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# ESG and Impact Investing 2023

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## Peter C. Fusaro

*Managing Director*
*Climate Tech, Decarbonization, ESG & Impact*
*Weild & Co.*

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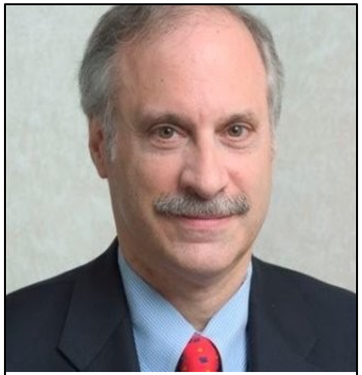
# Peter Fusaro – Creator of the Wall Street Green Summit



**Peter C. Fusaro**

**Managing Director - Climate Tech, ESG, Decarbonization & Impact**

**Weild & Co. Investment Banking & Advisory**

**Peter C. Fusaro** is a bestselling author, keynote speaker and thought leader on emerging energy and environmental financial markets. Peter has worked for **over 30** years on climate change issues and is currently advising companies worldwide on ESG, carbon trading, finance, clean energy technology, renewable energy, and cleantech software & hardware.

Peter is currently Managing Director of Climate Tech, Decarbonization, ESG & Impact at investment banking & advisory firm Weild & Co. Peter also serves as Chairman of New York-based energy & environmental consultancy Global Change Associates, a position he has held since 1991. Peter founded the Wall Street Green Summit in 2002, which convenes every March in New York City, and continues as its host (www.thewallstreetgreensummit.com).

Previously, Peter served as an adjunct professor at Columbia University's School of International and Public Affairs, where he taught renewable energy project finance. In 2009, Peter also launched the Global Change Foundation, focused on environmental education & projects, and held its first Green Jobs Summit in March 2010. Peter is known for coining the term "Green Trading" and was selected for Who's Who in America for Lifetime Achievement. Peter has written 16 books on energy & environmental financial markets, as well as bestseller *'What Went Wrong at Enron'*.

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# Today's Discussion

## Key Takeaways

- See how the supply chain and private companies in the United States will be  impacted by impending ESG regulation developed by the Securities & Exchange Commission (SEC).
- Be ahead of the learning curve on where sustainable investment opportunities will emerge in the coming years.
- Learn why asset diversification into Climate Tech, a noncorrelated asset class estimated to grow to $100 trillion by 2050, is a smart move.

# What is Environmental, Social & Governance?

**Environmental, Social & Governance (ESG) has three legs to its stool**

- **Environmental Factors:** Including pollution of the air and water, threats to biodiversity, and other damage to the environment.
- **Social Factors:** Including labor, supply chain, health & safety, communities, modern slavery, Indigenous rights, ethics, and diversity (S factor).
- **Governance Factors:** Including everything from sovereigns' policymaking to the distribution of rights & responsibilities among different participants in corporations, covering boards of directors, managers, shareholders, and other stakeholders (S & P Global).

**The Bottom Line**

Environmental, Social, and Governance-based investments often focus on **material financial risks** that affect companies.

# Much Misinformation Exists About ESG Investing

## ESG Today

- Beginning of a Market.
- Shift of capital to Sustainability.
- Funds branded as ESG were subsequently found not to be ESG compliant.
- EU MSCI starting to delist these ESG funds
  - According to the *Financial Times* (March 24, 2023), hundreds of funds are about to be stripped of their ESG ratings and thousands more will be downgraded in a shake-up being pushed through by index provider MSCI. The impact could be particularly acute in Europe.
- In 2022, ESG exchange traded funds accounted for 65 per cent of inflows into European ETFs (*Morningstar).*
- Numbers like $30 trillion of new ESG investment are being thrown around.
- Furthermore, the SEC is about to issue its final rule on ESG Reporting.
- The Real Market will now begin!

