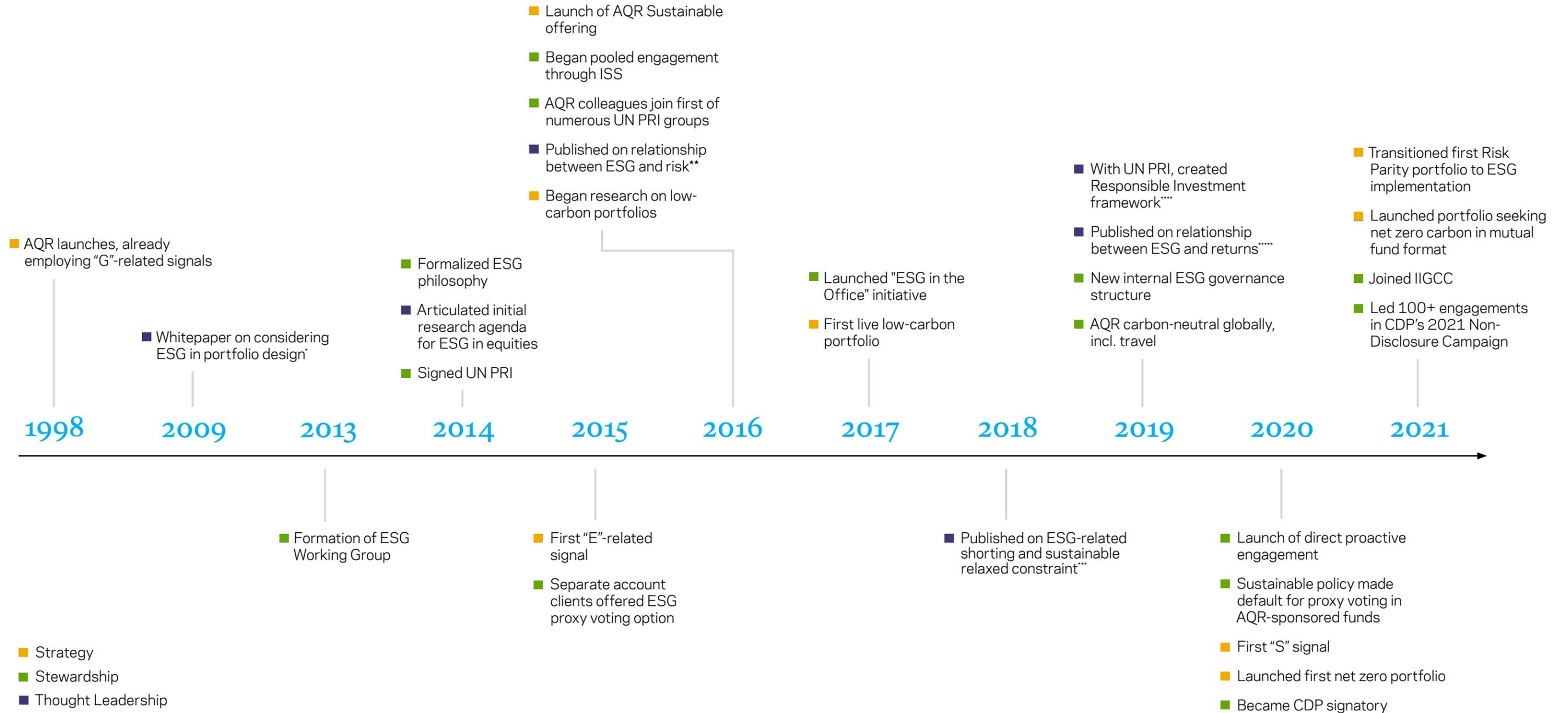
**Be transparent** with respect to its progress on ESG research and implementation solutions.

**Be a responsible steward** of our clients' investments, striving to create long-term value for our clients without compromising on our core values (our stewardship policy documents are publicly available on [AQR.com/ESG](https://www.aqr.com/ESG)).

**Ensure** it has the **resources** available to adhere to these guiding principles and to aid clients in their understanding of ESG-based investing.



# Our ESG Journey



\* "A Framework for ESG Consideration in Portfolio Design" – Jul. 2009  
 \*\* "Assessing Risk through Environmental, Social and Governance Exposures" – Dec. 2016 (Journal of Investment Management: Vol. 16, No. 1, 2018)  
 \*\*\* "Hit 'Em Where It Hurts: ESG Investing 2.0" published in IPE – Oct. 2018  
 \*\*\*\* "Clearing the Air: Responsible Investment" – May 2019, also published in The Journal of Portfolio Management Ethical Investing 2020  
 \*\*\*\*\* Responsible Investing: The ESG-Efficient Frontier – Oct. 2019  
 Source: AQR, UN PRI.

# ESG Governance Structure and Resources

## Executive Committee

Management and oversight of AQR's ESG agenda ultimately rests with the firm's Executive Committee. The Executive Committee serves as the firm's key governance function across business areas and is led by AQR's founders and principals from multiple business areas. Senior members of the ESG Working Group and Executive Committee meet on a quarterly basis to refine and review AQR's ESG agenda.

## ESG Working Group

AQR's ESG Working Group, which is responsible for day-to-day decision making on ESG matters, is led by our Head of ESG Strategy and the chairs of our four ESG committees: ESG Research, ESG Stewardship, ESG Reporting and Communication, and ESG in the Office. Our ESG committees are composed of subject-matter experts and leverage the broader resources of the firm to implement our ESG agenda across the four verticals and add ESG-specific value to clients. Over the past year, our collective efforts have enabled us to broaden our reach and grow our ESG-related capabilities and offering.

