

The economic realities of ESG

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Investors are increasingly calling for clarity about the ESG initiatives companies are undertaking and demanding more holistic, comparable and reliable decision-useful ESG reporting. New PwC research shows that if companies aren't doing enough, or transparently reporting their progress, investors will take action: they will engage and vote, and divest if needed.

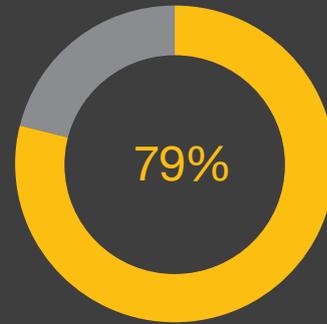
We surveyed 325 investors around the world, the majority of which were self-identified active asset managers making investments for the long term. Here's what we learnt.

For investors, what started out as a way to measure the environmental, social, and governance performance of a company for the purposes of gauging risk is now a major force driving investment strategy.

ESG risks are an important factor in investment decision making.

“ We're at a tipping point where ESG has gone mainstream. You can't walk into a financial institution now to talk about long-term themes without mentioning ESG.

Investment firm head of ESG, September 2021



% of respondents who agree

Expectations

Investors expect ESG to be a core part of a company's strategy and reducing Scope 1 and Scope 2 emissions¹ was the most cited issue investors think companies should prioritise.

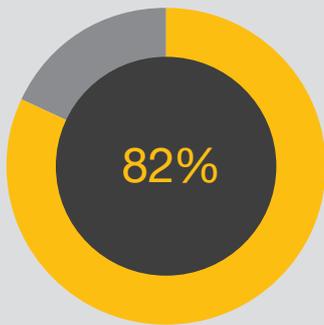
business, with the most common role identified for 'owning' ESG being the CEO (53%), however respondents also say that it needs to sit with more than one person to be effective. Investors are also calling for executive pay arrangements to include ESG performance measures and targets as a way to bring about real change.

The majority of investors we surveyed think C-Suite accountability helps them see how seriously a company takes ESG. Tone from the top helps it cascade throughout the

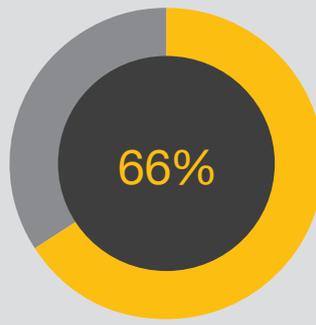
Companies should embed ESG directly into their corporate strategy.

I'm more confident that companies are on top of ESG risks and opportunities if someone in the C-suite is accountable.

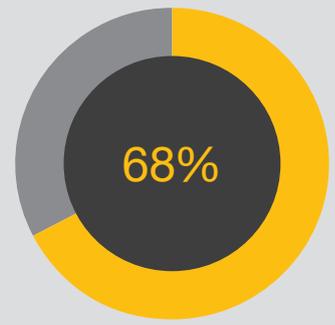
ESG performance measures and targets should be included in executive pay arrangements.



