

ESG reporting for investors

Created by Tara Deronzier and Edgar Lugo-Vasquez



“It’s not just 5 per cent of your money you give away that matters. What you do with the other 95 per cent is almost more important.”

Darren Walker
President of the Ford Foundation

ESG a framework on the rise

The practice of ESG investing began in the 1960s. ESG investing evolved from socially responsible investing (SRI), which excluded stocks or entire industries from investments related to business operations such as tobacco, guns, or products from conflicted regions.

Now, ESG is rapidly growing and evolving, as many investors look to incorporate ESG factors into the investment process. Also, international regulations ask investors to comply with new legislation on integrating ESG portfolios and mandatory reporting.

The ESG framework is shaping investment and is fast becoming an integrated norm. To help investors, financial institutions, and companies understand better the underlying criteria and implementing them, we designed a data-based document on ESG factors.

/ Environmental • Social • Governance /

ESG

ESG is the umbrella term for the components of sustainable and responsible finance. It is a framework considering Environmental, Social and Governance factors, alongside financial factors in the investment decision-making process¹.

¹ Harvard Business Review (2018) 25 years ago, I coined the phrase triple bottom line, John Elkington

The regulations

ESG are on the rise, pushed by new regulations and legislations in the EU.

The European Union SFDR

(Sustainable Finance Disclosure Regulation) entered into force on March 11th, 2021. It imposes mandatory ESG disclosure obligations for asset managers and other financial markets participants with substantive provisions.

Stress testing rules for banks

The EU commission is developing tools and mechanisms to integrate ESG factors into banking system, investments policies and risk management process-

The EU Sustainable Finance Action Plan

A major policy objective by the European Union which focuses on promoting sustainable investment across the continent. Parts of it will become effective from March 2021. The aim is to reorient capital flows towards sustainable investment and away from sectors contributing to climate change such as fossil fuels.

Taskforce on Climate-Related Disclosures (TCFD)

Guidelines for voluntary climate-centred financial disclosures across industries, in the UK.

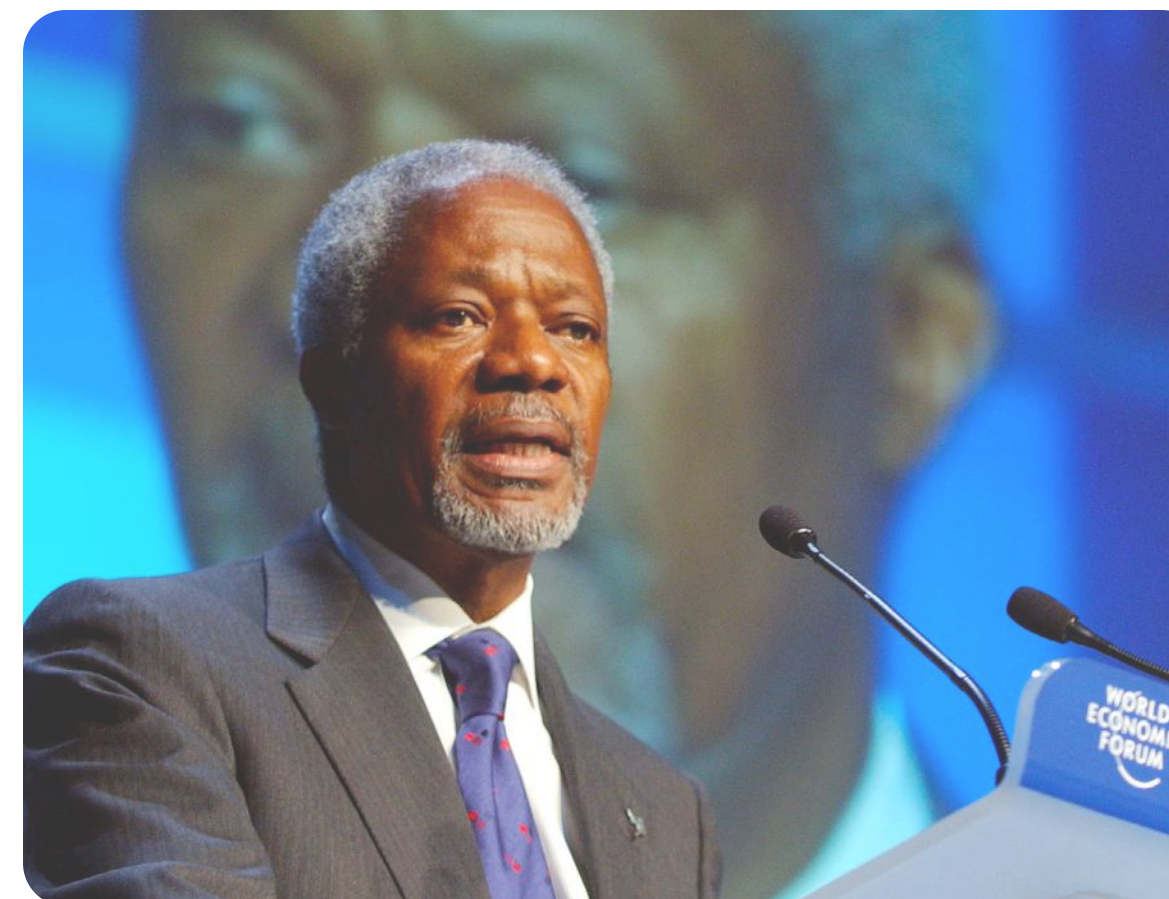
What are the benefits?

