Global Asset Management

Webinar

RBC Global Equity ESG: Inclusion or exclusion? Corrected transcript

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PRESENTATION

Ben Yeoh

Thank you for joining us for some current debates on ESG and sustainability and responsible investing. I am Ben Yeoh, Senior Portfolio Manager here at RBC for the Global Equity team. I am delighted that Cary Krosinsky has joined us, and for those of you who don't know, Cary teaches Sustainability Finance and Energy Studies at Yale and Brown Universities. He is also an advisor to Carbon Tracker. He also founded the Real Impact Tracker and is the author of books on sustainability and investing. We are here today to talk about everything to do with cutting edge ESG, so we are going to cover the U.N. SDGs (Sustainable Development Goals), sustainability ratings, stewardship, data, ESG data, carbon data, the work of the Real Impact Tracker and what is happening in China.

Cary Krosinsky

It's fantastic to be with you, Ben. For anyone who doesn't follow Ben on social media or read his fascinating weekly posts, what are you doing?

Ben Yeoh

Starting with the SDGs, if you don't know what these are, they are the United Nations' Sustainable Development Goals. They came out in December 2015 and were a reiteration of another set of goals - the Millennium Development Goals. There is a lot of chat in the sustainable investment space about whether or not investors can really use them. How useful are they? Are they for developmental economists, governments or NGOs? What are the pros and cons? It is a nice framework, but is it that useful? Cary, do you have any views, or would you want to start on some pros and cons?

Cary Krosinsky

Thanks for that, Ben. It is useful to have a set of outcomes in general and the SDGs are certainly a well-constructed set of outcomes. The challenge with investing directly in the SDGs is that it actually backwards in our view. Last September we held a symposium at Yale on the state of data in the ESG space and I think my comments are still valid. It's great to have a set of outcomes at a system level, which the SDGs are, but it really shouldn't be mapping for the SDGs, which we've seen done by pension funds in Europe, or to create an ESG database and then figure out what to do with it. Actually, it is the reverse of what we need, which is to find strategies that work - from a sustainability perspective and a business case – and build up those case studies and then figure out how to scale them for purpose.

The SDGs are a perfectly good set of system goals that can be measured seasonally, but what we really need are those strategies that can fix the problems and make a real difference. I would like to see more focus on investment strategies that **solve** SDGs as opposed to just having a set of outcomes. They are useful, but you have to put them in the right context.

Ben Yeoh

That is one of the main criticisms I hear. We have a backwards-looking framework and are trying to squeeze investment processes into it. That is the wrong way around, which is what you're suggesting. There have been some criticisms from people in the field, and from asset owners, that you get a very good market gloss, but it doesn't really do what you want it to do. This is because it should be the other way: that you have come up with your sustainable strategies, your process, your philosophy, how you think you might be doing, the impact, and then you can look at it. Is that something you would agree with?

Cary Krosinsky

Not only do I agree with it, but, to be very blunt - and I want to be as straightforward and honest as I can - my last full-time job was Trucost. They had another way of looking at the world, where you can measure and you can estimate, and you can get a sense of the cost to society or the impact. It is a very different thing if you are an investor and you're trying to figure out what to do about those natural capital challenges. However, when you think about the world and its problems, it all comes back to investor strategy. Can we change that strategy in a way that makes a meaningful difference? If we are not doing that, then we are just looking at a picture on a wall.

Ben Yeoh

I was putting in a plug there for the Human Development Index. There is a lot of talk about SDGs, but this thing called the HDI has actually been running for many years now. Some of the HDI people just launched a new iteration of their data set. When I asked them about the SDGs, they said that HDI is a doorway through which to look at some of the SDG topics. I think HDI is very interesting because it has been measuring things like inequality, healthcare, death rates and childbirth, and has been tracking them for quite a long time at a country level. Again, however, you can't really squeeze that backwards into investment strategies. We have a question. “Why is SDGs investment backward-looking while the targets are set to 2030, 2050? The feeling is that the SDGs set targets, objectives, and strategies as a way to achieve them, not necessarily opposed, but they could be complementary.” Any thoughts on that comment?

Cary Krosinsky

Yes, I agree with that, the point being that I think the problem with “SDG Investing,” is that you take an approach where you just map what you are already doing within the SDGs. We are seeing a lot of that. You say, “My fund maps the three SDGs,” but that does not mean your fund has changed its behaviour - and in fact it’s **not** going to change what it’s invested in, it’s **not** going to change what it’s asking companies to do. It is just mapping. What we need are strategies that will change the SDG outcomes specifically. It is about strategies that fix the SDGs. I agree with the question, but the challenge is when SDG investing is viewed as a thing in its own right.

