pi ESG CLUB

Climate change is not just an environmental issue, it has huge influence over our human rights. This month's ESG Club looks at why.

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RESEARCH REVEALS BIG BANKS ARE FALLING SHORT ON CLIMATE TARGETS

Share Action uncovers disappointing sustainability targets at some of Europe's largest lenders. *Andrew Holt* reports.

New analysis has exposed what looks like unambitious and incoherent climate targets at Europe's richest banks.
This means these lenders are unlikely to succeed in shifting enough financing away from fossil fuels and towards renewable power, green infrastructure and technologies at the speed and scale needed to prevent a dangerously overheated world.
The research by responsible investment campaigner Share Action, which analysed targets for reducing emissions from financing activities and those for increasing sustainable investment, found that overall banks' decarbonisation goals are too narrow.
They also discovered that their sustainable finance targets are not rooted in "robust methodology" and are not sufficiently aligned with one another.
Share Action's analysis showed that 18 of the continent's largest 20 banks, including HSBC, Barclays and BNP Paribas, are not on track to meet the $10-to-$1 ratio of green investment to fossil fuels investment the International Energy Agency says is needed by 2030.
It found that just Natwest and Nordea can realistically be expected to meet this milestone based on the sustainable finance targets they have set.
Despite sustainable finance being a critical driver to achieve emissions reductions, Share Action said that banks are "inconsistent" in their approach to target-setting, making it difficult for the public, regulators and investors to judge the "real impact" of banks' climate action efforts and be able to hold them to account.
Even some of the largest, most ambitious-sounding green finance targets are in reality small relative to a bank's size, Share Action believes.
For example, the campaigner cites that HSBC's goal of allocating up to $1trn (£770bn) towards sustainable investment by 2030 is just 1.8% of its total assets, while for Barclays' it's just 3.2% of its assets.

Different journeys

Five banks – BBVA, CaixaBank, Commerzbank, Deutsche Bank and HSBC – have set sustainable finance targets that cover their banking and asset management activities, but keep these activities separate in their decarbonisation targets, Share Action said.
Banks set decarbonisation targets over five years and sustainable finance targets, on average, over 10 years.
While almost all decarbonisation targets by banks are based on a clear methodology, just 13% of sustainable targets are backed by transparent, public methodology, Share Action claims.
All 20 banks have set at least one sectoral-specific decarbonisation target.

Vital role

Yet only nine banks have also set one for sustainable finance that illustrates how they are funding sectors that are crucial to a successful transition, such as renewable power and green technologies.
Banks rarely provide a breakdown for how much sustainable financing they provide to these sectors, Share Action said.
Xavier Lerin, senior research manager at the campaigner, said: "Europe's biggest banks have a vital role to play in financing the transition to a low-carbon economy, such as scaling up renewable energy, making real estate energy efficient and supporting important industries to decarbonise."
However, he added: "Our analysis shows that in the majority of cases, the climate targets banks are using as a roadmap to transition are not fit for purpose, which is putting at risk our ability to protect society from the worst impacts of climate change.
"We urgently need banks to set more ambitious and coherent targets that transparently map out how they will live up to their commitment to finance the renewable power, green infrastructure and technologies needed to protect people and our economies."
Responding to the research, a spokesperson for Barclays said: "Barclays is delivering against its target to facilitate $1trn [£776.7bn] of sustainable and transition finance by 2030 – a larger target than many peers, when viewed relative to total assets."
portfolio institutional also contacted HSBC and BNP Paribas for comment on this issue, but at the time of printing, neither had responded.
Investor concern over how banks are falling short on green finance is a rising trend.
Investor coalitions signed statements addressing this were read to the boards of Société Générale and HSBC at their annual general meetings earlier this year.
As a next step, Share Action is writing to the chief executive of each bank with recommendations about how they can set effective climate targets that will help them reach their net-zero goal.
In particular, it is urging banks to set sector-specific targets around sustainable finance that are grounded in science.
The banking standards team at Share Action has partnered with asset managers, asset owners and NGOs to call for Europe's largest banks to phase out financing to polluting activities and instead increase the flow of capital into low-carbon alternatives.

