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# **2019 SFGFOA Annual Investment Seminar**

## **Socially responsible investing for local governments**

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**August 15, 2019**

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# Agenda

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- Introduction to Socially Responsible Investing
- What is it?
- Why should local governments care?
- Is the trend growing?
- How do you integrate it into your investment program?
- How will it alter your return?

# What is socially responsible investing?

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*Responsible investment is an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions, to better manage risk and generate sustainable, long-term returns.*

– UNPRI

**Principle 1:** We will incorporate ESG issues into investment analysis and decision-making processes.

**Principle 2:** We will be active owners and incorporate ESG issues into our ownership policies and practices.

**Principle 3:** We will seek appropriate disclosure on ESG issues by the entities in which we invest.

**Principle 4:** We will promote acceptance and implementation of the Principles within the investment industry.

**Principle 5:** We will work together to enhance our effectiveness in implementing the Principles.

**Principle 6:** We will each report on our activities and progress towards implementing the Principles.

Source: [UNPRI.org](https://www.unpri.org)

# Socially responsible investing (SRI) and local governments





# DAPL – The Dakota Access Pipeline

- 1,172 mile pipeline to transport oil from North Dakota to Illinois
- \$3.7 Billion project
- Project financed by 17 banks
- Companies working on the project financed by an additional 35 banks
- Standing Rock Sioux Tribe filed suit in federal court to stop the pipeline



## Why should local governments care?

**THE**  
**Nation.**

# These Cities Are Pulling Billions From the Banks That Support the Dakota Access Pipeline

From Seattle to San Francisco, Albuquerque to Raleigh, cities are joining the fight to defund the controversial pipeline.



# Terms used in responsible investing

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- **Socially Responsible Investing (SRI):** describes an investment approach where certain companies are excluded from your portfolio through negative screening of businesses that are involved in practices which are excluded for moral or ethical reasons
- **Environmental, Social and Governance (ESG):** attempts to categorize areas of concern into one of these categories and to measure the companies' relative responsiveness to these areas of sensitivity. These categories have been accepted globally so that they can be measured
- **Divestment:** using a screen in your investment process to exclude companies that are involved in certain activities (e.g. South Africa, guns, fossil fuels)
- **Impact Investing:** Investing in projects or companies with the purpose of making changes in practices or behaviors