To be very frank, there is a danger of another buzzword emerging, which would be ‘SDG-washing.’ We need dynamic strategies that fix problems, not static pictures that map test SDGs. They are two very different things.

Ben Yeoh

SDGs as targets, as forward-looking targets, are actually a good thing, a good framework, but saying SDG investing is taking your own strategy and then just mapping SDGs to it, is not necessarily what it’s all about. You do not want to fall into the trap of people saying, “Okay, I'm doing that,” when actually you haven't changed. I guess with this phrase or this idea of SDGs investing, you don’t want to have it as a marketing wash but something that is really happening.

Cary Krosinsky

I think that is the challenge with ESG data as well, so maybe that’s a good segue.

Ben Yeoh

Yes, that is a good segue into sustainability and ESG ratings overall which, like you say, is a cousin issue. I would like to mention that Cary wrote an article that has been published in various media: **Failure of Fund Sustainability Ratings**. It focuses particularly on the fund side, although it also has comments on general ESG data. What would people say about the data? Well, they would say we need simple additional measures for investors, encouragement of critical thinking, useful measures for development in the field, raising awareness, those types of things. I guess on the other side, they would say the data we have is oversimplified and that it misses a number of intangibles and is hard on the positive side. There is a low correlation between ratings agencies although again in some ways that could be good, in terms of different opinions.

We also have insufficient data. The fund ratings themselves and the holding space have nothing to do with strategy or necessarily process and philosophy. You have been relatively critical about this over the last year or two. Are there any two or three things you would want to highlight in your thinking about where we are on sustainability ratings and then maybe on the ESG ratings dataset?

Cary Krosinsky

I don’t want to come across as just being critical of everything, definitely not. I'm not just a critic. I like to think of myself as a realist. I’m in my third career now. I started as a computer science tech - what might now be called a developer – and then moved into building the world's first global institutional ownership databases and investor behaviour. I have an innate sense of the ownership of companies and I thought that the field was becoming commoditised in the mid-2000s, but I knew that I really cared about environmental and social issues. What if I had this ESG data and I mapped it into the ownership of funds? Would that tell us something interesting? People may not want to own the worst fund in the world from a pollution or a corruption standpoint, for example. The reality is that the data is not that informative. The first fund I ever looked at was the Jupiter Ecology Fund. We used that as a case study in our second book. If you're not giving a fund like that full points on what it's trying to do, then I think the methodology is questionable.

Having said that, I think all ESG data is useful. Again, the question with ESG is putting it in the right context: Are you using it for something that is useful in decision-making? Are you actually able to use it to make judgments, to be a good reference for what you are trying to achieve as an investor?

Ben posted a great article from the Wall Street Journal this week showing the variations in ESG ratings between Tesla and ExxonMobil, between various providers. That article says it all. It depends on your weighting, calculation, priorities of the issues you are looking at. No company is perfect and so the data can be a scatter plot, but the real scatter plot here is the issues. There are many issues within ESG and so, of course, there is a scatter plot. The scatter plot is correlated to the weightings of the issues.

Ben Yeoh

Yes, the world is complex. Many people like to use the word "intersectionality". There is a lot of intersectionality there. You do need a weighting and a priority process. So the word that I think comes across a lot is intentionality; is there intentionality? And that springs from philosophy, from process, and then within that, do you think this process is working? Is it maybe helping to implement some of that internal philosophy and intentionality?

I think if you do not have the intentionality - and some of these outcomes are maybe second or third or accidental, in a way that is completely random, then an over-focus on this, as you suggested, is perhaps wrong. There is valuable information from the data itself or what it's saying. I always point out that a lot of the information that powers the world is in this area of intangibles or ESG - the stuff that is hard to measure. But we know that it has an impact, so we do need further work on that.

Cary Krosinsky

I could not agree more about the importance of intentionality. Because the more you dive into ESG and financial performance - and I've been doing quite a bit of that lately - the more you realise that the missing link in what we're all trying to achieve is the lack of adequate intentionality from investors overall. It is fantastic that you are doing the work at RBC.