ESG INTERVIEW – LEANNE CLEMENTS

"The goal is to do such a good job that dedicated responsible investment teams are no longer required."

The head of responsible investing at the provider of the People's Pension looks back over her almost 30-year career in sustainability and tells *Mark Dunne* about taking a targeted approach, the benefits of honesty, sharing the workload and serving 6.8 million members.

Today, saving the planet is a sexy job, but what was it like in 1997 when you started working in sustainability?

It was more about compliance and ticking boxes. Back then I was working for a consulting engineering firm doing contaminated site assessments in support of refinancing decisions for financial institutions. That was probably where I got my appetite for the finance sector.

When did you decide that you wanted to save the planet?

It started at university in the early 90s. I wouldn't say it was a grand passion. I studied psychology, but didn't pass the bar in my first year.

At that time, Queen's University started offering environmental science, and I was in the first graduating class. It was a great course and amplified my interest.

I then took a post-diploma in environmental engineering because I struggled with how to apply the course into a real job. As part of that, I did an internship for a consulting engineering firm where I drilled holes and collected groundwater samples. I thought: "So this is how I take all of that academic theory from university and practically apply it."

That was my foray into working for financial institutions. As part of a buy/sell you have to assess any properties. If there is contamination, it's taken off its value.

I did that for 10 years, but by 2007, I felt that if I wanted to move up a stage in my career then I should do a master's degree. So I did an MBA in corporate social responsibility at Nottingham University Business School.

That is when I realised I could take the lessons learned over 10 years, where I was evaluating risk at an operational level, and lift it up to a more strategic level.

Looking at things in a more holistic, macro context is in alignment with my skills. That is what piqued my interest in responsible investment, because I didn't want to abandon the 10 years. I was in my 30s and was up for a career change, but not a complete career change.

Looking back over your career, is sustainability where it should be by now?

There is an assumption that we have mainstreamed responsible investment. But have we?

What has occurred in the past few years is an explosion of products and services within ESG, but the question I would ask the industry is: have the corresponding beliefs moved with them?

If those products and services are moving in one direction, and your beliefs are not going with them, then they don't have a

solid foundation. So we aren't able to withstand shocks, for example, like what is happening in the US with the anti-ESG movement.

There have been a lot of people from the mainstream moving into our field. So I'm not saying there hasn't been advancement, but we need to be honest about the beliefs part of the picture.

You took on this role at People's Partnership two years ago. Why did it appeal to you?

I was in Spain working with the Association of Member Nominated Trustees (AMNT) on a campaign to address systemic barriers to split voting in pooled funds. That contract ended after four years.

I was pretty disgruntled at that point. I wasn't able to advance meaningfully in terms of my professional development, because it is important to me that I'm always learning. In other words, I was reaching a plateau.

So I was looking for opportunities in 2022 with a little trepidation, because I had that experience of not feeling fully integrated into the investment team, like the value proposition of responsible investment wasn't fully embedded.

I was a bit nervous about coming back in, but I talked to a lot of my colleagues in the industry, and they said it has moved on materially enough that the role will be different, and there will be an opportunity to learn and grow. So for that reason, I came back in.

What have you achieved in those two years?

There's no I in team. We have achieved a lot but could not have done it without the senior management's support and our wonderful trustees.

In terms of what we have delivered, we integrated climate-aware funds into the developed equities portfolio. It was £15bn and was the single biggest move in the UK at the time for defined contribution. That took about 18 months to process through various governance committees, so it was a huge accomplishment for everybody involved and a professional highlight for me.

The second is updating our responsible investment policy. The core of the update centered around strengthening our expectations of fund managers. That received good industry feedback in terms of its clarity and transparency. I'm quite proud of that policy.

There are many different pillars of those expectations. First, we look at whether the fund manager is aligned to our responsible investment objectives and beliefs. Then we unpack the governance piece. If it's for a passive mandate, we look at stew-

ardship resourcing. For example, if there's board oversight.

Then we look at voting and engagement. We have expectations across our stewardship priorities of climate, nature and human rights.

So we look at the degree of alignment between those expectations, our net-zero voting guidelines and what our fund managers are doing, to see if there are any gaps.

Then there is the quality of their reporting, because there's a lot of work that needs to be done here, with respect to getting more granular data on engagement.

