



# Demystifying Environmental, Social, Governance (ESG)



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**Sophie Sarsfield, Sustainable Investment & ESG Manager, provides an explanation of common terms associated with ESG (Environment, Sustainable and Governance).**

Sustainability and a desire to live in a more sustainable way, both personally and professionally, are topics we are hearing about more and more in our day-to-day lives. More frequently we are hearing about the many issues our world is facing, including climate change, inequality, and a lack of financial wellbeing and inclusion. There is a growing effort amongst policy makers and international bodies to put in place solutions to help alleviate these issues. Financial institutions, particularly wealth and investment managers, are also tackling what part they have to play in taking better care of our world and as fiduciaries of large pools of capital for investors & retirees globally.

In the investment world, sustainability and ESG (Environment, Sustainable and Governance) factors continue to be a driving force for positive change. There have been significant efforts by policy makers and regulators to drive capital towards sustainable investment regulation. With all of this change it can be hard to keep informed and well-versed on terminology that is used when discussing sustainable investment. With that in mind, we have taken some of the more common terms that are used today when discussing sustainable investment and try to demystify these for you.



## Sustainability

A concept

Sustainability is when the needs of the present generation can be met without compromising the ability of future generations to meet their own needs. In doing so, the aim is to achieve a balance between economic growth, social wellbeing and environmental care.



## ESG factors

A concept

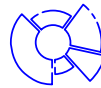
A set of non-financial factors that a company uses in their analysis process to identify material risks and growth opportunities related to sustainability<sup>26</sup>:



**Environmental** – the environmental impact of a company. Factors such as carbon emissions, energy efficiency, recycling practices, water pollution and supply chain sustainability.



**Social** – the social impact of a company in terms of their relationships with employees, customers, suppliers, and stakeholders. Factors such as equity, inclusion and diversity metrics measure how the company promotes social good within its operations.



**Governance** – the governance around policies that balance a company's financial goals with its social and environmental responsibility. This includes executive pay and political contributions, tax strategy and diversity on the board of directors.

ESG investment strategies may consider the following key issues in the investment process, alongside financial factors:

### Environmental



Carbon emissions



Water Stress



Opportunities in clean tech

### Social



Privacy and data security



Controversial sourcing



Community relations

### Governance



Business ethics



Pay figures



Tax transparency

<sup>26</sup> Source: ESG Investing and Analysis (cfainstitute.org)



## EU Sustainable Finance Disclosure Regulation (SFDR)

Regulation

The **EU Sustainable Finance Disclosure Regulation (SFDR)** came into force on the 10th March 2021. The regulations were introduced with the objective of implementing a harmonised approach in respect of sustainability-related disclosures for European investment funds. When fully implemented the disclosure regulations hope to enable greater transparency for investors and to allow for a direct comparison on investments when considering sustainability.

## Greenwashing

Definition

Greenwashing arises when a company provides misleading or inaccurate information about their sustainability credentials, making it appear that the company is more sustainability focused than it truly is. Greenwashing by a company can be intentional and can also occur unintentionally.

## Responsible investing

Definition

An investment approach that focuses on incorporating environmental, social and governance factors into investment decisions through ESG incorporation and active ownership/stewardship<sup>27</sup>.

## ESG incorporation<sup>28</sup>

A concept

This involves considering ESG issues when building a portfolio. ESG incorporation can be achieved using different approaches as follows:

**Integration** – Specifically including ESG issues in investment analysis and decisions, to better manage risks and improve returns.

**Screening** – Applying filters to lists of potential investments to rule companies in or out of contention for investment, based on an investor's preferences, values or ethics

**Thematic** – Seeking to combine attractive risk return profiles with an intention to contribute to a specific environmental or social outcome. Includes impact investing.



<sup>27/28</sup><https://www.unpri.org/an-introduction-to-responsible-investment/what-is-responsible-investment/4780.article>



## Active ownership/ stewardship<sup>29</sup>

### Definition

Where investors can encourage the companies they are already invested in to improve their ESG risk management or develop more sustainable business practices.

These are just some of the many terms that have developed as the area of sustainability and ESG investing has grown. There are many more terms and the differences between them can at times be very nuanced. So we recommend that you:

- ▶ carry out your own research to ensure that how an investment is described aligns with your personal goals.
- ▶ ask questions if you are unclear on meaning of some of this terminology and keep asking until you are comfortable you understand.

## Summary

- ▶ Sustainable investing is a great way to bring about positive social & environmental change by combining capital and the investors' desire to make a sustainable impact through their savings and investments. However, investing in this manner is not without its challenges, indeed greenwashing is currently a hot topic.
- ▶ Getting the balance right between enthusiastically embracing sustainability versus overstating the sustainability claims of products or services, intentionally or unintentionally, is proving difficult for all industries, investment management included. However, regulation and industry practices are improving.
- ▶ Making positive change starts with understanding. If sustainable or ESG investing is something that is of interest to you, be sure to discuss the options available to you with your **Private Client Manager**.

To find out more about our commitment to **ESG** and sustainable investing, visit [bankofireland.com/sustainableinvesting](https://bankofireland.com/sustainableinvesting)

<sup>29</sup><https://www.unpri.org/an-introduction-to-responsible-investment/what-is-responsible-investment/4780.article>

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