Ben Yeoh

That is a good link into narrowing in further, specifically on carbon and carbon data ESG. This is very interesting and I am obviously very passionate about many environmental matters, but carbon data is one of the intersectional things.

If you take the SDGs as your framework, there are 17 or so measures covering the world, and carbon data is obviously a very big, systemically important one. If you look at the work of energy historians, fossil fuels and energy have been a large driver of economic progress for quite some time, so they are going to stay around. Now there is a lot of talk about carbon footprints. There was a lot of chat about this at PRI recently: How good is carbon footprinting? Are scopes 1 and 2 enough? What about scope 3? This tilting towards scopes 1 and 2, is it even pointing in the same direction? There are a couple of people who are quite critical about that, and are saying that it is the wrong direction for some people to be going in, even though it is raising awareness. I am just wondering, from your perspective, what you are thinking about regarding the latest on carbon data, or any other kind of data questions that we are asking around these issues.

Cary Krosinsky

I think this goes back to the SDGs conversation. What are we trying to achieve? We need to start with what we are trying to achieve. We can measure anything for its own sake, but is there an actual purpose for the measurement?

I was often a harsh critic of the Montréal carbon pledge when that came out. I wrote a piece that I think was well received which is why I was invited to oversee the Climate Change Asset Owner Working Group for PRI in 2015. It featured some of the largest signatories and we came out with a very robust framework that I think has informed investors well. I am still happy with it, as I think many of the participants were.

Should everyone make a carbon footprint? Feel free to make a carbon footprint but maybe ask yourself why you are doing that.

King County, Washington, where Seattle is located, did a consumption inventory of the entire region years ago; it took two years and cost six figures. Ultimately, to measure the footprint of a region, you have to give half of the footprint of the flight to where the flight came from and the other half to Seattle. And the recommendations weren't any different; you could have predicted them from the start. Knowing Kering in Paris is another great company. I think it had a similar experience. If we are going to be honest about it, for all the measuring of environmental footprints, it's useful as evidence; there's nothing wrong with supporting your conclusions.

The question about this 'Wild West' of data that we are in - because we lack global mandatory auditable disclosure - the most important questions to start with are: what are you trying to achieve? Why are you creating this data? Is there a purpose? If there is a purpose, then you need data to fulfil that purpose, but the data should be used as follows:

a) at the system level, naturally SDGs are helpful, and

b) at the strategy level to see if your strategies are working.

–The danger here is that you are just taking a snapshot in time of something. It is just a picture on a wall that you can look at.

Ben Yeoh

There are two or three comments that I have heard on this, by thinkers in the field. First, the problem is you could be misled by a red herring; also, you get false precision, so gathering data to the nth degree is not the right thing. Second, some of it is as elusive as a unicorn. You are never really going to know because you cannot find it; it is mythical. Maybe you don't really need it in that sense. How are your 'unicorns' really going to save you?

I agree, at the system level, it's very interesting. You need to know if you are heading down the right path. At the strategy level, I think people who are well versed in this field can look at most portfolios and can actually tell you, roughly, what the carbon footprint is. You can tell from the industries. If I see a carbon footprint of most funds, without knowing their holdings, I can say roughly what they are holding and in what industries - because you know the people and you know, particularly on scopes 1 and 2, what the answers are. It is not to the degree of accuracy the data provides, so the question remains: is there enough data? But in some ways it might be the wrong question. Do you have anything else on the data point?

Cary Krosinsky

I was just going to say there are clearly data issues when it comes to certain regions of the world. So at best, we may have partial data. Regardless of that, it still comes back to: What would you do with the data if you had it?

Ben Yeoh

I am now going to get into the topic of divestment/investment. Then I will come back to the stewardship part of this, and spend a minute here on the data point, because I think some people might not know what I was talking about, carbon scope 1, carbon scope 2 and carbon scope 3.

Scopes 1 and 2 are more directional effects going into the company; scope 3 and beyond is more what you do with your products. The issue here is that we have very, very little data on scope 3 - maybe around about 5% or 10%, and it is very highly estimated. When you look at it at a systems level, scope 3 and beyond is probably around 60% - or at least a majority - of the carbon impact. We are dealing with uncertain data and scope on the minority of things and not really on the majority. This actually brings up a point that I think you have been mentioning in some of your posts, that actually maybe some of this is more on the demand side than the supply side. For example, we could do things on food waste, or sustainability, or bend behaviour, and we might be dealing with 60%-70% of the problem. Obviously, we have to think about the supply side, but which comes first? Supply or demand? Which will influence the other? This actually leads us neatly into thinking about divestment.

