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An Overview of Sustainable Investing

August 12, 2022

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What is Sustainable Investing (SI)?

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- Often used interchangeably with “Responsible Investing” (RI)

- UN–PRI:
  - “a strategy and practice to incorporate environmental, social and governance (ESG) factors in investment decisions and active ownership.”

- RIA Canada:
  - “the incorporation of environmental, social and governance factors (ESG) into the selection and management of investments.”

What are the UN-PRI Principles?

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- *Principle 1: We will **incorporate ESG issues** into investment analysis and decision-making processes.*
- *Principle 2: We will be **active owners and incorporate ESG issues** into our ownership policies and practices.*
- *Principle 3: We will seek **appropriate disclosure on ESG issues** by the entities in which we invest.*
- *Principle 4: We will **promote acceptance and implementation of the Principles** within the investment industry.*
- *Principle 5: We will **work together to enhance our effectiveness** in implementing the Principles.*
- *Principle 6: We will each **report on our activities and progress** towards implementing the Principles.*

- Source: https://www.unpri.org/pri/what-are-the-principles-for-responsible-investment.

SI has Gone "Mainstream"

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- UN–PRI Signatories - as of Q4, 2021
  - over **4,375** global investors / over USD **$121 trillion**
    - up from less than USD $6 trillion in 2006
  - includes over **200 Canadian** asset owners and managers
- RIA Canada report – by end of 2019:
  - CAD **$3.2 trillion** in assets managed in alignment with a "responsible" investment strategy
    - more than six times 2006 figure of $460 billion
  - **61.8%** of Canada's investment industry vs. 50.6% two years prior

Motivating Factors

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- Contributing factors include regulatory, reputational and ethical pressures.
- However, main force has been strong demands from **customers and investors**.
- E.g., BlackRock CEO Larry Fink's January 2020 Letter to Shareholders:
  - *I believe we are on the edge of **a fundamental reshaping of finance**.*
  - *Indeed, climate change is almost invariably **the top issue that clients around the world raise** with BlackRock. …*

RI Surveys

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- RIA Canada 2021 Investor Survey:
  - **73%** interested in RI (up from 60% in 2018)
  - However:
    - **69%** indicated no or limited knowledge of ESG considerations
    - **77%** indicated they wanted to discuss with their investment advisor
    - BUT - only **27%** said their advisor discussed with them

- These numbers indicate a **clear business opportunity**

RBC’s 2020 Institutional Investor Survey

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- 809 global institutional investors and investment consultants:
  - **75%** integrate ESG factors into their investment decisions
- Among the Canadians sampled:
  - **87%** believed that integrating ESG factors can help mitigate risk
  - **70%** believed ESG-integrated portfolios help generate long-term sustainable alpha
  - **63%** integrated ESG factors because they believed it was a component of their fiduciary duty

Investment Performance and ESG Considerations

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- A common misperception regarding ESG integration is that it sacrifices returns:
  - empirical evidence contradicts this
  - similar returns / lower risk on average
  - E.g., Deutsche Asset & Wealth Management and Hamburg University comprehensive review of over 2,000 empirical studies
  - Another meta-analysis of studies conducted in 2020, concluded that there existed a positive relationship between ESG and financial performance. It concluded that "ESG investing appears to provide downside protection, especially during social or economic crises." (Source: https://www.ussif.org/performance.)
- This seems logical – analysis of E, S and G factors can provide "material" insights into associated investment "risks" and "opportunities" – taking a comprehensive and structured approach to analyzing these factors should improve performance – just as it would for other material factors and considerations.