### AQR Executive Committee

### ESG Working Group

Responsible for day-to-day decision making on ESG matters and led by our Head of ESG Strategy and the chairs of our ESG committees.

### ESG Committees

#### ESG Research

Responsible for setting direction of ESG research agenda and collaborating on projects across research teams.

#### ESG Stewardship

Responsible for overall approach toward engagement with portfolio companies, the broader investment community, and regulators as well as oversight of proxy voting.

#### ESG Reporting and Communication

Responsible for ESG-related content shared internally and externally, including marketing collateral and reporting.

#### ESG in the Office

Lead internally-focused related actions to ESG including recycling, energy reduction, offsetting, and firmwide carbon neutrality and coordinate with Human resources on broad corporate social responsibility efforts.

Source: AQR.

# Our ESG Program

## 2021 at a Glance

~80%<sup>6</sup>  
of AUM  
Integrating ESG-  
Related Alpha Signals

~\$7 billion  
of AUM Launched or  
Converted to Dedicated  
ESG Implementations

20+  
ESG Conferences  
and Events where AQR  
Colleagues Presented

204  
Direct Engagements  
Conducted with  
Portfolio Companies  
(~3x Increase Versus 2020)

68,000+  
Proxies Voted

2  
New Portfolios  
Targeting Net  
Zero Carbon



Launched First of Its Kind  
Sustainable Long/Short Mutual Fund



Certified CarbonNeutral<sup>®</sup> Company 2021<sup>7</sup>



Shortlisted for the European Pensions Awards 2021  
“ESG/SRI Provider of the Year”

Source: AQR, Natural Capital Partners. AUM is approximate as of 12/31/2021, includes assets managed by AQR and its advisory affiliates  
<sup>6</sup> ~80% of AQR's assets under management integrated ESG-related alpha or risk signals. We include ESG-related signals in our multi-factor security selection models as standard, and have since AQR's inception; in all portfolios, we will incorporate ESG to the extent that we believe it improves the risk/return profile, consistent with our research on the ESG-efficient frontier.  
<sup>7</sup> CarbonNeutral<sup>®</sup> certification is issued by Natural Capital Partners and is based on a protocol updated annually to reflect developments in climate science, international policy, standards and business practice. View the latest protocol [here](#).

# Why a Quantitative Approach to ESG

We view our quantitative approach as naturally compatible with ESG and believe that a systematic investment approach to ESG offers several important advantages.

## **A quantitative approach can utilize and process more ESG data.**

A quantitative process is theoretically unlimited in its potential to look at ESG data, thanks to the massive computing power that underpins it. A systematic investment process considers both financial and non-financial data - including ESG - in a highly sophisticated, ever-evolving model designed to capture helpful information to evaluate the overall health and attractiveness of potential investments. This process seeks to avoid human bias and analyzes many securities across countless dimensions, covering more ground than would be possible for a team of human analysts.

## **A quantitative manager can offer more transparent ESG integration.**

We can state the weight of ESG in our models because we can precisely specify which of our signals are ESG-related.

We believe quantitative managers are well-positioned to incorporate and deliver on socially responsible and climate-oriented goals while maintaining the desired risk/return profile of a strategy.

Additionally, quantitative managers can estimate the impact an additional ESG consideration will have on a strategy's performance and ESG profile, given the ability to simulate historical strategy risk, characteristics, and returns.



## **Responsible ownership practices go together with a systematic investment approach.**

A quantitative manager is well-positioned to practice responsible ownership, such as engaging with company management and exercising support for ESG measures through proxy voting. We outline our 2021 responsible ownership efforts later in this report; our progress in this space continues to offer compelling evidence that quantitative managers can be successful responsible owners.

We have found that as a large quantitative manager, even though we are highly diversified across many different positions, our aggregate position across portfolios for many companies is oftentimes meaningful. When holding a material position, company management is typically receptive to a dialogue and our vote can be meaningful to the outcome of proxy issues. Additionally, there are certain ESG issues that appear on proxies - such as corporate restructurings - that we already analyze as part of our investment process. In those cases, our systematic investment process can help inform our responsible ownership approach.<sup>8</sup>

<sup>8</sup> Source: AQR. There can be no assurance that an investment strategy will be successful.

# Our ESG Approach

The many motives for responsible investing and the increasingly vast landscape of ESG-focused products often lead to confusion around the meaning and implementation of ESG. Our approach to ESG starts by clearly defining a structure of the terms and approaches within responsible investment.

We collaborated with UN PRI to develop a framework of the approach and terms necessary to have an informed discussion and investment policy on responsible investing. The most salient distinction in our framework is the division of ESG investment approaches and terms into two overarching halves – responsible asset selection and responsible ownership.

Responsible asset selection is the consideration of ESG issues that may affect the long-term pricing of an asset as well as the long-term sustainability of the issuer’s business model. Responsible ownership is a thoughtful awareness of the avenues to interact with companies to influence their business, beyond the simple decision of whether to invest.

The following discussion of our ESG program aligns with this clear distinction and details our progress on both. Our full responsible investing framework can be found [here](#).

## Responsible Asset Selection

As in prior years, our 2021 ESG Research effort included multiple projects on E, S, and G-themed alpha ideas, using ESG in risk models, and designing new ESG-focused portfolio solutions. As one 2021 example, we completed research on a set of E-related alpha signals, which will be added to our stock selection models in early 2022. These signals are intended to enrich our view of the Quality characteristics of a given issuer by measuring the resource efficiency of the company and its supply chain, focusing specifically on greenhouse gas emissions.

