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Roundtable Discussions

Beyond the Balance Sheet: ESG Integration, ESG Disclosure, and ESG Regulation

Standards and Solutions for Sustainable Development

Environmental, Social, and Governance Advisory in Emerging Markets

In collaboration with UN Sustainable Stock Exchanges Initiative

Hosted by London Stock Exchange Group

Report

January 24, 2018

Venue: London Stock Exchange Group

10 Paternoster Square, London, EC4M 7LS.

Beyond the Balance Sheet
**IFC Toolkit for Disclosure
and Transparency**

Summary

On January 24, 2018, IFC, in collaboration with the UN Sustainable Stock Exchanges, convened a Roundtable discussion on the topic, “Disclosure and Transparency and Environmental, Social, and Governance (ESG) Integration in Emerging Markets.”

A wide range of stakeholders participated in the meeting, which was held at the London Stock Exchange Group. They included investors, stock exchanges, regulators, reporting frameworks and standard setters, development partners, companies, and members of the IFC Corporate Governance Private Sector Advisory Group.

Participants discussed the needs of today’s investors for ESG disclosure, global trends in sustainability reporting regulation and policy, and the best platforms for stock exchanges and regulators to address sustainability.

They also provided feedback on IFC’s approach to governance of environmental and social issues in emerging markets as well as on its new Toolkit on Disclosure and Transparency.

Market-Opening Ceremony

The meeting kicked off with the opening of the London Stock Exchange, followed by a welcome by Mark Makepeace, chief executive officer of FTSE Russell, speaking on behalf of the London Stock Exchange, and Ethiopis Tafara, IFC’s vice president and general counsel, legal, compliance risk and sustainability.



Opening remarks set the context of the gathering by highlighting the central role of capital markets in bringing innovation and capital to tackle global challenges.

Public resources alone are insufficient to provide the \$7 trillion in annual investments needed to achieve the Sustainable Development Goals by 2030, thus giving the private sector a major role in meeting this objective. For example, one year earlier the London Stock Exchange listed the world’s first Forest Bond, issued by IFC, designed to prevent deforestation and promote development in emerging markets.



But leveraging the private sector is not an easy task. It requires vibrant capital markets across emerging economies—markets that foster investor trust and therefore must be based on a culture of disclosure and transparency.

It also means that investors must look beyond a company's balance sheet and evaluate nonfinancial drivers of corporate value, including the management and governance of environmental and social risks.

Stock exchanges, regulators, and IFC are key partners in advancing standards for increased disclosure and transparency to help build

investor trust and confidence in emerging markets.

Welcoming Remarks

Speakers

- **David Harris**, Group Head of Sustainable Business, London Stock Exchange Group
- **Ethiopsis Tafara**, IFC Vice President and General Counsel, Legal, Compliance Risk and Sustainability
- **Anthony Miller**, UNCTAD's Coordinator of the Sustainable Stock Exchanges Initiative
- **Miguel Marques**, Deputy Director, Multilateral Affairs & Development Aid, Ministry of Finance, Luxembourg

Summary of Key Points

The concept of disclosure and transparency is an essential part of IFC's mission to build liquid and efficient capital markets in emerging economies. Adhering to high standards of disclosure and transparency can mitigate some inherent risk associated with investments in emerging and frontier markets, such as weaker public institutions and governance as well as heightened social and environmental risk. The IFC Disclosure and Transparency Toolkit aims to help strengthen disclosure in emerging markets.

Stock exchanges have a responsibility to issuers to make sure they know what investors need. The London Stock Exchange participates in the Sustainable Stock Exchanges (SSE) Initiative and issued its own ESG reporting guidance last year, based on the SSE Model ESG Reporting Guidance, with the goal of generating investment grade data.

Japan's Government Pension Investment Fund, the world's largest, with \$1.3 trillion under management, plans to raise its allocation to environmentally and socially responsible investments to 10 percent of its stock holdings (about \$30 billion), using three ESG index funds (FTSE Blossom Japan Index, MSCI Japan ESG Select Leaders Index, and MSCI Japan Empowering Women Index).

Among the 84 exchanges in the UN Sustainable Stock Exchanges Initiative, 34 exchanges have issued guidance following the SSE Model ESG Reporting Guidance, and 12 more are interested but have expressed the need for technical support.