# What is the SEC is Proposing?

- The SEC is proposing amendments to rules & reporting forms to promote consistent, comparable, and reliable information for investors concerning funds' & advisers' incorporation of ESG factors on March 22, 2022, pending Final Ruling.
- Final rules by the SEC will accelerate market acceptance of ESG standards.
- Public Companies will be impacted by the SEC's final rules.
- Supply Chain may also be impacted by the SEC's final rules (Scope 3 Emissions).

# Defining the ESG Investment Opportunity

**Three of the world's largest businesses – Energy, Food and Water – are ripe for sustainable change**

- **Climate change** – find the leaders making an impact and creating solutions.
- **Social Impact** – the companies bringing people together through societal change.
- **Do more with less** – data & measurement lead shift to efficiency & smarter decision making.
- **Transitioning** – both new and old companies create a growing universe – "the move to mainstream".
- **Thematic growth** – secular opportunities that solve a problem and create competitive advantage.
- **Investors' desire to have an impact – t**ap into investor's desire to have an impact with their investments
- **The sustainability solutions opportunity** – large and growing
  - the CDP estimates a $2.1 trillion* opportunity for climate-friendly products and services that have an environmental impact in the coming 5+ years.

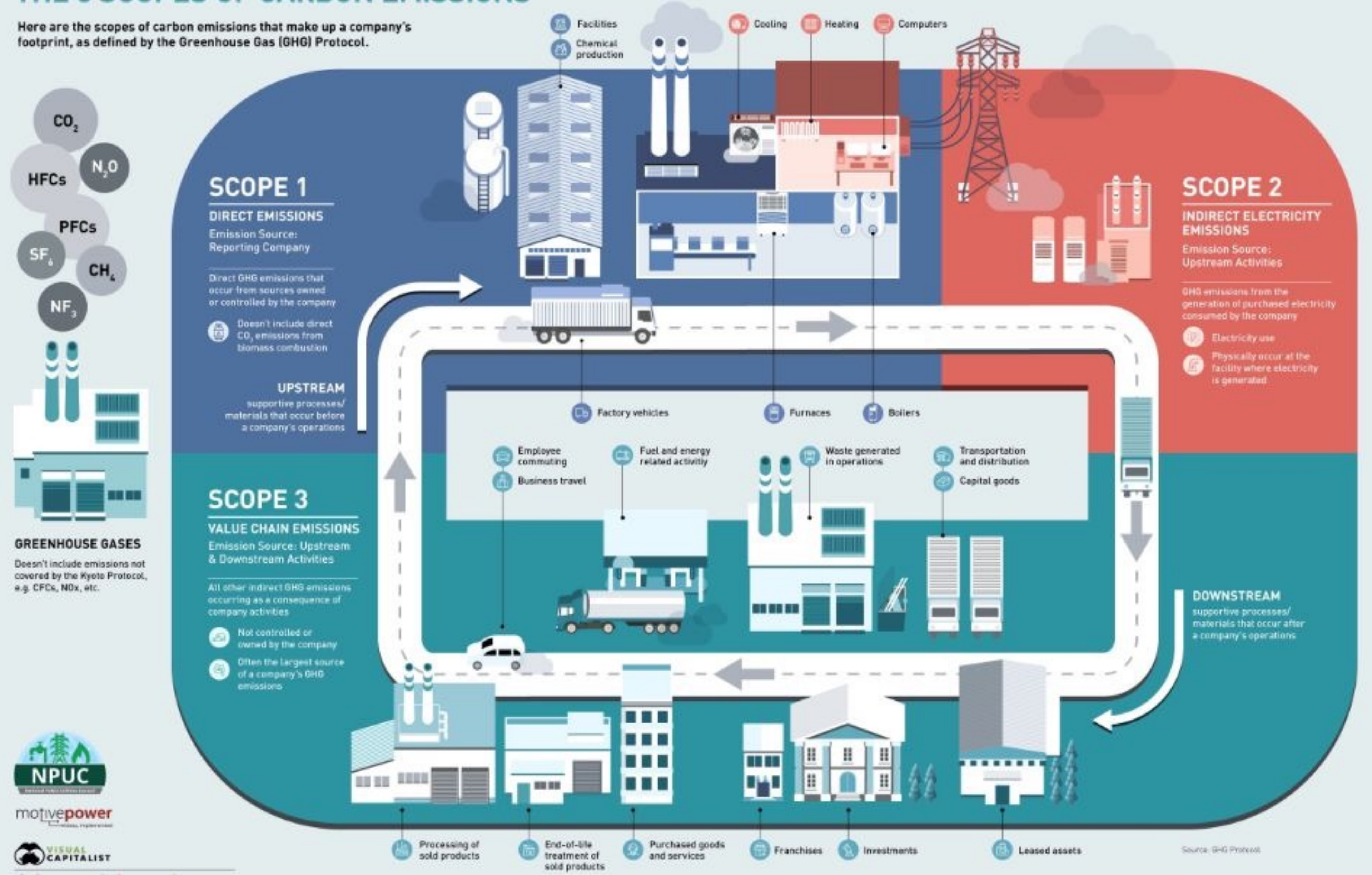
**ESG and sustainability investing started niche but has evolved to becoming a mainstream focus by investors broadly across all market sectors**