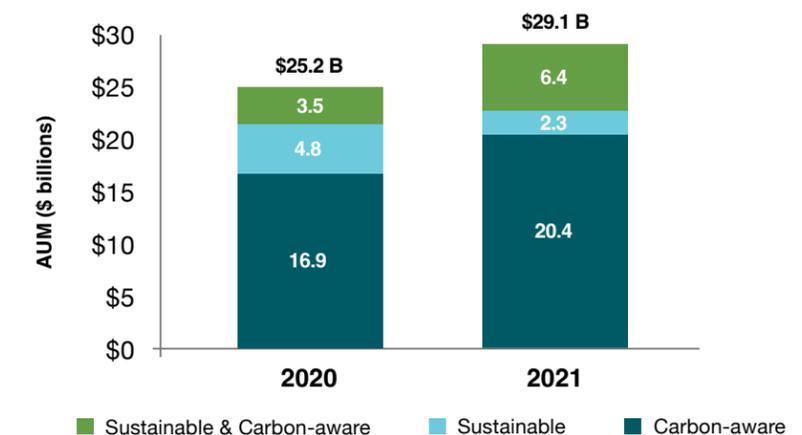
As of the end of 2021, AQR managed ~\$124 billion,<sup>9</sup> ~80% of which includes ESG-related investment signals,<sup>10</sup> consistent with our research on the [ESG-efficient frontier](#). AQR

begins 2022 managing ~\$30 billion in dedicated ESG strategies,<sup>11</sup> which employ sustainable themes that may reduce risk or achieve a specific ESG objective. These include our proprietary carbon-aware and Sustainable methodologies, two processes which may also be combined. Our Sustainable strategies seek to avoid investing in companies with the greatest ESG risks, while positively tilting toward companies with attractive ESG profiles, and our carbon-aware strategies actively manage carbon intensity and other metrics for significant carbon reductions in long-only accounts and zero carbon exposure where shorting is allowed. Our dedicated ESG solutions encompass customized implementations designed in service of clients’ specific ESG objectives, such as a custom dynamic screen or a tilt to manage reputational risk.

**AQR begins 2022 managing ~\$30 billion in dedicated ESG strategies,<sup>11</sup> which employ sustainable themes that may reduce risk or achieve a specific ESG objective.**

Dedicated ESG Assets

Year-end 2020 vs. 2021



<sup>9</sup> Source: AQR. Approximate as of 12/31/2021, includes assets managed by AQR and its advisory affiliates.

<sup>10</sup> ~80% of AQR’s assets under management integrated ESG-related alpha or risk signals. We include ESG-related signals in our multi-factor security selection models as standard, and have since AQR’s inception; in all portfolios, we will incorporate ESG to the extent that we believe it improves the risk/return profile, consistent with our research on the ESG-efficient frontier.

<sup>11</sup> As of 12/31/2021, AQR managed ~\$30 billion in dedicated ESG solutions, designed in service of our clients’ ESG-related objectives. These include ~\$27 billion in carbon-aware portfolios (which actively manage carbon intensity and other metrics for significant carbon reductions in long-only accounts and zero carbon exposure where shorting is allowed) and ~\$9 billion in our Sustainable strategies, two processes which may also be combined. The Sustainable process seeks to avoid companies with the largest ESG risk exposures by imposing static and dynamic exclusions, while targeting an improvement in portfolio ESG profile; in relaxed constraint and alternatives portfolios, we may actively short the worst ESG offenders.

## Responsible Asset Selection



## Responsible Ownership



In 2021, we continued to expand our range of dedicated ESG strategies through launches of new, and conversions of existing strategies. For example, we launched a Sustainable Corporate Arbitrage Strategy, currently available in a UCITS vehicle, which we believe is one of the first SFDR Article 8 products in the corporate arbitrage space. It incorporates AQR's Sustainable process, featuring a positive tilt toward deals with more attractive ESG characteristics, and a negative screen to exclude deals with relatively poor ESG-rated securities. We also launched a Sustainable Long-Short Equity Carbon-Aware Strategy in a US Mutual Fund format, which is both Sustainable and targets net zero exposure to carbon emissions. We believe that this fund is the first 1940 Investment Company Act fund to take a long/short approach to ESG. Finally, we transitioned our first Risk Parity portfolio to a Sustainable and carbon-aware implementation (note that these processes currently apply to the portfolio's equity sleeve).

Reflecting the diversity of our strategies and asset classes we invest in, our research projects covered not only corporate asset classes, but also investigated potential ESG-focused solutions in the macro space. We expect such projects to be an important part of our research program going forward too, supporting our multi-asset class and dedicated macro-type strategies.<sup>12</sup>

<sup>12</sup> Source: AQR. There can be no assurance that an investment strategy will be successful.



## Responsible Ownership

In keeping with the requirement that responsible investors pursue responsible ownership, we continued to enhance our approach to stewardship in 2021.

AQR's stewardship approach is grounded in transparency, as well as a desire to create positive long-term value for our clients. Our efforts cover a range of activities, including:

- | Voting our proxies in an ESG-aware manner
- | Engaging directly with management of companies where AQR may have a potential impact
- | Collaborating with asset owners and other investors on specific issues to hold management accountable for misuse of their positions or other issues that are inconsistent with our ESG core values
- | Participating in industry groups or bodies that advocate for specific changes or for greater disclosure on specific issues inconsistent with our ESG core values
- | Exercising litigation rights to address corporate mismanagement, breach of fiduciary duty, fraud, misrepresentation, or violations of other laws

AQR's Stewardship Philosophy, Engagement Policy and Proxy Voting Policy are publicly available on [AQR.com/ESG](https://www.aqr.com/ESG).

