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# ESG and Material Efficiency Perspective for Investors



**Presentation by Céline Méchain for the WMF**

**17-19th June 2021**



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Les transactions présentées peuvent être notamment exposées aux risques suivants : liquidité, taux d'intérêt, crédit, capital et de contrepartie.

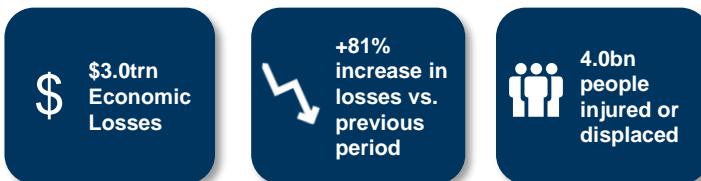
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# Growing awareness of Investors around Environmental Challenges, Carbon Emissions, Climate Risks and Scarcity of Planet Resources

## Global Natural Disasters

Consequences of global natural disasters from 2000 to 2019<sup>1</sup>



## The “Green Deal” in Europe (Dec-2019)

- Largest Economic stimulus since the Marshall Plan
- €7 trillion total investments needed by 2050E
- €1.85 trillion secured by the EU Recovery Package
- Acceleration of National Energy Plans through Covid-19 crisis

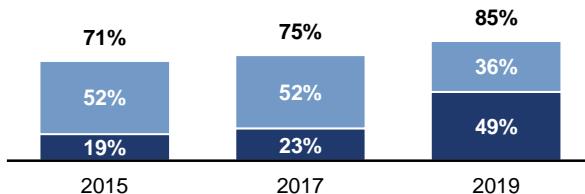


- c.\$5 of GDP by 2020 for every \$1 of capex invested in energy transition<sup>3</sup>
- First benefits expected in 2022/2023

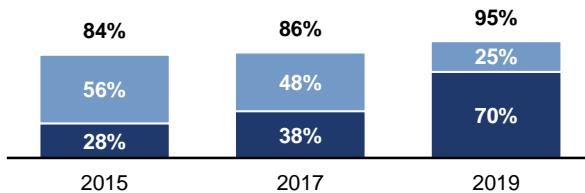
## Social Preferences

Growing interest by various demographic groups to incorporate ESG in investment decisions

### General Population



### Millennials



■ Very Interested   ■ Somewhat Interested

*Interest in sustainable investing continues to grow amongst both millennials and the general population*

Sources: PRI, U.S. Trust Wealth and Worth Survey, GS Research.

Notes: <sup>1</sup> UNISDR, Human cost of disasters, Oct-2020. <sup>2</sup> \$1,600 billion over the 1980-1999 period. <sup>3</sup> IRENA: International Energy Agency

## EU Sustainability Taxonomy Regulation (June 2020)

- In June 2020, the EU's Sustainability Taxonomy Regulation was formally adopted
  - Provides an EU-wide framework for classifying economic activity as environmentally sustainable
  - Expected to reduce "greenwashing", where financial products are marketed as environmentally sustainable without sufficient factual basis for their claims
- The objective of the EU Taxonomy is to encourage capital flows to green activities by enabling investors to identify:
  - Companies that fall under the scope of the Non-Financial Reporting Directive will have to disclose:
    - The proportion of turnover from activities aligned with Taxonomy
    - Capex and opex associated with Taxonomy-aligned activities
  - The first company reports and investor disclosures using the EU Taxonomy are due at the start of 2022

1

Substantially contribute to at least one of the six environmental objectives:

1. Climate change mitigation -- *adopted by 2020YE and enter into application by 2021YE*
2. Climate change adaptation
3. Sustainable use and protection of water & marine resources – *rest adopted by 2021YE, apply 2022YE*
4. Transition to circular economy, waste prevention & recycling
5. Pollution prevention & control
6. Protection of healthy ecosystems



2

Do no significant harm to any of the other five environmental objectives, where relevant



3

Comply with minimum social safeguards:

- UN Guiding Principles on Business & Human Rights – including 8 conventions of ILO<sup>1</sup>'s Fundamental Rights & Principles at Work; and International Bill of Human Rights
- OECD Guidelines on Multinational Enterprises



4

Comply with quantitative or qualitative **Technical Screening Criteria**: quantitative technical screening criteria will be tightened over time for CO<sub>2</sub> intensity metrics which trend towards zero by 2050