% of respondents who agree



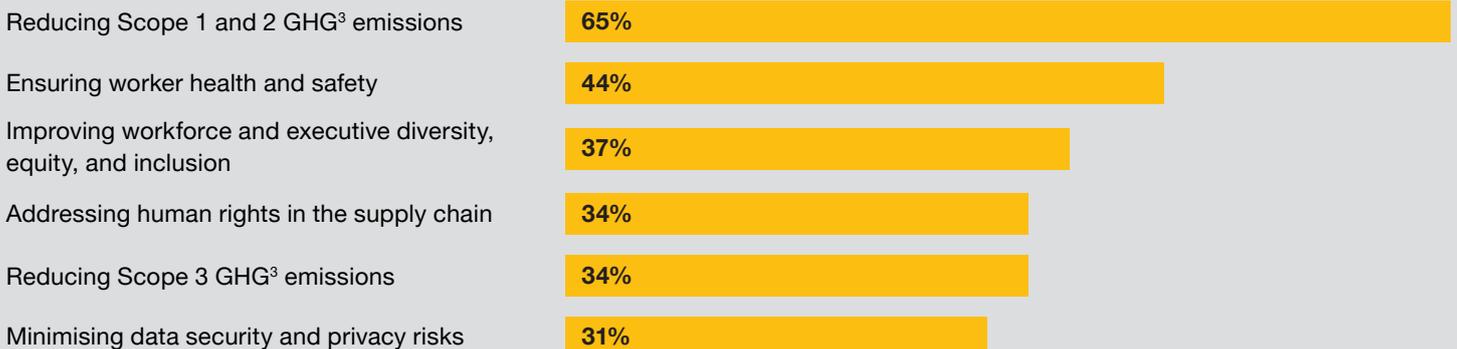
% of respondents who agree



% of respondents who agree

Top ESG issues in order of importance²

% of respondents



¹ Scope 1 emissions (direct emissions from a company's operations) and Scope 2 emissions (indirect emissions from purchased or acquired electricity, steam, heat, and cooling).

² For companies in the main industry the respondent covers.

³ Greenhouse gas.

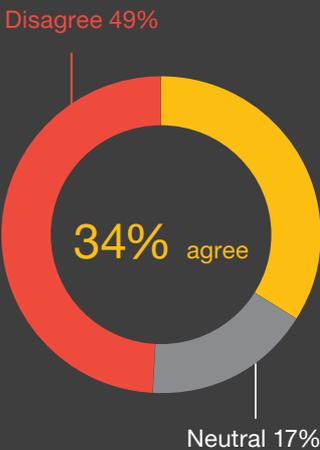
The reality

Our survey suggests that investors are torn between what they view as a responsibility to the planet and society and their fiduciary responsibilities to their clients.

Most of the investors we surveyed said they thought it was worth sacrificing short-term profitability to address ESG issues. These findings should give some comfort to companies who may worry that investors will be critical of reductions in EPS (earnings per share).

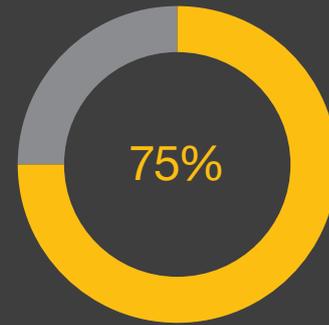
On the other hand, a similar percentage (81%) said they would only be willing to accept, in pursuing those goals, one percentage point or less of a haircut on their investment returns. Nearly half were unwilling to accept any reduction in return.

% of respondents willing to accept a lower rate of return on investment in exchange for societal or economic benefit.⁴



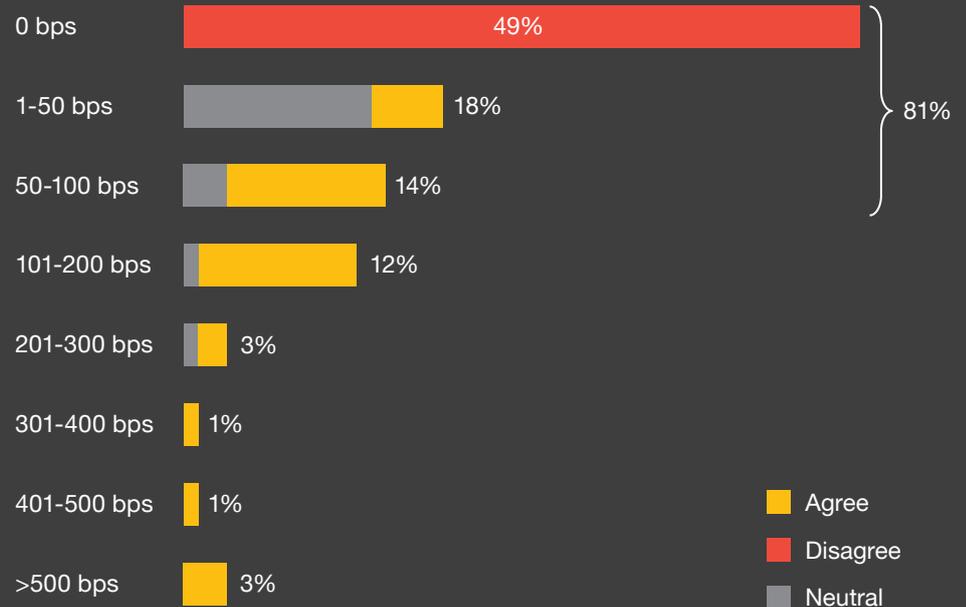
⁴ Institutional asset managers and asset owners.