(1) * Carbon Disclosure Project report "Major Risk or Rosy Opportunity: Are Companies Ready for Climate Change", 2019

## THE PATH TO
# DECARBONIZATION
## THE 3 SCOPES OF CARBON EMISSIONS

**As organizations face pressures to decarbonize, they need to define and minimize their carbon footprint.**

**Here are the scopes of carbon emissions that make up a company's footprint, as defined by the Greenhouse Gas (GHG) Protocol.**



# Direct and Measureable Environmental and Social Outcomes: SDGs Lead the Way

**Investing in companies that further the UN's 17 Sustainable Development Goals (SDGs), with an emphasis on the social and environmental impact an investment can make.**


## Green has to be Green

Funds targeting ESG and Impact need to be **performance focused, purpose-driven** and have an eye on the **impact delivered.**

Sustainable investing practices lead to **superior long-term alpha generation.** It is critical to own a **strategic and financial** interest in companies that make a measurable positive impact towards the transition to a lower carbon economy and social benefit.

The focus is not investing in a company just because it scores well on ESG measures -- it is finding the best companies that are leading their respective industries and driving above-peer returns through risk abatement, market share gains and cost reductions as a result of driving efficiencies through the organization.

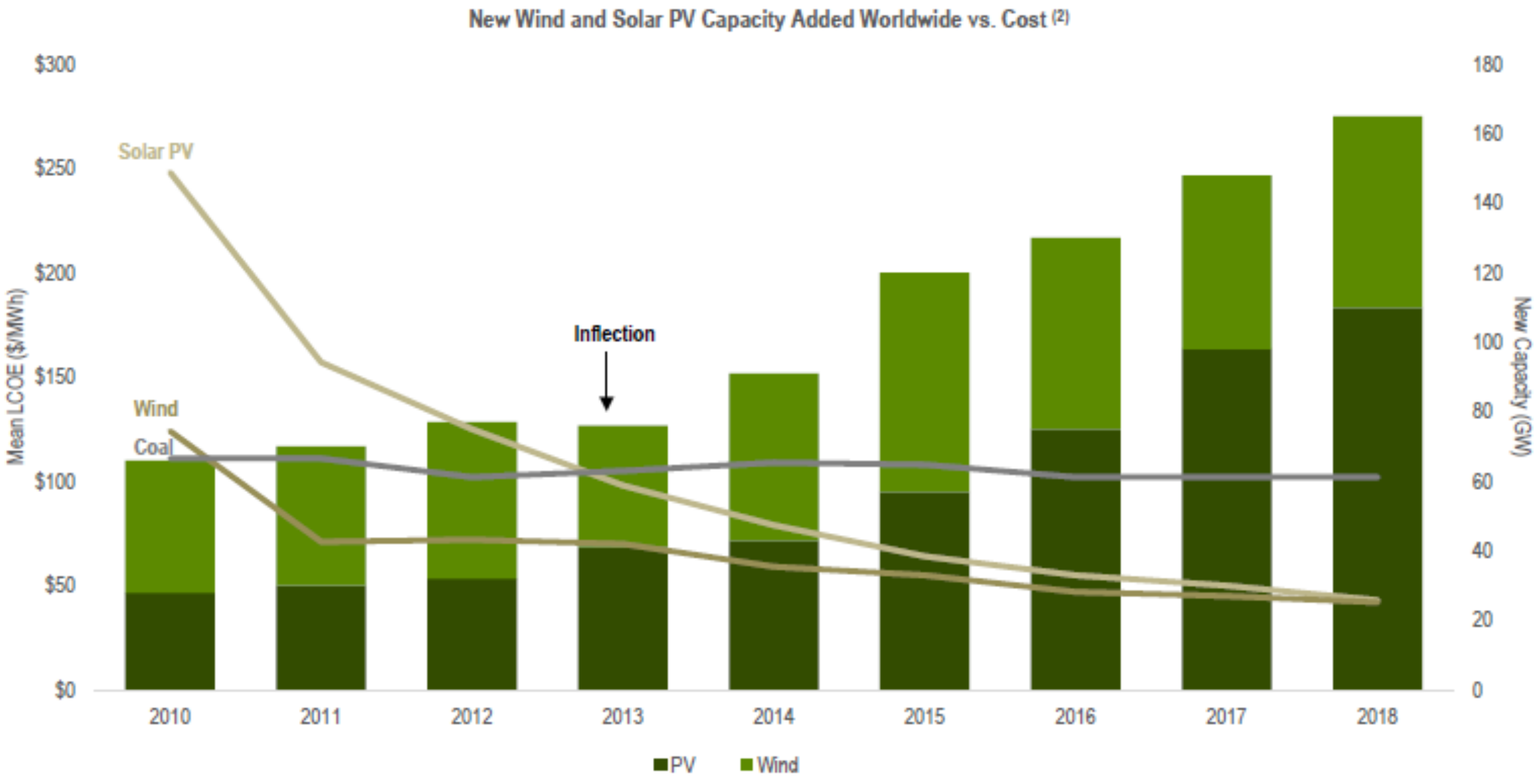
**Every investment has either a positive or a negative effect. Consequently, no investment is neutral by default.**

# Solutions: Impact and Disruption

- **Generational shift** in investor appetite towards ESG/sustainability/impact.
- **Sustainability** is evoking a once-in-a-lifetime change through society
  - Focus on measurement/data and driving efficiency,
  - Investable universe is growing – "evolve or become obsolete".