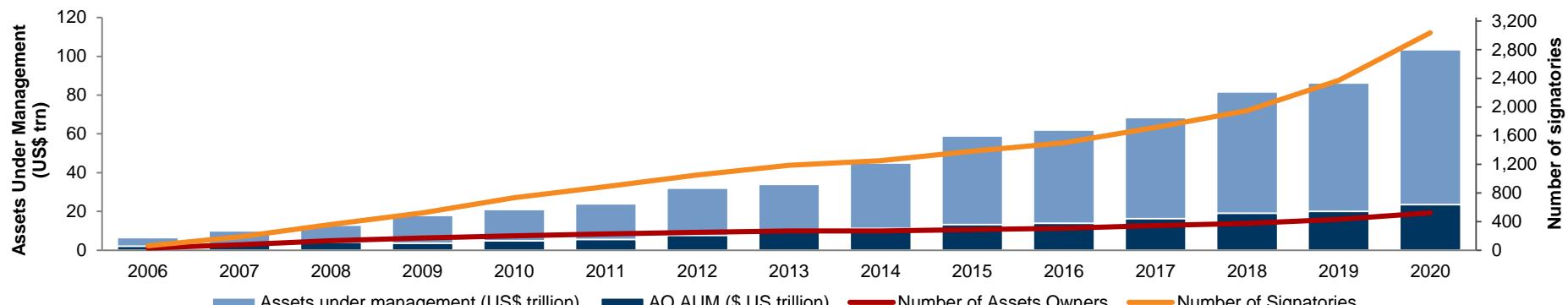


Currently covered in EU Taxonomy; Other objectives are to be covered at a later date

# Evolution of the Principles for Responsible Investment Signatories

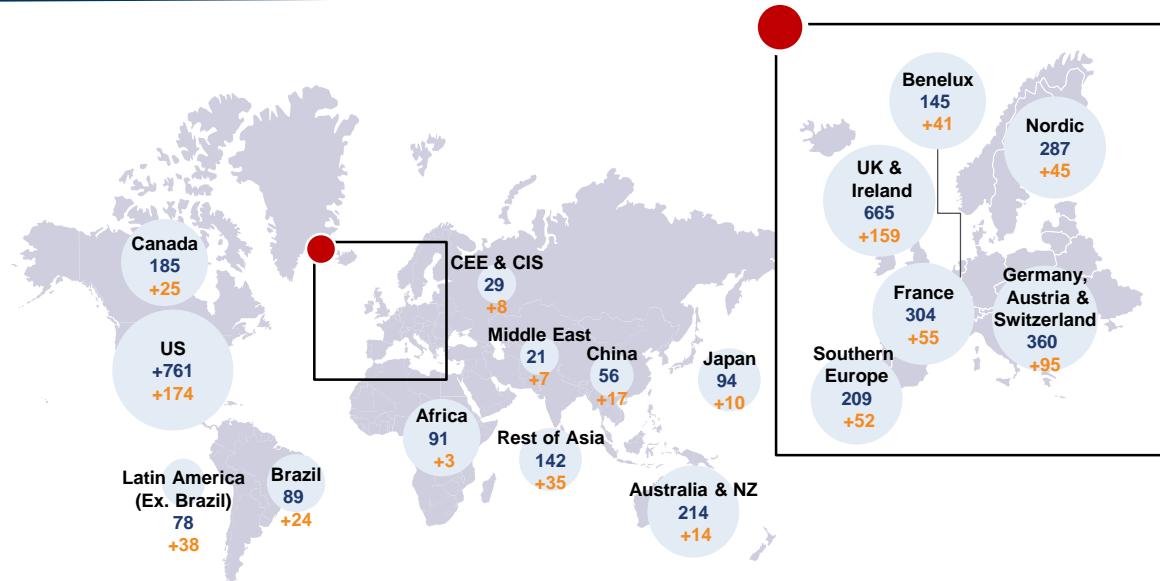
- PRI signatories have grown to more than **3,800 members**, with c.**\$100 Trillion** in assets under management

