Geneva, 6 June 2018

WELCOME

Prof. **Henry Peter**, Head of the Geneva Centre for Philanthropy

INTRODUCTION

Prof. **Rajna Gibson**, Professor of Finance at the Geneva Finance, Research Institute, Geneva School of Economics and Management, University of Geneva

PRESENTATION OF THE RESEARCH PAPER

"**Coordinated Engagements**" by Prof. **Elroy Dimson**, Research Director (Finance & Accounting) and Chairman of the Centre for Endowment Asset Management at Judge Business School, Cambridge University

"**The sustainability footprint of institutional investors**" by Prof. **Philipp Krueger**, SFI Junior Chair Associate Professor of Finance at the University of Geneva

PANEL

Prof. **Elroy Dimson**
Prof. Rajna Gibson
Bonnie Saynay, Global Head of Responsible Investment, Invesco
David Harris, Group Head of Sustainable Business, London Stock Exchange Group; and Head of Sustainable Investment, FTSE Russell
Moderated by Prof. **Henry Peter**

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CONCLUSION

WELCOME

Professor Henry Peter, Head of the Geneva Centre for Philanthropy, provides a brief overview of the Centre, it's mission, and its value proposition, he sets the stage for the afternoon's topic, which focused on the idea that Environmental, Social, and Governance ("ESG") investment is about not only finance and compliance, but also ethics and generally values, and this requires input from experts across multiple areas to be effective. Subsequently, Prof. Peter, introduces Pr. Rajna Gibson, Professor of Finance at the University of Geneva, who provides a deeper overview of the afternoon's main ideas and agenda.

PRESENTATION OF THE RESEARCH PAPER

"**Coordinated Engagements**" - **Professor Elroy Dimson**

Please see the attached pdf presentation. The slide deck is provided solely to attendees at the event, for their personal use. Please state that the pdf should not be redistributed to colleagues, and should not be uploaded to an intranet or external website.

"The Sustainability Footprint of Institutional Investors" – Professor Philipp Krueger

The next paper, on the "Sustainability Footprint of Institutional Investors" is presented by Professor Philipp Krueger, Associate Professor of Finance at the University of Geneva and Junior Chair at the Swiss Finance Institute.

Prof. Krueger begins his presentation by talking about the motivations for this study. Essentially, with stock markets being dominated by institutional investors today, it is surprising that there is relatively little research on these investors' preferences regarding sustainability issues. As such, this study looks to accomplish two objectives: 1) propose a new way to measure portfolio-level sustainability of institutional investors (the "sustainability footprint"), and 2) study the link between risk-adjusted performance and this measure to get a better understanding of why institutional investors might choose sustainable portfolio allocations.

Before introducing the sustainability footprint, Prof. Krueger examines theoretical motivations for why institutional investors might care about portfolio-level sustainability. To do so, he builds on a paper by Bénabou and Tirole[1] to come up with three views as to why institutional investors might care about sustainability issues. The idea of the paper is now to test these three views by examining the relation between risk-adjusted performance and sustainability.

The sustainability footprint is computed using stock-level sustainability scores in conjunction with data on portfolio holdings from 13F SEC filings of large institutional investors. The study covers over 4000 institutions between 2002 and 2015. The sustainability footprint is simply the weighted average sustainability of the stocks in which the institution is invested. The footprint is also split up into its two components (i.e., the environmental and social footprint).

[1] Bénabou, R., & Tirole, J. (2010). Individual and corporate social responsibility. Economica, 77(305), 1-19.

PANEL

After the paper presentations, a panel discussion takes place, in order to gather deeper perspectives from the speakers, as well as other experts. In addition to Prof. Gibson and Prof. Dimson, the panel introduces Ms. Bonnie Saynay, Global Head of Responsible Investment for Invesco, and Mr. David Harris, Head of Sustainable Investment at FTSE Russell. Prof. Peter invites the panel participants to give a feedback on the papers presented earlier in the afternoon.

Prof. Gibson provides two observations for thought on Prof. Dimson's study. Firstly, she notes that it was surprising to see no institutional Swiss activists as top performers in Prof. Dimson's study, and questions whether Switzerland is falling behind in this regard. In response to this, **Prof. Dimson** notes that historically investor activism has been more prominent in Nordic and Anglo-Saxon markets; however, with investment having an increasingly global view, this is something that is bound to change in the future, as clients continue to demand such activism regardless of geography. As a second thought, Prof. Gibson notes that the studies conducted so far appears to focus on large institutional investors, leading to the question of how mid-size institutions can be effective as active investors in this realm going forward. The general response to this concern is that these companies should look internally and ask themselves "what can I do?" – that is, choose the right benchmarks, hire the right asset managers, and do not underestimate your power as a smaller player.