A lot of the divestment people would point out we need the social political noise, that without it the political will might be missing. Last week Al Gore had this nice little phrase about political will being a renewable resource, which was quite an interesting little pun. They really want to raise that awareness, but then might go on to say, "Okay, there's financial asset risk as well," and put it in there, and then say, "For cost of capital reasons we really want to bend these companies."

On the other side, I think people may say, "Well, you know what? Cost of capital may be important in theory, but with the amounts of capital we are talking about, it's probably not going to make that much of an impact. Systemically, what are you going to do if you still want to have concrete or aluminium? If you want to go and fly? If you want to build?" They are still talking about a point estimate of 50% of energy is going to be fossil fuel-based. So surely bending incumbents and engagements is more of the key here. And maybe we need some of both.

I think you do need that socio-political noise, but here I can say financial services is what I'm in. As a service, I provide a fund that is a divested fund and fossil fuel–free. I also provide our main fund, which really works on the engagement piece. When I speak to divestment people, I always emphasise what you can get from thoughtful fund managers or people in this field who are doing proper engagement, challenging companies and having this two-way dialogue. Because if you miss this piece out, we are just not going to win on this.

You wrote a good article on this previously, Cary. I think it is available as a free article on Responsible Investor and a couple of other places. Any other thoughts you might want to highlight?

Cary Krosinsky

BP likes to talk about this sort of energy and climate conundrum that we are moving towards and recognises the dilemma that we face as a global society. Even if we create aggressive agreed global goals, we are still going to have at least 50% of our energy demand come from fossil fuels in the year 2040. That is the extreme case of what those who have been looking into this expect. So the question is: What is the transition that we are trying to achieve? What does that actually look like, country by country? What is likely to continue?

The Carbon Tracker Initiative published a gas report years ago. It predicted an increase in gas use, with gas being cheapest from countries in the Middle East. It also made a very clear statement in that document that it is not in favour of blanket divestment. At times, it might say different things, but for me the failure that we have, for whatever reason, is a failure to educate people. We all care about climate change, unless we're psychopaths. None of us wants the world to get into a horrible state. So why have we not sat down and spent the time to understand the supply and demand dynamics that are at play - and what really can make a difference? I just think the people who have been pushing straight divestment have done an enormous disservice - and continue to do an enormous disservice - from the standpoint of educating people.

After Superstorm Sandy in New York City, one of the more liberal places in the world, one of the first things people wanted was for gas to get back to the stations so that they could get back to work. Many Americans drive. Some innate things are being missed here by those who just take out the megaphone and call for straight divestment. I have nothing against a good sell discipline however. Look at Norges Bank. It is extremely transparent and divests from companies at the end of a thoughtful investment process.

In our fourth book, we wrote that divestment is the logical approach to the end of an investment process. Any good investment process looks at what you should buy, and your asset allocation from different perspectives. You should decide who your partners are and who is doing a good job. If you own positions in companies, you have a responsibility and there are a set of responsibilities that stewardship calls for. Then there are times to sell things, but, we should try hard to anticipate what would happen when we follow up on what we are asking for. I have written endlessly about divestment. I don't want to beat it to death, but I just think it's an enormous failure of our industry to educate people as to what outcomes are possible from which strategies.

Ben Yeoh

Following on the point that it's about education - for our industry and even wider - I'm a big fan of Hans Rosling. I think many people would have heard of him. If you haven't already, read his posthumous book, written with his collaborator, called **Factfulness**. 90% of policymakers really **don't** know the facts about what's driving our world, whether you look at extreme poverty, inequality, literacy rates, health etc. It's interesting that this is maybe the purposeful role of good asset managers and investment managers. We meet with so many companies and industries that we are actually one group that sometimes does know some of these facts and trends. Because they're very salient to how we think about the world or where we might want to invest.

On this education point, I think that Yale has this ongoing survey on climate perception. They always spin it positively but I always look at that and feel really, really depressed. Because there is such a large percentage who don't believe in human-made climate change. I think it's hovering around 30%, give or take. If you look at the number of people who want to do anything about it, you're actually hovering around 50%, or actually the majority. I think the last number I saw was that 51% were still saying, "Nah, let's not bother." That is interesting about the education piece. It still has to be some sort of failure on that.