Cumulative Index Performance — Gross Returns

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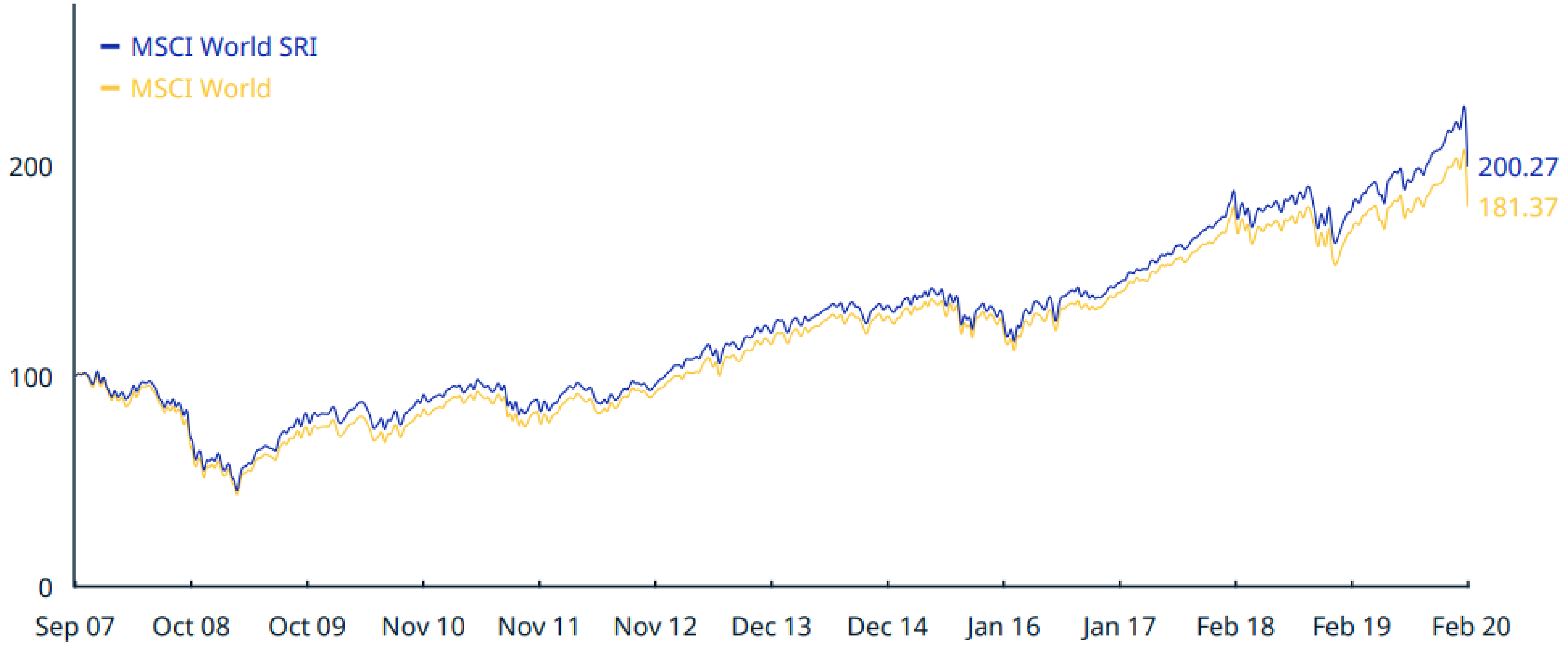

	10 Years (to Dec 2021)	Since Incept (01/01/2000)
Jantzi Social Index	7.17%	9.97%
TSX Index	7.01%	9.14%
TSX 60	7.15%	9.91%

The Impact of COVID on Responsible Investing

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- Early COVID evidence indicates higher ESG-rated stocks performed better during the first quarter of 2020, and similar since then
- During the “crash” period:
  - Q1/ March 2020 –significant evidence that higher rated ESG stocks/portfolios out performed:
- During the “recovery” period:
  - since April 2020 Mixed – some say better or the same
- Funds continue to flow into funds with an ESG focus, and other investments increasingly put or enhance the ESG lens they apply to investments
- Importance of "S" came through loud and clear during the COVID crisis
- The recognition that climate change (i.e. "E") represents another systemic crisis looming not so far on the horizon that will hit us hard, and is already having huge impact on economies ….

Approaches to RI

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1. Negative/exclusionary screening
2. Positive/best-in-class screening
3. Norms-based screening
4. ESG integration
5. Sustainability themed investing
6. Impact investing
7. Corporate engagement and shareholder action

Firms generally use more than one approach…

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- “our approach to investing sustainably includes **exclusion**, **integration** and **impact investing**.”
- … built upon **ESG integration** across all investments, **stewardship**, **screening**, … with allocations to **impact, thematic** and **socially responsible** investment opportunities.
- ...**integrate**, **engage**, **influence**, and **evolve**
- … shareholder **engagement**, **integration** of ESG criteria into investment analysis and decision making, and **exclusion**. Includes portfolio carbon footprint reduction targets.

Approaches (cont'd)…

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- …built upon three pillars: **fully-integrated ESG**, active **stewardship** and **client-driven solutions** and reporting.
- …**integrate** ESG factors into investment analysis, and employ **engagement** and **proxy voting**.
- …provide several **alternative investment options** to investors that enable them to choose
- … emphasizes **ESG integration**, **thematic and impact investing** opportunities, as well as exclusionary **screening**

ESG Integration

"The explicit and systematic inclusion of ESG factors in investment analysis and investment decisions."

- The emphasis of ESG integration is on identifying ***material*** opportunities and risks related to ESG factors that can contribute to total investment ***returns***, and minimize exposure to ***risks***
- ESG factors can be treated in the same way as other financial factors using existing fundamental strategy. For example, it is important to identify opportunities and risks associated with a company's **business model**
- Based on the expected impact of ESG factors, investors may adjust forecasted financials (i.e. revenue, operating cost, asset book value, CAPEX), or discount rates and price multiples within valuation models (i.e. dividend discount model (DDM), discounted cash flow (DCF) models, P/E approach, etc.)