## Engagements

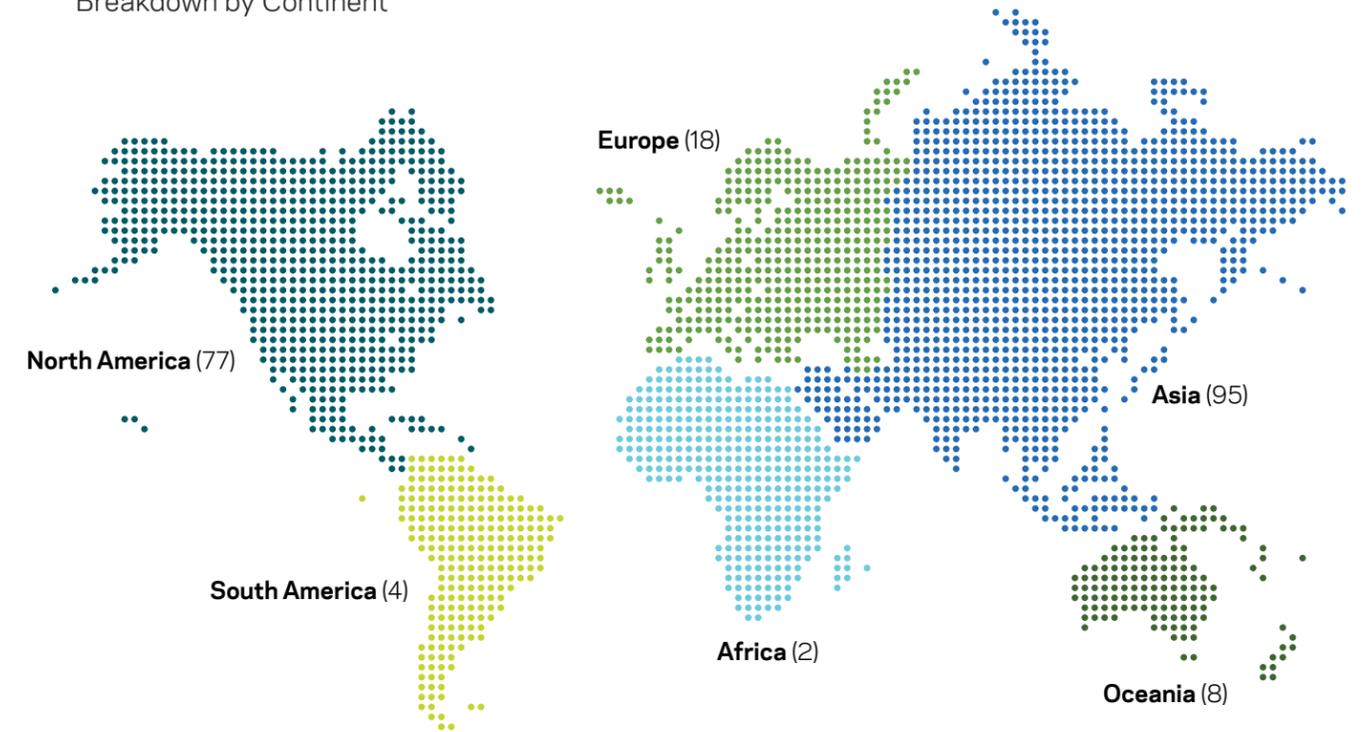
It is our fervent belief that greater transparency is positive for all market participants, hopefully leading to better alignment between companies and their investor base, as well as more accurate pricing of ESG risks and opportunities. Therefore, the guiding principle in all of our engagement activities is transparency in ESG disclosures. Consistent with AQR's investment process, our engagement program is conducted at the firm level, rather than tailored to individual portfolios.

Our approach to engagement is three-fold, involving direct - both proactive and reactive - and collaborative initiatives. As a quantitative manager, we utilize ESG data to identify potential opportunities for engagement with companies. For example, in 2019, we developed a proprietary process using various ESG data sources to cross-reference where problematic ESG exposures occur in our portfolio companies. For material positions with ongoing ESG concerns, AQR seeks to engage in a substantive dialogue with company management to better understand the drivers of related ESG risks, and what steps the company is taking to address these, including providing greater transparency to the market. As we describe further below, we also identify engagement targets and help to advance the collective ESG effort through

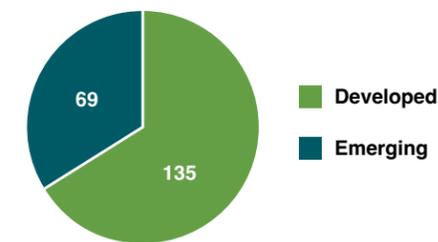
active participation in systematic investor-led initiatives, such as the CDP Non-Disclosure Campaign. AQR's Stewardship Committee oversees the engagement process, and any recommendations made to companies are done in a manner that is consistent with our desire to see ESG risks properly managed, and issues resolved in a fully transparent manner.