- **Capitalism** is best-suited to solve the environmental problems & risks of emissions, through economic disruptions that result in a "better way of doing things".
- **Regulations** are a catalyst, but economics will drive commercial market success and long-term sustainable solutions. We've seen this before with the "experience curves" of
  - LED lighting,
  - Solar/wind renewable energy, and
  - The recent electrification of cars/trucks.
- **Expandable offering** of infrastructure, disruption, water/ag/mobility funds.
- **Private investment** is accelerating across sub-sectors.
- **Rising demand** for finite resources mandates the disruption of essential infrastructure systems – creating a unique investment opportunity

**Investment model that capitalizes on value creation through an evolutionary societal shift toward sustainability**

# Example: Digitization and the Rise of Clean Energy




**Tech and energy efficiency are moving lockstep as cost declines**

Source: (1) BNEF Investment Trends, 2018, (2) Lazard annual LCOE analysis

# Green is now experiencing hockey stick growth

- **Emerging innovative technologies facilitate a low-carbon transition**
  - Renewable energy (solar, wind) have reached scale and resulting cost reductions open the door to commercialization,
  - Utilities and corporates shun coal and nuclear for the cost certainty of renewables. Why?  To retain and attract Next Gen employees.
- **ESG solution and transition leaders offer growth and value**
  - Small/mid-cap growth names w/attractive valuations ,
  - Wide array of enablers in the value chain.
  - In most cases, these names/sectors are not followed by the market .
- **Upcoming expansion of green technologies & solutions under-appreciated**
  - Vehicle electrification,
  - AI and sustainability,
  - Energy storage,
  - Renewables,
  - Emergence of the hydrogen economy.