There is a whole narrative missing from stewardship reporting: company engagement information milestones, progress against them and what are you going to do if engagement fails. We push our managers to improve in that space.

One of five workers in Britain save with People's Partnership. Other than an income in retirement, what are you offering them?

One of the differences of working in a large master trust, is a sense of responsibility to that one in five.

I'm keen to show that we have them at the heart of our decision making on responsible investment.

For example, we have completed a YouGov survey of UK savers. Our intention is to use the findings to shape our stewardship program.

Another area of focus is to create more member-friendly responsible investment content. In other words, our responsible investment policy is technical, but deliberately so, because the primary stakeholders are our fund managers. But in addition to that we want to create a more member-friendly version. A member-friendly version of the TCFD (Task Force on Climate Related Financial Disclosures) report is also coming soon.

You manage £30bn worth of assets. Is it possible to invest such a large amount responsibly?

One of the benefits of where we are in the industry, in terms of greenwashing risk and the anti-ESG movement in the States, is that it will put us in a much more honest place.

Honesty will be rewarded in this new environment. It is taking a staged approach, saying that this is what I'll be able to do by this time, and this, by this time.

It is an evolution, not a revolution. Just being honest that this is a journey, because the goalposts are always moving in terms of data and analytics frameworks.

You are not going to read that we 100% embed ESG into the investment process. This is the kind of statement the industry was making 10 years ago. Now we are in a much more honest place about what we have embedded into which asset class. It is a lot more rooted and grounded now.

100% responsibly? Perhaps not. As long as you are honest about it being a work in progress and evolving your process over time, you will have more credibility in today's market than saying we are 100% invested responsibly.

There is an assumption that we have mainstreamed responsible investment.

Back to fund manager standards. You once said that the days of "tea and cake" engagement are gone and you want to see a more targeted approach, routed in robust theory. Is that message getting through to your managers?

You are not going to read that we 100% embed ESG into the investment process.

It's a bit early for that. It's a work in progress. It's just about consistently sending that signal through the monitoring programme. Rome wasn't built in a day when it comes to these things.

It is a progressive responsible investment policy in the sense of it being stretched, but deliberately so.

What I'm hoping to see is that the conversations I'm hearing in the industry around us needing to take a targeted approach, that's rooted in a theory of change, will eventually be embedded into the stewardship approach.

This is why I thought it was important for us to root it in the responsible investment policy so that it's formalised and part of the monitoring programme.

It's part of how we score the managers on how well they answer these types of questions.

It is not something where you snap your fingers and it happens overnight, but conversations are happening.

It is early days, but I can see a positive evolution with respect to it. So let's talk in three years.

How widespread would you say that misalignments between asset owners and their managers are?

It's an interesting word, misalignment. It seems to have resulted in some polarization in the industry.

Ultimately, what's important here is creating a partnership between the asset owner and the fund manager to strengthen that stewardship chain.

If you use terminology like 'alignment' it can create tensions, which is not what we're looking to achieve.

We're in an interesting phase in stewardship, one of disruption. For years, predominantly speaking, the stewardship proposition was supply-led by fund managers.

What I'm seeing lately is a shift where asset owners are starting to rise in terms of their voice. You're seeing evidence of that through the new stewardship propositions that are being presented by fund managers.

Another disruptor working in this space is the Task force for Pension Scheme Voting Implementation, which I was on when at AMNT.

Seven years ago, no fund manager was willing to talk about it. Well, today the landscape is an entirely different world, and it's creating a lot of disruption.

People have an issue with it, but it is a necessary evolution to where we need to be as we move towards more of a demand-led industry when it comes to that stewardship proposition.

There will be growing pains along the way, but it's necessary in order for us to shift this system to a place where it always should have been, which is demand-led with the asset owners at the top of the chain, being the owners of the capital, driving what they need from their fund managers.

It's an interesting word, misalignment. It seems to have resulted in some polarization in the industry.

What big stewardship issues are you facing?

Where we are failing is we are spread too thin. You just see a heck of a lot of initiatives happening in all sorts of places. What we need to have is that targeted approach.