Cary Krosinsky

I could not agree more. Yes, we're close enough to 50% of Americans who want to do something about climate change. So for me, what that means is that climate change needs to be both politicised and depoliticised; that these are issues for everyone and so they should **not** be political. However, people are voting one way or the other and I am not sure either of the parties here are necessarily helping. There are many assumptions made. For that number to be 51% is **extremely** important and telling. Knowing that the majority of people are not looking for the calamity that climate science predicts, we are doing a real disservice to society to not have informed them about all the nuances, all the complications and the urgency. If that urgency is not shared by half of the public, that is just dazzling.

Ben Yeoh

Half the public of the largest economy in the world - that is problematic even before you then get into all of the questions about historic energy use and how developing economies - or, in Hans Rosling's terms, Tier Level 1 and 2 economies - how they're going to develop as a balance of everything. That intersectionality seems a long way behind.

I did have someone who joked about it, saying human beings are not designed for long-term thinking, long-term going over 10 or 20, maybe 50 years. So maybe there is something to that.

We have two kinds of comments here. I see we have somebody who agrees with that on divestment, when the conversation is not led by scientists or experts and just by misinformation. There is an interesting one here, quoting Raj from Preventable Surprises in a responsible investment article, saying, "Undoubtedly within the letter of the law to divest, but it is ethically and morally indefensible to be seeking financial advantage in selling off assets knowing full well the potentially catastrophic climate implications if they are subsequently developed. There are subtle implications on that, I think, on a country level".

Any comments on that?

Cary Krosinsky

Yes, there is interesting work going on in the impact investing space, which we're probably not going to talk about much today, but I'm fascinated with the metrics that TPG Rise is developing, perhaps the leading impact investor in the private equity space. One of the metrics it is looking at is the impact of positions after they are sold. I agree with the fact that we have to be holistic and systemic when we think about what we own and what the eventual outcomes are of those positions. So I get that.

The other way to look at this is: Who will own the stock if you sell it? What will the composition of the shareholder base of the organisation be if 5%-10% of investors divest? We are just going to end up with a shareholder base that is less responsible, most likely, until we have a situation where the enormous passive positions are divested. How are you going to get passive positions divested by BlackRock or the other asset investors? Without that even being thought through, you end up with a situation where, almost by definition, divestment will lead to less responsibility.

Sometimes it is useful to think things through, "If I get my way, what would happen?"

Ben Yeoh

I think this is thoughtful scenario analysis. Maybe this is something we should be asking people to think about earlier - and having that education, along with counter-factual thought experiments, which I know is a technique that is talked about. Maybe we just don't apply ourselves quite enough to that.

I had a conversation with a couple of people on Rio Tinto. Rio Tinto has essentially gone coal-free and it sold one set of assets to a set of Chinese owners and another set of assets to private equity and Indonesian owners. The conversation went something like this: "Well, from the point of view of the earth, or the point of view of responsibility of those coal mines - given that there is no way those coal mines are going to be shut down - they are going to be productive for many, many years. So you have probably done a kind of disservice in divesting." Now, obviously there is financial and other forms of intersectionality but if you took that divestment to the logical conclusion, this person was basically suggesting that those assets are now going to be run less well and in a less environmentally-friendly way, which is an interesting challenge.

Cary Krosinsky

Yes, is it useful to shuffle the chairs on the deck of the Titanic? That is the question coming to mind with this one.

Ben Yeoh

Very good analogy. We have another question:

"Any examples of investors divesting from fossil fuel-intensive companies leading to negative consequences on the actual company, for example, high cost of capital, less competitiveness?"

That is interesting. I will have a comment on that first. There is a saying if you come across any people involved in commodities for a long time, which is that “the cure for high prices is high prices.” And there is another saying which we have seen around coal to gas, which is, “Regardless of where there were Obama policies or Trump policies and we can argue about subsidies or subsequent things, that market forces are forcing a lot of coal into extinction just by where technology and the world is”.

When you look at investors divesting from fossil fuel-intensive companies, for example coal companies, which are the ones being divested most – were they heading to the wall anyway? It is interesting that you might want to divest because you are going to save yourself a lot of money. Yes, maybe cost of capital has gone up and they were not very competitive, but they were already not very competitive, which is why the writing is on the wall. Maybe this is the point on the passive side, that passive investors were the last owners on that.

