

ESG INTEGRATION

21-G-113

INVESTMENT MANAGEMENT ANNUAL REPORT

1. That the Report to the Investment Board concerning the 2020 Investment Management Annual Report and approved by the Investment Board on April 7, 2021, be received for information.
2. That staff in the Finance Department provide a presentation to City Council concerning the activities of the prudent Investment Board.
3. That staff in the Finance Department report back by way of memorandum regarding the longer term, historical information on the performance of the full Investment Portfolio.
4. That staff in the Finance Department and the Investment Board investigate the feasibility of adopting a Responsible Investment Screening Process for the City's Investment Portfolio using a structure of environmental, social and governance (ESG) factors and report back to the Finance and Corporate Services Committee in 2022.

This matter was recommended (Section "D") to City Council for consideration of adoption at its meeting to be held on 5/10/2021.

CFA INSTITUTE



GUIDANCE AND CASE STUDIES FOR ESG INTEGRATION: EQUITIES AND FIXED INCOME

WHAT ESG INTEGRATION IS NOT

ESG integration does not mean that:

- investment in certain sectors, countries, and companies is prohibited;
- portfolio returns are sacrificed to perform ESG integration techniques;
- immaterial ESG factors affect investment decisions and traditional financial factors are ignored; or
- major changes to your investment process are necessary.

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EXECUTIVE SUMMARY

Portfolio managers and analysts are increasingly incorporating ESG factors into their investment analyses and processes. However, ESG integration remains in its relative infancy, with investors and analysts calling for more guidance on exactly “how” they can “do ESG” and integrate ESG data into their analysis.

CFA Institute and Principles for Responsible Investment (PRI) set out to create a best-practice report (*Guidance and Case Studies for ESG Integration: Equities and Fixed Income*) and three regional reports [one for the Americas (AMER), one for Asia-Pacific (APAC), and one for Europe, the Middle East, and Africa (EMEA)] to help investors understand how they can better integrate ESG factors into their equity, corporate bond, and sovereign debt portfolios. We are able to achieve this goal by:

- surveying 1,100 financial professionals, predominantly CFA members, around the world;
- running 23 workshops in 17 major markets (see the table on the next page);
- interviewing many practitioners and stakeholders;
- publishing more than 30 case studies written by equity and fixed-income practitioners;
- analyzing Bloomberg’s ESG company disclosure scores; and
- reviewing data from the PRI reporting framework, the largest global database of information on investors’ ESG practices.

ESG INTEGRATION FRAMEWORK

FIGURE 1: THE ESG INTEGRATION FRAMEWORK



COMPONENTS

1. Research:

- *Information gathering:* Practitioners gather financial and ESG information from multiple sources (including but not limited to company reports and third-party investment research).
- *Materiality analysis:* Practitioners analyze relevant financial and ESG information to identify material financial and ESG factors affecting a company, sector, and/or country.
- *Active ownership assessment:* Practitioners discuss material traditional financial factors and ESG factors with companies/issuers and monitor the outcome of engagement and/or voting activities.

2. Security and portfolio analysis: Practitioners assess the impact of material financial and ESG factors on the corporate and investment performance of a company, sector, country, and/or portfolio. This can lead to adjustments to their forecasted financials, valuation-model variables, valuation multiples, forecasted financial ratios, internal credit assessments, and/or portfolio weightings (see “Qualitative Analysis versus Quantitative Analysis” for more information).

3. Investment decision: The material traditional financial factors and ESG factors identified and assessed influence a decision to either buy/increase weighting, hold/maintain weighting, sell/decrease weighting, or do nothing/not invest.

NEXT STEPS

IPS/IP Update