

Social media not necessarily socially responsible

● WHAT IS AN ESG CONTROVERSY?

From time to time, a company may become involved in an “ESG controversy”—an event that occurs when a company’s activity produces an unintended, negative environmental, social, or governance (ESG)-related effect.

Identifying and responding to these controversies can be critical to a portfolio’s success. CANDRIAM, a pioneer in ESG and sustainable investing since 1996, uses a proprietary framework to understand ESG risks and identify companies that they believe are managing their ESG risks relative to industry peers, and thus positioned to benefit in the future.

In the following case study, we look at CANDRIAM’s ability to allay recent controversies by excluding Facebook from the IQ CANDRIAM ESG US Equity ETF Index, which serves as the benchmark for the passively managed IQ CANDRIAM ESG US Equity ETF (IQSU).

● CASE STUDY: FACEBOOK

Facebook’s business model drives its appetite for user data: the company derives almost all its revenue from selling advertising placements and modeling users’ behavior to marketers. Due to the nature of the business and revenue model, CANDRIAM believes the company is not in a position to protect the privacy of its many users. Facebook’s involvement in numerous controversies related to its business practices suggests a pattern of ethical lapses that we believe will lead to more controversies in the future and an increased regulatory risk.

● PREVIOUS DATA PRIVACY AND SECURITY INCIDENTS

Facebook has had frequent privacy-related investigations and lawsuits as well as data breaches. These include allegations that the company was mining data and selling it to advertisers. It has also been accused of sharing information with third parties without informed-user consent.

MAJOR DATA PRIVACY SCANDALS INCLUDE:



Cambridge Analytica (CA), 2018: Facebook data of 87 million users was illegally used by third parties (Cambridge Analytica), which was used to influence the U.S. Presidential Elections.



High scrutiny regarding fake and unwanted news, 2017. More recently, Germany has proposed fines of up to €50 million for social networking sites like Facebook for not swiftly removing illegal content or defamatory fake news.



Facebook's decision to exempt campaign advertising from fact checking, 2019. The rise of "deepfakes" linked to political figures could also exacerbate reputational controversy.

● A WEAK GOVERNANCE STRUCTURE

Facebook has a dual-share class, with CEO & Chairman Mark Zuckerberg controlling approximately 65% of the voting rights. This structure gives Mr. Zuckerberg ten votes per share on his Class B holdings, while Class A shareholders, the majority of shareholders, have one vote per share. In fact, Mark Zuckerberg exerts complete control over the company because his majority voting power extends to the election of directors and other items requiring shareholder approval.

● CANDRIAM'S RESPONSE TO FACEBOOK CONTROVERSY

Facebook has been flagged as a high-risk company from an ESG standpoint by our proprietary ESG model since 2015. Our analysts believe that its monetization model, management of users' private data, and global scale put it at risk of regular controversies and scrutiny from regulators.

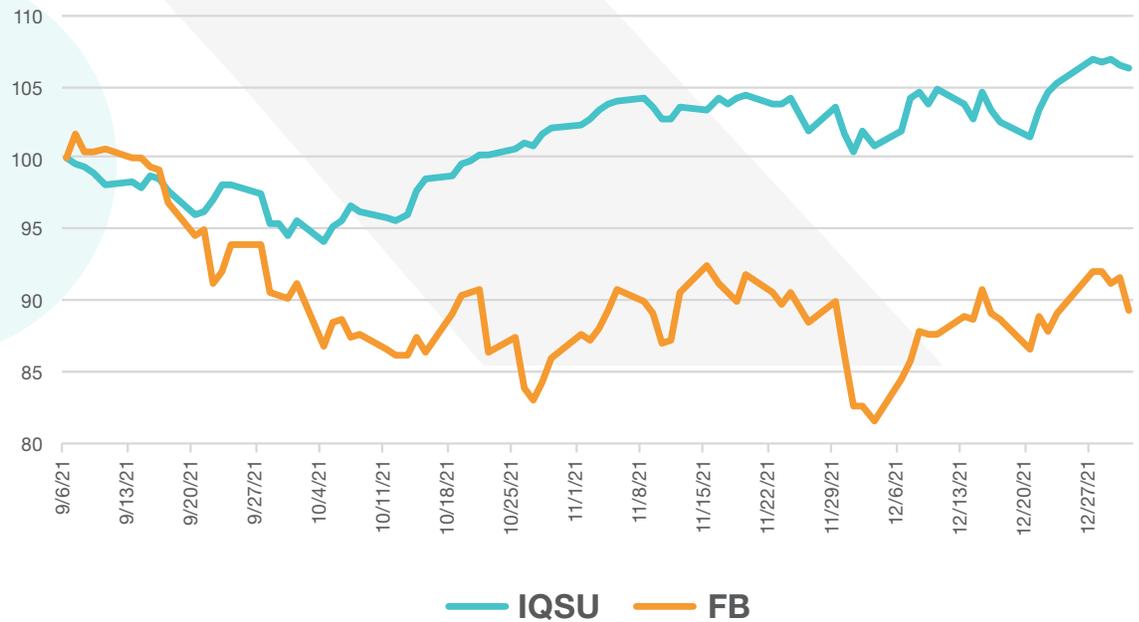
The company's recent involvement in user-privacy controversies reinforces CANDRIAM's conviction that Facebook's practices are incompatible with the ESG standards and practices that it expects from companies in the social media sector. This is due both to the company's business model, which exposes it to financially material, regulatory and reputational risks, and the weakness of its corporate governance structure.