Ms. Saynay then takes the floor. From a global asset management perspective, Invesco's view is that fund managers (those who make the buy sell decisions) are the only genuine answer to ESG integration, and the sustainability focus must be squarely focused on fund managers.

- Elroy Dimson's paper on active ownership driving performance results is clearly aligned with Invesco's view that dialogue and engagement, enhanced with the power of voting, can drive sustainability practices within firms and unlock value for clients.
- Rajna Gibson and Phillip Krueger's paper took this analysis a step further to analyze and quantify sustainability impact across the E and S categories with very compelling outcomes, as much research is heavily focused on the governance aspect of sustainability.
- Governance risk exists across all industries, whereas environmental and social risk may be and often time is industry specific from a materiality perspective.
- The focus on materially financial impacts across ESG should be part of the investment consideration process and this discretion should be maintained at the investment team level. Materiality is a fund managers core expertise.

- Asset managers should be less focused on outputs and more focused on outcomes.
- The industry around sustainability continues to become considerably more complicated, and it is now time to get "back to basics".
- Fund managers should be the movement's advocates and drive this change through their perspectives and "lens".
- Mandatory requirements around ESG could reduce ESG integration to a box ticking exercise
- Longer term benefits around ESG are more likely to stem from transparency and choice than from prescriptive legislation.

Mr. Harris then provides his perspectives on the discussion so far, commenting that the two studies presented this afternoon are excellent and cover two significant approaches used by investors, the integration of ESG into investment strategies/decision making, and the integration into investment stewardship ie engagement and voting.

Mr Harris reflects that increasingly larger institutional investors are also bringing these sustainable investment strategies into their usage of benchmarks and many are now integrating ESG into core passive strategies linked to an investment belief that this would help generate better long-term risk adjusted returns and to also influence market-wide corporate standards. Examples Mr Harris mention included GPIF, the Japanese government pension fund, and HSBC Pension Fund, both of which had made significant allocations to passive strategies that incorporated ESG in the index design.

Mr. Harris also notes that there was not the same data history for ESG as there was for risk premia factors, plus much of it was about future expectations with respect to economic impacts from themes such as climate change. The data issue was a major challenge in this space, which was that unlike standard financial data, most investors do not have decades of reliable data, and peer-reviewed credible academic analysis was only just starting to be developed. It was explained that ESG metrics are varied, complex, and there are many views over how to most effectively use this data within the investment process. This was not a barrier to action, and indeed asset owners were also learning from one another. It was critical that market participants continue to share experiences, and engage with policy makers, in order to further development of consistent global frameworks, enable more sophisticated use of this data and to make corporate engagement more powerful. Collaboration with academics in this regard was also extremely welcome and important.

Q&A SESSION

After the panel participants provided their high-level thoughts, the Q&A session begins. Prof Peter refers the panelists to the PRI guidelines, and wonders why despite this we do not see consistent benchmark-level standards across stakeholders in this space.

Ms. Saynay is the first to respond to this topic, stating her broad concern that in studying this topic practitioners have over-complicated and sometimes over-bureaucratized the effort. As of today, there are over 400 different benchmarking instruments globally across approximately 60 markets, and this creates a lot of noise. And in so-doing, many of these metrics focus on inputs (i.e. number of ESG engagements), as opposed to actual outcomes (i.e. effectiveness of these engagements), which undermines the ultimate intention of engaging in the ESG space. To conclude, Ms. Saynay comments that a "one-size fits all" prescriptive approach that focuses on a single global taxonomy is counter-productive. Instead parties should include fund managers in the dialogue, understand how they have assessed risk, and acknowledge that these topics should be tailored on a case-by-case basis.

Mr. Harris agrees that there is a huge amount of confusion in the marketplace since terminology and "noise" are getting in the way of the real issues. He breaks investment decisions down into two fundamental ESG perspectives – 1) how does the company operate? and 2) what does the company provide? Using TESLA as an example, he shows how a company can be very effective in one view (e.g. providing environmentally sustainable products), and yet very weak in another (e.g. treatment of employees, governance, etc.). This view then leads to another view on passive vs. active investors, and in what direction the industry is moving. With index funds, which have characteristics of both active and passive investing, managers can "tilt" funds in favour of basic ESG principles, and this seems to be the direction in which investor engagement is going today.