## Growing Initiative Since 2006



## Overview of Signatories

- Signatories as of April-2021
- Net new signatories since April-2020



Source: UN PRI Initiative website

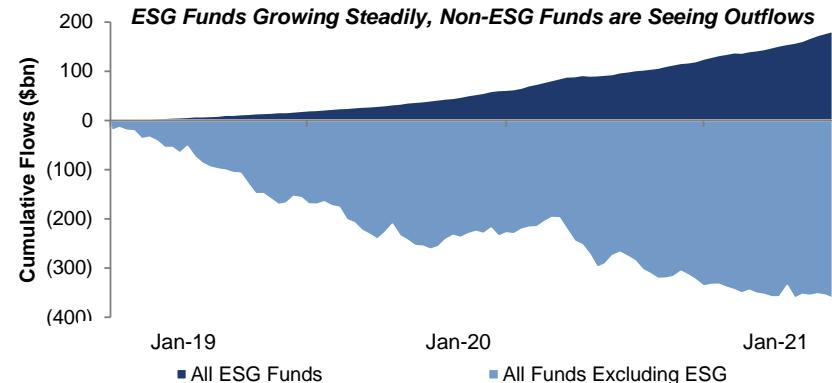
# ESG is Increasingly Material to Financial Investors

INVESTMENT BANKING  
DIVISION

... and is Becoming Increasingly Mainstream

**AuM<sup>1</sup> is Growing...**

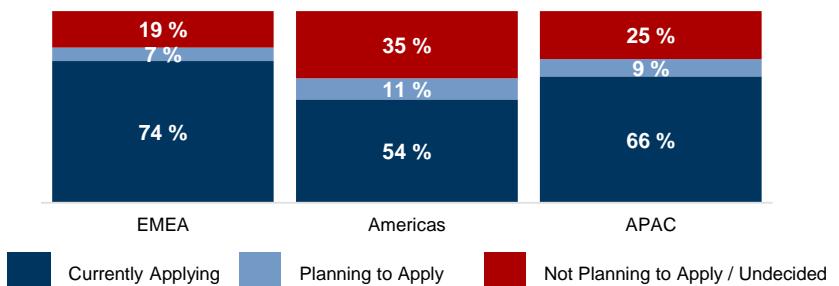
- 2020 saw ESG funds receive net inflows of \$153bn whilst non-ESG funds experienced net outflows of \$37bn



**... and Mainstream Adoption by Investors...**

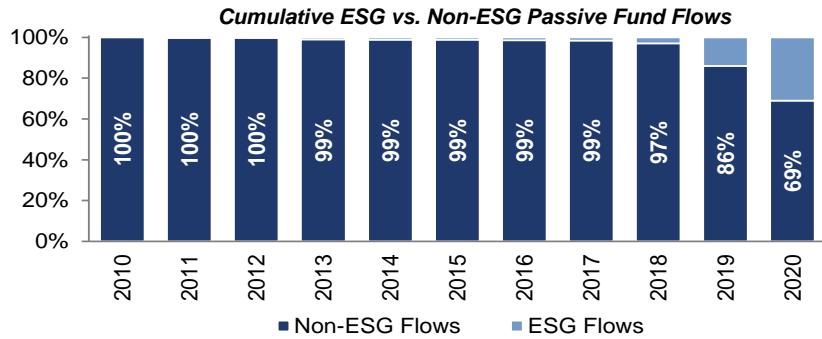
- GS survey of 1,600 investors revealed majority currently, or are planning to, incorporate ESG into investment process

**EMEA Leading the Charge**



**... and in Passive ETFs<sup>2</sup> too**

- The rise of ESG ETFs<sup>2</sup> continues to place an emphasis on having the right ESG score for companies



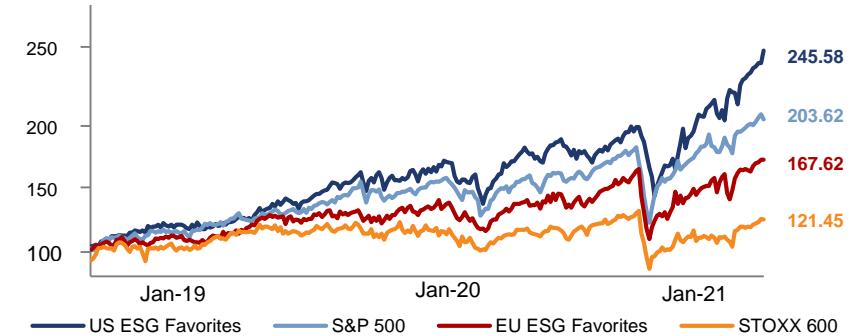
Notes: <sup>1</sup> Assets under Management. <sup>2</sup> Exchange Traded Funds.

