



# CHANGE THE CONVERSATION

Redefining How Companies Engage  
Investors on Sustainability

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# Acknowledgements

Ceres would like to acknowledge report author, **Kristen Lang**, Director, Company Network at Ceres, with special recognition of Amy Augustine for her leadership in the development of the report.

## Special Thanks

We would also like to extend special thanks to those colleagues that provided support, insightful feedback and guidance in the development and release of the report: Natasha Scotnicki, Peyton Fleming, George Grattan, Brooke Barton, Veena Ramani, Kirsten Spalding, Karen Rivera, Sara Sciammacco, Barbara Grady, Troy Shaheen, Dan Saccardi, Blair Bateson, Mary Ann Ormond, John Weiss, Alba Munoz and Laura LoSciuto.

## Project Contributors

Ceres would also like to thank those company and investor representatives that dedicated their valuable time and thoughtful insights to inform our recommendations and this report. The views in this paper are those of Ceres alone and do not necessarily reflect those of these contributors.

**Graphic design** by Patricia Robinson

**Ceres** is a sustainability nonprofit organization working with the most influential investors and companies to build leadership and drive solutions throughout the economy. Through powerful networks and advocacy, Ceres tackles the world's biggest sustainability challenges, including climate change, water scarcity and pollution, and human rights abuses. Our mission is to transform the economy to build a sustainable future for people and the planet.

## For more information, please contact:

Kristen Lang  
Director, Company Network  
Ceres  
[lang@ceres.org](mailto:lang@ceres.org)

# Letter from the President

In 1989, the investors who joined together to form Ceres in the wake of the Exxon Valdez oil spill were at the forefront of a transformative movement in business. They understood that the most profitable companies in the long run will be those that recognize the imperative to invest in more sustainable business practices. They knew then what we say at Ceres today: **sustainability is the bottom line.**

In 2017, investments guided by environmental, social and governance (ESG) criteria rose to \$12 trillion in the U.S. alone, nearly double from 2014 levels.<sup>1</sup> ESG investment now represents 1 of every 4 dollars invested in the U.S., and has risen to nearly \$23 trillion globally.<sup>2</sup>

Companies, in turn, are committing to sustainability like never before. Recent Ceres research shows that among 600 of the largest publicly traded companies in the U.S., nearly two-thirds have commitments to reduce greenhouse gas (GHG) emissions, half are actively managing water resources and nearly half are now actively protecting the human rights of their employees.

As ESG investment climbs, the business case for corporate sustainability only strengthens. In early 2019, the World Economic Forum included the following among its top global economic risks: extreme weather, biodiversity loss, failure to mitigate climate change and the water crisis.<sup>3</sup> While risk mounts, wide-ranging sources—including Oxford University, Harvard Business School, Morgan Stanley and Bank of America Merrill Lynch—continue to affirm that a focus on a sustainable business strategy can provide a competitive advantage in stock price, cost of capital and operational performance.<sup>4</sup> These trends underscore the link between ESG and financial performance, and further demonstrate that those issues once considered extra-financial are, in fact, material financial risks and opportunities impacting the bottom line.

And yet, when it comes to engaging investors on sustainability, the vast majority of companies are still missing the mark. With rare exception, they fail to present sustainability as an integral component of business strategy and decision-making, or as a driver of increased business resilience and revenue growth. Reflecting this, 41 percent of the CEOs surveyed by Accenture could not accurately quantify the business value of their sustainability initiatives. Such failures are missed opportunities.

Ceres envisions a future where sustainability is not a separate work stream, but an integral component of business planning and execution that investors routinely assess and reward. To get there, we must redefine how companies engage investors on sustainability.

**Simply put, we must change the conversation.**



# Letter from the President

“ Ceres is committed to a future where sustainability is not a separate work stream, but an integral component of business planning and execution that investors routinely assess and reward. To get there, we must redefine how companies engage investors on sustainability. ***Simply put, we must change the conversation.***”

Drawing from our interviews with more than 25 Ceres investor partners, *Change the Conversation* highlights key trends in investors’ evolving expectations for corporate sustainability. It presents **nine recommendations** to guide companies toward more meaningful and effective investor engagement on ESG issues, helping them to not only meet investor expectations, but also capture competitive advantage.

