TELOMERE | Capital

Business and sustainable investment at a crossroads

Talking is no longer enough!

In October last, Anna Sacks, American activist and influencer, published a video on the social network TikTok to denounce the doublespeak by Coach, the international luxury leather goods company. In actual fact, on its website, the company drew attention to a repair service for its products, boasting about its efforts in contributing to the circular economy and reminded its audience that every gesture counted. However, the short sequence by Anna Sacks – which was shared almost 3 million times -describes how returned or unsold products of the company are slashed by its employees before being discarded, thereby preventing them from being reused.

The listed company hastily added that the number of products destroyed represented less than 1% of its global sales, that these practices had now come to an end and that it was continuing in its efforts towards sustainable development and the circular economy.

Did the activist ever imagine the impact of her post? This event, which might seem to be of little consequence, is becoming more and more frequent and highlights the mindfulness of several citizens as regards the impact of their actions and their increasing desire to actively bring about change.

With social networks everywhere, that which is at stake in the fight against climate change, against discrimination, in reducing inequalities and social inclusion occupies an increasingly important place in public realms and opinions. Consumer trends are being felt and are applying additional pressure on companies with regard to their ecological and social commitments.

The time to take action has come

The demand to make decisions and take definite action is increasing across all ages. However, the youngest out there are particularly sensitive to these topics. Many of them are left disenchanted by the inaction of political leaders in the face of the climate crisis.

They want to contribute towards bringing about a renewal of a joint relationship and fundamental ways of thinking.

Student strikes for climate (Fridays for Future ou FFF) have been proof of this. Launched on 20 August 2018 before the Swedish Parliament by Greta Thunberg, this movement which aims to highlight the inadequacy of the climate policy and to encourage the emergence of swift and hefty measures for the protection of the climate, led to more than 1500 protests across 118 countries on 24 May 2019.

More recently, during the Glasgow Conference of 2021 on climate change (COP26), it was youth once again which cried out about the climate emergency, reproaching world leaders for making empty promises and comparing this conference to a greenwashing festival .

Impact investment

This increasing sensitivity as well as the almost instantaneous and global financial consequences of information, opinions and criticisms reported on social networks force businesses and investors to include strategies and practices which have a positive corporate, societal and environmental impact.

The criterion of the financial return of the investment thus loses its preponderance in favour of criteria of sustainability and social and environmental impact (impact investing).

The study by the Morgan Stanley Institute for Sustainable Investing demonstrated that almost 85% of individual American investors are mindful of sustainable investment.

It is in Millennials (people born between the start of the 1980s and the end of the 1990s) that one can see an increased sensitivity with a proportion reaching 95%. Also more than 90% of this group would like to receive an impact report regarding their investment. These figures are constantly on the up.

The correlation between the sustainability of a business and its financial performance has been highlighted for several years and the increasing demand from investors to have a more long-term view which is not exclusively financial gives businesses more scope to roll out wide-ranging sustainable practices.

Conducted alongside 50 directors of businesses in Europe and in the United States, a recent study has just confirmed that sustainability is now a core element of the business strategy; 92% of them are adapting their strategy and their business model to be more sustainable and anticipate increasing their investments in 2022 in order to improve their ESG (Environmental, Social, Governance) performance.

The need for a clear framework and objectives

The political initiatives aim to encourage sustainable business practices and to standardise and harmonise definitions and standards of sustainability.

Whether it is the 17 Sustainable Development Goals (SDG) from the UN 2030 Agenda or the Paris Agreement (COP21) signed by over 170 countries, the regulatory framework is becoming clearer and is harmonising. Numerous directives are being added to it, encouraging businesses and investors to make the transition towards sustainability.

On a European level, for example, the NFRD (Non-Financial Reporting Directive) directive sets out since 2014, the obligation for businesses to publish information relating to their impact on the environment, their corporate responsibility and diversity within their board of directors.

The European Commission wants to go further and trigger the redirection of financial flows towards projects and sustainable activities. This desire has come to pass through the proposal to review the NFRD directive and the Taxonomy of the EU for sustainable activities which allows all activities within the European economy to be identified, assessed and categorised. According to the European institution it is a question of "providing businesses, investors and political decision makers with appropriate definitions for which the economic activities can be considered as sustainable from an environmental point of view.