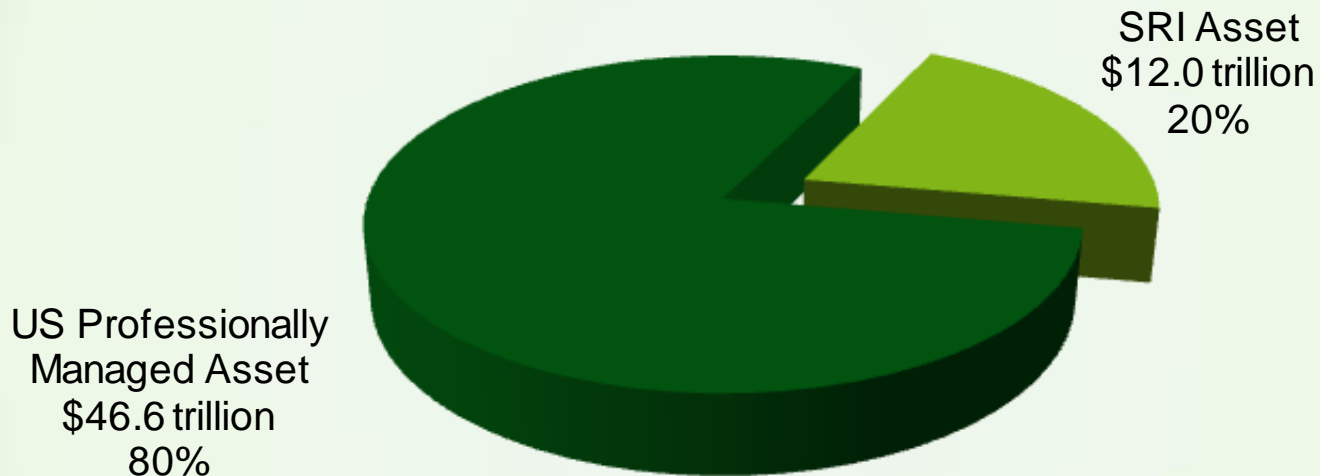


# Is the trend growing?

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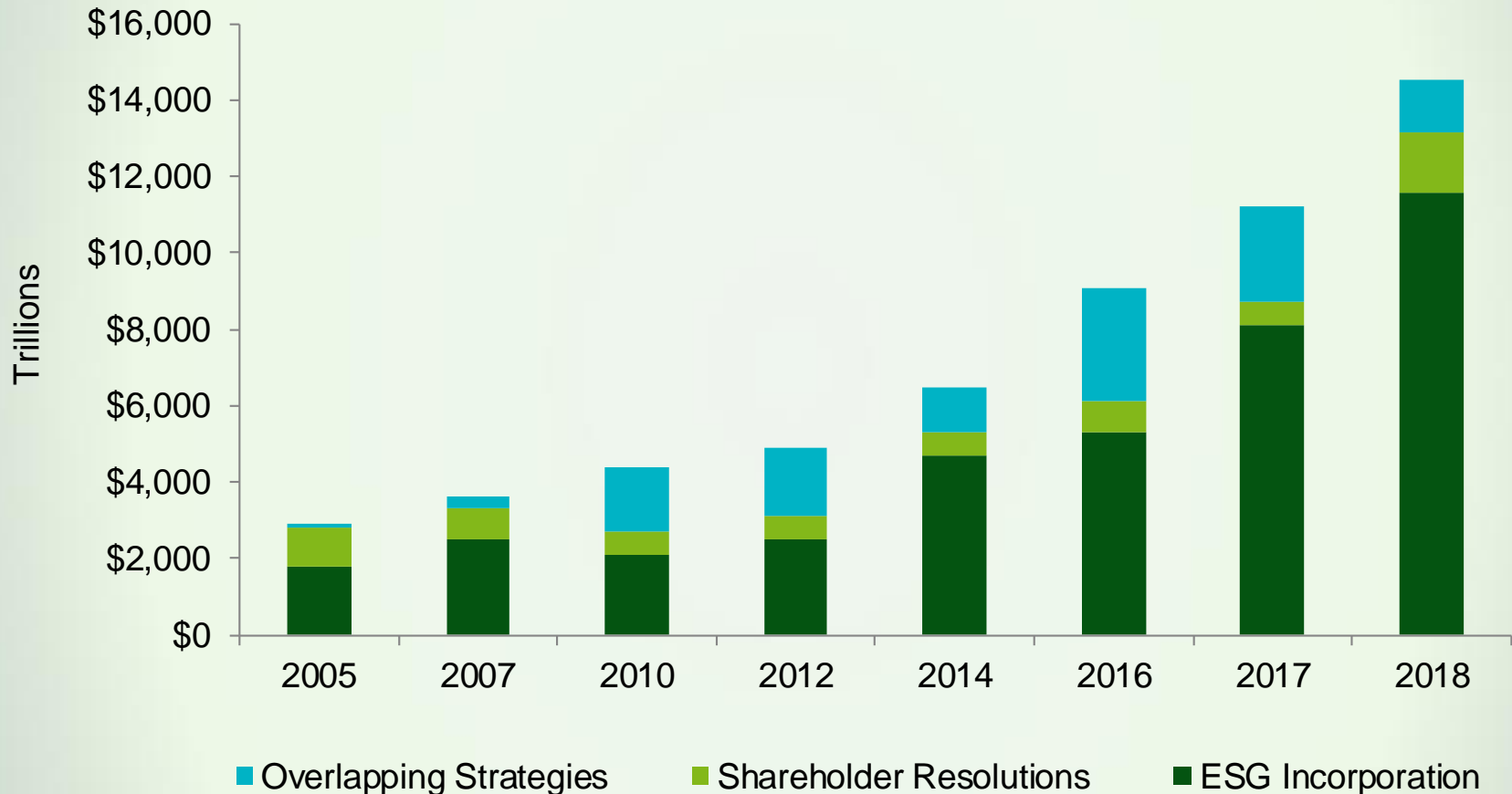
# Asset management and SRI

## SRI VS Total AUM



Source: US SIF Foundation, Report on US Sustainable , Responsible and Impact Investing Trends 2018

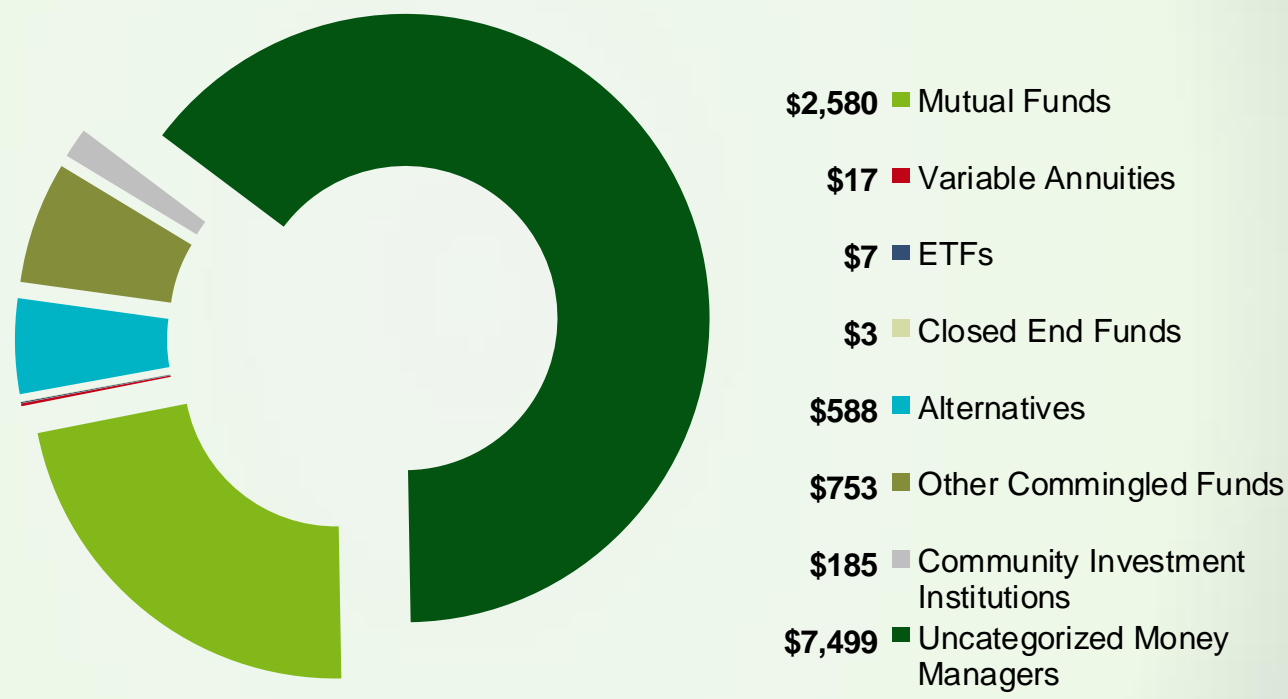
## Sustainable Investing Growth since 2014 - 33%