Companies performing on ESG practices

- initial growth and optimization
- lower volatility
- employee productivity
- reduced regulatory and legal interventions (fines and sanctions)
- top-line growth
- cost reduction².

Companies with poor ESG were associated with

- higher cost of capital
- Higher volatility due to controversies and other incidences such as labor strikes, frauds and other governance irregularities.³



Kofi Anna, former UN Secretary-General, United Nations, New York, delivers a speech during the session 'The Future of Global Interdependence' at the Annual Meeting 2004 of the World Economic Forum in Davos, Switzerland, January 23, 2004. Photo by Remy Steinegger

ESG was coined in 2004, by former UN Secretary-General **Kofi Annan**, and resulting in 2005 with the first study "Who cares Wins" developed jointly with the world's largest institutional investors.

² Mc Kinsey Quaterly (2019) *5 ways that ESG create value*

³ MSCI (2020), *Deconstructing ESG Ratings Performance: Risk and Return for E, S And G* by Time Horizon, Sector and Weighting

Why is ESG important?

€75Tn

Investment is needed by 2030 to meet the goal of limiting the global temperature increase to 1.5°C⁴.

€25Tn

Global sustainable investment assets in 2018, representing an increase of 34% in two years⁵.

63%

Of sustainable funds performed in the top half of their respective categories in 2018⁶.

€100Bn

Poured into sustainable investment options by European investors across 2019⁷.

17%

Annual growth of integration of ESG factors into financial analysis⁸.

49%

Proportion of sustainable investing in Europe relative to total managed assets⁹.

173%

Forecast growth of the UK socially responsible investing market by 2027¹⁰

2x

The ESG investment market is set to double in 2021¹¹.

⁴ KPMG report (2019), *The numbers that are changing the world*.

⁵ Bloomberg (2019), *Global sustainable investments rise 34% to \$30.7 trillion*, Emily Chasan.

⁶ John Hale (2020) *ESG funds outperformed conventional funds in 2019*, Morningstar.

⁷ Morningstar (2020), *Record-Shattering Year for Sustainable Investments*.

⁸ OECD (2020), *OECD Business and Finance Outlook 2020 : Sustainable and Resilient Finance*

⁹ Global Sustainable Investment Alliance (2018), *Global Sustainable Investment Review 2018*.

¹⁰ UK Investor Magazine (2018), *Socially Responsible Investing market worth £48 billion by 2027*, Dina Caruso.

¹¹ Institutional Asset Manager (2021), *ESG Investment market set to double in 2021*.



E

plan A

Environmental

How a company performs as a steward of nature. It analyses how its activities impact the environment and manage environmental risks. It includes both direct operations and across supply chain.

Environmental factors include:

- Climate change
- Waste and pollution
- Resource scarcity and management (including water)
- Natural resources preservation
- Animal treatment
- GHG emissions

Focus on

3M, which saved \$2.2 billion since the 1975 launch of its “pollution prevention pays” (3Ps) program, which involves reformulating products, improving manufacturing processes, redesigning equipment, and recycling and reusing waste from production. 3M scores AAA on the MSCI ESG Rating Index.¹²

“I think it is the kind of question that deserves lots of attention ... we do have one planet and we ought to pay a lot of attention to what’s going on.”

Warren Buffet

¹² MSCI (2021), *ESG Rating Tool*

Key Statistics

#1

Climate change and
environmental risks¹³

60%

potential improvement in operating
profits through reducing resource costs¹⁵

€19Tn

Potential cut by climate change to
World Economy in 2050¹⁴

88%

of studies found that companies that
adhered to social or environmental
standards showed better operational
performance¹⁶.

Key Objectives

- Set up common objectives, KPIs and strategy
- Disclosing your company's values/ethics to your stakeholders (investors and shareholders)
- Streamline investments with minimal regulatory and climate-related risks
- Calculate your carbon emissions, reduce your carbon footprint and aim to reach net-zero emissions
- Optimization of processes and supply chain management
- Any activities or operations shall not do harm to the environment
- No animal testing, mistreatment of animals
- Natural resources preservation

¹³ KPMG (2019) *CEOs name climate change as number one risk to organizational growth*

¹⁴ New York Times (2021), *Climate change could cost to the economy \$23 trillion*

¹⁵ McKinsey (2020), *How the E in ESG creates business value*

¹⁶ Morgan Stanley (2017) *Why sustainable companies outperform.*



S

planA

Social

Social criteria examines the strengths and weaknesses of how a company manages relationships with employees, suppliers, customers, and the communities where it operates.