Three trends are clear as we confront a rapidly changing world. *First*, sustainable investing is not a passing phenomenon or a niche investment strategy—it is a fast-growing movement redefining capital markets. As Larry Fink, CEO of asset manager powerhouse BlackRock, recently told the *Financial Times*, “Sustainable investing will be a core component of how everyone invests. We are only at the early stages.” *Second*, investors must quickly move to demonstrate with transparency how calls for corporate action on ESG will be rewarded in the marketplace. And *finally*, corporate commitments to “do better” are no longer enough. Instead, companies must proactively demonstrate how sustainability issues are fully considered and weighed equally as business concerns and how sustainable innovation is driving new business opportunity. In effect, they must show that they, too, understand **sustainability is the bottom line.**



A handwritten signature in blue ink that reads "Mindy A. Lubber". The signature is fluid and cursive.

**Mindy S. Lubber**  
CEO and President  
Ceres

# Executive Summary

When Ceres released [\*The Ceres Roadmap for Sustainability\*](#)—our vision for corporate sustainability leadership in the 21st century—in 2010, sustainable business leaders were easily identified and few in number. Now it is commonplace to find a “sustainability” or “corporate responsibility” section included on company websites. Increased public awareness, regulation and investor interest has made acknowledging environmental and social impacts, and claiming a commitment to be “sustainable,” a mainstream practice for doing business today.

Nearly half of the 600 largest public U.S. companies are formally communicating with investors in some way on sustainability, via annual meetings, quarterly earnings calls, investors days and more.<sup>5</sup> But how those companies are engaging, and the depth and value of those engagements, varies widely. For example, most companies still share information in ways that reinforce the misconception that these issues are extra-financial and not material. They also fail to provide investors with the information they need to understand and value the positive impacts of sustainable business strategies on corporate health and financial performance.

For 30 years, Ceres has partnered with leading global corporations and investors to better integrate environmental and social considerations into business strategies—effectively **working together to redefine business as usual**. As active advocates leading these corporate and investor dialogues, we understand that for many companies, engagement with investors on environmental, social and governance (ESG) issues is fraught with trepidation and resistance. This leads to reactive, less-effective interactions with interested investors. Without deeper insight on what ESG information investors value, how investors want to see this information and who they want to hear from, companies will continue to fall short in providing the decision-useful information investors need to fully understand and value the financial implications of critical sustainability risks and opportunities.

In collaboration with more than 25 Ceres investor partners—including some of the world’s largest asset managers and asset owners, ESG-oriented asset managers, ESG and governance analysts, and proxy advisors—we conducted a series of interviews to further explore the themes and observations gleaned from our decades of experience in corporate and investor dialogues.

**In these conversations, we sought to get answers to the most common questions we hear from companies every day:**

- What does meaningful ESG disclosure look like to the investor community, and where and how do they want to see it?
- What timeframes are investors interested in: short- or long-term?
- How do investors define sustainable business leadership?
- How, in an increasingly crowded space of companies claiming to be sustainable, can companies stand out and be rewarded by investors for their leadership?

# Executive Summary

What emerged is a set of **nine recommendations, outlined under three strategies**, to guide companies toward more meaningful and effective investor engagement on ESG issues.