Source: US SIF Foundation, Report on US Sustainable , Responsible and Impact Investing Trends 2018

# SRI — Who manages the money?

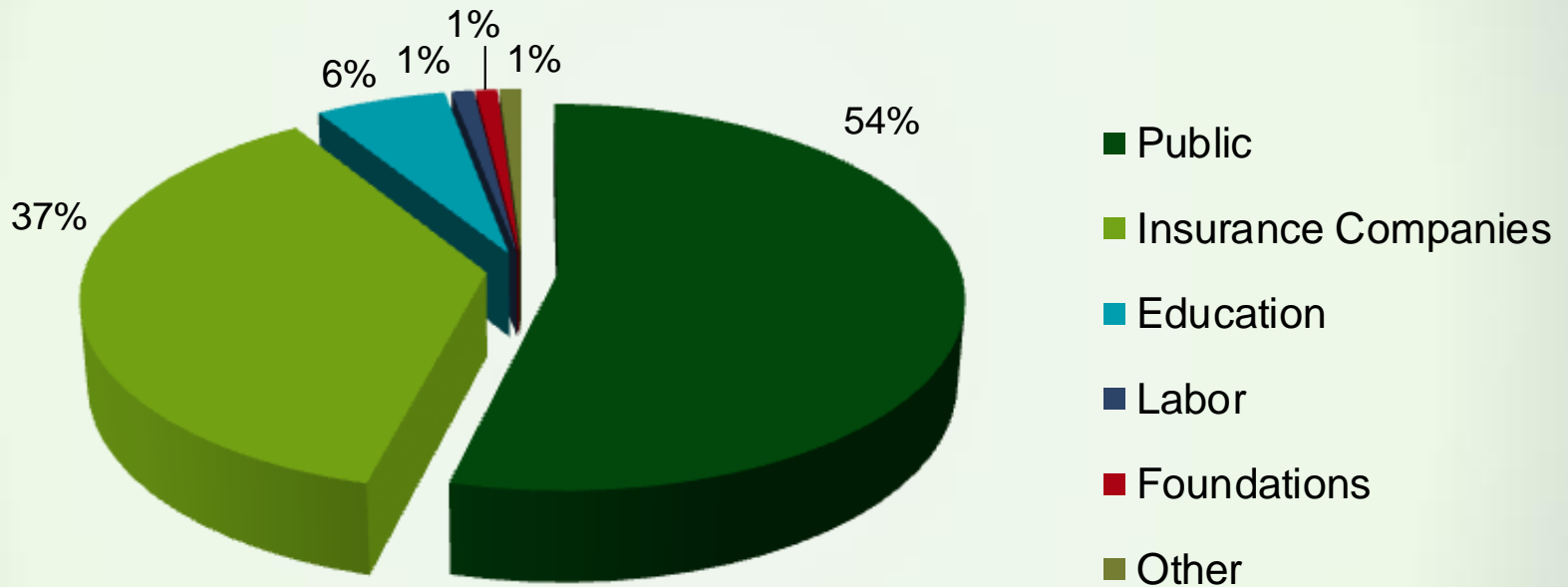
## Total assets under management (in trillions)



Source: US SIF Foundation, Report on US Sustainable , Responsible and Impact Investing Trends 2018

