**Sustainability Report Talking Points**

**Overview**

* Sustainable investing is critical to the sustainability *of* investing. The incorporation of sustainability in investment management is a necessary element in the industry’s mission to serve society by improving long-term outcomes.
* We are moving from sustainable investing as a good idea to a reality that has implications for all investment portfolios.
* Right now, we’re at a threshold moment – a point of strategic inflection where sustainability goes through a period of transformation.
* Sustainable investing goes further than its forerunners in three important ways:  
  + (1) It is additive to investment theory and does not mean a rejection of foundational concepts.
  + (2) It develops deeper insights about how value will be created going forward using environmental, social, and governance (ESG) considerations.
  + (3) It considers many stakeholders.

**Influences**

* The fundamental purpose of finance is to contribute to society through increases in societal wealth and well-being. Looking at finance as an ecosystem reveals important interconnections and points of friction in how finance currently works in relation to this purpose.
* For many years, sustainable investing could be characterized as “a slow-moving but unstoppable train” that had started to pick up pace. COVID-19 has accelerated it even further, but the challenge of balancing short-term and long-term needs has never been more stark.
* When we consider the history of sustainable investing, we see three phases and the speeding up of sustainability.
  1. The first phase began in the 1970s with the first sustainable mutual fund and the Sullivan principles addressing apartheid in South Africa and continued till the launch of UN PRI in 2006.
  2. This phase ushered in ESG integration and was marked by the increasing focus on climate risk following the Paris Agreement in 2015.
  3. Now we see 2020 as the start of a third phase, where mainstreaming is truly possible.
* The COVID-19 pandemic has encouraged a more holistic view of ESG versus the individual elements of E, S, and G.
  + The crisis is making people realize the financial importance and materiality of social factors, consistent with a stakeholder mindset. Because of relatively less focus historically, social factors tend to be the least defined, so this is an area for innovation.
  + Early performance metrics from the pandemic showed that well-rated ESG companies performed better and were more resilient, indicating that the higher quality embedded in many highly rated companies had paid off.
    - We are seeing a similar pattern with the Experimental Partners program, namely that organizations that had invested in inclusion & diversity have been more resilient during the pandemic.
* Other evidence of a speeding up includes:
  + In the practitioner survey of CFA Institute members in March 2020, a total of 85% said they take E, S, and/or G factors into consideration in their investing, up from 73% just three years ago.
  + Client demand as a motivation for investment organizations to consider ESG factors increased significantly in the last three years. Demand as a motivator was highest in the Americas region (65%), an increase of 20 percentage points since 2017.
  + In the first half of 2020 alone, the Principles for Responsible Investment (PRI) signatories increased by 28%, to more than 3,000 entities, and the assets under management grew 20%, to more than US$100 trillion.
* An acceleration of regulation, combined with the longer-lasting impacts of the pandemic, has positioned the industry to come together with a convergence in standards and best practices.

**Drivers**

* The business model for investment organizations pursuing sustainable investing must make commitments on the full range of resources, processes, and incentives that are necessary to drive innovation of this magnitude. It’s critical that senior leadership set the sustainability orientation and embed these plans throughout the organization into values, beliefs, and extend into culture.
* Sustainability in financial terms is embedded in the investment model and should not be regarded as an ancillary part of the process.
* There is a variety of ESG investing approaches that exist in the market. Our survey findings showed that two primary methods have emerged as favored by investors: ESG integration and positive screening – or “best-in-class”.
  + ESG integration explicitly considers ESG-related factors that are material to the risk and return of the investment, alongside traditional financial factors, when making investment decisions.
  + Best-in-class aims to invest in companies and issuers that perform better than peers on one or more performance metrics related to ESG matters. Some think of this as a form of “positive screening”, as opposed to negative screening or “ESG Exclusion” which excludes securities, issuers or companies based on certain ESG related or values-based considerations
  + Positive screening is now more popular than negative screening, which had initially been the predominant approach.