# The Market is Differentiating Already Between “Good” and “Bad”

... Missed Opportunity to Maximise Value

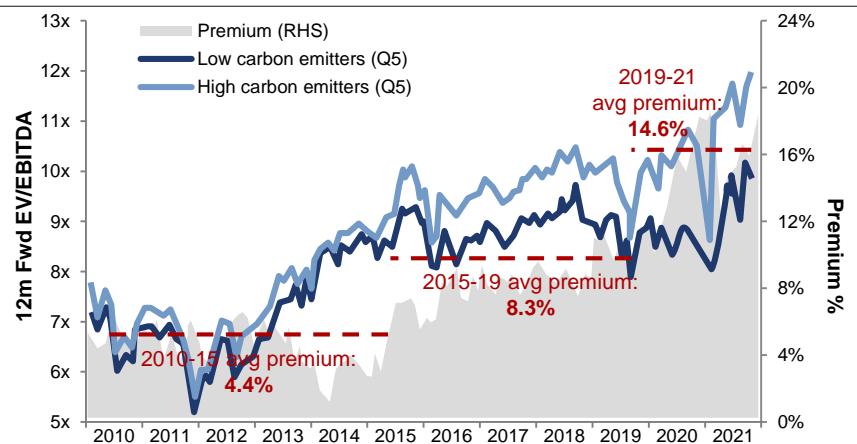
## ESG Favourites Outperform...

- Strong market bias towards ESG Fund favourites



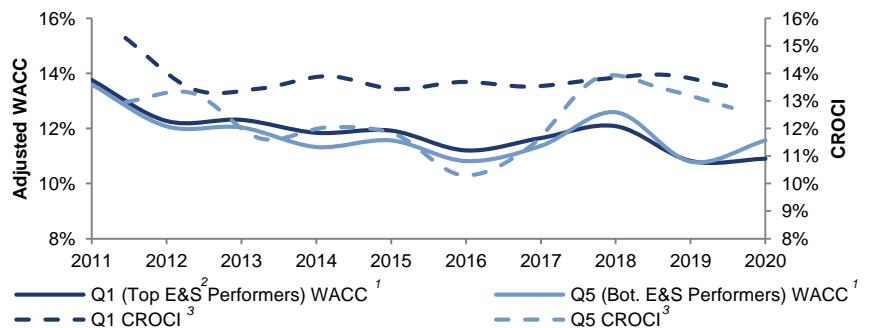
## ... High Carbon Emitters Penalised too...

- Low Carbon intensive companies trade at increasingly elevated premia vs. high carbon sectors



## ... and impacting WACC<sup>1</sup>

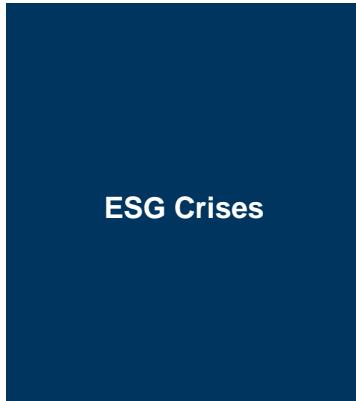
- Top ESG Disclosers have an average 104bps lower WACC<sup>1</sup>



Notes: <sup>1</sup> Weighted Average Cost of Capital. <sup>2</sup> Environment and Social. <sup>3</sup> Cash Return on Capital Invested

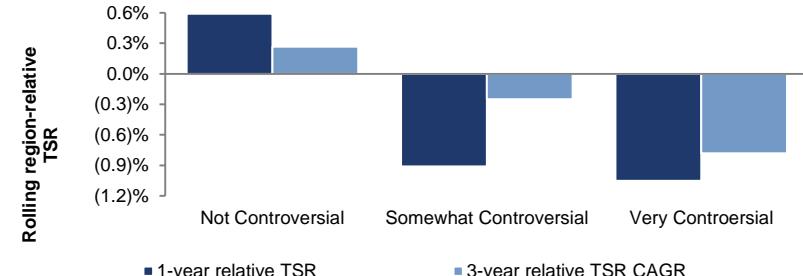
# Growing Sophistication of Investors Means Risks from Getting it “Wrong” are Greater

.....With Potential For Rapid Value Impact For Communication Missteps



- ESG missteps can have an enduring impact on value

GS SUSTAIN ESG Universe Listed Since 2010, SUSTAIN Absolute Controversies Scores (2010-2017); TSR is GICS 2 Relative



