WEBINAR

ESG: A Practical Guide for IR Practitioners

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niri

Speakers

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Environmental, Social, Governance Defined

ESG is not to be confused with SUSTAINABILITY!

"ESG is the systematic integration of non-financial factors into the investment process."

Sustainable investing is a long-term approach to investing that incorporates ESG **considerations** into the investment process. ESG refers to environmental, social, and governance issues that **sustainable** investors, and increasingly, traditional investors, consider when making **investment decisions**.

E: looks at how company performs as steward of natural environment

S: examines how company manages relationships; supply chain risk; labor

G: deals with company's leadership, executive pay, audits and internal controls, shareholder rights

Related definitions[1]

- Socially Responsible Investing (SRI) (from 1920's)
  - Rooted in religious values; first SRI fund launched in 1928 (Pioneer Fund) focused on exclusionary screens based on social issues
- Responsible Investing (RI) (1930's)
  - Differing views resulted in dropping "S" from SRI
- Sustainable Investing (SI) (1990's)
  - Ecological word 'sustainability' was introduced in the 1990s
- ESG Investing (2000's)
  - UK Pensions Act amended in 2000 to require consideration of ESG issues during the investment process; 2006 UNPRI launched

[1] *https://www.ssga.com/investment-topics/environmental-social-governance/2017/understanding-and-comparing-ESG-terminology.pdf*

SSGA Framework for Understanding and Comparing ESG Strategies[1]

- Exclusionary (or avoidance) screening
- Positive screening
- ESG integration
- Impact investing
- Active ownership

[1] https://www.ssga.com/investment-topics/environmental-social-governance/2017/understanding-and-comparing-ESG-terminology.pdf

SRI / RI / SI / ESG Investing

- What is it?
  - A set of standards for a company’s operations that socially conscious investors use to screen investments
  - Investors purchasing securities that have been screened for ESG criteria
  - Avoidance screening (out) on the rise

- Why is this important to investors? Why is it important to companies?
  - Pre-2015
    - International demand on the rise
    - In U.S.: Gadflys (Chevedden), Activists (social or other)
  - Post-2015
    - Significant increase in international demand; some regulatory statutes
    - Sharp increase in past 12-18 months in U.S.
    - Morgan Stanley Sustainable Investing website
    - Blackrock annual CEO letter
    - State Street Letter to its Board of Directors
    - CALPERS, Neuberger Berman, Wellington Management

ESG: Business case, timing, bottom line

- The business case
  - Seen to **minimize risk**, while enhancing **sustainability**
  - Investor demand
  - Supplier demand
  - Customer demand

- Why now?
  - Risk reduction
  - Millennials AND Boomers asking for more socially conscious investments
  - With shift to passive investing, ”active” asset managers need to differentiate themselves

- Bottom line
  - “Hockey stick” shift in demand / perception in past 12-18 months
  - Lack of infrastructure = scrambling to address requests
  - Not a fad, companies should create proper frameworks to address concerns, drive performance and minimize risk

ESG: Do Boards and C-Suites Need ESP to Figure Out What Investors Want?

- ESG concerns are on the rise. Investors are laser-focused on Sustainability and Investing for the Long-term.
- ESG-related advocacy issues include board diversity; board composition, including a matrix approach; executive compensation tied to long-term strategies; low carbon business models and package recycling; climate risk reporting; clawback policies; the risk of material loss; human capital management; among other issues.
- Are investors using any Guidelines or Standards, or just targeting companies for E, S or G issues?

Guidelines for Investors- ICGN

ICGN adopted its Global Governance Principles in 2017, which include:

- Principle 1: Board role and responsibilities
- Guidance
- 1.1 Responsibilities
- The board is accountable to shareholders and relevant stakeholders and responsible for preserving and enhancing sustainable value over the long-term. In fulfilling their role effectively, board members should:

  a) guide, review and approve the company’s mission and purpose, its corporate strategy and financial planning, including major capital expenditures, acquisitions and divestments;

  b) monitor the effectiveness of the company’s governance, environmental policies, and social practices, and adhere to applicable laws;

Guidelines for Investors- ICGN (continued)

- Principle 4: Corporate culture
- The board should adopt high standards of business ethics, ensuring that its vision, mission and objectives are sound and demonstrative of its values. Codes of ethical conduct should be effectively communicated and integrated into the company's strategy and operations, including risk management systems and remuneration structures. (Emphasis added.)
- Principle 5: Risk oversight
- The board should proactively oversee, review and approve the approach to risk management regularly or with any significant business change and satisfy itself that the approach is functioning effectively.
- …
- Principle 7: Reporting and audit
- Boards should oversee timely and high quality company disclosures for investors and other stakeholders relating to financial statements, strategic and operational performance, corporate governance and material environmental and social factors. A robust audit practice is critical for necessary quality standards. (Emphasis added.)[1]

[1] ICGN Global Governance Principles 2017. 5th Edition

Guidelines for Investors-CII

- The Council of Institutional Investors (CII) adopted its policy in September 2017 to include information on a Board's role for Risk Oversight-
- 2.7 Board's Role in Risk Oversight: The board has ultimate responsibility for risk oversight…Effective risk oversight requires regular, meaningful communication between the board and management, among board members and committees, and between the board and any outside advisers it consults, about the company's material risks and risk management processes. The board should disclose to shareowners, at least annually, sufficient information to enable them to assess whether the board is carrying out its oversight responsibilities effectively.
- CII Corporate Governance Policies Updated September 15, 2017 https://www.cii.org/files/policies/09_15_17_corp_gov_policies.pdf

Guidelines for Investors-SASB

- Sustainability Accounting Standards Board (SASB), established in 2011 as an independent, private-sector standards setting organization. SASB develops and maintains sustainability accounting standards—for 79 industries in 11 sectors—that help public corporations disclose financially material information to investors in a cost-effective and decision-useful format. The SASB's transparent, inclusive, and rigorous standards-setting process is materiality focused, evidence-based and market informed.

- SASB https://www.sasb.org/

ESG Takeaways:

- A “One Size Fits All” approach will not appease Investors. *Don’t do it.*
- Policies from organizations like ICGN, CII and SASB, among others, provide roadmaps for Boards and Management. *Check them out.*
- Investors want clarity: Employees and Investors should know where the Company stands on ESG issues. *No ESP needed.*
- Investors appreciate transparency- Reports must be substantive. *Fluff will be noted.*
- The Buck Stops With The Board- Role to set the course for long-term strategies. Investors will be engaging the Board members. *Help them be prepared.*

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Thursday, May 17, 2018
2:00 pm ET

Questions 

Submit your questions in the Q&A chat window

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