# SRI — where does the money come from?

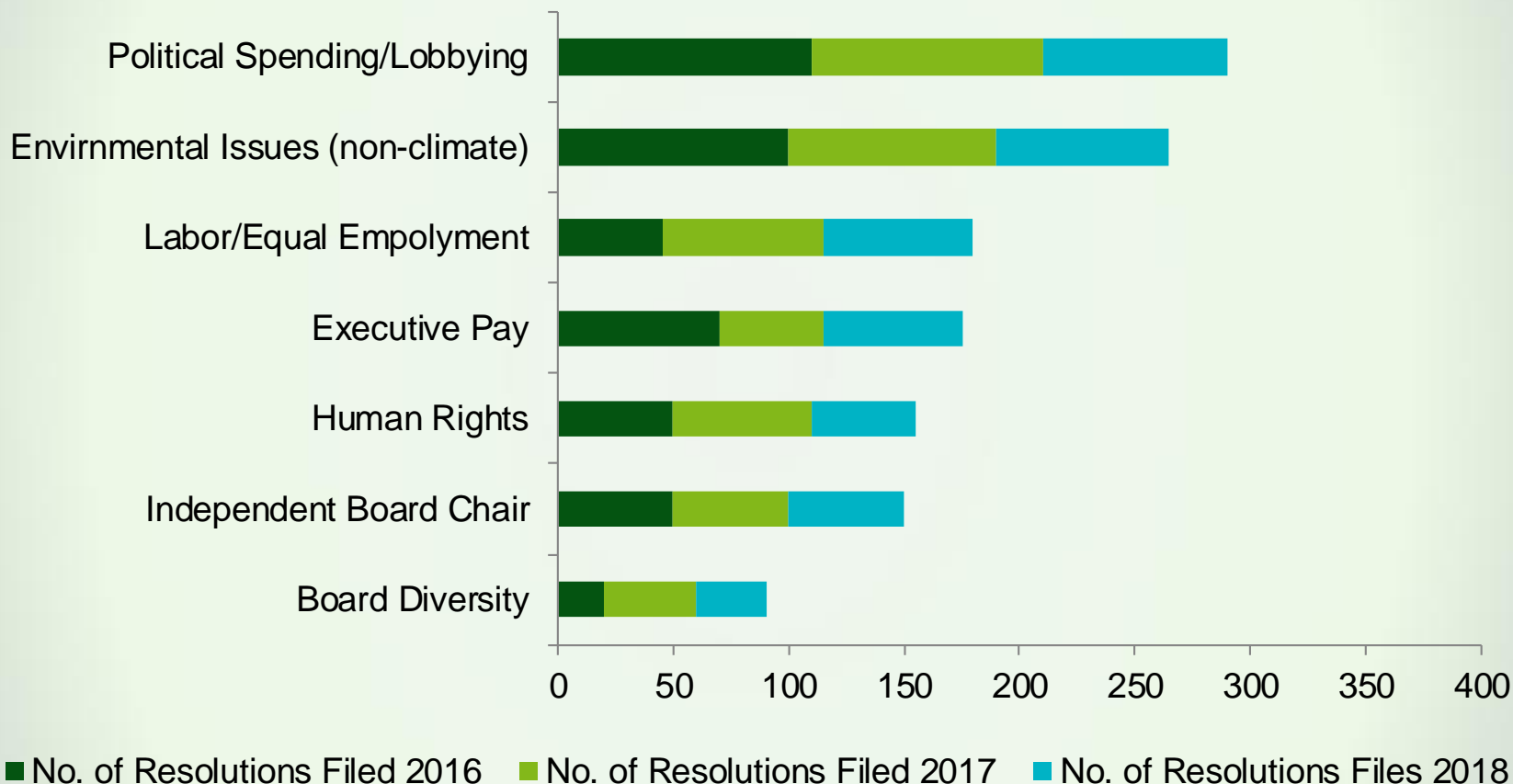
## Institutional Investors in ESG Assets



Source : US SIF 2018 Report on US Sustainable , Responsible and Impact Investing Trends

