ESG & SUSTAINABILITY NEWS

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THE FORGOTTEN FACTOR DRIVING THE RISE OF SUSTAINABLE INVESTING.

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The intersection between sustainability and investing is driving systemic change in the capital markets. Bloomberg estimates that ESG investing (investment strategies considering Environmental, Social and Governance factors, in addition to financial factors) will represent a third of global assets under management by 2025.

Younger generations (who will inherit $73 trillion of wealth over the next two decades) champion ESG investing as a way to solve issues they care about, like climate change. Pension funds (focused on lower-risk and longer-term returns) are conditioning their investments to the adoption of ESG policies. Governments, wanting to maintain transparency in the capital markets, are pushing for ESG disclosure.

The rise of ESG investing has not come without a backlash. While advocates of sustainability believe capital markets can be a force for good, pragmatics argue that a business's mission is to maximize shareholder value, and it should not be subjected to ethical judgments. ESG investing has been condemned for being a mere PR effort - all talk and no actions - and even labeled as "woke capitalism".

ABOUT THE AUTHOR

Anna Alemani is Managing Partner at Pinnacle ESG Services, helping asset managers integrate long-term sustainability into their value-creation proposition to investors.

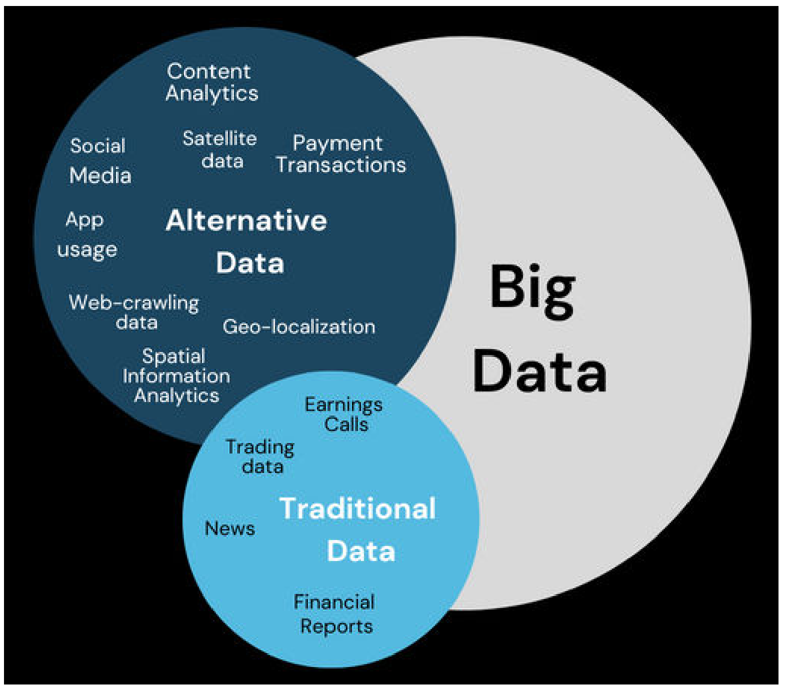
Anna's career in the financial industry started in 2006 at Standard & Poor's, where she was a Corporate Bond Rating Analyst covering the Energy sector. From 2011 to 2017 she worked as a Senior Credit Risk Analyst for Noble Group, managing due diligence, risk assessment & credit underwriting for a portfolio of investments in Power & Gas and Renewable Energy sector.

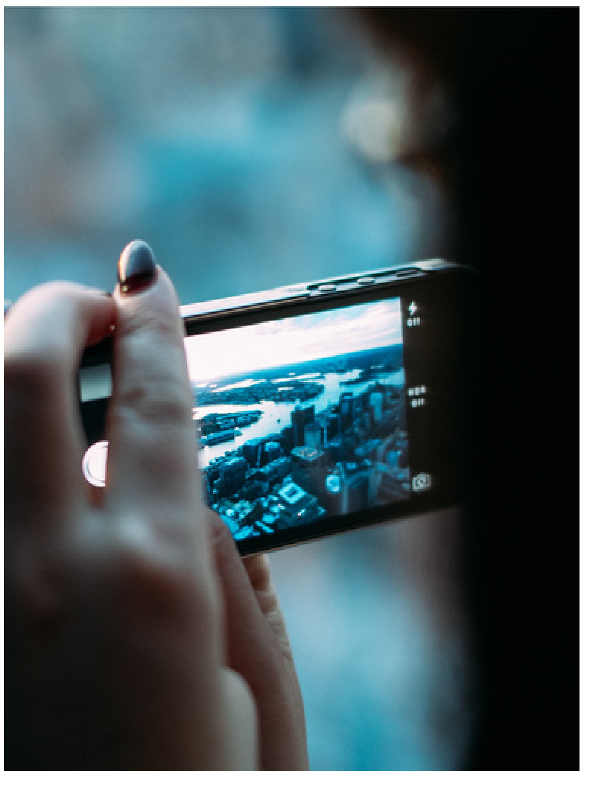
Anna holds a BA in Business Administration from Bocconi University in Milan and an MBA from Columbia Business School in New York. Anna also holds a certificate in ESG Investing from Columbia Business School.