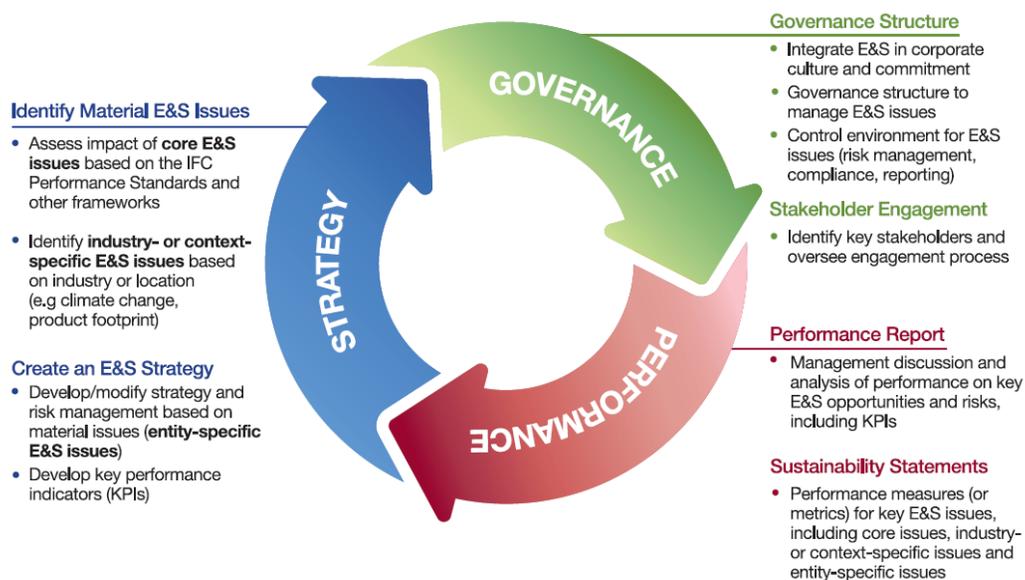
Since 2005, Luxembourg has provided funding for many global IFC corporate governance tools. Today, the tools have expanded beyond governance issues and now also focus on ESG. In keeping with that focus, Luxembourg's Ministry of Finance is providing financial support for the development of IFC's Disclosure and Transparency Toolkit.

Overview of the IFC Toolkit on Disclosure and Transparency

The toolkit was developed to help companies and financial institutions in emerging markets prepare comprehensive and best-in-class integrated annual reports that are appropriate for their size and organizational complexity, and adapted to the context of their operations.

It provides guidance on the disclosure of material information about a company's strategy, governance, and performance, following a holistic and integrated reporting approach (see Figure 1).

Figure 1. Holistic and Integrated Reporting Approach



This practical tool draws on our track record in applying IFC's Performance Standards for Environment and Social Sustainability and established Corporate Governance Methodology to assess and manage risks and opportunities that come with investing in emerging markets. The toolkit references and integrates internationally recognized standards and frameworks (GRI, IIRC, OECD, SASB, IFRS, and others), legal requirements, and best practices relevant to the preparation of a comprehensive annual report.

Who Will Find this Toolkit Useful?

Companies: The toolkit is designed to guide emerging-market companies (including IFC clients) in the preparation of their annual reports.

Investors and banks: It will support their valuation and credit analyses. **Stock**

Exchanges and Regulators: It will help them prepare reporting guidelines or regulation.

Panel 1. The Investors' Perspective

This panel explored recent trends in encouraging investors to integrate ESG factors into investment decisions and in measuring impact. The following were panel members:

- **Paul Lee**, Head of Corporate Governance, Aberdeen Standard Investment, United Kingdom
- **Ann Marie Jourdan**, Chief Legal Officer and Public Relations, Head of Corporate Governance, Fonds de réserve pour les retraites, France
- **Mandy Kirby**, Director of Reporting, Assessment and Accountability, UN PRI
- **John Plender**, Financial Times, and member of the IFC Corporate Governance Private Sector Advisory Group (Moderator)

Summary of Key Points

Increasing pressure for disclosure (regulatory, investors, voluntary)

- The French Energy Transition Law (Article 173) is a leading example of increased pressure for disclosure of ESG information. The law requires listed companies and institutional investors in France to disclose their exposure to physical and transition risks of climate change, and their contribution to international targets of limiting global warming.
- The Task Force on Climate-related Financial Disclosures did a great job of pulling together different guidance on the topic. One key recommendation relates to the role of boards in overseeing companies' future plans on climate change.
- The recent change in proxy voting by large U.S. institutional investors (Vanguard, BlackRock, State Street) in favor of climate-related shareholder resolutions to have ExxonMobil report on the impact of climate change is seen as a watershed.
- ESG integration has become a daily activity for some investors, and a part of the conversation with every client.
- PRI and a group of investors are working with the IIRC Corporate Reporting Dialogue to convey a consistent set of requirements for information needed from companies.
- In emerging markets, there is a need to better communicate that ESG standards are not imposed as a political agenda but rather as a way to support economic and social development.