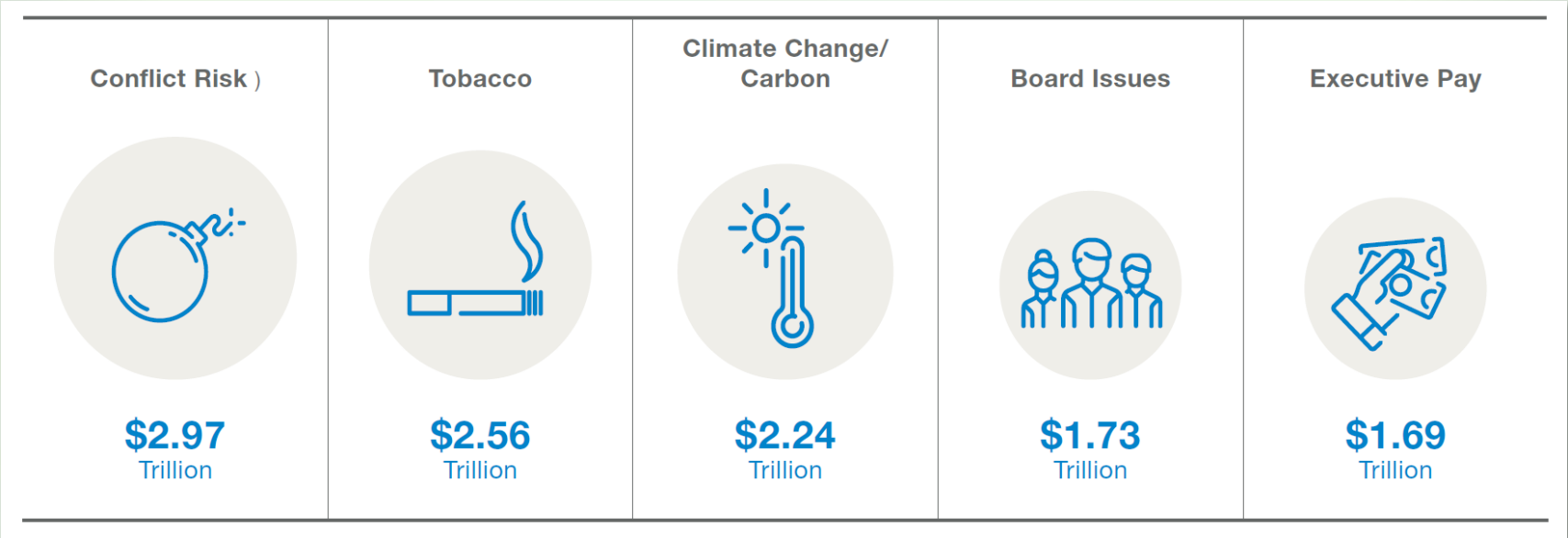


# Leading Environmental and social issues – shareholder proposals



Source: US SIF 2018 Report on US Sustainable, Responsible and Impact Investing Trends

# Top Specific ESG Criteria Institutional Investors, 2018



Source: US SIF 2018 Report on US Sustainable , Responsible and Impact Investing Trends

# How do you begin to incorporate ESG into your investment program?

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# Incorporating values into the investment policy

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- **Standard Investment Objectives**

- Safety
- Liquidity
- Yield
- Comply with state statutes
- Risk tolerances

- **Community Values**

- Values statement
- Community input
- Produce a policy statement

- **Reach agreement on approach**

- Screening
- ESG Risks
- Best in Class
- Impact

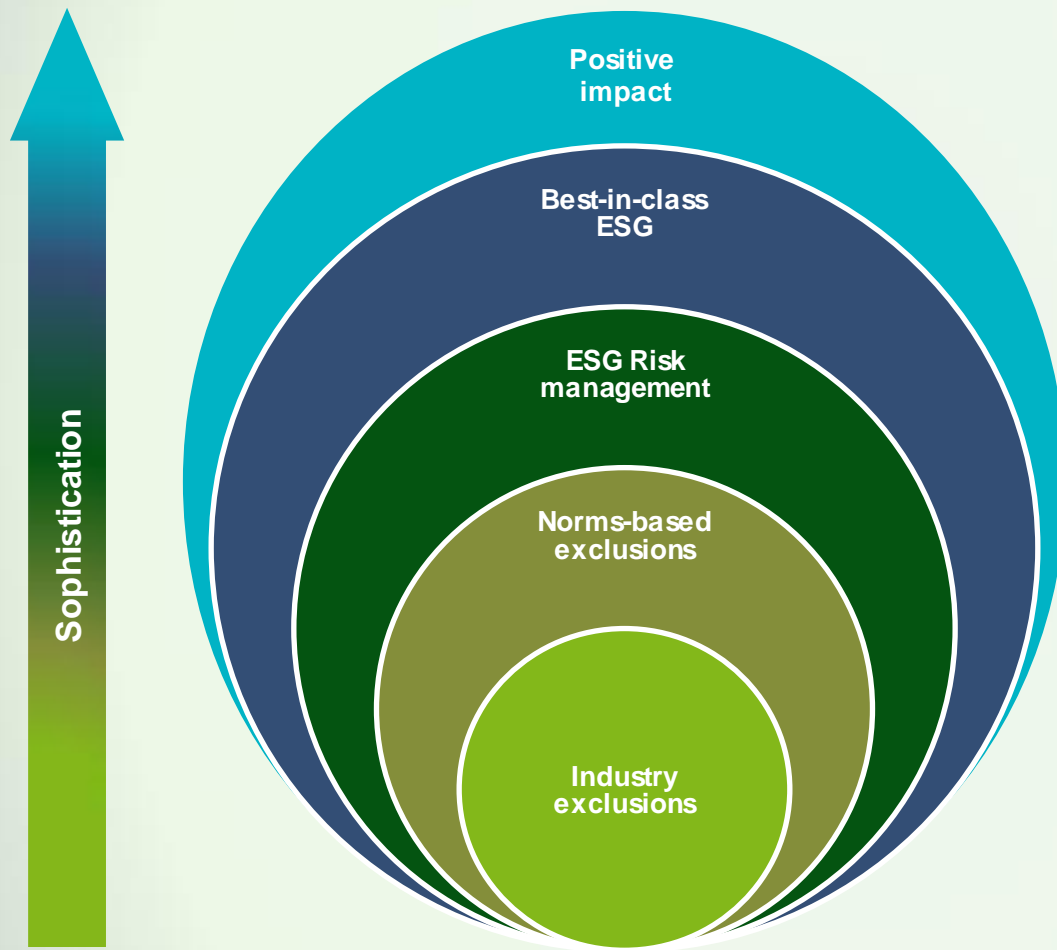
## Sample Policy Statement

**“If all of the other objectives required by state statutes and as outlined in this Investment Policy are met, investments in corporate securities and depository institutions will be evaluated for social and environmental concerns. Investments are encouraged in entities that support equality of rights regardless of sex, race, age, disability, or sexual orientation, as well as those issuers that practice environmentally sound and fair labor practices. In addition, Investments are encouraged in those issuers that maintain good governance practices and those issuers that conduct their businesses in a socially responsible manner. Investments are discouraged in entities that receive a significant portion of their revenues from the manufacturer or distribution of tobacco products, firearms, or weapons not used in our national defense.”**

For illustrative purposes only.



