Responsible Investment: *Drivers, Trends and Actions to Take in Response to Covid-19*

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Since December 2019, headlines around the world have been dominated by one thing: Coronavirus (or Covid-19). The scale and severity of the pandemic means that it has (understandably) taken centre stage in every forum. Discussions cover the facts and figures, the rate of spread, attempts at solutions, and the likely impacts for economies. In the context of the short- and long-term impacts of the pandemic, the sheer number-as well as the breadth and depth of these conversations- comes as no surprise to many investors. It might surprise you though, to learn that what these conversations are actually about - at their core - is a rethinking of current economic models, specifically those of asset allocation and ownership. As their fundamental foundations, the discussions we are having around how to address Covid-19, are conversations about implementing responsible investment approaches.

Indeed, the COVID-19 pandemic – and the global response to it – is a serious threat not only to global health, but to our communities, our economies and our investments. As long-term stewards of capital, investors can and should act to help reduce harmful short- and long-term impacts of the pandemic. In other words, they should be making investment decisions and practicing stewardship in a way that is aligned to a responsible investment approach.

What is Responsible Investment?

Responsible investment (RI) is an approach to investment which prioritises the generation of sustainable long-term financial returns, achieved through strategies and practices that incorporate environmental, social and governance (ESG) factors into investment decisions and active ownership (engagement).

RI argues that to ignore ESG factors is to ignore risks and opportunities that have a material effect on the returns delivered to clients and beneficiaries (see Covid-19 as the latest in a long list of examples of ESG issues impacting financial returns). RI presents a holistic approach to investment that aims to include any information that could be material to investment performance.

In practical terms, what this means is not that investors need rule out investment in any particular sector or company, but that ESG information is included in investment decision-making to ensure that all relevant factors are accounted for when assessing risk and return, to maximise shareholder and stakeholder return.

As such, in addressing the impacts of the Covid-19 pandemic, many investors are finding themselves intuitively practicing responsible investment – with many others fast realising that they too should be doing so!

What is Driving the Global Uptake of this Approach?

The Covid-19 pandemic is only one example of a complex ESG issue that has generated significant financial implications. And while this latest ESG crisis has shifted the needle for many investors, far more have already been practicing ESG integration approaches as standard. According to a recent Morgan Stanley report, 84% of asset owners globally are pursuing or considering investing approaches that integrate ESG.

The rationale behind the mainstreaming of the responsible investment approach worldwide can be boiled down to three key factors: materiality; market demand, and; regulation.

Academic studies consistently demonstrate that effective integration of material ESG factors into company operations can lead to meeting or exceeding market benchmarks, with these companies experiencing more effective risk management, lower costs of capital, better loan spreads and even improved customer loyalty. The latter is especially powerful in a market where 86% of millennials stated in a recent global investment study that they believe sustainable investing is important, a view shared by 79% and 67% of GenX and baby boomer investors, respectively. Arguably, the investors of today – and, importantly, of tomorrow – are demanding more from their investments than mere short-term financial performance. What they are looking for is a more holistic approach to investing.

Internationally, the regulatory environment is responding with vigour. More than 700 responsible investment-related regulations are currently in play around the world. Of those, more than half have been instituted over the past five years. The regulations in place and those proposed reflect an inevitable build-up of pressure from the market in recognition of the fact that the materiality of ESG integration feeds directly into fiduciary duty – because ESG issues can affect the value of investments, investors have a legal duty to their clients and beneficiaries to integrate ESG considerations into their investment processes. The practice of regulators within the UAE, for example, are already aligned to this trend, with bodies such as ADGM prioritising sustainability within their regulatory focus for the financial services sector.

What Does a Responsible Investor Response to Covid-19 Look Like?

The COVID-19 crisis impacts all investors and their beneficiaries regardless of holdings, strategy or role in the investment chain. Responses to the crisis must therefore be predicated on the basis of systemic integrity and long-term universal returns being more important than relative company performance.

Outflows from funds have seen some asset owners and managers facing liquidity pressures, as well as declining fee revenues resulting from those outflows and from overall market falls. Despite this, responsible investors can and should respond by using their influence with companies and governments, and through their investment decisions. They should be supporting sustainable companies through this crisis – in the interests of public health and long-term economic performance – even if that limits short-term returns.

Notwithstanding, the roles and responsibilities of companies and governments in managing the short- and long-term impacts of the pandemic, and the role of investors in sending the correct signals to the market in this regard, cannot be overemphasised.