**An expanding universe of companies in higher growth areas yet still attractive relative valuations**

# Investment Themes Permeate: The Rise of Big Data

### Energy Supply Shift

Advantageous economics and zero emissions are driving a shift toward renewables and natural gas, and away from coal, oil, and nuclear

### Focus on Climate Change, Resource Scarcity

Companies self contract renewables.  CERES, UNPRI focus companies on lowering their CO2 footprint, reusing water and minimizing scrap and waste

### Clean Water Supply

Supply challenges are complicated by geographic imbalances, rising water demand and increasing concerns over water quality

### New Solutions for Transportation

Electric and natural gas vehicles approaching mainstream adoption; ridesharing and urban autonomous driving are poised to scale

### Biofuel Mandates

Biofuels are gaining traction globally and could add to pressure on already tight crop inventories and farmer planting priorities

### Need for Storage

Electrification on the rise: massive cost declines of lithium ion due to EV growth supplants fossil fuel demand, reduces emissions and helps solve the intermittency of renewables within the electric grid

### Constraints on Arable Land

As population and incomes rise, the pressure to improve agriculture yields intensifies

### Building and Lighting Efficiency

Lower acceptance of energy waste and more energy management; lower LED and advanced building materials costs creates NPV positive projects

### Grid Upgrade

Distributed renewable energy leads to a decentralized, digital and storage enabled smart grid

### Sustainability-Focused Consumer

Higher secular growth of organic and sustainable products due to increased awareness and the rise of millennials

**The sustainability paradigm: data and measurement drive secular change, cost reductions and efficiency**

# Investing in Solutions with a Long-Term Perspective

**The Investment Universe will consist of companies that are:**

- Impact-driven,
- Either providing solutions or leading the transition,
- Benefiting from global focus on sustainability / do more with less,
- Driving superior long-term returns amid secular growth / disruption.

**Forces Driving Sustainability:**

- Economics Driving a Shift Towards Renewables
- Increased Focus on Climate Change
- Mandates for Lower Transportation Emissions
- Rising Populations and Consumer Incomes, Urbanization
- Water Scarcity and Quality Concerns
- Need for Grid and Infrastructure Upgrades
- Rise in Sustainability Focused Consumers, Brands

# Where are the ESG leaders today?

**Big Companies will not create the sustainable technologies of the future. Earlier stage and maturing companies are nimble, entrepreneurial and will take the risk.**

### Deep Fundamental Research

A value-chain approach uncovers the enablers across the widening expanse of sub-sectors that encapsulates >400 global companies

### ESG Integration

Integrating material ESG factors into the research process helps find the factors that drive performance, mitigate risk and create positive change for stakeholders

### Long Term Approach

Take a long-term view and invest in high quality companies with a secular growth driver, a competitive advantage and defined strategy that you want to own for many years

### Active Ownership

Know the management teams well and engage actively with the portfolio companies where there are opportunities to create additional value for all stakeholders

**The result is sustainable, long-term alpha generation driven by secular growth alongside a definable catalyst**

# Impact Focused Strategy

**Our mission is to find companies that have a positive environmental and social impact, as these companies will grow market share, have stronger returns, exhibit better risk awareness and see a lower cost of capital than those that do not embrace sustainability as a core tenet.**

## ESG/Impact Investing

### OBJECTIVE

- Superior long-term alpha generation
- Identify key value differentiators: initiatives to dramatically decrease CO2 emissions and enhance sustainability
- Invest in companies making a measurable impact towards the transition to a lower carbon economy

### OPPORTUNITY

- Companies addressing energy and resource challenges are positioned to outperform
- The sector's wide dispersion of returns underscores the value of deep fundamental analysis, management relationships leading to superior stock selection and active management