# ESG strategies



- Evidence a positive impact
- Engagement for impact
- Tilt to best-in-class ESG issuers
- Reduce carbon footprint
- Avoid worst-in-class ESG issuers
- Monitor carbon footprint
- Adherence to key global norms
- UN Global Compact, ILO principles
- Regulatory or legal reasons
- Alignment with ethical values

For illustrative purposes only.

# What's considered in ESG scores

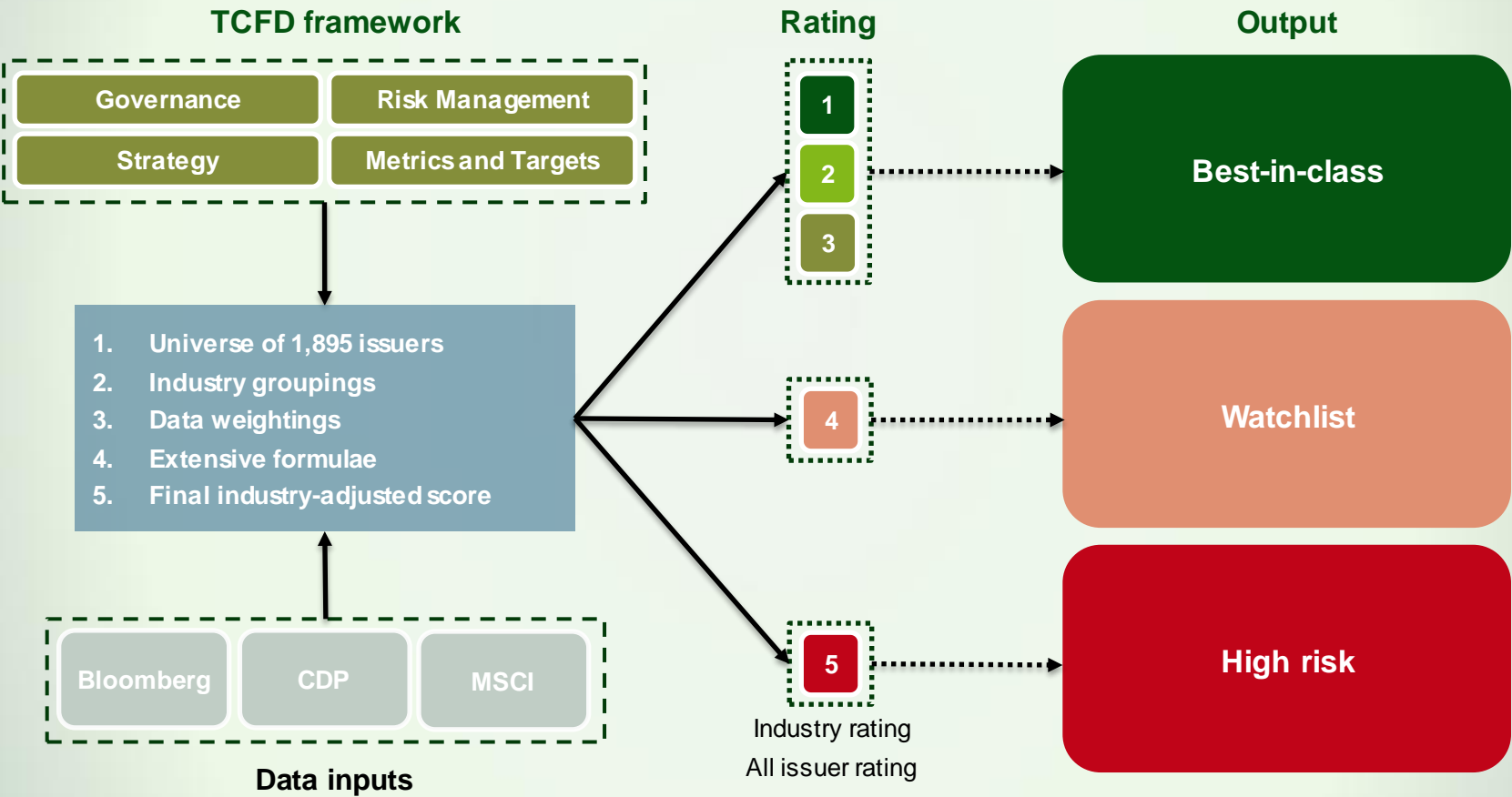
Use external ESG research to determine the key issues facing each sector and form part of materiality assessment.

ESG Overall Score Normalized industry-adjusted score 1-5								Ratings used in Risk Checklist
Environment Pillar Absolute score 1-5			Social Pillar Absolute score 1-5			Governance Pillar Absolute score 1-5		
Carbon	Natural Capital	Pollution	People	Products	Place	Corporate Governance	Behavior	ESG issues
Carbon Emissions	Water Stress	Toxic Emissions	Labor Management	Product Safety and Quality	Controversial Sourcing	Board	Business Ethics	
Carbon Vulnerability	Biodiversity and Land Use	Waste	Health & Safety	Chemical Safety		Pay	Anti-Competitive Practices	
Product Footprint	Raw Material Sourcing		Human Capital Development	Financial Product Safety		Ownership	Corruption and Instability	
Financing			Supply Chain	Privacy and Data Security		Accounting	Financial System Instability	
			Health and Demographic Risk	Responsible Investment			Tax Transparency	
Assessed category for all issuers								

Illustration only. Based on MSCI ESG ratings framework.