Actually, we have seen it with some other companies, which have gone bankrupt in other ways, like Carillion, a U.K. company. Arguably, again, their business model was not sustainable - or at least that is what our form of capitalism has suggested. Actually, most active investors were not in the stock in the last year, because that is what they thought was going to happen. It was not a competitive business model.

Do you have any thoughts on that? Are there any examples of investors divesting and this actually having negative consequences for the company? If so, can we unpick that from the fact that these companies were not great to begin with?

Cary Krosinsky

For me it comes down to root cause, root strategy, root goals. If you were an asset owner, why would you have wanted to own Peabody Energy back in the early part of this decade - when the company was selling for $70 a share within the S&P 500 and you could tell that coal’s days were perhaps numbered? You had some value investors jumping in at $70 a share, famous large value investors and the company subsequently went bankrupt. Divestment is fine if you perceive correctly that there is a business case challenge, or that the company is not listening to you and is heading towards a problem? In general, one that you just won't tolerate for some particular reason - hopefully financial. I do think we are getting to the point where ESG issues are material when it comes to engagement, so that is great.

I am less concerned, frankly, about the consequences on the company. As you say - and I totally agree - whether it is effective altruism, or **Enlightenment Now** by Steven Pinker, or Hans Rosling or the others who are suggesting that the path of business has been largely good for people in energy poverty. ESG is both a way to make sure that we do not miss the bad side effects, but also that we to try to seize the opportunities. I am less concerned when a company fails if, perhaps, it should.

I am going to be frank here. I do not really like this conversation about the ‘just transition’. We don’t seem to mind when the music industry disappears or Walmart destroys small business. For some reason, we care about the consequences of the fossil fuel industry. I am not concerned about that. I think there are tons of jobs to be created in the transition, lots of reports showing that there are trillions of dollars to be made. The goal of investors is not to miss the transition; to help it, to encourage it, but yes, some companies will fail. This is the Jack Welch approach to running a business. You expect 20% of your people to be fired, because they are no longer useful. Maybe we should retrain them and make sure they have a good job, but I am less concerned about the companies that fall out of the system when maybe they should.

Ben Yeoh

I have heard that is what sustainable capitalism does. It makes bad ideas go bankrupt and good ideas flourish. Well, there probably is a valid question about retraining and things like that on a population basis. But maybe that is rightfully a governmental responsibility, with maybe some company responsibility for retraining.

We are not certain that we have any examples of divestment leading to negative consequences for a company where that company was not already facing tough consequences.

Now we have another question:

“To what degree are we expecting more from ESG finance than can be delivered on some of these issues, especially in the U.S. absence of policy and regulatory leadership, how much change can be really driven by the financial system without that central Government leadership and global collaboration?”

This actually goes back all the way to the roots of when I first was studying this 20 years ago. What is the responsibility of government? What is the responsibility of companies/business? What is the responsibility of civil society, NGOs and things like that? There are some interesting examples, like Bill Gates and his foundation. And you have the “no-impact” person. Interestingly, in terms of mainstream ESG finance, what can be delivered?

I guess one theory here is that, if you just simply direct your investment really well for sustainable long-term ideas, in the most holistic sense of the word, things are going to be in a better place in 10 or 20 years' time, systematic matters aside. Essentially, through that mechanism or tool, you get capital hopefully flowing to the better ideas and away from the weaker ideas.

Any comments on that in the absence of policy and regulatory leadership? How much can you expect ESG in the finance world to deliver or not?

Cary Krosinsky

First it is important to recognise where policy works and where it doesn't work. For those who haven't seen the video that Dr Ma Jun did for PRI last week, watch that video because China is very much becoming, in many ways, a global leader. It has put into place policies that most people are not aware of, such as pollution pricing mechanisms to actually transition the energy landscape in the country over time. Everyone in China knows they need to fix the air. These are becoming global competitiveness issues. China is putting into place mandatory disclosure on pollution from companies by 2020. I don't hear about that happening in most places.

There are places where policy can work and is that going to be a global competitiveness advantage in China? Regardless of the trade war noise, China is going to open up for investment to the world. That will happen very soon and what does that mean? That means this conversation becomes critically important in China, because investors have such a critical role to play when it comes to signalling to companies. All too often you hear about companies saying "Hey, we're putting all this sustainability stuff into place, but the investors don't care." So when investors care, when investors have those intentions around ESG that can encourage companies to change. If that intention is not there, then companies maybe won't put ESG issues high on their lists of all the things that they need to consider from a strategy perspective.

