World Business Council for Sustainable Development

UNEP Finance Initiative
Innovative financing for sustainability

## Workshop Outcomes

# Valuation Workshops 2, Montreux 12 March 2008

***Integrating Sustainability Value into the Capital Markets***

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## Investor Side Participants

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|---|---|---|
| Susan | Aagenes | Innovest |
| Monica | Aguilar | Allianz |
| Cecile | Churet | HSBC Investments |
| Lutz | Cleeman | Allianz |
| Angela | de Wolff | Conser Invest |
| Dominique | Habegger | Asset 4 |
| Gianluca | Manca | Eurizon Capital |
| Marc | Mattes | Zürcher Kantonalbank |
| Philippe | Rohner | Pictet |
| Philippe | Spicher | Centre Info |
| Henrik | Steffensen | Asset 4 |

## Background

**Context**

It is believed that only if capital markets adequately capture and reflect the sustainability performance of companies will the latter have the ultimate incentive to entirely integrate ESG considerations into their core business strategy. And only then will the corporate community be able to fully align sustainable development with one of their key missions: maximization of shareholder value.

Despite the recent surge in CSR reporting and responsible investment activities, however, the corporate valuation mechanisms of capital markets appear to stubbornly remain indifferent when it comes to the sustainability-related success or -failure of traded companies. Usually, only one-off events of catastrophic magnitude are recognized (e.g. Enron, WorldCom, Tyco, Parmalat, Exxon Valdez).

**Objective**

It is clear that capital markets will adequately capture and reflect corporate sustainability performance, only:

I. if, on an aggregate basis, market makers deem it to be **financially relevant**,
II. if corporate ESG information is fed to the markets in a way that the investor community can use, and
III. if capital market makers - and all other actors along the investment chain – actually do integrate the ESG-information delivered into core decision making processes in a consistent and systematic way.

Due to the "death of distance" caused by the internet revolution, increasing public ESG–consciousness, tightening environmental/social regulation, resource scarcity and the launch of environmental markets, even mainstream investors are realizing the materiality of ESG issues: 14 Trillion of AuM signed up to the PRI show that ESG has at least reached their agendas.

While the materiality perceptions on capital markets, as under point I. above, are, hence, appearing to shift towards the inclusion of ESG issues, points **II.** and **III.** still had to be addressed.

Therefore, the *WBCSD's influencing the capital markets & valuation workstream* together with *UNEP FI's Asset Management Working Group (AMWG)* bring together a group of WBCSD companies with a group of UNEP FI signatories. The aim is to provide a platform for business and capital market actors to jointly discuss common challenges and build consensus on how sustainable development can be better valued by the capital markets.

**Work program**

This workstream builds on past work conducted by the WBCSD (Finance sector project, Accountability & Reporting project, 2007 workshop on communicating sustainable development with the capital markets) and the work of UNEP FI's Asset Management Working Group.

*Outputs to-date:*

- Analysis of existing initiatives conducted and presented January 2008.
- Pilot valuation workshop conducted in January 2008 (10 "investee" companies, 10 investor-side companies participated)
- Second valuation workshop conducted in March 2008 (35 companies, 10 FIs participated)

**Pilot valuation workshop – January 2008, London**

A first pilot workshop was held in London, January 2008. The following key messages for companies and investors emerged:

**Investor perspectives**

- Mainstream investors (including asset managers and analysts) will only consider ESG information as long as it is clearly material. They feel that the conventional sustainability reporting of most companies is too broad, too voluminous and the information disclosed too often financially irrelevant. The investment community would appreciate sustainability reporting schemes to be materiality-focused and specifically catered to unique investors rather than the whole plethora of external stakeholders. "Less is more"!

- The investment community expects companies to create, within their reporting, a clear link between the ESG information disclosed and its financial materiality, ideally, as a core component of annual reports.

- The investors present were also aware that in order to systematically gather, process and integrate ESG information into investment analysis and decision-making, investment tools such as company valuation models need to be further developed to be able to adequately capture ESG information.

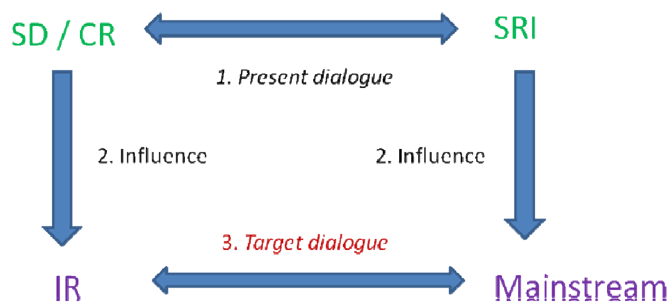
**Investee (company) perspectives**

- Investee companies felt that when it comes to ESG factors, a series of key aspects is constantly overseen by investors and therefore undervalued by the markets - - i.e. the quality of companies' internal risk management, the degree to which sustainability is integrated into product development and the companies' ability to seize sustainability opportunities (e.g., bottom of the pyramid markets), as well as to attract and retain talented staff.