- Mass organised online social engagement can rapidly amplify perception and value from a crisis

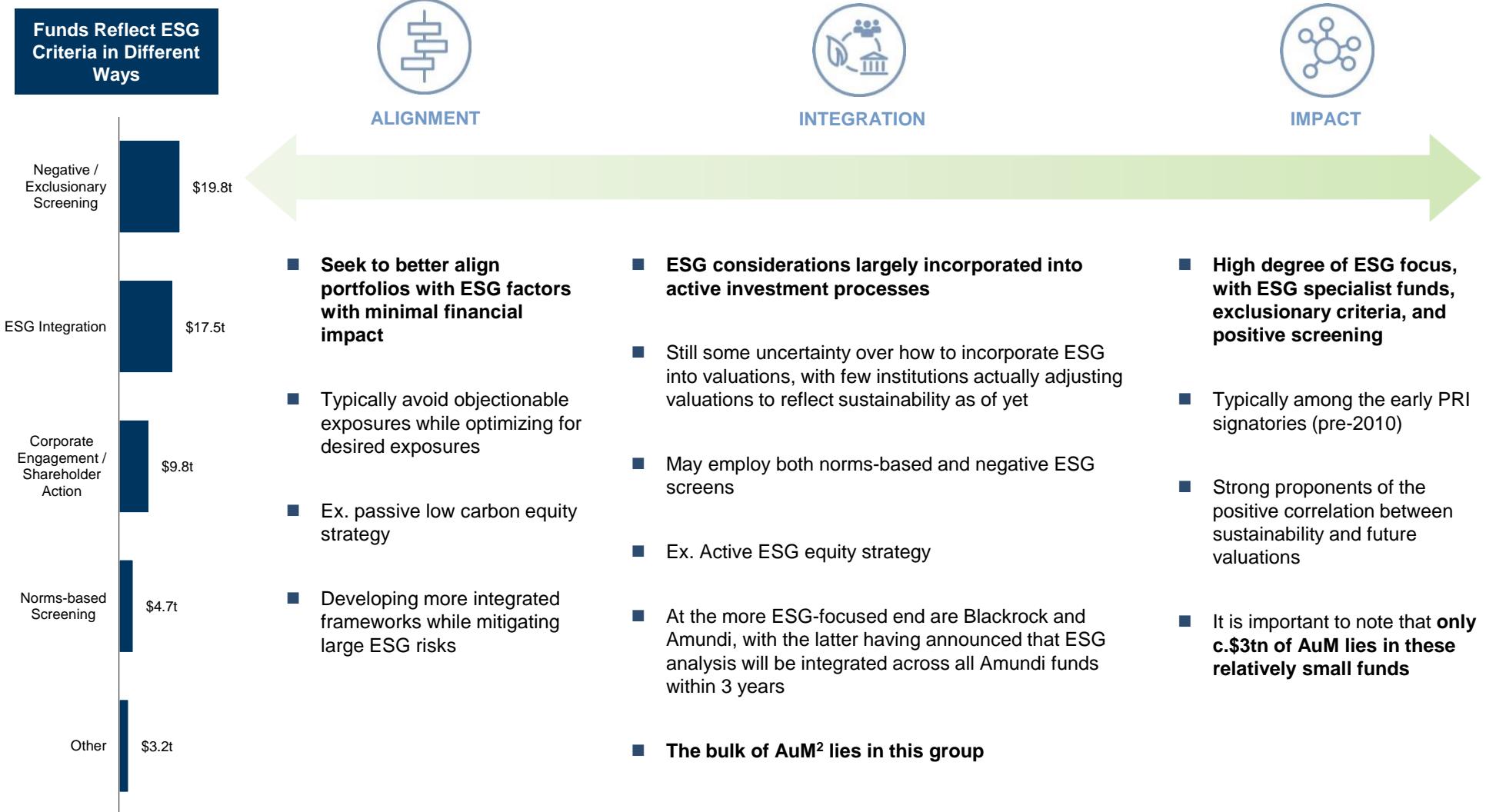


- Growing use of ESG as a ‘wedge’ issue and greater investor engagement

Company	Crisis	Activist	Activist Value Thesis	Influence on Board Changes?
Sempra Energy	Gas Leak	ELLIOTT <sup>®</sup> <i>bluescape</i> RESOURCES	Break-up	✓ Board Representation
BARCLAYS	Epstein Connection	SHERBORNE INVESTORS	Break-up	?? Situation Ongoing
BAYER	Round up Litigation	ELLIOTT <sup>®</sup>	Break-up	?? Situation Ongoing
Volkswagen	“Dieselgate”	HERMES INVESTMENT MANAGEMENT TCI Fund Management Limited	Cost Reductions, Remuneration Reform	✓ Director Resignations

