

INVESTMENT INSIGHTS

PERSPECTIVES ON INVESTMENT STRATEGIES

Three-quarters of global respondents to RBC's 2020 Responsible Investment Survey said they integrate environmental, social and governance (ESG) principles into their investment approach and decision-making. That number is even higher in Canada, at 89%. Guillaume Mascotto, American Century Investments' vice-president and head of ESG and investment stewardship, discusses investors' growing commitment to ESG and the evolving areas of focus in ESG analysis.

WHAT IS DRIVING INCREASED INVESTOR INTEREST IN ESG?

We see four big trends driving interest for ESG investments:

- **New business risks stemming from non-financial issues, including climate change, are appearing.** As governments around the world adapt to the Paris Agreement, increasingly toughened environmental regulations are pressing the fossil fuel industry, presenting risks from increased compliance costs to customer defection to stranded assets. If sea levels continue to rise as polar ice caps melt, this could have an impact on real estate asset valuations. Additionally, cybersecurity concerns are leading a shift in businesses' focus from "know your customer" to "protect your customer."
- **Technology is changing consumer demand patterns.** Most sectors of the

economy are seeing paradigm shifts in the way business is conducted. Companies with solid fundamentals and a willingness to adapt at the governance and strategic levels will outperform, but others are likely to put investors at risk.

- **Social media is sensitizing people to global issues in real time.** Investors are watching companies' behaviours and social licence to operate, as well as compliance oversight and organizational transparency. "Just-in-time ESG issues" are increasingly becoming part of the overall investment quality factor. The internet makes fact-checking easier, and social media enables swift condemnation.
- **Millennials are increasingly taking over from baby boomers in positions of influence, changing business, financial and political landscapes.** In today's globalized world, issues such as climate change and resource scarcity, affordable health care, and education and income inequality are becoming global issues that will reverberate in the future. When you add the factor of social and environmental consciousness, particularly strong among millennials, asset owners and managers will need to adapt to this global investment mentality shift.

YOU'VE WRITTEN THAT YOU EXPECT MORE FOCUS ON THE SOCIAL PILLAR OF ESG IN THE AFTERMATH OF THE PANDEMIC – WHY IS THAT?

As a tangible consequence of COVID-19, we think investors will increasingly pay attention to companies' social performance – particularly, issues

around human capital and business continuity. We expect more focus on emergency response mechanisms, supply chain controls and employee benefits.

WHAT ARE SOME OF THE SOCIAL INDICATORS YOU LOOK FOR WHEN EVALUATING BUSINESSES?

For emergency response mechanisms, we want to know how a company will protect business continuity if one part of the business experiences an unforeseen disaster – examples include telecommuting and distributed management programs. With supply chains, we look for ISO 9001 certification for quality management, as well as a "certified chain of custody" to ensure traceability of raw materials or outsourced manufacturing and evidence of an audit-subjected supplier code of conduct. Related to employee benefits, there is a growing focus on aligning the success of a company with the success of its employees. That translates into aligning executive and rank-and-file compensation with sustainability targets. Additionally, we evaluate a company's paid sick leave, health and well-being programs, short-time work, and telemedicine programs.

Also, when people become more digital at work or adopt practices such as telemedicine, data privacy and security risks may increase, so we also look for best-in-class ISO 27001 certification and security protocols for IT security staff mingling with other workers.

WHAT ELEMENTS DO YOU CONSIDER WHEN ASSESSING A BUSINESS'S DIVERSITY, EQUALITY AND INCLUSION (DE&I) STRATEGY?

We believe the workforce should represent a diversity of backgrounds,

experiences and thought. We also believe that companies lacking transparency or trailing their peers may see negative impacts on their long-term competitiveness, brand reputation or financial condition.

Therefore, we consider DE&I to be a sector-agnostic key issue and include it under both the social and governance pillars. Our ESG framework helps identify investment opportunities to help advance DE&I. Current long-term growth trends and improving corporate practices in emerging markets (EM) are providing various investment opportunities. Several EM companies are making positive social impacts by contributing to the U.N. Sustainable Development Goals, including Goal 5 (gender equality).

HOW DO YOU ADDRESS “GREENWASHING” AND ENSURE A BUSINESS IS BEING TRANSPARENT WITH ITS ENVIRONMENTAL CLAIMS?

We expect ESG-conscious consumers to grow increasingly impatient with companies that make misleading or false claims. Investors require clear, verifiable evidence that ESG considerations are formally integrated into a manager’s investment process. Investors will likely focus on disciplined, bottom-up ESG risk evaluation to complement impact assessments and help mitigate the potential downside risk from ESG issues. While one company may clearly meet an investor’s impact criteria from an environmental perspective, that investor should also determine whether the company aligns with the other two pillars of ESG risk assessment. Encouraging improvement through active engagement with companies is also very important.

HOW DOES AMERICAN CENTURY INVESTMENTS’ UNIQUE OWNERSHIP STRUCTURE TRANSLATE INTO OPPORTUNITIES FOR INVESTORS?

A central component of American Century Investments’ approach to investing is that investors do not need to choose between impact and returns.

Our late founder, James Stowers, Jr., and his wife, Virginia, transferred their equity ownership stake in American Century to the endowment supporting the Stowers Institute, which has resulted in more than 40% of our firm’s annual dividends being directed toward medical research. From an investment standpoint, our focus on health-care impact targets companies involved in new or innovative treatments for diseases including cancer; access to medicines and health-care services in both developed and emerging markets; new solutions that lead to lowering the cost of health care; and more productive and efficient equipment, services and software used for research, diagnostic tests and therapies.



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GUILLAUME MASCOTTO
VICE-PRESIDENT AND HEAD OF ESG
AND INVESTMENT STEWARDSHIP



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