## Strategy #1: Formalize sustainable business integration

RECOMMENDATIONS



1. Demonstrate accountability for sustainability.



2. Develop the sustainability business case.



3. Cultivate collaboration between sustainability, investor relations and governance teams.



## Strategy #2: Identify what to disclose and where to disclose it

RECOMMENDATIONS



1. Focus investor-directed disclosures on what is material, but don't ignore emerging trends.



2. Disclose decision-useful information, both quantitatively *and* qualitatively.



3. Disclose sustainability information consistently where investors are already looking.



## Strategy #3: Implement a proactive investor engagement strategy

RECOMMENDATIONS



1. Use language that investors understand and value.



2. Leverage the C-suite and board of directors as key messengers.

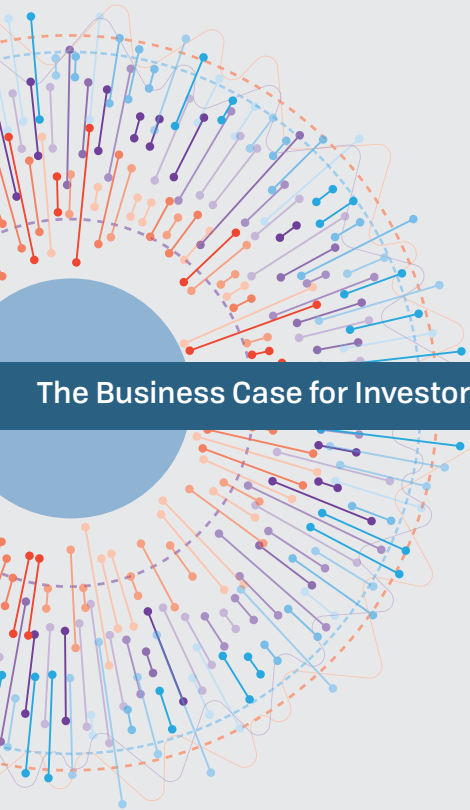


3. Diversify investor engagement strategies.

This report describes how these recommendations relate to and build upon one another. Most importantly, it explains how companies that take these steps can be better positioned to meet investor expectations and capture competitive advantages.

# The Sustainable Investment Landscape

Integrating environmental, social and governance (ESG) factors in investment decision-making is fast becoming a mainstream practice among investors of all types and sizes. Today, ESG investing\* represents about one quarter of all professionally managed assets around the world.<sup>6</sup> In 2017, investments guided by ESG criteria rose to \$12 trillion in the U.S. alone, nearly double from 2014 levels,<sup>7</sup> and these investments have risen to nearly \$23 trillion globally.<sup>8</sup> And wealth transfers to a new generation of millennial investors will likely drive this trend to accelerate even further and faster.



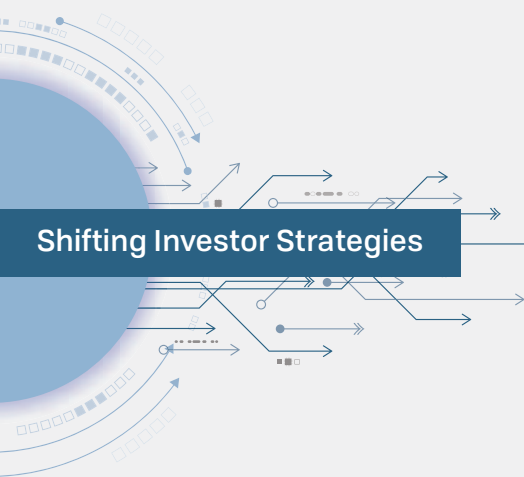
## The Business Case for Investors

- A comprehensive analysis of existing research done by Deutsche Asset Management and the University of Hamburg concludes that the large majority of research shows a positive relation between ESG criteria and corporate financial performance.<sup>9</sup>
- According to 2017 research by Bank of America Merrill Lynch, ESG attributes are a better signal of future earnings volatility than any other measure. The research demonstrates that if investors had focused stock holdings in companies with above average ESG scores, they could have avoided 90 percent of the bankruptcies occurring since 2008.<sup>10</sup>
- Academic research analyzing 2,000 US companies from 1993-2013 shows that companies that make significant investments in material ESG issues relevant to their industry have better future performance than companies that do not address these issues. High growth in profit margins and superior risk-adjusted stock returns are among the benefits.<sup>11</sup>
- Research by MSCI using data for 1,600 stocks between 2007-2017 found that ESG ratings for companies are a useful financial indicator. The data reveals that high ESG-rated companies showed higher profitability, higher dividend yields and lower business-specific tail risks, in addition to displaying less systemic volatility and higher valuations.<sup>12</sup>

\* Environmental, Social and Governance (ESG) investing is a term often used as an umbrella term for socially responsible investing, impact investing and mission-related investments. At their core, ESG investments consider environmental, social and governance factors alongside—and as critical influencers of—financial performance.