Navigating ESG is becoming increasingly more complex.  
Understanding your ESG strengths and vulnerabilities are key to ensuring a robust investment case

# ESG Investing Across the Fund Manager Spectrum

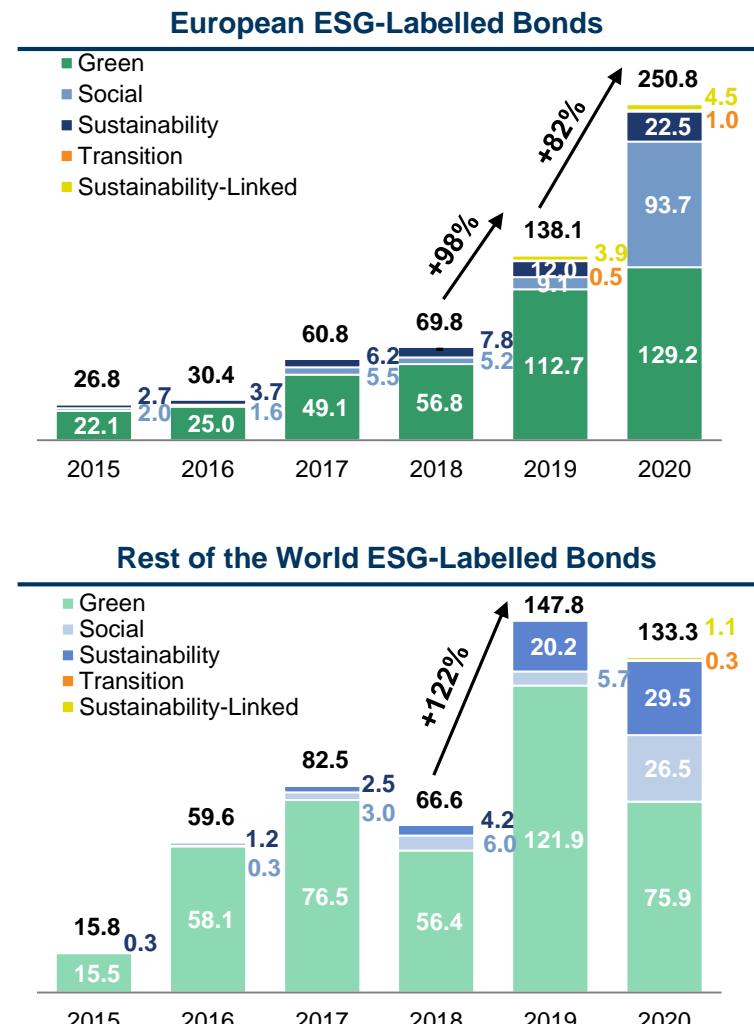
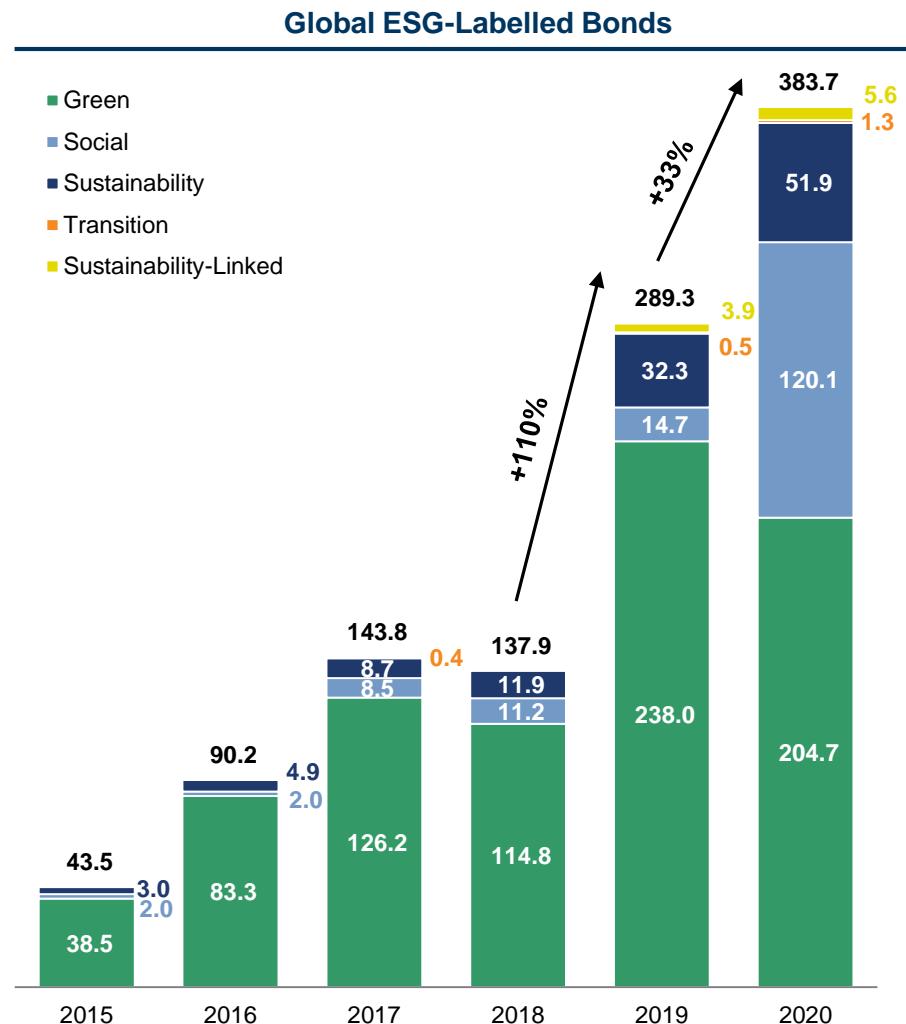