● IMPACT

Since Facebook’s stock price peaked at \$384.33 in September 2021, it is down significantly through the end of 2021 and has been dropped from several ESG indices and index funds. The chart below illustrates the performance of IQ CANDRIAM ESG US Equity ETF (IQSU), along with Facebook’s stock price from the recent whistleblower controversy, through the end of 2021.

GROWTH OF \$100 INVESTED IN IQSU AND FACEBOOK

9/6/21 through 12/31/21



Source: Morningstar (9/6/21 through 12/31/21); [Click here for the most current IQSU fund page](#), which includes the prospectus, investment objectives, performance, risk, and other important information. Returns represent past performance, which is no guarantee of future results. Current performance may be lower or higher. Investment return and principal value will fluctuate, and shares, when redeemed, may be worth more or less than their original cost. Visit nylinvestments.com/funds and for the most recent month-end performance. Performance data quoted represents past performance. Past performance is no guarantee of future results.

The Facebook example above is shown for illustrative purposes only to provide an example of CANDRIAM’S ESG process. The chart includes the past performance of Facebook and the past performance of IQSU to illustrate that Facebook wasn’t held in the portfolio during the listed time period. No comparison should be made between the performance for Facebook and IQSU, which has fees and expenses and multiple holdings that could have helped or hurt performance. IQSU should never be sold based on an individual security.

● **IDENTIFYING ESG CONTROVERSIES**

Standards for corporate sustainability are generally set by the United Nation's Global Compact Principles, which focus on:



Supporting and respecting human rights



Promoting greater environmental responsibility



Eliminating forced labor, child labor, and discrimination in employment



Opposing corruption in all forms, including extortion and bribery

ESG controversies arise when a company fails to comply with these principles. In addition to reputational damage, controversies can result in costly product recalls, financial penalties, and remediation. A tarnished reputation can hurt sales: A study of 141 serious ESG incidents found that 49% resulted in slower revenue growth, and 24% produced a revenue decline¹.

● **CANDRIAM'S PROPRIETARY APPROACH TO ESG CONTROVERSIES**

While third-party ratings providers such as MSCI and Sustainalytics investigate ESG controversies, CANDRIAM conducts assessments of its own, applying "norms-based analysis²" to determine whether a company's operations, governance practices, or products and services violate national or international laws, regulations, or other commonly accepted global norms.

1. Source: MSCI Research - Have corporate controversies influenced consumer behavior?

2. Norms-based analysis: The purpose of the norms-based analysis is to determine whether a company complies with the universal principles set forth in the United Nations Global Compact (UNGC).

Any company, which voluntarily complies with the UNGC, undertakes to respect human rights, apply labor law standards, protect the environment, and combat corruption. This additional analysis makes sure the companies comply with the principal international treaties and conventions.

About risk

IQSU: Before considering an investment in the Fund, you should understand that you could lose money.

As with all investments, there are certain risks of investing in the Fund. The Fund's Shares will change in value, and you could lose money by investing in the Fund.

The Fund is a new fund. As a new fund, there can be no assurance that it will grow to or maintain an economically viable size, in which case it may experience greater tracking error to its Underlying Index, or it could ultimately liquidate.

The Fund employs a "passive management" investment approach designed to track the performance of the Underlying Index. There is no guarantee that the Fund's investment results will have a high degree of correlation to those of the Underlying Index, or that the Fund will achieve its investment objective.

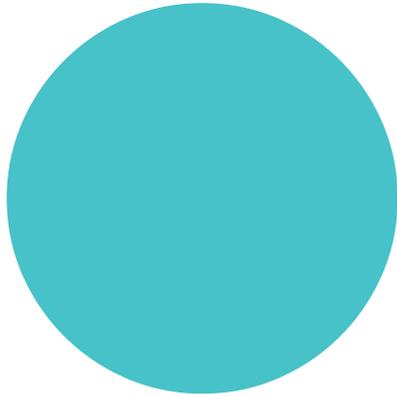
The Underlying Index seeks to provide exposure to the equity securities of companies meeting environmental, social, and corporate governance investing criteria, and the Fund may forego some market opportunities available to funds that do not use these criteria. The application of environmental, social, and corporate governance investing may impact the Fund's relative investment performance. There is no guarantee that the construction methodology of the Underlying Index will accurately provide exposure to issuers meeting environmental, social, and corporate governance criteria.

Small- and mid-capitalization companies may be more vulnerable to adverse general market or economic developments, and their securities may be less liquid and may experience greater price volatility than larger, more established companies.

ESG Investing Style Risk: Impact investing and/or Environmental, Social, and Governance (ESG) managers may take into consideration factors beyond traditional financial information to select securities, which could result in relative investment performance deviating from other strategies or broad market benchmarks, depending on whether such sectors or investments are in or out of favor in the market. Further, ESG strategies may rely on certain values-based criteria to eliminate exposures found in similar strategies or broad market benchmarks, which could also result in relative investment performance deviating.

Consider the Fund's investment objectives, risks, charges and expenses carefully before investing. The prospectus and the statement of additional information include this and other relevant information about the Fund and are available by visiting nylinvestments.com/etfs or calling 888-474-7725. Read the prospectus carefully before investing.

The Underlying Index was developed by IndexIQ LLC with CANDRIAM Belgium S.A. acting as index consultant. New York Life Investment Management LLC engages the services of CANDRIAM Belgium S.A. ("CANDRIAM"), a registered investment advisor, as subadvisor to the Fund. CANDRIAM is an affiliate of New York Life Investment Management LLC.



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Fund shares are not individually redeemable and will be issued and redeemed at their NAV only through certain authorized broker-dealers in large, specified blocks of shares called “creation units”, and otherwise, can be bought and sold only through exchange trading. Creation units are issued and redeemed principally in-kind.



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