2020 was the first year that AQR conducted direct engagements with company management of our portfolio holdings. In 2021, we significantly expanded our program by conducting 204 direct engagements, which represents a nearly 3x increase versus 2020. With a focus on transparency, our specific goals are typically for companies to publish more data and/or reports publicly so investors can review and track how companies are responding to ESG-related issues. This signals to the investment community how seriously companies are responding to such risks, if they are making any changes to processes, what goals they are setting for themselves, and how they are tracking progress towards those goals. We believe this increased transparency should reduce future ESG risks at the company level. Beyond proactive direct engagement, we also engage directly on a reactive basis, for example on upcoming proxy issues where underlying firms seek out AQR to present issues which may be material for the vote.

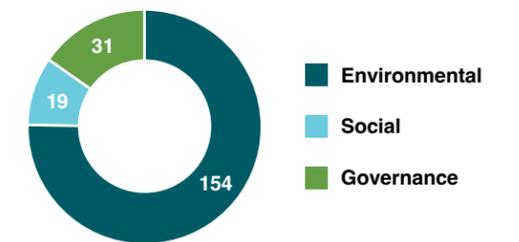
2021 Engagements  
Breakdown by Continent



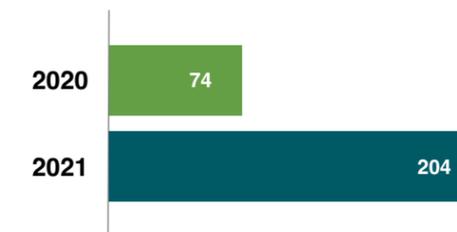
2021 Engagements  
Breakdown by Market



2021 Engagement  
Breakdown by Theme



2020 vs. 2021 Direct Engagements



Source: AQR. AQR's engagements from January 1, 2021 to December 31, 2021.

## 2021 Engagement Focus: Climate Change

As is evident from the charts above, environmental issues, particularly those related to climate change, were a significant focus of our 2021 engagement program.

AQR became a signatory to the CDP (formerly Carbon Disclosure Project) in 2020. Each year, the CDP surveys thousands of companies, cities, states, and regions to measure and manage their risks and opportunities on climate change, water security, and deforestation. Since 2020, we have actively targeted companies that are not meeting CDP's carbon data disclosure requirements along the lines recommended by TCFD.

As part of CDP's 2021 Non-Disclosure Campaign, we participated in 1300+ collaborative engagements, 100+ of which were led by AQR on behalf of a broader investor signatory group, targeting portfolio companies which did not meet disclosure requirements.

We are pleased to share that CDP has recognized AQR as a particularly effective engagement lead in terms of influencing subsequent portfolio company disclosure.

Their recently published [Annual Report](#) features AQR's efforts and broader engagement program.

### Excerpt from CDP 2021 Annual Report:

“ Consistent with the core principles of the UN PRI, AQR firmly believes that responsible investors should not only consider ESG issues in the investment process, but also engage with portfolio companies on such issues. A central tenet of our engagement program is transparency: we believe that greater transparency is beneficial for all market participants, leading to better alignment between companies and their investor base and more accurate pricing of ESG risks and opportunities. This, along with our continued focus on climate-aware investment innovation and ongoing research on climate risk, were key factors in our decision to become a signatory to the CDP.

In 2021, we led engagements with numerous companies not meeting disclosure expectations on behalf of the CDP and an investor signatory group. In addition to helping the broader investment community, we believe this effort also benefits our clients by strengthening the feedback loop between our engagement program and our investment selection process. By successfully encouraging companies to disclose their carbon-related data, we are not only improving the transparency they provide, but also enhancing both the breadth and the quality of data inputs we use in our own sustainable, climate-aware portfolios.

”

### AQR Capital Management

In addition to our CDP-related engagements, AQR also directly engaged with 38 companies which we identified as being heavy fossil-fuel emitters. Our key objectives were to determine what steps these companies planned to take to decarbonize as well as review the quality of their commitments. For example, we requested that each company provide sufficient reporting to the public so that shareholders like AQR can actively monitor their progress against these commitments.

## Collaborative Engagement and Industry Initiatives

We strive to advance our industry's collective ESG effort, and continuously look for opportunities to engage with other members of the investment community. AQR plays a sustainability-related role in numerous organizations focused on legislative and standard-setting initiatives.

As an overview of our contributions in this area during 2021, AQR:

Became a member of the Institutional Investors Group on Climate Change (IIGCC) and joined their Derivatives Working Group.

Became a founding member of MIT Sloan's Aggregate Confusion Project, established to improve ESG data.

Completed collaborative engagement with the New Zealand Superannuation Fund and 50+ other institutional investors, targeting social media companies to strengthen controls against the livestreaming/distribution of content containing terrorism or extreme violence.

Served on the MFA ESG Working Group, AIMA Responsible Investment Committee, UN PRI Hedge Fund Advisory Committee, and CFA UK Climate Change Disclosure and Reporting Working Group.

Additionally, AQR has been a regular participant in Fintech Innovation Lab, an annual program run by the Partnership Fund for New York City and Accenture that helps early- to growth-stage companies who are redefining the fintech industry grow their business with support from the world's top financial service firms. One of the companies we advised in 2021 was Util, a sustainability data provider differentiated by the use of natural language processing to quantify tens of thousands of listed companies' effects on the United Nations Sustainable Development Goals. Our interactions included idea-sharing on how such data can be used for building investment portfolios, as well as helping to refine reporting on SDG exposures. The process was informative for our own views on SDG data and brought us new perspectives on ESG reporting.

