Update on the FTSE ESG data model - RC5 (2018/2019)

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‘Trending’ in Sustainability

The trust deficit (Edelman Trust Barometer) – trust of civil society in business, governments and NGO’s continues to deteriorate

The ‘divest’ movement – move to divest from fossil fuel-related assets

Millennials and ethical investing – millennials are prizing “doing good” over doing well

The plastic pollution disaster – surge in global awareness

Circular economy – emergent model for sustainable development

TCFD – substantial acceptance that climate change disclosure in relation to financial implications must be done, and using the TCFD framework

ESG regulation – slew of regulation/codes in the last 4 years compelling greater ESG disclosure

Smart beta – using ESG factors for performance differentiation

Growth in ESG integration (26% of professionally-managed AUM globally)
What is informing investor decision-making in ESG

- Greater awareness of the magnitude of ESG risks
  - Climate change (TCFD)
  - Corporate failures
    - BP, VW etc.
- Increasing ability to quantify ESG factors
  - ESG rating frameworks, laws on disclosure, reporting requirements
- Social media
  - Millennials
  - Speed of communication
What investors are looking for from corporates locally

- Good governance first and foremost
  - Robust processes
  - PEP’s
  - Conflicts of interest
- Integrated thinking
  - Meaningful data
  - Comparability
  - Balanced reporting
- Quantification of risks as well as opportunities
- Investible products
JSE’s hybrid approach to sustainability

**Regulatory Framework**
- Mandatory governance requirements
- King III apply or explain (integrated reporting)
- King IV (apply and explain, required from late 2017)

**Investment tools**
- SRI Index since 2004
- FTSE/JSE Responsible Investment Index Series and FTSE ESG Ratings from 2015
- Other asset classes – Green Bonds, etc.

**Engagement and Facilitation**
- ESG Investor Briefings
- Training
- Related events

**Advocacy**
- Signatory of UNPRI, partner to SSE, Chair of WFE SWG, member of ASEA SWG and AIRC
- Represented on CRISA, SAICA, Integrated Reporting Committee
- Other ad hoc advisory groups
FTSE/JSE Responsible Investment Indices

- Index Series launched October 2015
  - Aspirational benchmark
  - Evolution of SRI index to meet investor demands and expand value proposition

- Broad sustainability assessment
  - ESG foundation – based on adoption of FTSE Russell ESG Ratings
  - Focus on investor usability and access to data

- Two indices in series at present
  - FTSE/JSE Responsible Investment Index
    - Benchmark, weighted by market capitalisation
    - 76 constituents as at June 2018
  - FTSE/JSE Top 30 Responsible Investment Index
    - Tradable, equally weighted
Eligibility for FTSE/JSE RI Indices

- Base universes:
  - FTSE All World Index AND
  - FTSE/JSE Shareholder Weighted (Swix) All Share Index

- Ineligible if excluded from either index at any time during process or after quarterly reviews

- If eligible, assessment against the FTSE ESG Ratings methodology is conducted
  - Each company assessed once per year
  - ESG Rating applied at semi-annual index reviews in June and December
  - Minimum inclusion for benchmark index is currently 2.5 overall ESG Rating
FTSE ESG Ratings Model: snapshot
Score and exposure levels

- **Scoring: theme, pillar and overall**
  - Covers six levels from 0 to 5
  - A score of 3 is considered good practice

- **Theme exposure**
  - Measures the relevance / risk exposure of the company relative to the theme
  - Considers factors such as industrial sector, geographic presence and revenue generated from secondary / subsidiary activities
  - If not applicable, theme not assessed
  - Impacts weighting of theme in scoring at pillar and overall level – higher exposure themes have larger impact on rating – therefore advisable to focus on areas with high exposure and low score
MODEL UPDATES
Why update the model?