**Enablers**

* The current reporting ecosystem has been a work in progress for more than a decade. There is a high level of dissatisfaction among investment industry stakeholders with the present status of data and reporting. Going forward, we expect greater urgency from the industry to make significant progress, with a stronger framework likely to emerge, albeit slowly.
* Sustainability analysis is currently dependent upon financial reporting, which is famously incomplete, and therefore needs to be supplemented with more current, alternative data sources.
  + 71% of industry roundtable respondents saw alternative data as benefiting the robustness of sustainability analysis, and 43% saw sustainability as benefiting from the application of artificial intelligence.
  + Natural language processing and related programs are used to process data in some firms, but it will take time for data to become more structured and ESG analysts will need to be able to explain the significance of the output, combining human and artificial intelligence.
* Greenwashing exists across the investment industry ecosystem. In fact, 78% of practitioners surveyed think there is a need for standards to mitigate greenwashing.
* ESG factors should be integrated into the process, and it is a recipe for failure to simply have someone conduct an ESG review after the rest of the analysis has been done. All investment professionals need to understand risk, and it is the same with sustainability. Investment professionals need to be able to contemplate risk associated with sustainability as part of a company or industry’s overall risk profile.
* The talent pool for ESG specialists is in high demand from a hiring standpoint, but sustainability expertise is relatively limited.
  + Of the 1 million+ core investment profiles we analyzed on LinkedIn, less than 1% had sustainability expertise, but it is growing quickly (up 26% in the last year).
  + Meanwhile, nearly 20% of all portfolio manager job postings were seeking sustainability expertise.
  + When trying to attract and retain talent, a clear commitment to sustainability and demonstrated adherence to those commitments can help. Many employees want to work at an organization that makes a difference and one that has values they agree with.
  + Women represent 42% of ESG analysts, which is much higher than the 26% of women overall in the sample.
* Training in ESG has increased, but still fewer than half of respondents say their firm provides ESG training. Only 11% of respondents consider themselves proficient in the area, but an equal number are currently being trained, and more than 70% have interest in training — half of these within the next year.

**Actions Needed**

* We introduce a rubric for progress, which provides a **grade** and a **guide** to improve performance. There are six elements:
  + The first two relate to investment *thinking*.
    - **ESG education**: Sustainability knowledge and skills must be developed to a critical threshold across the industry so that ESG thinking is embedded in all investment settings.
    - **System-level thinking**: Investment professionals need to understand the main features of systems theory and use this thinking when considering sustainability topics.
  + The next two relate to the *technologies* and networks needed for success.
    - **Collaboration synergy**: Strengthened collaborations within and across organizations drive engagement and combinatorial power. Sustainability is an area where working together creates more benefits than anyone working alone could.
    - **ESG data**: ESG data practices need to be further developed to support more substantial decision-useful application, and we expect a shift in the coming years where data go from being part of the sustainability problem to an important part of the solution.
  + The last two relate to *teamwork* and culture.
    - **Sustainability innovation:** Organizations can demonstrate commitment to sustainability innovation through organizational agility in people and processes and iterative improvements.
    - **Purposeful culture:** Organizational transformations will produce purpose-driven organizations with a strong fiduciary culture, recognizing the need for more balance.
* As the largest global association of investment professionals, CFA Institute has committed to the development of sustainable investing in the following ways:  
  + **Educating investment professionals** via a specialist certificate, professional development, practitioner-focused research, and the CFA Program curriculum.
    - In the next edition of the curriculum, ESG content will increase by 130%, with 23 readings in seven topic areas. This is equivalent to ESG coverage in 16% of readings, and ESG coverage will likely reach 20% or more as ESG standards develop and practice advances.
    - In addition, the CFA Institute Research Challenge added ESG analysis as an evaluation component in the 2021 competition year, showing those just beginning their investment studies that these factors are part of any thorough analysis.
  + **Publishing research** for ongoing education. Sustainability is an area that is dynamic, and continuous learning is essential. The growth of new data sources further drives the need to keep learning. In addition to this study, we have done a series of case studies on climate risk analysis, extensive work with PRI, and a literature review showing how ESG has developed over the years.
  + **Creating standards** to improve product transparency and comparability in investor reporting, with the CFA Institute ESG Disclosure Standards for Investment Products expected in late 2021.
  + **Collaboration** is essential on this topic, and we are engaged with many organizations to provide the investor view on advisory committees and working with accounting standard setters to look for harmonization opportunities.
* Within sustainable investing lie the fundamental elements of the sustainability of investing. Investors and the investment industry have a considerable role to play in determining the pathway and shaping a future worth investing in.