# The Sustainable Investment Landscape



- A 2018 Morgan Stanley survey of 118 global asset owners found that 84 percent are pursuing or actively considering ESG integration in their investment processes. Sixty percent began doing so in the last four years and 37 percent within the last two.<sup>13</sup>
- Schroder's 2018 Global Institutional Investor Study found nearly three quarters of institutional investors globally believe sustainable investing will grow in importance in the next five years. Almost half report they had increased their allocations to sustainable investments over the past five years.<sup>14</sup>
- Bank of America Merrill Lynch predicts that within the next two to three decades, millennials could put upwards of \$20 trillion into U.S.-domiciled ESG directed investments. This would roughly double the size of the U.S. equity market.<sup>15</sup>

These trends are accompanied by increased investor activity focused on improving and accelerating company ESG performance and commitments. To enable effective engagement and accurate assessment, investors are coupling increased activity with demands for improved access to more and better information. More than ever, what companies publicly disclose and proactively share with investors on ESG issues is critical in distinguishing leadership among sector peers.

While investor engagement strategies vary—including direct dialogues, proxy voting, collective requests and shareholder proposals—those related to environmental and social issues are increasing in frequency, influence and impact. Shareholder proxy proposals that at one time received only single percentage points in voting support are now reaching majority levels. The 2017 and 2018 proxy seasons, for example, saw majority votes for climate change-related shareholder resolutions at some of the largest energy companies in the world, including ExxonMobil, Occidental Petroleum, PPL and Kinder Morgan. The 2018 proxy season also saw many shareholder resolutions withdrawn in response to proactive corporate commitments and actions driven by investor dialogue and engagement.

Beyond asking companies to recognize, assess and mitigate sustainability risks they face, investors also want to see sustainability as a path toward future success. In 2018, the then CEO and Chairman of Vanguard called on companies in its portfolio to proactively integrate sustainability into business strategies.

“ For too long, companies have sacrificed long-term value creation to generate short-term results, which erodes the sustainability strategic investors seek.”

**Bill McNabb**  
former Vanguard Chairman and CEO



# The Sustainable Investment Landscape

## The Impact of Collective Investor Engagement

Launched in 2017, the global investor collaboration Climate Action 100+ is supported and coordinated by Ceres, Asia Investor Group on Climate Change ([AIGCC](#)), Investor Group on Climate Change ([IGCC](#)), Institutional Investors Group on Climate Change ([IIGCC](#)) and Principles for Responsible Investment ([PRI](#))—with investors representing more than **\$31 trillion**. Focused on the biggest GHG-emitting companies in the world, Climate Action 100+ investors are calling on these companies to set science-based targets for GHG emissions reductions and improve climate-related financial disclosures—specifically to be in line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). In just one year, the Climate Action 100+ campaign has spurred action from some of the biggest emitting companies in the world.

After extensive negotiations with investors, **Royal Dutch Shell** agreed to strengthen its commitment to reduce GHG emissions 20 percent by 2035 and 50 percent by 2050. Importantly, the company's targets will include "Scope 3" emissions—specifically, direct and indirect emissions from consumers, including drivers' use of its fuel. The company will also tie executive compensation for a wide swath of its leadership to achievement of these commitments. While these commitments do not align the company with Paris Agreement goals (a demand of many impact investors), the commitments do stand out among its oil and gas peers.



And in his 2019 letter to CEOs, Larry Fink, the CEO of BlackRock explains that as fiduciaries for its clients, BlackRock advocates for practices that it believes will drive sustainable, long-term growth and profitability. The letter again argues that companies without purpose will deliver subpar financial returns.

“ Profits are in no way inconsistent with purpose—in fact, profits and purpose are inextricably linked. Purpose unifies management, employees, and communities. It drives ethical behavior and creates an essential check on actions that go against the best interests of stakeholders. Purpose guides culture, provides a framework for consistent decision-making, and, ultimately, helps sustain long-term financial returns for the shareholders of your company.”