All four panelists are then asked whether there is truly a measurable correlation between compliance with ESG principles and financial performance.

Prof. Dimson looks at this question from a more academic perspective, noting that although research does seem to suggest that the two are positively correlated, in the long-run, given a sufficient amount of time and data, total financial returns would likely be a wash. As such, as active managers, the real question should be whether active investment can beat the market in the short-term before long-term normalization effects come into place.

Prof. Gibson makes an important distinction between *returns* and *performance*. Although returns may not necessarily correlate with ESG compliance, performance appears to be improved. This is because ESG compliance can be viewed as a sound risk management strategy that can essentially reduce the risk of an investment and therefore improve the performance of that investment. She furthers her point by making reference to her study (presented earlier in the afternoon by Prof. Kruger), noting that she finds evidence of a causative relationship between ESG compliance and overall performance, particularly as it relates to environmental compliance (relative to social compliance, for which the impact is insignificant, a finding would require follow-up research).

Ms. Saynay responds to this issue and Prof. Gibson's perspectives by warning participants to not discount the value of the "governance" dimension of ESG strategies. While environmental and social issues can vary in content and magnitude across companies and industries, all companies need to have sound governance compliance in order to drive returns, and this is a critical view that should not be forgotten by asset managers. At the end of the day, managers are not willing to sacrifice returns for sustainability; as such managers need to find a way to maximize returns in a way that is sustainable in all respects.

The final set of questions came from the audience, whereby panelists are asked about who has the fiduciary duty in this case (asset managers, or asset owners?) And what the role of government regulation should be in this space?

Ms. Saynay provides the response to this, referencing her work, "Lost in Translation", where she looked at the fiduciary responsibility of investors and asset managers. She notes that we have created an environment where asset owners are not very educated with regard to the ESG space and, as such, the fund managers, not necessarily the owners, should be the central parties in this discussion, as their actions can be the most impactful.

Mr. Harris, conversely, notes that the asset owners are in fact already driving this agenda (particularly the larger ones). This led to asset managers who are not well-informed on ESG issues to fall behind their competitors, which over time drove effective asset managers to get up to speed on responsible investing in order to remain competitive in their industry. This can be already seen with many banks and managers creating funds that by default have ESG-tilted features in their products (i.e. funds in favour of investing in companies with green revenues, carbon reserves, high environmental efficiency, etc.).

CONCLUSION

After gathering perspectives during the study presentations and Q&A session, the panelists are asked to share their concluding messages with the audience.

Prof. Gibson begins by asking why responsible investing is not as mainstream as it should be, noting that stakeholders, broadly (including the media, educational institutions, and even boards), are not yet sensitive enough to these issues, though this is starting to change. She also notes that the next major issue to dive into relates to measurement – there is so much heterogeneity in terms of data quality, data types, measurement, key performance indicators, etc., that we need to find a way to focus on *outcomes* going forward in order to keep responsible investing effective and bring it to the mainstream.

Ms. Saynay concludes by stating that, ultimately, ESG integration is about investment. To be more effective going forward, stakeholders need to go back to the basics, be authentic, and truly try to understand what *drives* sustainability. She agrees with Prof. Gibson that measurement should focus less on outputs, and more on outcomes.

Prof. Dimson summarizes his concluding thoughts suggesting “next steps” from two perspectives – that of the asset owners and that of the asset managers. For asset owners, they should be asking their managers about how they vote and how they engage on ESG matters; i.e. understand how they engage in responsibility on their behalf. For asset managers, the focus should be on sharing information, learning about how their colleagues have set up their responsible investment strategies, and how they influence their investees through active investing.

As a final concluding thought, **Mr. Harris** mentions that the discussion excluded a key stakeholder – smaller investors (retail, wealth management, smaller institutions). He notes that this a significant challenge, and more thought should be given into how we can simplify responsible investing in order to get engagement from these smaller participants as well.

Before closing the seminar, besides thanking all speakers and panel members for their outstanding contributions, **Prof. Peter** considers that it is interesting to observe and keep in mind how much the context is moving both in terms of perception and behaviour by the stakeholders, but also of a clear shift in the way the upcoming generations are looking at the issues, and therefore behaving.