Source: Guidance and Case Studies for ESG Integration: Equities and Fixed Income (CFA Institute 2018):: https://www.cfainstitute.org/-/media/documents/survey/guidance-case-studies-esg-integration.ashx.

Sample ESG Assessment

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Sample Assessment Using the SASB Five Factor Test

SUSTAINABILITY ISSUE / OPPORTUNITY	Direct Financial Impacts & Risk	Legal, Regulatory & Policy Drivers	Industry Norms & Competitive Drivers	Stakeholder Concerns & Social Trends	Opportunities for Innovation	Total Score	Notes / Comments
ENVIRONMENT							
GHG Emissions	10	10	7	7	7	41	*Hydrocarbon reserve exposure to climate change mitigation efforts*
Air Quality	5	7	5	5	5	27	*More strategic approach to pollutants including NO_2, VOCs, and PM*
Water Management	8	6	7	5	10	36	*Need plan to secure water supplies without exacerbating stressed regions*
Biodiversity Impacts	3	7	2	6	2	20	*Some exposure to protected areas and endangered species*
SOCIAL CAPITAL							
Security, Human Rights & Rights of Indigenous Peoples	4	8	6	9	4	31	*Improve risk management plan for operations in areas of conflict*
Community Relations	3	5	5	10	2	25	*Strengthen community outreach in later project stages*
LEADERSHIP & GOVERNANCE							
Business Ethics & Payments Transparency	5	9	5	8	1	28	*Significant operations in areas of high corruption*
Health, Safety & Emergency Management	5	8	6	7	3	29	*Renew focus on emergency preparedness and response, safety culture*
Reserves Valuation & Capital Expenditures	10	9	3	7	7	36	*Significant CAPEX for exploration/development of new fossil fuel reserves*
Management of the Legal & Regulatory Environment	3	4	5	3	4	19	*Minimal political activity around company's core operations*

0 = no impact
5 = potential for impact
10 = significant impact
(immediacy, likelihood, magnitude of impact)

36-50	high risk/opportunity = likelihood of significant impacts
21-35	medium risk/opportunity = potential for modest impacts
0-20	low risk/opportunity = not significant at this time

SASB Materiality Map - by Sector

Sector Level Map

- Issue is likely to be material for more than 50% of industries in sector
- Issue is likely to be material for fewer than 50% of industries in sector
- Issue is not likely to be material for any of the industries in sector

Dimension	General Issue Category ⓘ	Consumer Goods	Extractives & Minerals Processing	Financials	Food & Beverage	Health Care	Infrastructure	Renewable Resources & Alternative Energy	Resource Transformation	Services	Technology & Communications	Transportation
Environment	GHG Emissions											
	Air Quality											
	Energy Management											
	Water & Wastewater Management											
	Waste & Hazardous Materials Management											
	Ecological Impacts											
Social Capital	Human Rights & Community Relations											
	Customer Privacy											
	Data Security											
	Access & Affordability											
	Product Quality & Safety											
	Customer Welfare											
	Selling Practices & Product Labeling											
Human Capital	Labor Practices											
	Employee Health & Safety											
	Employee Engagement, Diversity & Inclusion											
Business Model & Innovation	Product Design & Lifecycle Management											
	Business Model Resilience											
	Supply Chain Management											
	Materials Sourcing & Efficiency											
	Physical Impacts of Climate Change											
Leadership & Governance	Business Ethics											
	Competitive Behavior											
	Management of the Legal & Regulatory Environment											
	Critical Incident Risk Management											
	Systemic Risk Management											

Columbia Treadneedle Investments (CTI)

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- SASB Case Study: https://www.sasb.org/knowledge-hub/esg-integration-insights-2019-edition/, pages 13-17.
- Developed internal RI ratings for nearly 6,000 companies based on two models - the interaction of which yields a quality rating between 5 (low) and 1 (high)
  - First - Financial Stewardship Model - measures "financial prudence".
  - Second - ESG Materiality Model - focuses on the financial materiality of ESG factors, **using the SASB materiality framework as a basis**
- Internal ratings are **integrated with traditional information** such as external ratings in an interactive CTI RI dashboard (depicted in Fig 1 of the CTI case study).
- This dashboard provides several interactive tools that contribute to the systematic integration of ESG insights into the **investment process** to guide:
  - portfolio formation, monitoring, risk management, performance measurement and attribution analysis
- Further feeds into CTI's **engagement practices** by identifying data gaps, and identifying questions for management teams regarding ESG issues that are particularly relevant for individual companies

What is Stewardship?