# Carbon risk management

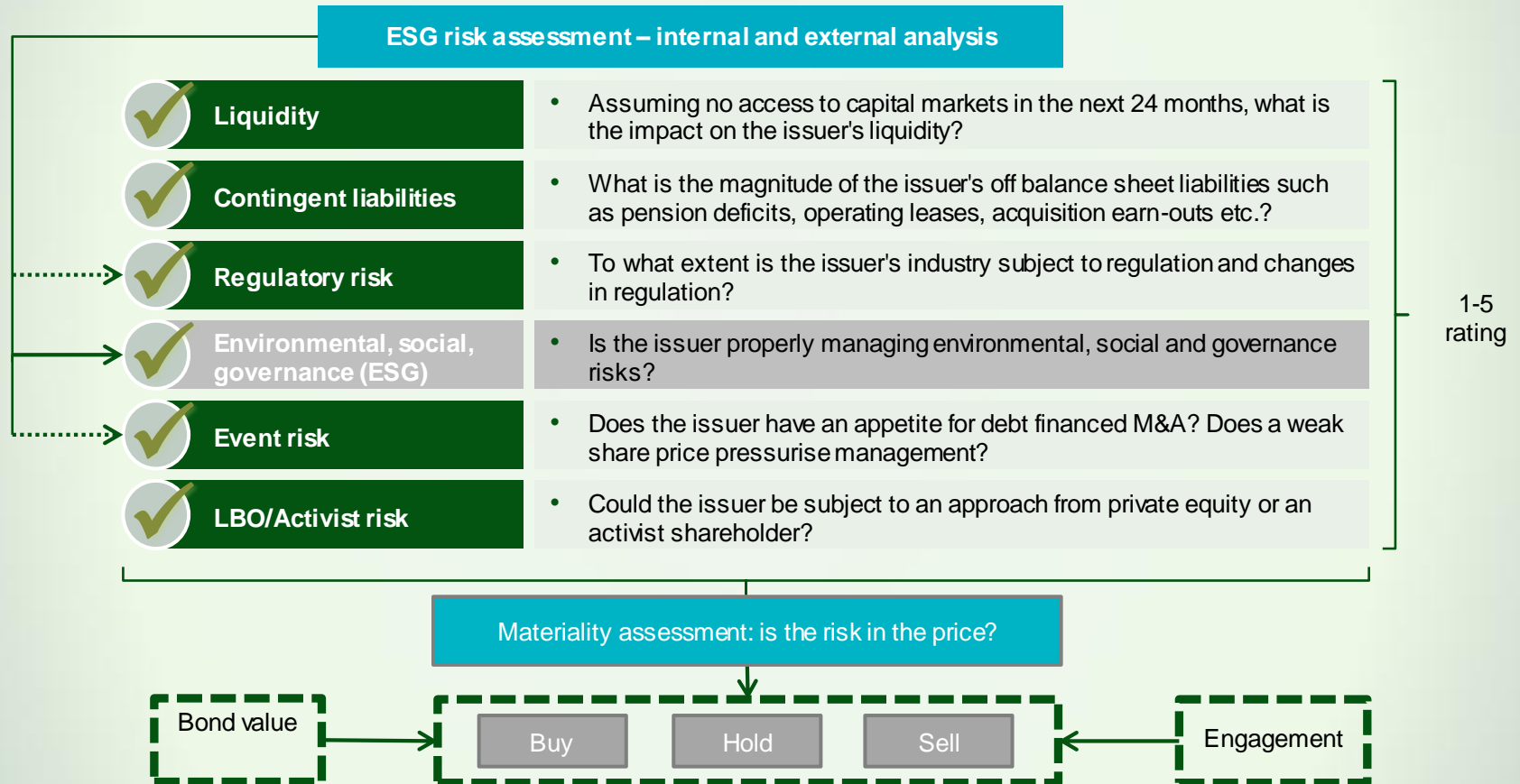
The Insight carbon risk model analyzes companies' carbon risk against the Task Force on Climate-related Financial Disclosures (TCFD) framework



Source: Insight Investment. For illustrative purposes only.

# Integrating ESG into the investment process

## ESG analysis included as part of our fundamental review of credits



Source: Insight Investment as of December 31, 2018. For illustrative purposes only.