We expect that of our managers and are clear on the areas we want them to focus on. But what we need to do is share the workload.

There are industry leaders doing good work in targeted areas. A good example is Adam Matthews [Church of England Pensions Board] and his mining work. Railpen on dual-class shares is another pocketed area.

We need more of these focal points and more people leading them like they are. We will achieve much more of a maximum impact, as opposed to us all working in silos, spreading ourselves too thin.

What's your focus going forward?

Building the team. I just hired a new stewardship manager, so we now have three. We're looking to double that in the next few years.

Ultimately, that will allow me to focus more on industry and policy engagement, which is important for the head of responsible investment to do.

Then we are looking to integrate climate beyond developed equities into other markets and asset classes.

We are also looking to embed nature and human rights more formally into our stewardship processes.

When will your work at People's Partnership be complete?

There's tension there. Do I want to be out of a job? I suppose I do. Ultimately, the goal is to do such a good job that dedicated responsible investment teams are no longer required.

And we are so successful in industry and policy engagement, that we create a sustainable financial system, and then everything will work the way it should by making me redundant.

Will it happen before I retire? No. But there will be work to do over the next 10 to 15 years.

LEANNE CLEMENT'S CV

Sept 2022 – present
Head of responsible investment
People's Partnership

Oct 2021 – Aug 2022
Head of stewardship UK/EU
Carbon Tracker

Mar 2017 – Aug 2021
Campaign manager
Association of Member Nominated Trustees

Apr 2016 – Sep 2016
Responsible investment manager
Pension Protection Fund

Jun 2014 – Mar 2016
Responsible investment officer
West Midlands Pension Fund

Jun 2013 – Apr 2014
Responsible investment consultant

Nov 2011 – May 2013
Responsible investment officer
London Pensions Fund Authority

Mar 2009 - Jul 2011
Researcher – proxy voting and shareholder services
PIRC

Jun 2008 – Sept 2008
Sustainable supply chain internship – MBA dissertation
Arcelor Mittal

Apr 1999 – Aug 2007
Intermediate to senior project manager
Exp Global

Jul 1997 – Apr 1999
Environmental Consultant
AMEC Earth & Environmental

HUMAN RIGHTS: SOME RIGHTS, MANY WRONGS

Human rights are not just a social issue, so the investment risks are huge. *Mark Dunne reports.*

Bad publicity is a great motivator, especially if it involves rubber gloves.

Back in 2021, Top Glove, which makes more disposable gloves for doctors, nurses and surgeons than anyone else in the world, found itself in trouble with the NHS and the US government. The authorities in its home country Malaysia uncovered evidence of forced labour and insufficient Covid protections in their factories.

Its customers were not happy. In fact, the US banned its products from being used in the country, which mean that 22% of its revenue disappeared. Investors were equally unimpressed and a planned $1bn (£771bn) stock market listing in Hong Kong was scrapped.

The US ban was lifted after it convinced the authorities that working conditions had improved. Compensation totalling $30m (£23m) made to those effected also helped reverse the decision.

Loss of revenue can result from being accused of exploitation and can be rectified by improving conditions for your employees, but repairing a damaged reputation could take longer. A clear example of why human rights is a major risk for investors.

Indeed, the health and safety of workers, eradicating forced and child labour and displacing communities are areas where institutional investors should be using their influence over the corporates sitting in their portfolios to improve the standard of human rights in the supply chain.

This is a huge issue. Around 27.6 million people are believed to be victims of forced labour globally, according to Anti-Slavery International, a charity. It also claims that a fifth of global cotton production is linked to slavery in China.

Making a stand

A range of industries, from fashion to mining and manufacturing have found themselves at the centre of human rights scandals. Many are repeat offenders.

The pressure on institutional investors to hold companies to account if they are infringing these rights is growing. And many are taking action.

Blackrock was an investor in Top Glove when it hit the headlines over the forced labour in its factories. The asset manager decided to voted against the re-election of directors sitting on the company's board. Blackrock was using its influence on behalf of the pension schemes it manages capital for to drive change at the company. But this isn't just about ethics.

In an Edelman Trust Barometer survey of 700 global investors, 90% agreed that companies prioritising ESG integration represent better opportunities for long-term returns than those who do not. And the market share of those thinking this way is expected to move in the right direction.

