Challenges in Valuing ESG-Related Risks and Opportunities:  
Reflections of a Fund Manager

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Agenda

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- Responsible Investment – Defined
- Responsible Investment – Key Concepts
- Integrating ESG Issues
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Insight Investment - Overview

- Asset management business of HBOS plc, a leading UK financial services company

- £79.2 billion in funds under management (as at 31 March 2005)

- A leading shareholder activist in the UK

- Member of UNEP Finance Initiative since October 2004
  - Responsible Investment Initiative
  - Asset Management Working Group
Responsible Investment Defined

“Investment where social, environmental or ethical considerations are taken into account in the selection, retention and realisation of investment, and the responsible use of rights (such as voting rights) attaching to investments”

Responsible Investment – Key Concepts

- **Enlightened Shareholder Value**

  *Investors have a financial interest in taking account of environmental, social, and governance (ESG) issues that could have material impacts on companies’ earnings and/or share price.*

- **Responsible Ownership**

  *Investors have a financial interest in using the rights associated with share ownership to engage with companies to support good corporate governance and corporate responsibility practice, as well as challenge poor practice.*
Integrating ESG Issues

- **Investment Analysis**
  1. Consider the potential effects of ESG issues on investment value drivers, such as:
     - Regulation Risk
     - Legal Liability
     - Brand Value Risk
     - Intangible Value Risk
     - Human Capital Risk
     - Competitive Advantage
  2. Exploit market inefficiencies

- **Engagement / Activism**
Case Studies

- Registration, Evaluation and Authorisation of Chemicals (REACH) – EU’s Proposed New Chemicals Regulation
  - Lack of research / analysis by brokers
  - Insight conducted in-house research / analysis
  - Detailed understanding of company positioning re: Reach is important when forming an overall view of the company
  - Risks as well as opportunities
Case Studies (cont.)

- **Climate Change**
  - Significant broker research / analysis re: GHG trading in the near term (2005-07)
  - Less re: 2008-12 (Kyoto) – period during which more likely to be material
  - Risks as well as opportunities
  - Insight is currently engaging with companies to:
    - Better understand potential materiality
    - Encourage the development of strategies for the future
Observations re: Challenges of ESG Integration

- Currently material ESG issues are already being taken into account

- Broker research is focused on short-term, easily quantifiable issues

- However, many ESG issues are longer-term in nature, intangible – so difficult to value

- There may be investment opportunities

- Need more research on and analysis of mid- to longer-term ESG issues
UNEP FI – Asset Management Working Group (AMWG)

- Explores the association between environmental, social and corporate governance considerations and investment decision making.

- Consists of 13 asset managers with combined mandates of 1.7 trillion USD:
  
  ABN AMRO Asset Management (Brazil)  
  Acuity Investment Management  
  BNP Paribas Asset Management  
  Calvert Group  
  Citigroup Asset Management  
  Groupama Asset Management  
  Hermes Pensions  
  HSBC Asset Management  
  Insight Investment  
  Morley Fund Management  
  Nikko Asset Management  
  RCM (UK) (Allianz Dresdner)  
  Sanpaolo IMI Asset Management
AMWG’s Materiality Series

- **2004 - MAT1** - “The Materiality of Environmental, Social and Corporate Governance Issue to Equity Pricing”

- **2005 AMWG Work Programme: MAT2**
  - Financial Services, Automobile, Aero Defence, Food and Beverage, Chemicals, Pharmaceuticals, and Basic Materials (Forestry, Iron and Steel, Other Extractives
We would point out:

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