# What about “Green Bonds”?

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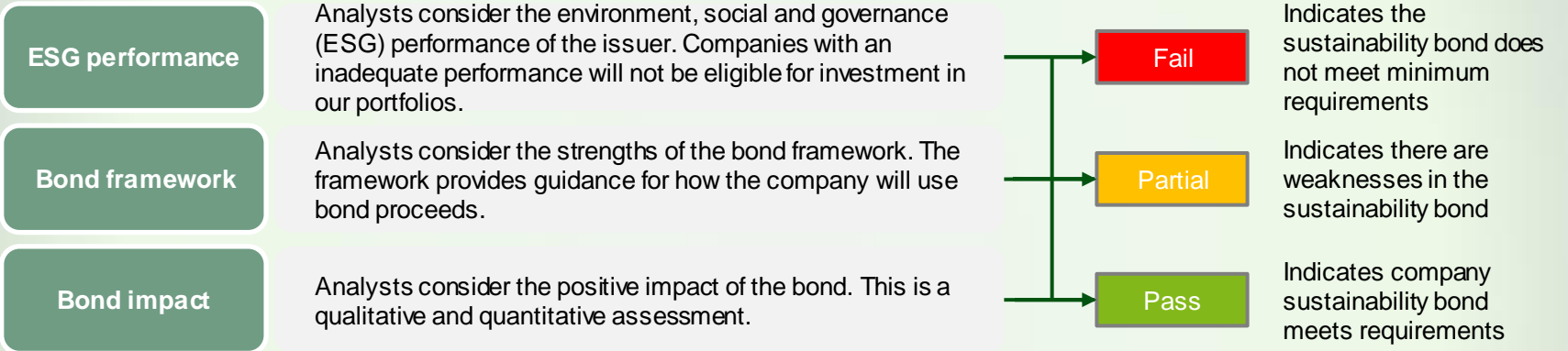
# Who is issuing Green Bonds?



Source: ICMA.org (Green-Social-Sustainable Bonds database)

# Assessing green bonds

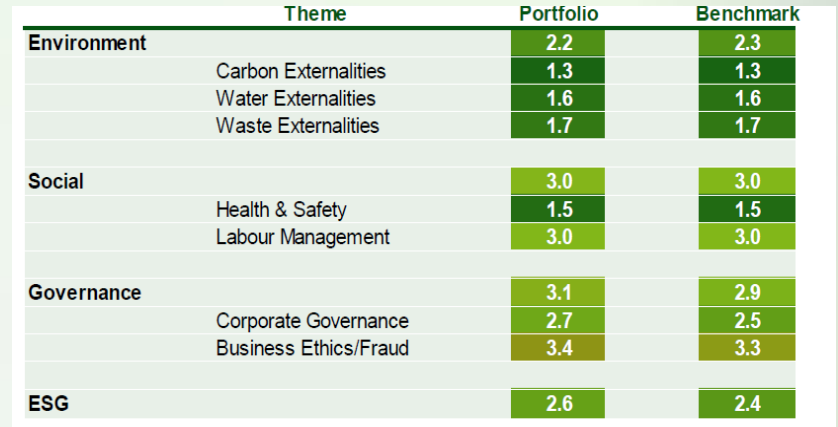
## Adopted a framework to evaluate ESG criteria of new sustainability bond issues



Corp Ticker	ISIN	Date of Assessment	Bond type	ESG performance met?	Bond framework criteria met?	Impact criteria met?	Traffic light score	Analyst assessment
Company 1	TBA	14/11/2017	Green	Yes	Yes	Yes	Green	The green hybrid proceeds will be used to finance and/or refinance Renewable Energy projects in the UK and Germany: onshore and offshore wind farms (1,136MW of capacity). Iberdrola has a best in class ESG rating and will report on the annual GHG emissions avoided (in tCO2e) in its Annual Sustainability Report.
Company 2	TBA	14/11/2017	Green	No	No	No	Red	The bond proceeds are to be used to fund retail lease and financing sales of Toyota's petrol-electric hybrid vehicle models. This "Green" bond will not change the usual operations of Toyota Motor Finance and the green credentials of these hybrid vehicles is questionable. Toyota also fails on the ESG front with "worst in class" governance practices and weak labour management practices.
Company 3	TBA	14/11/2017	Green	Yes	Yes	Yes	Green	Proceeds will be used to fund existing assets, 49% for renewable power (7 wind farms) and 51% for low carbon commercial property (5 CRE assets) totalling AUD 1.04bn of lending. The Commercial property must meet Climate Bonds Initiative's Climate Bonds Standards for low carbon and all have 5 star NABERS ratings (National Australian Built Environment Rating System). Westpac scores very well with MSCI with an Environment score of 9.2.

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## ESG key issue ratings



## Lowest rated ESG companies

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# Impact of screens on performance

Year	Index Total Return %	Ethical Screen Basis point difference	Ex –Fossil Fuels Basis point difference
2007	6.58	4	1
2008	2.71	-20	-17
2009	3.83	-34	-17
2010	15.09	14	32
2011	6.37	11	-18
2012	9.04	-11	-14
2013	1.90	18	5
2014	7.71	8	-3
2015	1.02	-5	38
2016	7.43	-16	41
Total	61.68	-31	48

Source: Insight Investment study using US Investment grade Corporate index, each period was for 12 months ending on June 30<sup>th</sup> of the year indicated.

# Summary

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- **Responsible investing and ESG investing have growing importance**
- **Local governments will be impacted**
- **Community values set the tone and direction of the changes**
- **Consensus must be reached before the investment program can be changed**
- **Many different approaches**
- **“Green Bonds” are also growing**

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