- Many terms are used: **Stewardship, active ownership, shareholder action, shareholder engagement, corporate engagement** or simply **"engagement"**
- UN-PRI:
  - "The use of influence by institutional investors to maximize overall long-term value including the value of common economic, social, and environmental assets, on which returns and clients' and beneficiaries' interests depend."
- RIA Canada:
  - "The use of shareholder power to influence corporate behaviour."

2020 Canadian RI Trends Report

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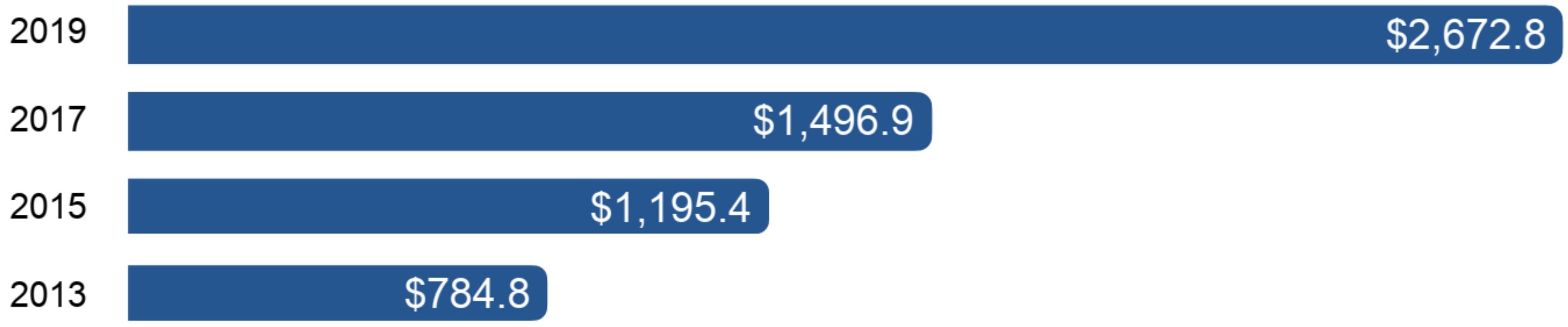
- Stewardship ("shareholder engagement") was the second most prevalent RI strategy in Canada in 2019, applied to around 84% of total RI assets
- Assets subject to stewardship grew 78% over the period 2017-2019 - notably because of increasing application in fixed income
- The most common stewardship topics were climate change, diversity and inclusion, and ESG disclosure

(Source: 2020 Canadian RI Trends Report)



Stewardship Practices

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- **Engagement:** Meetings, calls, and correspondence with investee's Board or management on ESG issues (also called **"dialogue"**) - all asset classes
- **Shareholder proposals:** Shareholders may file proposals (also called **"shareholder resolutions"**) on ESG issues, to be put to a vote of all shareholders at an investee's annual general meeting (AGM)
- **Proxy voting:** Shareholders incorporating ESG when exercising their right to vote on ballot items at an investee company's AGM
- **Public policy:** Engaging with regulators, policy makers, and standard-setters on ESG issues - all asset classes
- Collective actions such as Climate Action 100+ can make a difference (i.e., by 2021: 167 companies, 615 signatory investors with $60 trillion in assets).

UPP's 2021 Climate Action Plan – June 2022

Exhibit 1. UPP's financed greenhouse gas emissions

	Public Equity	Private Equity	Private Debt	Infra-structure	Real Estate	Fixed Income	Total
Value of exposure analyzed ($M CAD)	5,683	731	773	196	400	1,245	9,028
Total carbon emissions (tonnes CO_2-eq)	301,131*	27,786	27,464	29,221	4,421	84,516	474,539
Carbon footprint (tonnes CO_2-eq / $M CAD invested)	53*	38	36	149	11	68	53
Weighted average carbon intensity (tonnes CO_2-eq / $M CAD revenue)	135	73	77	583	31	202	139
Emission weighted data quality score	2	5	5	5	5	3	3

Scope 3 emissions associated with our energy (oil & gas) and mining investments totaled approximately 1 million tonnes CO_2-eq.

UPP’s 2021 Climate Action Plan – June 2021

Exhibit 2. Description of data quality scores

	Data quality score	Source of GHG emissions data
More certain	1	Reported by issuer and issuer indicated emissions have been verified or assured by a third party
	2	Reported by issuer
	3	Estimated by third-party data provider using physical activity data (for example, electricity generation)
	4	Estimated by third-party data provider using historical issuer emissions or geography/industry averages
Less certain	5	Estimated by UPP using geography/industry averages

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THANK YOU!