Role of disclosure

- These days, corporate disclosure matters, because we live in a “show me” world. Investors will not invest unless they can trust a company's information. Disclosure provides the foundation that investors can build their analyses on.

- A key reason for the tendency to neglect ESG is the unknown—we don't know what is going to happen and when. However, this dimension is critical when investors take a long-term approach.
- Disclosure is especially important in emerging markets, because it is a way for companies to truly differentiate themselves. The story a company tells on environmental and social issues shows how ready it is for the future.
- PRI investors have a commitment to report on their integration of ESG into investment and engagement processes. Recently, investors have started to look at the SDGs.
- One major issue is the lack of information in emerging markets.

Use of disclosure by investors

- The *Fonds de réserve pour les retraites* is leading by example, systematically incorporating ESG into its portfolio management, assessing the carbon footprint of investments, and reporting voluntarily on its exposure to the risks of climate change.
- Lack of common methodologies to measure environmental and social impact is a real barrier for asset owners and managers attempting to aggregate information and gain a sense of their overall impact—including, for example, the carbon footprint of investment portfolios.
- Quality of information on energy transition is rather poor, leading a continued misallocation of capital. However, the situation is improving, and companies in industries with the greatest impact are starting to understand that they compete for investments based on carbon intensity.
- Aberdeen Standard Investment is an active manager with substantial investments in emerging markets. With an average investment-holding period of eight years, the company integrates ESG as a core driver of value in its financial analysis.
- ESG analysis is a tool for large investors to increase investment in emerging markets.
- It is important for companies to balance their self-reported information with that from other sources (big data).

Best practice in corporate ESG disclosure

- Investors want the following information from companies: 1) what the key risks are, 2) how those risks are managed at the operational level, and 3) how they are overseen at the board level.
- The IFC Toolkit on Disclosure and Transparency takes a holistic approach—covering strategy, governance, and performance. It shows companies how to provide the context that helps investors understand the company's position relative to environmental and social issues.

Panel 2. Perspectives of the Stock Exchanges and Regulators

This panel explored practical examples of sustainable regulatory frameworks (codes, listing rules, ESG reporting guidelines) by stock exchanges and regulators. The following participants discussed recent trends, challenges, and recommendations:

- **Nader Azar**, CEO, Amman Exchange, Jordan
- **Alina Aldambergen**, CEO, Kazakhstan Stock Exchange
- **Moremi Marwa**, CEO, Dar es Salaam Stock Exchange, Tanzania
- **Mohamed Farid Saleh**, Executive Chairman of the Egyptian Exchange and Chairman of the Federation of Euro-Asian Stock Exchanges
- **Jane Wilkinson**, Head of Sustainable Finance, Luxembourg Stock Exchange
- **Ethiopia Tafara**, IFC Vice President and General Counsel, Legal, Compliance Risk and Sustainability (Moderator)



Complementing the panel discussion were the following representatives of other stock exchanges and organizations, who shared their own experiences:

- **Natalya Khotosevskaya**, Deputy Chairman, Kazakhstan Stock Exchange
- **K. A. M. Majedur Rahman**, Managing Director, Bangladesh Dhaka SEL
- **Pham Hong Son**, Vice Chairman, State Securities Commission of Vietnam
- **Nguyen Quang Long**, Deputy Director, State Securities Commission of Vietnam

- **Edwin Ongera**, Senior Officer, Kenya Capital Market Authority
- **Tidimalo Poonyane**, Head of Legal Services and Board Secretary, Botswana Stock Exchange
- **Sergio Ricardo Liporace Gullo**, Head of Corporate Governance, Brazil Bolsa Balcao
- **Rebeca Franco de Abreu**, Sustainability, Brazil Bolsa Balcao
- **Felipe Pezo Riquelme**, Secretary MILA/ Trading & Postrade Product Manager, Santiago Exchange, Chile