Social factors include:

- Working conditions, including slavery and child labour
- Local communities, including indigenous communities
- Operating and conducting business in conflicted regions.
- Health and safety
- Employee relations and diversity
- Data Security
- Geopolitical events

Focus on

Patagonia, the outdoor clothing brand, works closely with factories to mitigate human harm and increase their living wages: 35% of their factories pay their workers a living wage, on average. Also, 82% of their line is certified Fair-Trade sewed, and more than 72,000 workers are supported by the Patagonia Fair Trade Program¹⁷.

“A company is more than an economic unit generating wealth. It fulfills human and societal aspirations as part of a broader social system. Performance must be measured not only on the return to shareholders but also on how it achieves its environmental, social and good governance objectives.”

Davos 2020 Manifesto

¹⁷ Patagonia (2021), *Our carbon footprint*.

Key Statistics

49%

Of millennial millionaires make their investments based on social factors¹⁸.

19%

Companies with higher than average diversity have 19% higher innovation revenues²⁰.

30%

Companies with more than 30 percent women executives were more likely to outperform companies¹⁹.

67%

Of millennials expect the companies they work for to be purpose-driven and their jobs to have societal impact ²¹.

Key Objectives

- Consider company's values: shared values and applied across stakeholders
- Create a positive and empowering work environment
- Build a diverse workforce (e.g gender, ethnicities)
- Implement a code of conduct and supply chain labour standards
- Empowering local communities where the company operates
- Product Liability (e.g chemical safety, health and demographic risk)
- Avoid controversial sourcing
- Social opportunities: access to communications, finance.

¹⁸ KPMG report (2019), *The numbers that are changing the world*.

¹⁹ McKinsey & Company (2020), *Diversity wins: how inclusion matters*

²⁰ Harvard Business Review (2018), *How and where diversity drives financial performance*

²¹ BCG (2020), *The future of ESG opportunities*



G

planA

Governance

Governance deals with a company's leadership, executive pay, audits, internal controls, and shareholder rights. Investors want to know if they can trust the company and what kind of decisions is going on behind closed doors.

Governance factors include:

- Executive pay
- Gender equity / Equal Pay
- Bribery and corruption
- Political lobbying and donations
- Board diversity and structure
- Tax strategy

Focus on

Atos, the global leader in the IT & Software industry classifies AAA on the MSCI Index²² for its leading corporate governance and human capital development. Its board of directors is composed of 46% females and has 80% of independent directors. The group has a zero-tolerance policy for corruption and bribery. The group is issuing yearly a transparent report on its corporate governance, accessible publicly²³.

"If people are good only because they fear punishment, and hope for reward, then we are a sorry lot indeed."

Albert Einstein

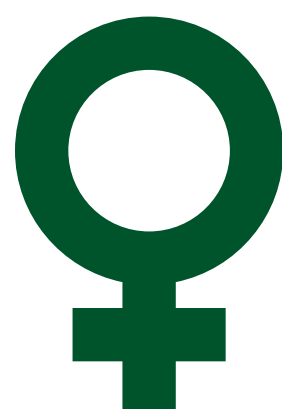
²² MSCI (2021), ESG Corporate Research Tool

²³ Atos (2021), *Corporate Governance G.2*

Key Statistics



“firms with more diverse boards (gender, race, age, tenure, and expertise) are more risk-averse ... exhibiting lower volatilities of stock returns than those with less diverse boards.”²⁴



Firms with more women on their boards of directors and in C-suite positions had greater financial performance than less diverse companies.²⁶

75%

of the investors surveyed by KPMG said they plan to ask investment teams to report their diversity efforts (up from 60% last year).²⁵

40%

Norway, Spain, France, and Iceland all have laws requiring that women comprise at least 40% of boards at publicly listed companies.²⁷

Key Objectives

- Ensure the board comprises directors with relevant ESG expertise and experience (e.g. “climate competent” and future-looking board members) to minimise/avoid the potential ESG-related risks.
- Ensure the board has a good understanding of the mandatory or voluntary ESG-related requirements of organisations.
- Include ESG as one of the criteria for selecting future candidates for the board
- Engage a third-party consultant to help enhance the board’s capabilities in ESG
- Tax transparent and zero-tolerance for corruption and bribery

²⁴ Jason Gold (2017), *Standard ESG framework is key*, S&P Global.

²⁵ KPMG Report (2019), *The call to act*.

²⁶ John Welling (2021), *Global Islamic Indices Advanced in Q1 2021, But Lagged Conventional*, S&P Global.

²⁷ Harvard Business Review (2019), *When and why diversity improves your board performance*.

Climate change is everyone's business

Discover how you can make a difference today, using Plan A to take control of your emissions.

Learn more

plana.earth

Stay informed on business and sustainability



Linkedin



Twitter



Instagram



Facebook