## Proxy Voting

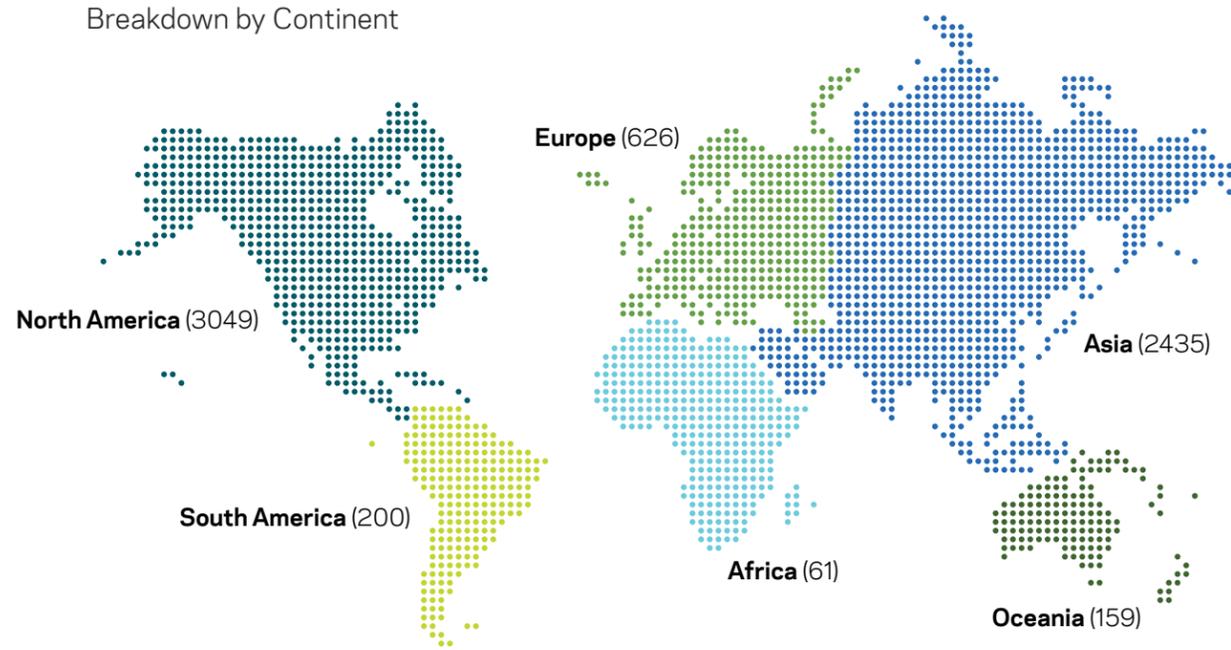
Finally, no stewardship program is complete without an understanding of how we vote our proxies. Since 2003, AQR has been using Institutional Shareholders Services for ISS, an independent third-party advisor, for a variety of proxy voting services. In 2021, we also partnered with Glass Lewis to further enhance our proxy-related research capabilities.

Our portfolios tend to be highly diversified, often entailing many small positions across a wide range of companies and industries. For our AQR-sponsored funds, we vote using a Sustainable policy and incorporate internal proprietary research to make informed decisions on individual votes.

The following statistics provide a broad overview of AQR's proxy voting activities during 2021.

<b>6,530</b>	Meetings Voted
<b>63,634</b>	Proposals Voted
<b>90%</b>	of Total Votes With Company Management
<b>10%</b>	of Total Votes Against Company Management
<b>62%</b>	of Shareholder Proposals Supported in our AQR-sponsored Funds

2021 Meetings Voted  
Breakdown by Continent



Source: AQR, ISS. AQR seeks to cast votes for all of its portfolio companies, with the exception of those that are domiciled in markets where there are beneficial ownership disclosure and/or Power of Attorney requirements. Diversification does not eliminate the risk of experiencing investment losses.

## Applied Research and Conferences

AQR frequently participates in academic and practitioner dialogue regarding ESG. We seek to understand the broader implications and challenges stemming from ESG issues to help our clients navigate them too, and we feel our thought leadership distinguishes us in the space. Many colleagues publish ESG-related papers that can be found at [AQR.com/ESG](https://www.aqr.com/ESG).

In 2021, AQR employees authored or co-authored several notable publications that contribute to the academic and industry literature on ESG, with a particular focus on climate:

### [Investment and Pensions Europe: Viewpoint: To Kick or Not Kick the Proverbial Can Down the Road](#)

*Investment & Pensions Europe*

In an op-ed published in Investment & Pensions Europe, we review the practical difficulty of achieving a “Net Zero” investment commitment. We demonstrate that the incorporation of shorting can facilitate the creation of net zero, or even net negative, carbon exposure portfolios.

### [Can Machine Learning Help Manage Climate Risks?](#)

*AQR Q4 2021 Alternative Thinking*

As climate change is becoming an increasingly observed phenomenon and understood to be caused by carbon and carbon-equivalent emissions, investors are adjusting their portfolios to prepare for a future regime shift to a lower-carbon economy. The primary approach taken to prepare for this change is to incorporate carbon emissions in investment selection. However, albeit a practical approach, carbon emissions can be a narrow measure of overall climate risk.

In this article we explore the insights of Engle, Giglio, Kelly, Lee, and Stroebe in “Hedging Climate Change News”, 2020, where they use textual analysis and machine learning techniques to create a broad climate hedging portfolio based on stocks’ sensitivity to climate news. We find that, subject to further research, these insights could be used as a complement to carbon-aware investing in defending against climate change.

### [Sustainable Systematic Credit](#)

*AQR White Paper*

Interest in sustainable investing has exploded in recent years, initially focused on public equity markets, but now evolving into fixed income. We assess various aspects of sustainable investing for public corporate bond markets (both Investment Grade and High Yield).