**Larry Fink**

CEO of BlackRock

Asset manager giant State Street is also weighing in affirmatively for stronger ESG actions. In 2018, the firm used its voting power to influence companies in its portfolio on board gender diversity, voting against 511 companies for failing to address gender diversity. State Street's interest and engagement resulted in 152 companies adding a woman director to their boards and another 34 agreeing to do so in the future.<sup>16</sup>

# The Sustainable Investment Landscape

Investors are pushing for these measures because they recognize that **sustainability is core to business value creation**. Studies from wide-ranging sources, including Oxford University, Harvard Business School, Morgan Stanley and Bank of America Merrill Lynch, all affirm that a focus on a sustainable business strategy can provide a competitive advantage in stock price, cost of capital and operational performance.<sup>17</sup>


As an analyst from a major U.S. asset management firm explained to us, “I think it is inevitable and positive that these issues will get more weight in the future. Consumers are going to care more and more about this. It’s already happening. And clients too. One reason we have an ESG staff that is three times bigger than it was a few years ago is because clients are asking more questions.” Socially responsible investment (SRI) firms are also seeing these shifts. As one SRI analyst observed, “There are big changes we are noticing—like the majority vote at Exxon with BlackRock and Vanguard. These large firms are building up their teams in this area. **What was once on the fringes is now the mainstream.**”





The background of the page is a dark blue, almost black, color. It features a subtle grid pattern that is slightly out of focus. There are several circular bokeh light effects scattered across the image, primarily on the left side, in shades of yellow, orange, and light blue. The overall aesthetic is modern and technological.

# RECOMMENDATIONS



For 30 years, Ceres has been an advocate at the table with companies and investors; and we understand that for many companies, engagement with investors on environmental, social and governance (ESG) issues can be met with apprehension, skepticism and confusion.

The main touchpoint for many companies can be limited to that of third-party ESG surveys rather than direct investor engagement. The significant time and resources required to respond to surveys means these ESG information requests are frequently handled independently by the sustainability team in isolation from other investor relations activities. Internal misalignment and the absence of clear business case for sustainability can lead to reactive, less-effective interactions with interested investors. In the end, many companies are left wondering exactly *what* information is being presented to investors, *who* is accessing it and *how* investors are using the analysis in their investment decision-making.

To date there has been much intellectual capital spent analyzing and suggesting *which* information companies should disclose to investors—with Ceres' own thought leadership and standard-setting frameworks (The [Ceres Roadmap](#), [Investor Water Toolkit](#) and [Engage the Chain](#)) complementing disclosure guidance offered by the Global Reporting Initiative, Task Force on Climate-related Financial Disclosures and Sustainable Accounting Standards Board, among others. This report aims to provide deeper insight on *how* investors want to see this information and who they want to hear from, so that companies can provide the decision-useful information investors need to fully understand and value the financial implications of critical sustainability risks and opportunities.

Ceres research and interviews with investors helped us to identify **nine recommendations** that companies can pursue across **three strategies**. This approach underscores a critical theme that emerged from our investor interviews: credible and meaningful communication of ESG information to investors requires that companies not only talk the talk, but are prepared to demonstrate how they are walking the walk.

- **Strategy #1: Formalize sustainable business integration:** The recommendations included in this first strategy respond to increasing investor expectations for companies to demonstrate accountability for ESG, a desire to understand the business case for sustainability and the importance of internal alignment and buy-in.
- **Strategy #2: Identify what to disclose and where to disclose it:** Investors are calling for more robust and comparable disclosure that gives them the information they need to make better investment decisions. The recommendations within this strategy guide companies toward the disclosure of decision-useful ESG information and provide insight into where investors go to find it.
- **Strategy #3: Implement a proactive engagement strategy:** Building on the foundation of improved business integration and alignment, and more robust and targeted ESG disclosure, the recommendations focused on engagement help companies to shift from reactive to proactive. By using language investors value, positioning leadership as key messengers and diversifying investor engagement strategies, companies can leverage their sustainable business strategy to differentiate from peers and effectively position sustainability as an important driver of business value.



The nine recommendations identified across the three strategies—building from integration to disclosure and finally, engagement—reinforce one another, and also provide companies with a structure for evaluating their own progress. For some companies, the recommendations may be implemented sequentially; for others that have already established internal alignment across teams, there may be an opportunity to simultaneously implement recommendations across the three strategies.

In the sections below, we **explore each of the nine recommendations** under each of the three strategies, share investor insights that led to them and **provide examples of companies** that are already putting these recommendations into practice.



## Strategy #1: Formalize sustainable business integration

RECOMMENDATIONS





1. Demonstrate accountability for sustainability.
2. Develop the sustainability business case.
3. Cultivate collaboration between sustainability, investor relations and governance teams.