This nexus of companies and investors is so critical to make sure that business moves in the right direction.

That said, it is also important to recognise that companies cannot do everything. When you look at the global footprint, a large component of that - Ben, you and I have talked about this offline - the majority of the global footprint is in the hands of **people**, not companies. I think this is often overlooked, that it is the actual aggregate of people's decisions, their consumption, their investment. That is where the change can be made, when people change their understanding of what they are consuming, both from a standpoint of what they buy and where their money is deployed. That is where we can actually have more impact.

We can exaggerate what investment can do, but we can also underestimate the importance of what investment can do.

Ben Yeoh

Some good thoughts there on the China piece. You can check out that China video on Cary's Twitter and LinkedIn feeds. You can also get it straight from the PRI. I was listening recently to some of the initiatives China is undertaking and it was fascinating.

Let's move on to stewardship, both proxy voting and stewardship. Some people might say that proxy voting is only the tip of the iceberg but hopefully there is a lot of activity underneath. I think critics would say that there isn't anything happening underneath, so this is why they are very worried about proxy voting. Actually, over 90% of votes cast mainly during the proxy season are just in favour of everything that the company says, so where is this stewardship?

People like Dr Raj Thamotheram from Preventable Surprises would go so far as to say that we need **forceful stewardship**, which is probably a more extreme idea. This interaction with investors is quite interesting and goes through, I think, to the link to education, what we said about the ways consumers can alter their own behaviour. Maybe that is rightly something that governments need to be doing more about. That takes time. Look how long it has taken to get our education around tobacco right? We're talking decades. It is not something that happens overnight.

In terms of the proxy voting season, I wrote an FT op-ed piece about this. In group meetings amongst investors the questions asked are not, a lot of the time, about the long term. Because we, as a group, are very focused on what is happening over the shorter term - probably because of a lot of agency problems with incentives and where the price is. Even though, arguably, you are saying that in an efficient market hypothesis, all those long-term factors should be discounted back into the share price today, I think it is obviously true in perfect markets and a little bit flawed.

How much of an issue is it, do you think, that the votes aren't being cast this way? I am concerned that stewardship over the long term by the asset management industry has not been good enough, and is maybe not good enough to bend some of these things. To the earlier point, how much is it within business control and how much is it within government control? Any thoughts or observations on that comment or question?

Cary Krosinsky

This is an extremely complicated subject. It is related to the previous question we received, which was very nuanced and complex: At the end of the day, what can investors really achieve? What is in the toolbox? What are the options? The options really are limited. The options are: what can you buy? What do you decide to own as an investor, whether you are a fund manager or an asset owner? What do you own? Who are you partnering with in this goal for returns and outcomes? Once you do decide what to own, what are your responsibilities? At what point do you no longer want to own that instrument or that organisation?

That is a fairly limited set of tools. There is also awareness raising; there is advocacy with governments. There are a lot of things investors can do. Their own culture is extremely important, for example.

If we are going to ask about companies, we have to focus on what those questions are, so that they actually make an impact. The danger in advocacy and engagement and shareholder resolutions is that we are asking for things that are not meaningful; is a company really failing to do something that it should be doing. This is where the system level approach is useful.

I think the work of the UNEP Inquiry correctly identified the three main categories of gaps in the financial system: effectiveness, efficiency and resilience. The effectiveness gap refers to the fact that the ESG sustainability impact was not integrated into the system fully. Efficiency talks more to the financial services sector, which is getting more efficient. The resilience side, of course, is that can you stress test the system, or any part thereof.

Can companies do more? Transparency is increasing. We have all these rankings coming out from JUST Capital and the transition pathway initiative and the human rights benchmark work. We are getting increasing transparency: there are drones, there are satellites, there is machine learning. It is harder to hide and so the data will get better.

We have to make sure we are asking companies the right questions and we have to make sure we're also putting all the pieces of the system together to get the outcomes that we seek.

It is important to understand when something is helpful or not. The business case will be increasingly essential. When we talk about the things that are essential on the demand side, the energy transition is clearly one of the important components. Also essential is deforestation, as is the future of transportation. What can really transition, when and how? These sorts of questions:

How can we really reach the levels of efficiency that the IEA talks about in its two-degree scenario? How do we really do that? How efficient can buildings be? Can we really generate millions of new jobs from retrofitting? Is that really going to be financially viable or is the efficiency potential a myth? What is it that companies really can do to make a difference for their shareholders and for society?