Using a representative set of sustainability measures spanning environment, societal and governance (ESG) constructs we find: (i) credit spreads are only marginally associated with ESG measures, (ii) ESG measures are only marginally associated with standard return forecasting measures for corporate bonds, and (iii) ESG measures are not reliably associated with future credit excess returns.

# Corporate Sustainability Initiatives

AQR has several initiatives to help promote sustainability and social responsibility within our operations and with respect to our community interactions.

## ESG in the Office

We strive to create a more sustainable workplace through education, conservation, and innovation. AQR's ESG in the Office Committee began as an employee-originated initiative in 2017, bringing together colleagues from across the firm to enhance the management of ESG in our own business practices. The group has implemented several notable projects, ranging from reducing the consumption of single-use non-recyclable material, organizing environmental volunteer projects for employees, to reducing our carbon footprint and offsetting what we cannot eliminate with Renewable Energy Credits and other carbon offsets. Over the past year, this included initiating a large-scale transition of our physical data centers to the cloud, which is estimated to be 3.6x more energy efficient than on-premise.

As of 2021, AQR is a CarbonNeutral® certified company through Natural Capital Partners,<sup>13</sup> a third-party climate specialist. Our carbon neutral commitment spans all offices globally and includes homeworker and business travel related emissions.

Our ESG in the Office Committee led a number of other initiatives during 2021. These ranged from soliciting information from third-party vendors to minimize ESG-related risks in our supply chain, to holding volunteer events for our London and US offices. These included US colleagues participating in Keep America Beautiful's third annual TrashDash, a "plogging" activity where volunteers picked up litter while

jogging and in London, volunteering with The Conservation Volunteers, to build new hedges and create more green corridors within North London. The ESG-related volunteering program will continue to expand in 2022, partnering with new organizations, such as the Billion Oyster Project, a marine restoration project based in the New York Harbor.

## Culture and People

Our people are our most valuable asset. We strive to give our employees an exceptional experience driven by intellectual curiosity, constant improvement, and collaboration. Our approach to fostering a diverse and inclusive environment where all employees have a true sense of belonging is multi-faceted across recruiting strategies, community-building activities, leadership development programs, policies and training. We also invest significantly in our employees' careers as well as leadership and personal development.

We have implemented numerous diversity initiatives and events over recent years. AQR's Diversity & Inclusion governance committee, comprised of senior leaders across the firm to further drive focus and progress, led a "Pride Month Pronoun Initiative" in 2021 to raise awareness and invite employees to voluntarily share their personal pronouns in our internal systems. We have highly engaged employee-led networks such as AQR WIN (our women's network) and AQR Pride (our LGBTQ and allies' network) that continued to hold virtual connectivity events throughout the year.

<sup>13</sup> CarbonNeutral® certification is issued by Natural Capital Partners and is based on a protocol updated annually to reflect developments in climate science, international policy, standards and business practice. View the latest protocol [here](#).

While the direct investment impact of sustainability may be unclear/modest, there is still considerable interest from asset owners to ensure credit allocations are sustainable. We find that it is possible to incorporate (i) both static and dynamic exclusion screens, (ii) positive tilts toward more sustainable issuers, and (iii) economically meaningful reduction in carbon intensity, with minimal portfolio distortions. Thus, a well-implemented systematic approach has the potential to offer attractive risk-adjusted returns in a sustainable manner.

## Shorting Your Way to a Greener Tomorrow

*Cliff's Perspective*

In this piece, Cliff explains why, in calculating a portfolio's ESG score, it is critical that shorts are properly accounted for so that investors can use shorting to reduce carbon exposure, to get to net zero, or to achieve other ESG goals.

Additionally, in 2021, AQR colleagues presented at over 20 ESG-related industry engagements and conferences. A few highlights include:

- UN PRI Academic Week and UN PRI Digital Conference
- AIMA webinars on Putting ESG Into Practice and ESG North American Trends
- JP Morgan Capital Advisory Hedge Fund ESG Forum

Furthermore, in 2021, the AQR Asset Management Institute at London Business School hosted its seventh annual Insight Summit covering the tectonic shift in global finance currently underway, ESG investing, decentralized finance, and climate financial risks. The conference attracted an audience of over 600 attendees. Speakers included leading scholars working on ESG in academia, for example Robert Engle (2003 Nobel Prize Winner in Economics). AQR's Head of ESG Research also presented at the conference, on ESG in Alternatives.

## Awards and Recognition



AQR was named one of the “Best Places to Work in Money Management” by Pensions & Investments for the fifth year in a row and ranked first in our category in 2021, a recognition that is largely driven by anonymous employee feedback.<sup>14</sup> Each year, through this survey, we consistently hear the following things from our employees about what makes AQR a special place to work - the academic culture, learning opportunities, our focus on employee well-being and benefits, and a strong sense of community.



AQR received a perfect score in the Human Rights Campaign’s Corporate Equality Index (CEI) for the fourth year in a row, again making the firm one of the “Best Places to Work for LGBTQ Equality.”<sup>15</sup> Measuring LGBTQ workplace equality, the CEI is a national benchmarking survey administered by the Human Rights Campaign, the largest national LGBTQ civil rights organization. A score of 100 on the survey requires comprehensive benefits, policies, training, education, community involvement and senior sponsorship.