Companies should address ESG issues even if doing so reduces short-term profitability.



% of respondents who agree

% of respondents citing an acceptable lower rate of return in basis points (bps)



Please note: due to rounding, percentages may not add exactly to 100%

These findings aren't surprising. Investors operate in competitive markets, where capital chases returns and underperformers are weeded out. In addition, 'asset managers have a fiduciary duty – and can't prioritise social [issues] over return on investment,' noted one credit ratings analyst we interviewed. There are also time horizon issues at play: investors are always balancing short-term results with longer-term, more existential – but also more uncertain – risks to the value creation prospects of their portfolio companies.

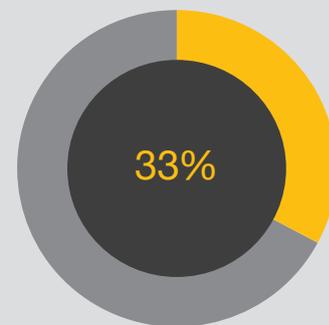
The challenge – as we see it

As PwC global chairman Bob Moritz **wrote** late last year, the global capital markets, as they currently operate, cannot be expected to single-handedly solve society's biggest problems. Governments, business, the capital markets, and society all play a vital role – and so does high-quality information, including information about non-financial matters.

Information needs

Our survey highlighted a number of deficiencies in current ESG reporting: only one-third of investors, on average, think the quality of the reporting they're seeing today is good enough. Simply put, much of today's ESG reporting lacks relevant, timely, complete and comparable information – such that stakeholders cannot easily differentiate between companies on ESG-related performance – making capital allocation decisions difficult for all in the ecosystem.

The quality of current ESG reporting is good.



