Covid-19: Highlighting the forgotten 'S' of ESG

Covid-19 highlighting the glaring weakness in most ESG Managers toolkit

When reviewing responsible investment processes through the spectrum of asset managers that claim to integrate ESG in their investment processes, you tend to find some pretty common attributes. Mainly:

1. High focus on the E (Environment) aspect through measurement and reporting of GHG emissions, water usage and waste. This is mostly done as, even if a company does not disclose its data, there are plenty of parallels that can be used to make reasonably accurate estimates. Let's be clear here, this is absolutely necessary as we are facing a climate crisis and immediate action is a must. Many asset managers focus on this area either through direct climate impact funds or enhanced reporting on these metrics. The issue does not lie here but in all the other funds they run that pay little attention to climate impact, particularly in the passive investment space. So, from a marketing popularity standpoint, it's fair to say that Environment is the new black.

2. Connection to UN Sustainable Development Goals (SDGs). The SDGs are a popular framework around which impact can be described using a commonly understood, universally accepted language. Many asset managers now present their portfolios in relation to the number and variety of SDGs they support. Many will apportion the percentage of revenue a holding might achieve from a particular SDG related activity (say the percentage of electric vehicles, a car manufacturer sells or the percentage of energy from renewable sources) as indicators of positive contribution to relevant SDGs. Conveniently, the aspects of many businesses that have a detrimental impact on SDGs are rather less precisely documented.

3. Numerous and detailed examples of governance failures across companies, both by sector and geography. Governance or lack of it, has for a long time been a key yardstick for investment and so this is no surprise. This is also the area where most engagement is focused as it typically sits in the CFO/CEO inbox and much voting is related to governance issues. Many commendable initiatives exist in this space that sits very much within the traditional investment manager's toolkit.

The above is a far cry from where the industry was just a few short years ago and reflects the rapid development of responsible investment from a niche activity into the mainstream.

The industry as a whole has been "pushed" into this space by asset owner demands and public opinion, rather than from an internal desire to change decade old investment models and practices. It is only when you have significant market dislocations or in the case of Covid-19, a universal dislocation, that a crack begin to appear in the façade.

The coronavirus pandemic is shining a bright spotlight on the often conveniently forgotten "S" or social aspect of ESG. More than anything before, the coronavirus pandemic is bringing to the fore a company's relationship with its employees and communities and how it will hinder or help their ability to survive through the pandemic.

So why is this area such a blind spot for asset managers?

One theory is that most investment education pays very little attention to HR strategy or its impact on business performance. Generally seeing it as a "nice to have" rather than material to the financial success and viability of a company. So confronted by an HR challenge, many fund managers would not know what to ask or how to ask it, to gain any critical insight. This is scary, when you consider that in most businesses, the human resources cost line is usually in the top 2 or 3 and it's the only asset that walks out of the door every evening. How the company treats its employees during this pandemic, will without a doubt have a bearing on its ability to survive and recover. Not allowing sufficient social distancing in the work environment will lead to higher likelihood of infection and loss in productivity. Clear staff furloughing and redundancy planning will enable companies to lower costs whilst maintaining employee and community goodwill, which if lost, may have severe consequences when hiring again after the pandemic. Also, remember, that employees are customers themselves and the reputational impact can be severe.

At Alquity, **we recognised very early on in the development of our ESG approach that the S factor was critical**. One of our earliest examples was Lonmin, a South Africa platinum miner. We had approached them about working conditions and pay for workers after we had learnt that they had numerous issues in this area. Our approach was rebuked as they did not seem to see it as an issue. We, of course, did not invest. Six months later, 44 miners who were protesting the conditions were shot dead outside one of their facilities. The company's share price crashed and never recovered.

Today, as well as drilling deeply into the company's employee and community relations, **we have established specific progress indicators for our engagement with companies**. This includes seeking all our companies to have staff training plans in place as well as staff turnover disclosure. We have also just embarked on a critical review of how our holdings are responding to the Covid-19 pandemic within their facilities, with specific focus on health and safety and the fair treatment of employees and customers.

Some of the highlights include:

GENTERA®

Mexico based microfinance bank which has responded to the crisis by deferring payments and interest on loans for 8 weeks as well as continuing disbursements of loans to customers, many of whom are the most vulnerable in society.

magalu

Magazine Luiza is a Brazilian retail/ecommerce. To preserve jobs, executives reduced their salaries by between 50-80% versus a 10-20% reduction for lower earners. In addition, by adjusting the holiday schedule, employees were able to use the shutdown for vacation. This means that at the busy Christmas period, the company will have less reliance on temporary staff and manage costs.

Chola
Enter a better life

Cholamandalam is an Indian financial services company which is providing company-wide insurance that covers Covid-19 infection. In addition, they have established an Employee Assistance programme which includes counselling support to deal with anxiety and other issues caused by the pandemic. Their HR Department has also conducted one-to-one calls with all employees.