Summary of Key Points

The role of stock exchanges and regulators

- Participants discussed various tools that stock exchanges and regulators can use to drive ESG disclosure and transparency. While each exchange had a unique approach, a consensus emerged on the need to balance listing and other requirements with market-based incentives—for example, the creation of ESG indexes and guidance for issuance of innovative financial products such as green and social bonds.
- Participants expressed broad support for the need to build capacity for companies through ESG reporting guidance as well as education and training of companies, including the board of directors.
- Representatives of the exchanges saw the IFC Toolkit on Disclosure and Transparency as a great tool to support a number of these activities, including educating and training, producing locally adapted disclosure guidance, provide it to the issuers as a practical guide to help in the preparation of the annual reports and establishing ESG disclosure and other listing requirements.

The importance of making the business case of ESG disclosure

- IFC and many others have studied the investment case for ESG, and the impact is clear, especially on the cost of capital. However, more scientific studies are needed to establish correlation, especially in emerging markets.
- The business case can also be made through more empirical study, based on examples from around the world, where indexes have been launched and have performed well.
- Another avenue is to use testimonials to aggregate and publicize the commitment of asset managers to integrate ESG into investments.

Balancing the cost benefit of ESG disclosure

- Corporate governance requirements and the need for periodic reporting can deter companies in emerging markets, such as Tanzania, from listing on the stock exchange. It adds a layer of complexity. At the same time, 80 percent of market activity in that country comes from international investors. Therefore, there is a

need to find a good tradeoff between encouraging issuers to list and responding to Investors' demands.

- It is important not to disadvantage companies that report on sustainability but still use conventional energy. Environmental and social impacts must be evaluated within the macro-economic context.
- Another danger is to create a dichotomy between listed and nonlisted companies, where only listed companies have to report. This can create a disincentive to list. A partial solution is to require banks to disclose the environmental and social impact of their loan portfolios with privately owned companies.
- It is important to recognize that companies are at various stages of evolution, with very different resources.

Green bonds and social bonds

- Disclosure and transparency are critical for the development of green and social bonds, especially regarding impact metrics, methodology for measuring impact, use of proceeds, and additionality.
- The main issue is a lack of consistency and transparency in the methodology used to measure impact. For example, two issuers financing the same project can have two completely different measures of CO2 emissions because of different methodologies, and those differences are not always explained.

ESG rating agencies

- Participants highlighted the limited number of companies that are covered by ESG rating agencies—and the need to expand the coverage.
- Another challenge raised was the lack of integration of ratings on finance and sustainability.

Sustainability-related indexes

- Sustainability indexes are a very important tool to reward companies. Many markets have introduced them. Others are exploring it.
- Some indexes have generated superior returns for several years, but these results have not been properly communicated and advertised.

Closing

Closing remarks reminded participants that corporate governance is a key enabler of environmental and social management, and that disclosure is an essential part of corporate governance.

The meeting ended with the famous quote from U. S. Supreme Court Justice Louis D. Brandeis: "Sunlight is said to be the best of disinfectants."

Next Steps

The Roundtable was an opportunity to refine IFC's strategy to promote disclosure and transparency in emerging markets and leverage the IFC Disclosure and Transparency Toolkit.

It helped strengthen IFC's partnerships with exchanges and the Sustainable Stock Exchange Initiative as well as regulators and investors in key markets.

Potential next steps, use and dissemination of the Toolkit include:

Educating and training: IFC's new toolkit could be used to educate market players in emerging markets and to center the dialogue around disclosure and transparency through conferences, roundtables and training of issuers.

ESG reporting guidance: Producing locally adapted guides/roadmaps on ESG disclosure. Providing the Toolkit to companies in emerging markets as a practical guide to help in the preparation of the annual reports as supplement to the ESG reporting guidelines.

Partnerships: Partnership with UN Sustainable Stock Exchanges Initiative and exchanges in promoting disclosure and transparency and providing technical assistance, particularly in emerging markets. Partnership with investors and investor associations.

ESG Codes: Updating and integrating environmental and social issues in corporate governance codes and scorecards.

Listing rules and other requirements: Review existing listing rules and propose amendments based on the toolkit.

ESG indexes: Development of ESG related indexes and rating instruments.

Studies: Joint studies to demonstrate a business case for ESG investment through capital markets.

Companies: How-to guide for companies in developing annual reports.

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