• Sustainability imperatives are evolving
• Gives companies a robust and helpful framework for ESG disclosure on an on-going basis
• Help alleviate “framework fatigue”
  • Align with emerging best practice and global trends
  • Considers other more widely-used frameworks
    • CDP
    • GRI
    • TCFD
    • WBCSD etc.
## ESG methodology enhancements 2018
For 2018 – 2019 Research Cycle

### Environmental Pillar

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Biodiversity (EBD)</td>
<td>No changes</td>
</tr>
<tr>
<td>Water Security (EWT)</td>
<td>Major enhancements to improve relevance for investors and better align with other disclosure frameworks</td>
</tr>
<tr>
<td>Pollution &amp; Resources (EPR)</td>
<td>No changes</td>
</tr>
<tr>
<td>Climate Change (ECC)</td>
<td>3 new indicators applicable to high impact subsectors aligning with Climate Action 100</td>
</tr>
<tr>
<td>Environmental Supply Chain (ESC)</td>
<td>No changes</td>
</tr>
</tbody>
</table>

### Social Pillar

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Responsibility (SCR)</td>
<td>No changes</td>
</tr>
<tr>
<td>Health &amp; Safety (SHS)</td>
<td>No changes</td>
</tr>
<tr>
<td>Human Rights &amp; Community (SHR)</td>
<td>No changes</td>
</tr>
<tr>
<td>Labour Standards (SLS)</td>
<td>2 new indicators</td>
</tr>
<tr>
<td>Social Supply Chain (SSC)</td>
<td>2 new indicators</td>
</tr>
</tbody>
</table>

### Governance Pillar

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anti-Corruption (GAC)</td>
<td>No changes</td>
</tr>
<tr>
<td>Corporate Governance (GCG)</td>
<td>1 new indicator</td>
</tr>
<tr>
<td>Risk Management (GRM)</td>
<td>No changes</td>
</tr>
<tr>
<td>Tax Transparency (GTX)</td>
<td>No changes</td>
</tr>
</tbody>
</table>
Water Security theme - re-named from Water Use (EWT)

- Water increasingly considered a risk and investors need more information to be able to assess the risks
- Key changes affect high and medium impact sectors
- Changes relate to:
  - governance, strategy, risk management, metrics and targets
  - focus on withdrawal and discharge over consumption

Full details available in handouts
Labour Standards Theme (SLS)

To reflect the trend on diversity the following 2 indicators have been added to the theme.

<table>
<thead>
<tr>
<th>Legend</th>
<th>Indicator type</th>
<th>Indicator description</th>
<th>Applicability:</th>
</tr>
</thead>
<tbody>
<tr>
<td>SLS32</td>
<td>Quantitative</td>
<td>Percentage of global staff with a disability.</td>
<td></td>
</tr>
<tr>
<td>SLS33</td>
<td>Quantitative</td>
<td>Percentage of women in the global workforce.</td>
<td></td>
</tr>
</tbody>
</table>
To reflect focus on animal welfare the following indicator has been added for companies in the food and pharmaceutical sectors.

<table>
<thead>
<tr>
<th>Legend</th>
<th>Indicator Type</th>
<th>Indicator Description</th>
<th>Subsectors</th>
<th>Exposure</th>
</tr>
</thead>
<tbody>
<tr>
<td>SSC56</td>
<td>Qualitative</td>
<td>Supplier policy addresses animal welfare:</td>
<td>3573 Farming, Fishing &amp; Plantations</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. Statement addressing the issue / comply with local laws</td>
<td>3577 Food Products</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. Policy / Principles / Code</td>
<td>5337 Food Retailers &amp; Wholesalers</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>5757 Restaurants &amp; Bars</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>4577 Pharmaceuticals</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>4573 Biotechnology</td>
<td></td>
</tr>
</tbody>
</table>

The following indicator has been added for companies in the banking sector.