In addition, it is now that responsible investors must step up to the plate and take responsibility for their own actions as much as the companies, they invest in. **How they behave in this crisis will define their brands long after a vaccine has been found for Covid-19**. Despite extremely challenging business conditions, **Alquity chose to respond by launching our 40-40 Campaign**. Increasing our donation from 10% to 40% from new investments into our funds from campaign partners. Alongside the Alquity Foundation kickstarting the campaign with an initial US$40,000, we hope to accelerate our donations and support 40,000 people during this dreadful pandemic.

"The ultimate measure of a man is not where he stands in moments of comfort and convenience, but where he stands at times of challenge and controversy"
(Martin Luther King, Jr.)

So, next time you are reviewing an asset manager ESG presentation or report, just ask yourself where is the Social aspect? If all you hear is a deafening silence, just skip the rest of the report because you've probably read it before somewhere else.

For more information on Alquity, please contact:

Europe
Benoit Ribaud
+44 207 5577 862
benoit.ribaud@alquity.com

Asia
Suresh Mistry
+44 207 5577 854
suresh.mistry@alquity.com

United Kingdom
Susannah Preston
+44 207 5577 850
susannah.preston@alquity.com

Latin America
Cyn Cano
+44 207 5577 871
cyn.cano@alquity.com

North America
Renee Arnold
+1 215 350 9063
renee.arnold@alquity.com

United Kingdom
Alex Boggis
+44 207 5577 850
alex.boggis@alquity.com

www.alquity.com
/Alquity
Alquity Investment Management
@Alquity

DISCLAIMER

The information in this document (this "Document") is for discussion purposes only. This Document does not constitute an offer to sell, or a solicitation of an offer to acquire an investment (an "Interest") in any of the funds discussed herein. This Document is not intended to be, nor should it be construed or used as, investment, tax or legal advice. This Document does not constitute any recommendation or opinion regarding the appropriateness or suitability of an Interest for any prospective investor.

This material is for distribution to Professional Clients only, as defined under the Financial Conduct Authority's ("FCA") conduct of business rules, and should not be relied upon by any other persons. Issued by Alquity Investment Management Limited, which is authorised and regulated in the United Kingdom by the FCA and operates in the United States as an "exempt reporting adviser" in reliance on the exemption in Section 203(m) of the United States Investment Advisers Act of 1940.

The Alquity Africa Fund, the Alquity Asia Fund, the Alquity Future World Fund, the Alquity Indian Subcontinent Fund and the Alquity Latin American Fund are all sub-funds of the Alquity SICAV ("the Fund") which is a UCITS Fund and is a recognised collective investment scheme for the purposes of the Financial Services and Markets Act 2000 of the United Kingdom (the "FSMA"). This does not mean the product is suitable for all investors and as the Fund is invested in emerging market equities, investors may not get back the full amount invested.

This Document is qualified in its entirety by the information contained in the Fund's prospectus and other operative documents (collectively, the "Offering Documents"). Any offer or solicitation may be made only by the delivery of the Offering Documents. Before making an investment decision with respect to the Fund, prospective investors are advised to read the Offering Documents carefully, which contains important information, including a description of the Fund's risks, conflicts of interest, investment programme, fees, expenses, redemption/withdrawal limitations, standard of care and exculpation, etc. Prospective investors should also consult with their tax and financial advisors as well as legal counsel. This Document does not take into account the particular investment objectives, restrictions, or financial, legal or tax situation of any specific prospective investor, and an investment in the Fund may not be suitable for many prospective investors.

An investment in the Fund is speculative and involves a high degree of risk. Performance may vary substantially from year to year and even from month to month. Withdrawals/redemptions and transfers of Interests are restricted. Investors must be prepared to lose their entire investment, and without any ability to redeem or withdraw so as to limit losses.

The Fund's investment approach is long-term, investors must expect to be committed to the Fund for an extended period of time (3-5 years) in order for it to have an optimal chance of achieving its investment objectives. This Document may not be reproduced in whole or in part and may not be delivered to any person (other than an authorised recipient's professional advisors under customary undertakings of confidentiality) without the prior written consent of the Investment Manager.

SWISS INVESTORS:

The prospectus, the Articles of Association, the Key Investor Information Document "KIIDs" as well as the annual and semi-annual report of the Fund is available only to Qualified Investors free of charge from the Representative. In respect of the units distributed in Switzerland to Qualified Investors, place of performance and jurisdiction is at the registered office of the Representative. Funds other than the Luxembourg domiciled Alquity SICAV mentioned in this document may not be admitted for distribution in Switzerland.

Swiss Representative: FIRST INDEPENDENT FUND SERVICES LTD.,
Klausstrasse 33, 8008 Zurich
Swiss Paying Agent: Neue Helvetische Bank AG, Seefeldstrasse 215
CH-8008 Zurich