Source: PRI Signatory Directory

Notes: <sup>1</sup> Preqin Ltd report. <sup>2</sup> Assets Under Management

# Market Update | Growth of ESG-Labelled Bond

## Diversification From Pure Green Bonds



Sources: Bloomberg, ClimateBonds, as of Dec-2020 – foreign exchange used as of the date of the bond issuance  
Note: In bn€-eq

# ESG Debt Instruments Available

## Recent Evolution of Moving Away from “Project-Based” Structures to “Target-Based” Structures

	“Project-Based” Structures					“Target-Based” Structure
	Green Bond	Social Bond	Sustainability Bond	Transition Bond	SDGs Bond	Sustainability-Linked Bond
<b>Short Description</b>	<ul style="list-style-type: none"> <li>Funds dedicated to strict green projects</li> <li>Follow the ICMA GBPs framework</li> </ul>	<ul style="list-style-type: none"> <li>Funds dedicated to social projects</li> <li>Follow the ICMA SBPs framework</li> </ul>	<ul style="list-style-type: none"> <li>Funds dedicated to both green and social projects</li> <li>Follow the ICMA SBPs and GBPs frameworks</li> </ul>	<ul style="list-style-type: none"> <li>Funds dedicated to a wider range green / energy efficiency projects</li> <li>Follow the ICMA GBPs framework</li> </ul>	<ul style="list-style-type: none"> <li>Funds dedicated to a wider range of both green / energy efficiency and social projects</li> <li>Follow the ICMA SBPs and GBPs frameworks</li> </ul>	<ul style="list-style-type: none"> <li>No requirements for the use of proceeds</li> <li>The issuer is indirectly committed to meet green target(s) otherwise coupon/return will increase</li> </ul>
<b>Subject to a Framework?</b>	✓	✓	✓	✓	✓	
<b>Project Based?</b>	✓	✓	✓	✓	✓	✗
<b>Funds Committed?</b>	✓	✓	✓	✓	✓	
<b>Issuer Retains Flexibility?</b>	✓	✓	✓	✓	✓	✗
<b>Return / Coupon Increase?</b>	✓	✓	✓	✓	✓	
<b>ESG Investors’ Attractiveness</b>	✓✓	✓✓	✓✓	✓	✓	
<b>Included in Green Indexes?</b>	✓	✗	✗	✗	✗	✗
<b>Will Attract Dedicated Green Investors?</b>	✓	✗	✗	✗	✗	✗
<b>Positive Marketing?</b>	✓✓	✓✓	✓✓	✓	✓	✓✓✓
<b>Size Available (Limited to the Issuer’s Projects)</b>	✓	✓	✓	✓✓	✓✓	✓✓✓✓✓