Regardless of the ESG political debate, one unavoidable (but often overlooked) factor is fueling the growth in sustainable investing: technology.

The digital revolution gave consumers and investors access to virtually unlimited information. Financially material information about a company is no longer limited to SEC filings, ratings, and buy/sell recommendations from few trusted sources. Social media and other alternative data sources expose good or bad corporate behavior, allowing us to compare organizations on previously hidden areas of operations.

Non-traditional data sources enable investors to form expectations and make assessments on softer and more immaterial aspects of corporate conduct.





While the speed at which this information circulates (and the potential negative impact of misinformation) has increased, new technologies have also increased access to investing. Using digital platforms to get financial advice, younger generations of investors are increasingly drawing on unconventional digital dataset to support their decision making.

Most of the newly produced data (research shows that the amount of data generated globally in 2025 will be 10 times the amount of data generated ten years ago) is coming from end-user devices, making it largely unstructured.

Countless raw pieces of information do not always combine into knowledge or understanding. On the contrary, because it is easily available but not easily verifiable, more information can increase uncertainty and distrust. Storytelling facilitates consumption of quantitative and qualitative data.

A shared narrative around financial and non-financial aspects of how a company is managed can provide investors with meaning and orientation.

"The most powerful person in the world is the storyteller."

STEVE JOBS

Businesses must make money to survive. But to make money they must create value for customers, communities and society at large.

Traditional financial metrics tells us how "good" the actions taken by a company are on one yardstick: financial success. They do not fully explain "how" the company achieved its financial success. The "how" of being a profitable company is more complex and requires dealing with ambiguity, a wide range of disparate factors, and tradeoffs between short and long-term goals.

ESG gives investors an additional set of factors to highlight some of these trade-offs and make more informed decisions.

"Today's largest companies by market value do not need any tangible assets."

WARREN BUFFET

WHICH COMPANY WOULD YOU INVEST IN?

Metric	COMPANY A (Software & IT Services)	COMPANY B (Software & IT Services)
Annual Revenues	$2.4B	$2.2B
EBITDA	$650M	$500M
Stock Performance	+ 1.8% in 2022	+ 2.1% in 2022
Employee Turnover	25%	7%
Losses from Legal Proceedings	$9M	$2M
Cyber Security Accidents	8	1
Total Energy Consumed	20 GWh	15 GWh

GAAP accounting was developed when intangible assets (customer intangibles, brands, intellectual property, and human capital) represented about 15% of a company's value. Studies show intangibles assets today represent 90% of S&P500 market value and yet, financial statements have little information about them.

Non-financial reporting beyond standard financial reporting matters greatly to investors. ESG reporting is a complex task to do in the real world due to the lack of consistent and structured data, but this should not be a reason for not implementing it at all. Financial accounting as we know it also arose from a stakeholders' pull (not from a regulatory push); it did not materialize fully formed but was the product of a long evolution and a sharp debate. **Progress stems from unperfect trials.**

Increased transparency and accountability will pressure corporations in the short-term, but in the long-term businesses will benefit from sharing a narrative around non-financial aspects of their operations with a broader set of stakeholders. The growing adoption of alternative data in investing will translate into increased standardization and improved data quality. Companies will have more non-financial data available to report more broadly on their performance, which, in turn, will make sustainability reporting more reliable.

We might not refer to ESG ten years from now, but the underlying proposition of sustainable investing remains essential to maintain transparency and trust in the capital markets.

Learn more about how Pinnacle ESG helps clients prepare for enhanced disclosure: visit our website or email us at aalemani@pinnaclefundservices.com