With effect from 1 January 2022, European companies will have to disclose the portion of their turnover and of their expenditure which adhere to sustainability indicators based on the calculation methods and criteria specified by activity sectors. The broadened range of the scope of the European regulation therefore targets publication obligations but also a higher number of entities. The revised directive shall also apply to investment consultancy. Product managers and financial advisors will therefore have to include sustainability factors in the design of financial products and in their discussions with their customers.

ESG Rating: a multitude of rules and frameworks

The obligations of non-financial reporting are therefore being clarified for all activity sectors. The up-to-now individual and voluntary approach is becoming compulsory and regulated. Highlighted by the 2006 UN Report on Principles for Responsible Investment (PRI),
the ESG criteria are a precious instrument for maintaining the achievement of these common goals and for helping businesses and capital investors to comply with the new rules and requirements.

The ESG analyses, relying on the 3 pillars of sustainable development (*Triple bottom line*), allow the direct or indirect impact of the activity of a business on the environment, on the stakeholders and its governance to be measured.

To do this, this rating takes account of a vast array of high varied data such as, for example, CO_2 emissions, recycling of waste, practices with regard to security and labour law, the relationship with customers and suppliers and the way in which the business is run, administered and monitored.

However currently there is more than a dozen methodologies and systems for ESG rating, each with its own criteria which allow businesses to have a baseline in order to identify, gather and send the required information.

As a result, it is sometimes difficult to succeed in analysing and comparing the data based on the same criteria. Depending on the referential used, the same business may therefore have different scores. This lack of clarity risks eroding collective trust.

Countless non-governmental organisations and associations protecting consumers are investigating misleading practices. The supervisory authorities of the financial markets of several countries have also started to check the conformity and veracity of the information which has been circulated by businesses regarding their products or services.

In Switzerland, Finma carries out inspections, notably on financial products which are known as a socially responsible investment.

Concentration and emergence of new players in ESG rating

In the hope of bringing about clarity and standardisation, 5 key ESG rating agencies have revealed their intention to collaborate in order to standardise the framework and the rules behind the ratings and reporting with regard to sustainable development.

In the same vein, the financial services company MSCI and the provider of data and analysis solutions for investors Burgiss Group recently announced the launch of a new analysis tool (*Carbon Footprinting of Private Equity and Debt Funds*) allowing asset managers to give an overall assessment of the risks linked to the climate.

For its part, Moody's, the company specialising in financial analysis solutions announced a new solution on 21 October last (*Taxonomy Alignment Screening*) which was specifically designed to help it comply with EU Taxonomy criteria .

Lastly, another major player in ESG rating might emerge soon. The IFRS Foundation, the body monitoring the International Accounting Standards Board - IASB announced the creation of the International Sustainability Standards Board (ISSB) with a view to laying down standards regarding information linked to sustainable development.

A vital international player at the level of accounting standards which apply to listed companies, the IFRS Foundation could benefit from this competitive advantage in order to make its presence felt and introduce a global baseline of standards for reports on sustainable development by offering a much-needed comparability to investors all the while allowing jurisdictions to add their own standards

From Climate Change to Climate Chance

Above all the climate emergency needs decisive and definite actions. Everyone can and must participate at their own level. However, one must not lose sight of the fact that the economic reality requires companies, in order to guarantee their stability and their continuity, to turn towards sustainability in a gradual way.

> Each industry faces up to separate challenges with different priorities in relation to sustainable development.

ESG standards allow companies to navigate within this demanding regulatory context and to steer their business activities all the while brining clarity to investors when making decisions. They must establish a basis for discussion between the investor and its asset manager in order to better ascertain and analyse the specific objectives and sensitivities with regard to sustainability so as to lead to a truly impactful investment.

Investors have a leading role to play by accepting their moral and societal responsibility and by placing sustainable development at the heart of their decisions. The companies who seize this opportunity to adopt a sincere and heartfelt sustainable vision as well as a strategy and audacious practices with a positive corporate, environmental and societal impact will be in line with demand and as a result will be more capable of attracting capital.

Political strategies, international standards and regulations with regard to sustainability must continue to foster, to bring about, and to go hand in hand with change; the incentivising aspect must last and prevail over punitive inclinations.

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