Indeed, global ESG assets surpassed $30trn (£23trn) in 2022 and are expected to be worth at least another $10trn ($7.7trn) by 2030, which would be a quarter of all assets under management, according to Bloomberg Intelligence.

The eye of the storm

Being at the centre of an exploitation scandal is a concern for business leaders on both sides of the Atlantic, if surveys are to be believed.

Indeed, research carried out last year by Proxima, a consultancy, found that most chief executives in the UK and the US are aware of the risks that could be lurking in their supply networks.

The survey of 2,000 companies with at least 50 employees found that 69% of their leaders are concerned about benefiting from human rights abuses in the companies they contract services from.

Proxima's executive vice president, Simon Geale, said at the time that addressing human rights issues across the supply chain is a "huge challenge" for businesses and is high on the agenda for their leaders.

"We've seen a number of businesses fall victim to human rights issues," he added, "and as we see increased scrutiny from customers and regulators, supply chain transparency is going to become increasingly critical.

"This is the emerging priority for CEOs at a time when business leaders are spending more time than ever tackling supply chain issues."

Unsurprisingly, the figure for leading retail businesses is higher, at 79%. This reflects the greater scrutiny the fashion industry is under following a series of scandals involving those making clothes to be sold on high streets across the developed world.

There was Rana Plaza, the eight-storey building in Bangladesh that collapsed back in 2013 taking the lives of more than 1,100 people with it. Substandard materials were used in the construction of the building, which was not designed to be a factory and more floors were then added than were deemed safe. It made clothes for companies including Primark.

It was not the only example of a disaster in Bangladesh's manufacturing sector, as a fire hit another factory in the country a year earlier. Faulty wiring was named as the likely culprit.

Safety standards have improved since the disaster. They have had to if Bangladesh is to maintain its position as the world's second largest clothing maker behind China. In 2022, the industry employed 4 million people and was worth $42.6bn (£32.8bn) to the economy.

Boohoo

It is not only in the developing world where institutional investors need to be vigilant against workforce exploitation. They have been closer to home with one particular scandal involving online clothing retailer Boohoo.

As businesses struggle to meet demand for what is known as 'fast fashion' – mass produced low-cost garments sold online and on Britain's high streets – at least one supplier had cut corners. In 2020, undercover reporters found that a factory in Leicester making clothes for the company was paying workers as little as £3.50 an hour, less than half of the £8.72 minimum wage at the time. They were also operating as usual during the Covid lockdowns, putting its staff at risk.

The home secretary at the time, Priti Patel, launched a modern slavery and human trafficking investigation. A barrister-led review backed up the journalists' claims of low pay and poor working conditions and labelled Boohoo's monitoring of their supply chain as "inadequate".

Those holding Boohoo's stock also suffered. Shares in the company plunged by 44%, wiping off more than £2bn of value.

There have since been allegations that the changes made since the story broke have not been adequate.

Full disclosure?

Most large companies have divisions that tackle risks such as anti-corruption or cybercrime, so why not human rights?

In North America, only 85% of companies with human rights commitments publish such disclosures related to their supply chains. This has risen from 56% in 2017, so it is moving in the right direction, but why isn't the figure 100% if they have a policy in this area.

One reason could be due to the visibility of the supply network, which, if it involves companies in the emerging world, might be difficult to monitor.

"A key concern is poor transparency of organisational supply chains, which is hampering progress on these topics – and many CEOs bemoan their inability to make informed decisions and manage risks based upon supply chain data available today," Geale says.

Upholding human rights often relies on voluntary agreements and some regulation, which seeks to improve corporate practices.

Legal frameworks that require companies to report on human rights and environmental issues include the European Union's Corporate Sustainability Reporting Directive (CSRD).

Then there is the UN Guiding Principles on Business and Human Rights. Principle number 17, for example, calls on companies to undertake human rights due diligence to identify, prevent, address and mitigate adverse human rights risks and impacts.

However, a survey of 1,300 corporate executives in 13 countries found that more than 70% lacked confidence in their own ESG reporting, according to business data specialist Workiva. That was two years ago, so it is hoped that confidence is growing.