### STRATEGY

- Value with a catalyst and fundamental bottom-up approach to stock-picking
- Value-chain driven approach to finding enablers, ideas
- Opportunites to find the disruptors, the enablers and winners/losers

### DIFFERENTIATION

- Limited knowledge of US investment professionals
- Deep understanding of fundamental value chains across core sectors
- Wide range of enablers, companies looking for growth
- Portfolio of idiosyncratic risk/reward opportunities

(1) MSCI World Index is a broad global equity benchmark that represents large and mid-cap equity performance across 23 developed market countries.

# ESG Integration into the Investment Process

**Environmental, Social and Governance analysis is integral to identifying successful investment ideas that also reduce risk; corporate transparency as well as consistent data from providers will enable widespread adoption of ESG practices.**

**ENVIRONMENTAL**

- Emissions
- Resource intensity

**SOCIAL**

- Customers
- Employees
- Communities

**GOVERNANCE**

- Corporate governance
- Transparency
- Shareholder rights

**SUPERIOR GROWTH**

- Serving fast growing, dynamic markets by providing lower carbon, more efficient products and services
- More resilient pricing power as customers factor in ESG benefits rather than just seeking the low-cost provider
- Greater customer loyalty and market share gains

**HIGHER PROFITABILITY**

- Pricing power allows cost reductions to flow to the bottom line
- Lower input usage and reduced waste lower bill-of-materials
- Greater employee satisfaction lowers headcount turnover, lowering recruitment and training expenses

**GREATER VALUATION**

- Stability of earnings and cash flows allows for greater confidence in projections
- Lower regulatory and litigation risk through engagement of all stakeholders
- Lower cost of capital leads to higher financial returns and translates into higher valuation multiples

Fundamental Bottom-up Investment Analysis

# Active Engagement with Portfolio Companies

## ENGAGEMENT

- ESG-related disclosure continues to improve for publicly listed companies, however there is a lack of consistency on reported data-driven factors amongst companies
- It is imperative to engage directly and constructively with management teams to evaluate sustainability factors – quite often, we've found companies do not know how to how to effectively convey management's sustainability actions to investors
- Company management teams increasingly ask us how they can and should be reporting on sustainability initiatives to the investor community; many have noted rising ESG processes being incorporated by investors
- Engagement allows feedback to management and advocate for improvements in policies and practices
- Engagement strategies need to be prioritized by where investors can help create sustainable value – examples include plastics use, carbon emissions, energy efficiency and labor practices

**Funds flows are directing to socially and environmentally responsible companies with measurable impact**

# Now is the Time to Focus on Next Gen Investing

**ESG investing is going mainstream as investors demand companies become better corporate citizens. ESG and Impact are profit-laden movements as companies have realized they can “do good” by investor values as well as earn a strong rate of return for shareholders and other constituents.**

- Record inflows being reported to ESG funds; seen as resilience amid uncertainty
- ESG funds have outperformed relative to broader market funds with less downside (MS)
- Investors seeing growth potential of products/services that have impact
- Investor base – significant appeal to the “next generation”
    - Growing recognition of secular growth opportunity
    - Strong attraction to disruption, secular change
    - Younger investors demanding change
- Investor advocacy – rise of millennial, women investors
- Deloitte study sees $24 trillion wealth transfer to millennials over the next decade
- Firm belief (increasingly supported by data) that sustainable investing can generate investment returns as good or better than strategies that do not incorporate ESG principles

**Currently roughly one-quarter of all US assets under management are in sustainable strategies; inflows are poised for a fifth consecutive record growth year in 2020**

# Redefining the Investment Landscape

## Market Drivers

- Renewables continue their cost reductions and wider market deployment
- Energy Storage is now Ready for Prime Time
- Electrification of Mobility now underway
- Hydrogen is still an outlier, but 150 corporates can't be wrong
- Carbon Markets are now maturing
- Young Investors are very engaged

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# Q & A

## For more information, please contact

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