% of respondents who agree

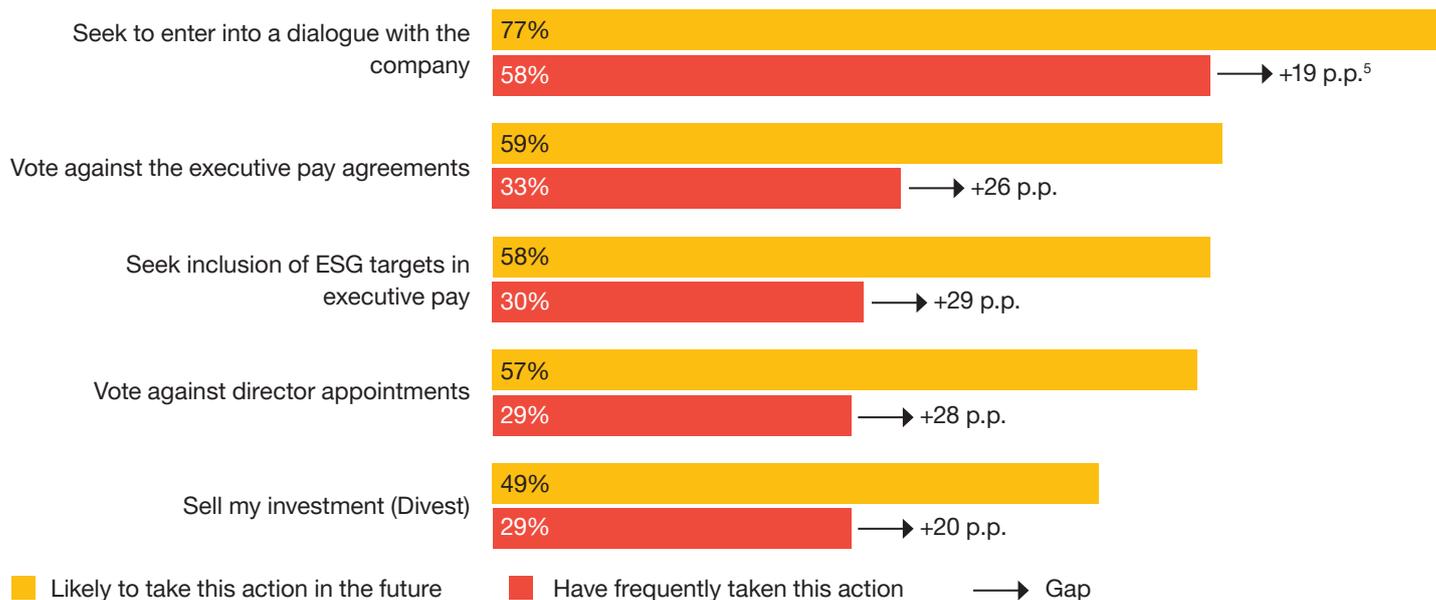
“ That is why trust is so critical. More is required for investors before they pull the trigger and invest money.

Investment firm head of engagement, September 2021

Actions

Investors said they want to engage with companies on their ESG journey, but in the absence of real action and transparent communication through reporting, they will take action too – using their power to vote and, if necessary, selling their investment and walking away.

% of respondents citing they will take action if they think a company is not doing enough to address ESG issues



Please note: due to rounding, percentages may not add exactly to 100%

⁵ percentage points.

The investors in our survey sent a clear message: if companies take the right actions on ESG, investors will support it, but they want to be brought along for the ride, however bumpy it might be. That means being upfront about your prospects for long-term value creation and the ways in which you'll manage risks, including unexpected ones. When you tell investors and other stakeholders how you plan to reset your strategy, reimagine your reporting, reinvent your operations, and drive toward new outcomes, you build trust while creating sustainable value for the long term.

About our survey

In September 2021, PwC conducted an online survey in which we received responses from 325 investment professionals from 43 territories. We also conducted 40 in-depth interviews in 11 territories during September and October 2021. The respondents to the online survey were spread across a range of industries, roles and specialisms. The online research was undertaken by PwC Research, our global centre of excellence for primary research and evidence-based consulting services. The in-depth interviews were conducted by partners and staff of PwC.

Respondent demographics

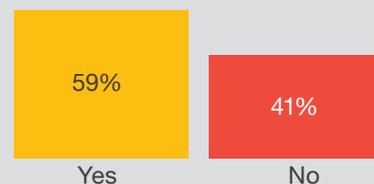
Location



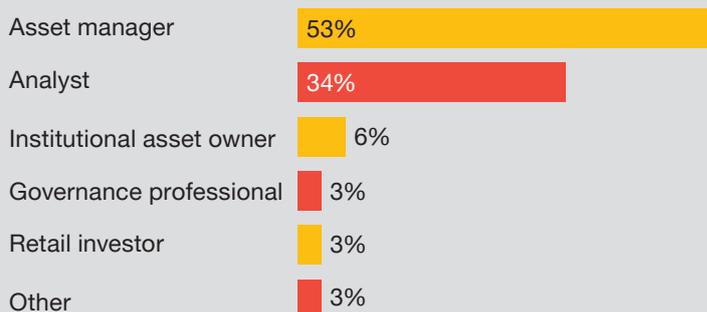
Equity investment horizon



Signatory of a responsible investing body or initiative (e.g. PRI, IIGCC)



Role



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