When we get to root causes, then engagement, shareholder resolution and proxy voting will become aligned. Maybe at times we get too excited about this but without adequate checks and balances, the system will not work, so there has to be something in the middle.

Ben Yeoh

I was just going to end on a couple of things: where we go next, and stewardship. On the stewardship part, I was going to give this example:

I own a couple hundred million dollars of this $200 billion market cap company. I probably spent a cumulative 100 hours studying this company, meeting with them and aspects like that. When I did have one-to-one meetings with the CEO, it was interesting we had this two-way conversation. He asked me some questions and I asked him questions. We had a two-way dialogue. The IR person who was in the room said later, that it was the first meeting in the whole of this year where the CEO took notes. He listened. There were some things that had not been brought to his attention.

The other surprising thing is that you need to understand the business level and what is happening at that level, to ask these kind of stewardship questions. Because this is a man who spent thousands of hours - years and years - with his company and all of the minutiae from operations to everything else. If you come around with something that just doesn't make sense, then the response would be, "Well, why should I be listening to you about how I should be running my business?" I do think investors on the stewardship arm do have something to do and they can nudge businesses.

Arguably, some companies are ahead of the curve of where investors are, because they are much closer to their actual customer stakeholders. The only people who give them any money are customers. And if you don't give your customers what they are asking for, if you don't treat your employees well, they leave you. So all of these things matter.

Cary Krosinsky

Of course, there are always issues that will play out in 5-10 years, whereas investors and companies themselves have to prioritise short-term versus long-term goals. Investors have a role to play in that conversation as well.

Ben Yeoh

Definitely, because I think if we could just weight more of our questions to long-term, then you give this signal and similarly on the ESG-type questions. CFOs have told me, “I have just sat through hours and hours of meetings and no one has asked me anything which would come under the ESG heading. No one has asked me anything about my long-term plan. Therefore, is it just not important to you?” I have to say, no, it is not, and I have to say this still is an interesting challenge to the stewardship from the passive funds.

Where do you go next or what you can do? Follow us on LinkedIn as we have an archive webinar on people and purpose. For our team, our purpose is to add value to companies, to society and to our clients. That is why we do it through long-term responsible investing. We have an interesting seminar coming up with Croda. It is interesting because people say, “Croda is a chemicals company. How is a chemicals company part of sustainability?” But, to our previous conversation, they are going to be vitally important for the solutions of this world and we think Croda is doing a lot of good things.

The final question is: “You talked earlier about identifying the objectives of ESG investing, although I say investing overall. What are the appropriate goals? Are we being too ambitious or not ambitious enough?” I guess this intersects with the questions: What can investors or companies do? What are the appropriate goals? Any thoughts about that?

Cary Krosinsky

I will wrap up a few of the final things I wanted to say into this answer because they are related. I am hosting an event in Shenzhen, China, in November*. I think we are not being ambitious enough when we don’t think about the global nature of sustainable investing and where it is being practised. For China, this is a brand new conversation, for all the work of the government. We’re not being ambitious enough in thinking about the global opportunities, because they are very clear in China and countries like Indonesia, which are very complicated. I think we’re not being regionally thoughtful on a global basis as much as we might be.

One of the other things I am doing is working with a company called Real Impact Tracker where we have done an in-depth job on helping financial services organisations understand better what they could put into place as impactful strategies, how they can better understand their culture and what they can do to improve from a balanced score-carding perspective. We are very excited about that, because we are actually able to answer very specifically some of the questions we have been talking about today to help organisations prioritise their strategies.

Companies have a long history of transformation that is successful in many sectors and this can be a 5-10-year process. You have to first make sure that you are asking the right questions, develop your strategy and your capacity to execute and implement your strategy and then circle back after you see how you are doing and make sure you are continuing that. You need to ask the right questions.

The financial services sector has largely not done that yet, so this is where I think the opportunity lies. I think the financial services industry has an enormous opportunity to take hold of these issues and continue to drive their success by showing what they are capable of and actually solving these problems.

Ben Yeoh

I would just like to say thank you very much. That was an excellent conversation. Maybe we will have it again, because we just touched on some of these subjects. I would end by asking: What are the appropriate goals?

I think we should be creating wealth for all. I think wealth -generation is a great thing and I think we are not being ambitious **enough**. I think we can do that using the tools of ESG and sustainability.

*now in January

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