<table>
<thead>
<tr>
<th>Legend</th>
<th>Indicator Type</th>
<th>Indicator Description</th>
<th>Subsectors</th>
<th>Exposure</th>
</tr>
</thead>
<tbody>
<tr>
<td>SSC57</td>
<td>Qualitative</td>
<td>Evidence of green or sustainable bond issuance and lending mechanism:</td>
<td>8355</td>
<td>Banks</td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. Evidence of at least one green / sustainable bonds / lending mechanism.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. Evidence of multiple green / sustainable bond issuances or of multiple lending mechanisms.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: FTSE Russell
To reflect growing focus on equal opportunities the following indicator has been added to the Theme.

<table>
<thead>
<tr>
<th>Legend</th>
<th>Indicator type</th>
<th>Indicator description</th>
</tr>
</thead>
<tbody>
<tr>
<td>GCG50</td>
<td>Quantitative</td>
<td>Percentage of women on the Executive committee or equivalent.</td>
</tr>
</tbody>
</table>

Applicability: Subsectors Exposure: M
The following 3 indicators have been added to the Theme for high impact subsectors.

<table>
<thead>
<tr>
<th>Legend</th>
<th>Indicator type</th>
<th>Indicator description</th>
<th>Applicability: Subsectors</th>
<th>Exposure</th>
</tr>
</thead>
<tbody>
<tr>
<td>ECC73</td>
<td>Qualitative</td>
<td>The company discloses:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. Its memberships of trade associations that engage on climate-related issues.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. Its involvement in those trade associations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECC74</td>
<td>Qualitative</td>
<td>The company has a stated policy or commitment to ensuring:</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. Consistency between its climate change policy and the positions taken by the trade associations of which they are members</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. For responding appropriately in those instances where the trade association position is significantly weaker than or contradicts that of the company</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ECC75</td>
<td>Qualitative</td>
<td>Does the company's remuneration for senior executives incorporate climate change performance?</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>a. CEO.</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>b. At least one other senior executive.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: FTSE Russell
Key points

- FTSE process of updating the model has changed
  - Cycle is June to June
  - Governance process enhanced to include advisory committee sign-off
  - Model shared with all assessed companies
- Model updates already effective for the current research cycle
  - Companies being assessed for the Dec 2018 index review already affected
NEW FEATURES ON YOUR FTSE QSD PORTAL
You can access details on the review process via your company user access to the FTSE QSD portal in this way.

**Useful information for Company Review**

Please also see “Resources” for some useful information

Please click **Resources > Guides & Contacts > Further information**
New features on FTSE QSD portal - CPC

CPC refers to a new feature called Corporate Peer Comparison.

Your company name

Your company ICB classification details

Welcome to the Corporate Peer Comparison tool (CPC)

FTSE Russell’s CPC provides:

1. The most recent ESG Rating for your company
2. Comparative ESG Rating data for your company versus its peers, and
3. Our assessment of your company’s Green Revenues

Note: No actions are required. This site is separate from the Company Review process.

The information provided is confidential and intended for the use of this audience only. Additional distribution is prohibited.

<< Please use the menu on the slide to navigate the CPC
Company vs. sub-sector and industry averages (using dummy data)

This refers to the global average scores for your sub-sector and Industry globally (i.e. compared to your global peers as assessed by FTSE Russell)

Data used here is sample data for illustration purposes only
Company vs. top 5 global peers

A comparative view of your company vs. its top 5 peers in the same sub-sector globally. Each peer is named.

Data used here is sample data for illustration purposes only.
PARTING SHOTS
Index performance – SWIX All Share vs FTSE/JSE RI Benchmark and FTSE/JSE RI Top 30 indices

Debunking the notion that sustainability considerations (ESG factors) negatively impact returns?
Key messages

• **Climate change risk** is front and centre – pressure for disclosure and mitigation action growing exponentially

• **Water risk** is an issue of rapidly growing concern

• **ESG integration** in investments is here and is growing AND debunking the notion that it negatively impacts returns

• **ESG disclosure is a key part of communicating** a credible story to stakeholders in a society that is mistrustful
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