# Which KPIs Have Been Retained to Define Sustainability in Recent Debt Issuances?

Increased Diversity of Criteria and Issuers Across All Sectors

- Single or multi-criteria KPIs
- Influencing the cost of debt issuance in case of non-compliance: “Greenium” vs. “Coupon step-up”
- Donation to charities and reinvestment in environment

Bond KPIs		Loan KPIs	
	 <b>Constellium</b>		 <b>ELSAN</b> Notre Santé autrement
<b>EQT</b>  Apr-2021 Greenhouse gas emission reduction, Board diversity and investment advisory professionals diversity	<b>Feb-2021</b> 25% reduction in greenhouse gas emission by 2025 and 10% increase in recycled aluminum input by 2026	<b>Feb-2021</b> 30% of recycles materials, 20% reduction of Scope 1 and 2 CO2 emissions and 10% reduction of Scope 3 emissions from fabric production, garment manufacturing, raw materials and upstream transport by 2025	<b>Feb-2021</b> Patient satisfaction, medical waste reduction and improvement of work / life balance for employees
 <b>Klabin</b> Jan-2021  Water consumption, waste reuse / recycling and reintroduction and / or reinforcement of wild species intro ecosystem	 <b>TESCO</b>  Jan-2021 Reduce Scope 1 and 2 greenhouse gas emissions by 60%	 <b>LAFARGE</b>  Nov-2020 Target of kg net of CO2 emitted per ton of cementitious material	 <b>FLENDER</b>  Jan-2021 Volumes of the company's products being used in wind turbines
 <b>Schneider Electric</b>  Nov-2020 CO2 emissions, gender diversity and training of underprivileged people	 <b>enel</b>  Sep-2019 / Oct-2020 Increase installed renewable energy and reduce greenhouse gas emissions	 <b>NOVARTIS</b>  Sep-2020 Increase number of patients reached in low- and middle-income countries (LMICs) with strategic innovative therapies	 <b>Logoplaste</b>  Jun-2020 Reduction in CO2 emissions

Protect environment, Resources and Humanity

Sources: Company reports and press releases. <sup>1</sup>Novartis global health flagship programs target leprosy, malaria, Chagas disease, and sickle cell disease.  
Note: A positive “greenium” implies an estimated pricing benefit for the Issuer vs. a similar “vanilla” transaction

# Goldman Sachs Research on Thematic Deep Dives



**1st of 40 years: China de-carbonization: Reshaping of upstream**  
Apr-2021



**ESG Sector Roadmaps: E-commerce**  
Apr-2021



**Investing in the Sustainable Development Goals**  
Feb-2021



**Top of Mind: Investing in Climate Change**  
Jan-2021



**The Green Deal: EU Green Deal estimate up 50%, now at €10trn**  
Jan-2021



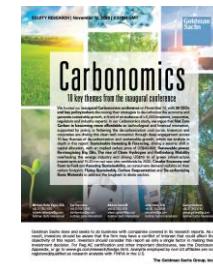
**ESG Sector Roadmap: Brands & Apparel**  
Jan-2021



**Carbonomics: China net zero: The clean tech revolution**  
Jan-2021



**ESG Sector Roadmap: Banks**  
Dec-2020



**Carbonomics: 10 key themes from the inaugural conference**  
Nov-2020



**ESG Sector Roadmap: Utilities**  
Nov-2020



**Carbonomics: Innovation, Deflation and Affordable De-carbonization**  
Oct-2020



**Green Hydrogen: The next transformational driver of the Utilities industry**  
Sept-2020



**ESG Sector Roadmap: Food & Beverage, Alcohol & Tobacco**  
Sep-2020



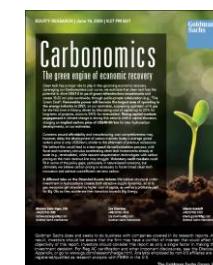
**The EU Green Deal: Green Upside**  
Jul-2020



**Carbonomics: The Rise of Clean Hydrogen**  
Jul-2020



**GS SUSTAIN: Carbon offsets: Tools for the low carbon transition**  
Jun-2020



**Carbonomics: The green engine of economic recovery**  
Jun-2020



**The EU Green Deal: Towards 'net zero': A plan to fight climate change**  
Jan-2020

Source: Goldman Sachs Research