<sup>14</sup> For five years in a row, AQR was named one of Pensions and Investments’ Best Places to Work in Money Management in 2017, 2018, 2019, 2020, and 2021

<sup>15</sup> The Human Rights Campaign named AQR a 2019, 2020, 2021, and 2022 Best Place to Work for LGBTQ Equality

## Community Partnerships and Philanthropy

AQR’s community partnerships and philanthropic initiatives are centered around five priority areas: Crisis Response, Diversity, Education, Environment and Health. AQR is committed to becoming part of the support system that provides the foundation of early engagement, education, and mentorship to increase college and job readiness for underserved people of color in the communities in which we work.

We have identified local community partners in North America, Europe, and Asia who are creative and innovative in their approaches and where our engagement can help catalyze their efforts.

In 2021, we continued our partnership with BLK Capital Management through Diversity Recruiting efforts and with Norwalk Grassroots Tennis and Education to promote academic and athletic opportunities to underserved communities. In Europe, we partnered with IntoUniversity, which supports young people from disadvantaged backgrounds across the UK to attain either a university place or another chosen aspiration. In India, we partnered with the Agaram Foundation for a long-term commitment to sponsor a number of students, who are first generation college attendees.

We remain focused on programs that provide exposure to the financial services industry, access to role models, and educational support to help expand the pipeline of underrepresented talent entering university programs.

On environmental causes, we partnered with several charities including the Clean Air Task Force, Billion Oyster Project, and The Conservation Volunteers to provide financial and volunteer support.

## Employee Network Partnerships



We partnered with AQR’s Pride Network and Women’s Initiative Network on philanthropic efforts throughout 2021. For PRIDE, we supported the Ali Forney Center—a youth center in New York City to help support LGBTQ+ youth. With the Women’s Initiative Network, we supported Girls Who Code. In 2021, we partnered with City Harvest, a food rescue network based in New York City, on a continuing basis. In response to the Winter Storm in Texas, we supported six food banks throughout the state. We supported Cooperative for Assistance and Relief Everywhere (CARE) for the Afghan refugee crisis and Partners in Health for the earthquake in Haiti of August 2021. Finally, we donated to the Chief Minister Relief Fund to support India in its COVID-19 relief efforts.

# Looking Ahead

AQR continued to expand and refine its responsible investing solutions in 2021, translating our active internal research agenda into enhancements to our ESG signals, risk models, and portfolio solutions. We expect 2022 to be similarly active, and we anticipate further expanding our research efforts in multi-asset and macro portfolios. We are also working on a number of new climate-related whitepapers to further advance the industry dialogue, which we look forward to sharing on our [ESG webpage](#).

We will continue to develop the proxy and engagement programs that moved meaningfully forward in 2021. This will include further refining our proxy voting approach, improving the breadth, depth, and impact of our engagements with portfolio companies, and continuing to participate in systematic investor-led industry initiatives to advance the collective ESG effort. Our aim is to partner with other

like-minded investors in order bring greater strength to our engagement programs. If you are an investor that would like to partner on a specific corporate engagement, please reach out to us at [ESGengagement@aqr.com](mailto:ESGengagement@aqr.com).

Finally, we plan to strengthen our position as a business committed to corporate social responsibility. For example, we will continue to organize volunteering events to increase ESG engagement in the community and promote ESG education internally through a variety of mediums, including a speaker series. We are also working on further reducing our emissions, for example by encouraging the use of greener modes of transport by our employees. We believe that having a diverse, inclusive, and engaged workforce is key to a successful long-term company that continues adding value to its clients.



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The hypothetical performance results contained herein represent the application of the quantitative models as currently in effect on the date first written above and there can be no assurance that the models will remain the same in the future or that an application of the current models in the future will produce similar results because the relevant market and economic conditions that prevailed during the hypothetical performance period will not necessarily recur. Discounting factors may be applied to reduce suspected anomalies. This backtest's return, for this period, may vary depending on the date it is run. Hypothetical performance results are presented for illustrative purposes only. In addition, our transaction cost assumptions utilized in backtests, where noted, are based on AQR Capital Management, LLC's, ("AQR")'s historical realized transaction costs and market data. Certain of the assumptions have been made for modeling purposes and are unlikely to be realized. No representation or warranty is made as to the reasonableness of the assumptions made or that all assumptions used in achieving the returns have been stated or fully considered. Changes in the assumptions may have a material impact on the hypothetical returns presented. Actual advisory fees for products offering this strategy may vary.

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#### **Human Rights Campaign Corporate Equality Index and Best Place to Work for LGBTQ Equality**

Measuring LGBTQ+ workplace equality, the Corporate Equality Index is a national benchmarking survey administered by the Human Rights Campaign, the largest national LGBTQ+ civil rights organization. A score of 100 on the survey requires comprehensive benefits, policies, training, education, community involvement and senior sponsorship.

#### **Pensions & Investments' Best Places to Work**

Pensions & Investments Best Places to Work is based on a questionnaire about the firm's policies, practices, benefits and demographics, as well as an engagement and satisfaction survey of employees. AQR was recognized for the priority it places on the well-being of employees, its efforts to foster connectivity with colleagues even while working remotely, its plans to adopt a hybrid work model and the effort made to support employees' work-life balance.

#### **European Pensions Awards 2021**

The European Pensions Awards recognize and to and honor the investment firms, consultancies and pension providers across Europe that have set the professional standards in order to best serve European pension funds over the past year. The "ESG/SRI Provider of the Year" award recognizes the leaders in this significant and increasingly sophisticated market.

Diversification does not eliminate the risk of experiencing investment losses.

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