Global Biofuture Solutions
(866) 480-4405
results@gbs.earth

Measuring and Managing ESG to Attract Financing

By Cynthia Thyfault, Founder & CEO

In an exclusive Special to the Digest, Cynthia Thyfault, Global BioFuture Solutions, Founder and CEO shares a 2-Part Series on ESG Investing and the Bioeconomy. In this second part, we look at the importance of measuring and managing environmental, social, and governance criteria to attract financing.

Today's prevailing corporate responsibility strategies took shape in the final decades of the 20th century. In an age of intense competition, one of the key areas that differentiates companies is the public perception of its value system, which is demonstrated by how it handles its corporate social responsibility (CSR) – areas such as global warming, climate action, sustainability, adherence to diversity and inclusion principles, and building a kind and empathetic corporate image. Its roots go back to the 1050s and 60s and was developed as a way to determine the impact companies have on society. In 2010, the International Organization for Standardization (ISO), an independent nongovernmental organization established to develop a system of industry standards, created ISO 26000 to clarify the meaning of social responsibility and to help businesses translate their principles into actionable insights and provided guidance, not measuring results.

Corporate social responsibility today reflects a global mindset and increased attention on companies by consumers and investors alike, not just around their sustainability and climate action objectives, but also their ethics, how they treat their employees, and extend a helping hand to the community. What is now important in this current climate is a way to measure and manage the return on investment (ROI) measurement through the development of new international standards such as SASB (Sustainability Accounting Standards Board), TCFD (Taskforce on Climate-Related Financial Disclosures), and the United Nations (UN) 17 Goals of Sustainable Development, which are based around environmental, social, and governance ("ESG") criteria which are now a requirement for financing consideration for impact investors and ESG funds.

What Is the Difference Between CSR and ESG?

CSR, which stands for "corporate social responsibility," has been on the business radar for years and refers to "softer," qualitative issues. As time went by, social issues came into focus and measurement technologies and scientific reporting has also advanced and it now has become possible (and desirable) to quantify a company's sustainability and societal impact, using metrics that matter to investors.

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Ten years ago, ESG was a grassroots initiative. Today, it is top-down. ESG issues are important to businesses that prioritize sustainability, and to investors looking for socially responsible investment opportunities. To attain ESG status, organizations must build an ESG program, create awareness with an ESG rating, make this information publicly accessible, and hit metrics that matter to forward-thinking investors.

ESG investors Now Have Deep Pockets

In spite of all of the 2020 challenges that the Covid pandemic brought to the business community, it was a record year for ESG investments. According to Blackrock's first Global Client Sustainable Investing Survey, $23 billion was invested in ESG companies in 2020, compared to $450 million in 2019. Further, half of the C-suite respondents wished to double their organizations' exposure to sustainable assets within five years.

It turns out, sustainability is just as good for the bottom line as it is for society and the planet. According to Barron's, in 2020, ESG stocks outperformed the stock market by 46% in the U.S., by 20% in Europe, and by 77% in Asia.

Investors Now Have Better Tools to Manage ESG Investments

A wide variety of business services for ESG investors have been created or expanded to measure and manage the evaluation and quantification of ESG data. BlackRock has recently released Aladdin Climate, a new feature of BlackRock's Aladdin portfolio management software that helps advisors quantify climate risk and low-carbon opportunities in portfolios, along with Moody's data on physical climate change risks and MSCI's climate change scenario analysis, provided by Carbon Delta, which it acquired in late 2019. These new data points and features are helping financial advisors and investors become much more knowledgeable about ESG factors and socially responsible investments and allowing them to make more rapid investment decisions

Why Is ESG Important to the SEC?

The United States does not have a mandated and standardized ESG disclosure framework on the books today – but that is likely to change soon; and in the meantime, high performing companies are finding ways to build resilience, satisfy investors, and be transparent with their customers.

There's every reason to believe these issues will be part of the federal regulatory landscape in 2021 and beyond. The new head of the Biden Administration's Securities and Exchange Commission (SEC), Gary Gensler, "is likely to heavily reform and broaden ESG investing and corporate disclosure rules in the U.S.," according to NASDAQ. The acting committee chair noted that investors and the public need better information about how companies are managing climate risks, adding, notably, "Realistically, that can happen only through mandatory public disclosure."

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Despite the lack of a standardized federal disclosure framework, many state-level laws exist. The best-known example is California's Public Employees' Retirement System (CalPERS) and its State Teachers' Retirement System (CalSTRS), which use ESG factors to direct its massive pension investments. Elsewhere, for example, Illinois' Sustainable Investing Act became effective January 2020; Massachusetts, Minnesota, New Jersey, New York, and Vermont all have pending legislation limiting fossil fuel investment from publicly managed funds, according to Bloomberg Law.

Outside the U.S., regulation abounds for companies that operate in or sell to the E.U. and England. The European Parliament, for example, finalized a landmark ESG agreement in December 2020 establishing standards to determine whether an economic activity is environmentally sustainable. According to Compliance Week: "Under the [ESG agreement], all financial products that claim to be 'sustainable' will have to prove it based on strict criteria, supported by scientific evidence and drawn up by scientists and academics."

Rules of Engagement for ESG

Below are the top five strategies I am recommending to companies to get in and stay in this new ESG arena:

1. Ensure that your company's ESG data and strategy are easy to access and find in one single place on your website. You want to get credit for all of the great work you are doing.
2. Discuss your ESG positioning internally and develop strategies and written materials to share with your stakeholders. Demonstrate that your company is going the extra mile and that you are planning now and into the future as the ESG standards continue to grow and develop.
3. Understand your company's ESG positioning and how it is being evaluated relative to a peer set. Have a good understanding of what your peers are doing in terms of ESG disclosure and strategy. If you are not at parity, there are probably areas of improvement you can make to elevate your ESG strategy.
4. Engaging with an ESG ratings agency should be seen as a learning process; ESG ratings have been developed based on interactions with investors and the companies themselves. Understand which ESG ratings are most important to investors and ensure they have the correct data available.
5. ESG is creating a new language that we all have to learn and somehow develop. Financial markets are fast-moving, and you need to move with them. This is a new language that you must learn and become fluent in it to succeed in today's financial arena.

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