To this end, an immediate, robust response to the Covid-19 crisis is needed across the global economy. For investors, this takes the form of seven key action points:

Action 1: Engage companies that are failing in their crisis management

Action 2: Engage where other harm is being hidden behind, or worsened by, the crisis

Action 3: Re-prioritise engagement on other topics

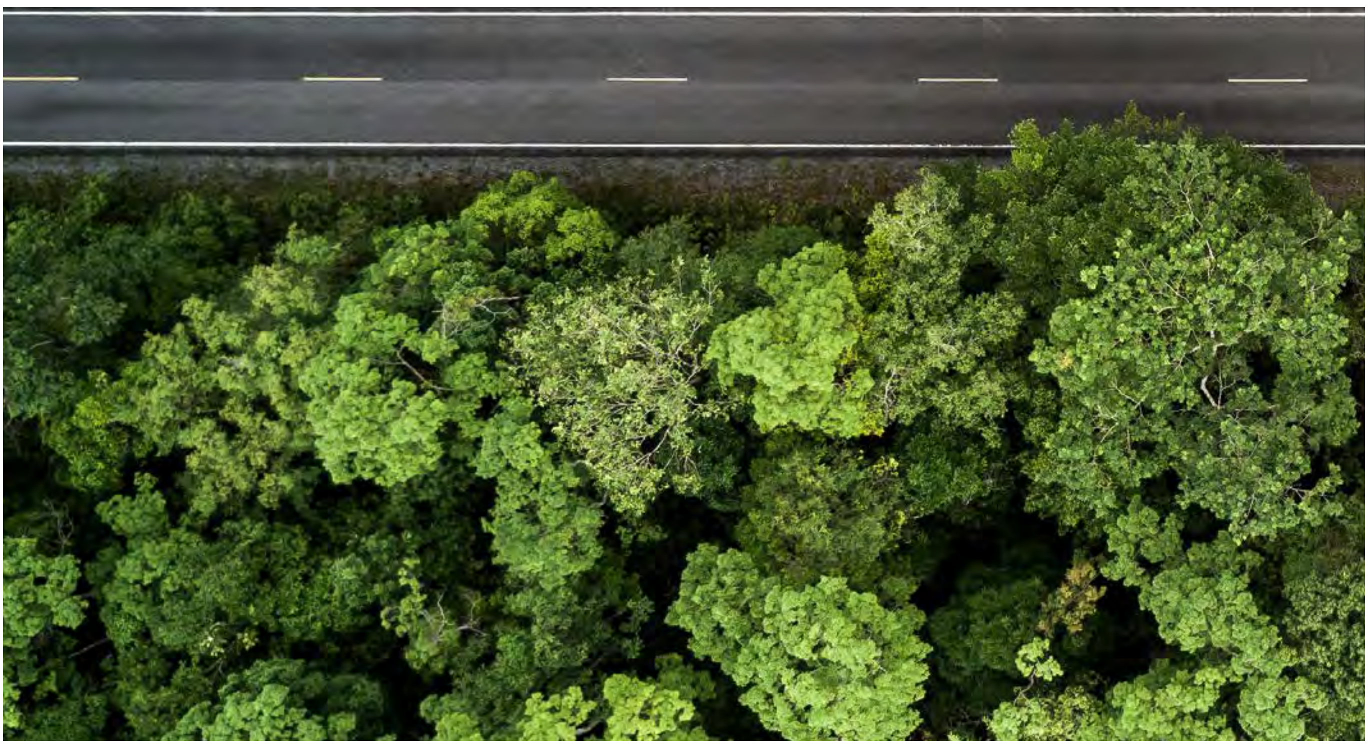
Action 4: Publicly support an economy-wide response

Action 5: Participate in virtual AGMs

Action 6: Be receptive to requests for financial support

Action 7: Maintain a long-term focus in investment decision making

Longer-term, the crisis will continue to raise broader questions on how our financial system is structured to respond to such threats. When



the public health emergency of Covid-19 starts to subside, the approach to recovery must be aligned with other key priorities: in particular, the climate emergency and global levels of inequality. The crisis has highlighted the attention that social issues, including emerging labour practices, must receive in the responsible investment community.

In this context, the practical face of responsible investment takes the form of reporting on and managing for long-term environmental, social and governance outcomes during the survival and recovery phases of this crisis. This is important for a number of reasons:

• To enable economies to enter the recovery phase with a clear view of the financial and non-financial baseline from which to start to rebuilding

• To ensure the optimal protection of human, natural and capital resources which will enable faster growth during recovery phase

• To prevent and mitigate the effects of other social and environmental crises that may emerge post Covid-19

As we continue to face such issues, a review is needed of the structure and readiness of markets to respond to such economic and societal threats, including how to better prioritise and address key systemic issues over narrower company- or portfolio-specific ones, and how to increase collaboration between investors.

Now is the time for responsible investors to embrace decisive, collective action. It's time to demonstrate that the market can respond to the immediate crisis while simultaneously setting in place a recovery plan which prioritises social and environmental sustainability. In the coming months, it will be critical not to allow the current circumstance to distract us as a global community from the ultimate objective of sustainable, inclusive economies and resultant prosperous societies.

For more detail on these action points, as well as guidance on other Responsible Investment-related issues, visit www.unpri.org/covid-19

The PRI is the world's leading proponent of responsible investment.

It works to understand the investment implications of environmental, social and governance (ESG) factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The PRI is truly independent. It encourages investors to use responsible investment to enhance returns and better manage risks, but does not operate for its own profit; it engages with global policymakers but is not associated with any government; it is supported by, but not part of, the United Nations.

For more information, feel free to check out www.unpri.org