- Companies acknowledged that they have struggled in communicating sustainability performance value in investor relevant language.

- Investee companies highlighted that many ESG factors may become material because of their impact on brand, reputation and market standing. This also implies the opportunity of translating good ESG performance into incremental brand value, especially against the background of rapidly increasing ESG awareness among consumers. Investors should start to pay closer attention to this new "kind" of materiality.

***Key gap identified –** need to influence and facilitate similar conversations taking place between* investor relations *representatives and* mainstream *money managers:*




## Workshop Summary – Montreux March 12, 2008

*Scale up valuation workshop – March 2008, Montreux*

This WBCSD/UNEP FI Learning by Sharing Workshop builds on the pilot valuation workshop held in January 2008 (listed above).

The 'speed-dating' format provides a unique opportunity for companies to dialogue with the investment community with the aim to accelerate progress on valuing sustainability in the capital markets.

The aim of this session was to introduce a new set of companies and financial institutions (FIs) to the dialogue platform; in order to test the hypotheses developed in the pilot workshop; and to explore questions around sustainability value, materiality and how to communicate ESG performance at the Investor/Company Interface. Questions included:

- Which sustainability factors are material to different business sectors?
- What do investors need if they are to incorporate sustainability considerations in mainstream investment decisions?
- How should this value be communicated to the capital markets?

Additionally and in a separate discussion-round, UNEP FI asked specifically the present "investor-side" participants on what is needed from them in making the capital markets more ESG-efficient: are capital market actors capable of integrating ESG performance integration into decision making? If not, what must and what can they do about it?

*Summary / Outcomes:*
Participants in attendance agreed that they want another date! - - That this format was a valuable opportunity for companies and the investment community to engage in a mutually-beneficial dialogue.

Key take-aways from both Workshops:

- It is not necessarily self-evident that the investment community understands business – there are strong perceptions and miss-perceptions about how a company / sector is (and should be) managing its material sustainability issues.
- Sustainability reports are not valuable for the investment community - - investors / money managers want to hear only sustainability performance material to the core business (and why!) in investor friendly language. Companies could go one step further and express, where possible, sustainability performance issues monetarily.

- The investment community recognizes the materiality of many sustainability-related issues; even in the "mainstream", "value-oriented" investors with a longer term view are already looking at ESG-issues when deemed appropriate and "worth it". It is the task of investee companies, however, to raise awareness of further ESG-issues worth looking at from an investor's perspective. **This should be done by reporting ESG performance specifically to the capital markets, conveniently, integrated into financial reporting.**

- **Sustainability reporting is now where financial reporting** - the essential foundation of all valuation processes on capital markets - **was 100 years ago**. It therefore makes sense to look back at how financial reporting became what it is today. A key development was the legal requirement of having financial statements audited by independent entities. Likewise, in order to enhance the transparency and credibility of their ESG reports, companies should insist in having them verified as well. As with financial reporting, the entities advising on the reporting should be different from those auditing it!

- **Leveraging the short-termism of capital markets for the benefit of long-term sustainability?** Even long-term investors today require instant and updated financial information rather than just one report per year. Investee companies should report on their sustainability performance as often as they do on their financial performance: **Less & More Often could be More!**

- A dramatic lack of ESG-data was described as a major problem, especially of such data which is not based on third-party estimates. At the same time, proprietary valuation tools must be developed by the investment community to integrate the data once it becomes available. Adapting proprietray valuation methodologies - already developed for the spheres of brand or intellectual property value - to the ESG area could be a promising way forward. These could easily be based on extended versions of input-output models. A UNEP FI project dedicated specifically to the development of ESG valuation methodologies/tools will be undertaken in 2009.

## Next Steps

April 08 – *Homework for WBCSD SD managers & UNEP FI asset managers*

- Company SD managers will meet with their IR manager internally to discuss outcomes of these workshops / sustainability factors material to their core business (and why!)

- SRI asset managers will meet with their mainstream colleagues to internally discuss outcomes of these workshops / sustainability factors material to companies' core business (and why!)

- **Conference call – Wednesday April 23 2008 to discuss progress**

*Output discussed:* Guidance document for corporate officers & money managers.

*This summary note has been prepared in order to capture the key themes from this WBCSD – UNEP FI workshop. Our intention is to provide the reader with an overview of the key discussion points and outcomes rather than precise record of all statements. As with any meeting of this nature, many of the points are subject to interpretation; any inaccuracies are unintentional and are the responsibility of the authors.*