No guarantees

Investing in specifically labelled sustainable investment products may not save investors from reputational damage when it comes to human rights abuses.

The Business & Human Rights Resource Centre had a shock when they looked into the shareholders of the companies that funded and equipped Myanmar's military, which the UN has accused of crimes against humanity. They found that more than $13bn (£10bn) of capital flowed from 344 ESG funds into 33 of those companies, which included weapons manufacturers, energy giants, tech companies and even Facebook, which was accused of facilitating hate speech on its platform against the Rohingyas, a minority being persecuted in the country.

But ESG is not about investing in companies with high ethical profiles. It is about changing badly behaved companies, improving their practices and how they make money. If necessary, the goal is to make them greener and fairer.

Spotting such abuses is on the agenda for Abrdn. The asset manager believes a focus on human rights provides a valuable insight into a company's risks and opportunities.

There are two approaches it uses to assess and integrate human rights risks into portfolios.

The first is a top-down assessment of the human rights environment in a given country or region, particularly drawing on political and social research, to understand the potential impact on potential investments. Proprietary ESG frameworks and indices are used to identify key rights at risk.

We've seen a number of businesses fall victim to human rights issues, and as we see increased scrutiny from customers and regulators, supply chain transparency is going to become increasingly critical.

Simon Geale, Proxima

Then there are bottom-up assessments of how companies face human rights issues depending on their activities. For instance, land rights and community consent are more relevant for a mining firm, while the right to privacy would be more of a priority for a software provider.

It's not just about the S

But human rights are not just about how much an employee is paid or the number of breaks they are allowed. It is an issue that stretches far beyond the social pillar of ESG.

Indeed, cutting the amount of carbon in the atmosphere could help in the fight to ensure a higher quality of life, as the two are interlinked.

Human rights include a right to live in a clean and healthy environment free from pollution and hazardous weather patterns. It is also a factor in not just building a greener economy but to facilitate a just transition, too, where communities are not decimated as livelihoods disappear.

But it goes further than that. In 2019, a Dutch court ordered the government to cut carbon emissions, describing climate change as a threat to human rights. A few years later, Brazil's supreme court declared the Paris Agreement a human rights treaty. Then in 2021, the UN passed a non-legally binding resolution declaring that a healthy environment is a human right.

So climate change, nature loss, pollution and waste are human rights abuses as they are major threats to humanity. The heatwaves, droughts, floods and wildfires climate change create are a threat to our food and freshwater supply, our health, our sources of energy and drives migration.

At the time the UN's resolution was passed, Inger Andersen, executive director of the UN Environment Programme, said: "This resolution sends a message that nobody can take nature, clean air and water, or a stable climate away from us – at least, not without a fight."

New direction

It is clear that in today's market, companies cannot afford to ignore human rights abuses in their supply chains or, indeed, within their own operations. Employing risk assessments or using a compliance programme could be crucial to helping companies maintain strong relationships with their clients and suppliers, make their operations more efficient and to guard their reputation.

Aside from helping to make the world a better place, it could also avoid causing social unrest in economies where an enterprise is exploiting its local workforce.

If you need convincing, just ask the investors who were exposed to Boohoo when it made the front pages over how its workforce was treated. It could make for an interesting conversation.

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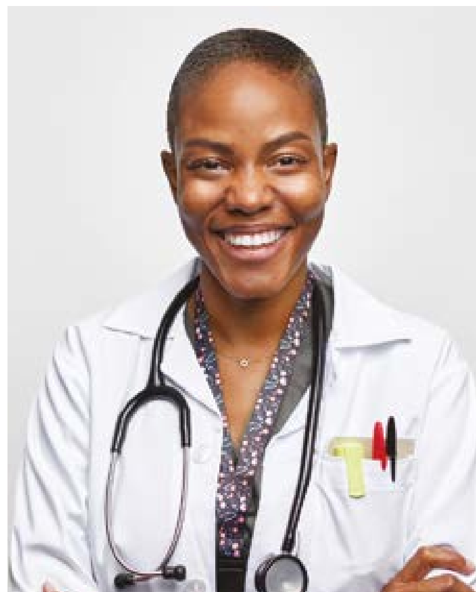

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