## Strategy #2: Identify what to disclose and where to disclose it

RECOMMENDATIONS





1. Focus investor-directed disclosures on what is material, but don't ignore emerging trends.
2. Disclose decision-useful information, both quantitatively *and* qualitatively.
3. Disclose sustainability information consistently where investors are already looking.



## Strategy #3: Implement a proactive investor engagement strategy

RECOMMENDATIONS





1. Use language that investors understand and value.
2. Leverage the C-suite and board of directors as key messengers.
3. Diversify investor engagement strategies.

# Strategy #1: Formalize sustainable business integration



1. Demonstrate accountability for sustainability.



2. Develop the sustainability business case.



3. Cultivate collaboration between sustainability, investor relations and governance teams.

Investors increasingly recognize that companies are operating in a more crowded, resource-constrained world, where climate change threatens to disrupt global supply chains and where profound and ongoing human rights abuses undermine not only business operations, but also the lives and livelihoods of employees, customers and stakeholders. Importantly, academic and investment research also underscores the financial benefits of integrating sustainability challenges into core business strategies.

Consider research by Deutsche Bank and Columbia University's Earth Institute that found 100 percent of the academic studies reviewing links between financial and sustainability performance agree that companies with high ratings for corporate social responsibility (CSR) and ESG factors have a lower cost of capital in terms of debt (loans and bonds) and equity.<sup>18</sup> Similarly, a Harvard Business School (HBS) study of 180 companies broken into two groups ("high sustainability" and "low sustainability") found that high sustainability companies significantly outperform their counterparts over the long term, both in terms of the stock market as well as in accounting performance. The same HBS study found that given a \$1 investment in 1993 in a value-weighted portfolio of high sustainability versus low sustainability firms, the high sustainability portfolio would have grown to \$22.60 by 2010, while the low sustainability portfolio would be only \$15.40, a difference of over 46 percent.<sup>19</sup> In effect, the market recognizes that higher ESG performing companies are lower risk than other companies and rewards them accordingly.

But as more companies move to make claims of "sustainability," how are investors identifying "high ESG performers" that represent this lower investment risk and potential for growth? When we asked our investor partners how they recognize a "sustainable business leader," the most commonly cited characteristic was a clear demonstration of how sustainability is integrated into business systems and decision-making. The recommendations included below respond to rising investor expectations for sustainable business integration and guide companies to demonstrate this integration in public disclosures and other investor communications.

# Strategy #1: Formalize sustainable business integration

## RECOMMENDATION



### 1. Demonstrate accountability for sustainability.

“ We generally look at formal oversight of ESG at the board level, how it is integrated through the board charter, and demonstration that key material issues are integrated into the committee discussions. The number of companies that have formal oversight has been increasing and pretty significantly. We are also looking at management accountability, either centrally or distributed, with senior executives being held accountable.”

**Evan Hornbuckle**

Global Industry Analyst, Wellington Management Company

Investors are looking for companies to put smart governance systems in place that proactively identify, assess and manage the financial consequences of ESG risks like climate change, water scarcity and human rights abuses. Importantly, investors are looking at the *quality* of those governance systems to predict the resilience of a company's future performance. A 2017 CFA Institute survey, for example, reveals that financial analysts believe board accountability is the most important sustainability issue in their investment analysis and decision-making.<sup>20</sup>

As one Ceres partner company recently put it, “For many investors we engage with, ESG integration is seen as a proxy for good management.” This observation affirms what we heard in our investor interviews, with the majority agreeing that a defining characteristic of a sustainable business leader is the presence of a clear governance structure that explicitly includes oversight for material environmental and social impacts. While data on environmental and social issues provides a good sense of a company's current and past performance, details on governance systems give investors and other stakeholders key insights into whether the company is likely to sustain this performance in the future.

**Formalize board oversight for ESG.** Formal mandates and accountability for ESG performance and strategy for both management and corporate boards increase investor confidence that these issues are being managed effectively and that the company is well positioned to identify potential business opportunities. As Tim Goodman, director of engagement at Hermes Investment Management observes, “We think that the lead independent director should talk about [ESG]. If there is a board committee—and we think there should be one, whether it's part of another committee or stand-alone—the chair of that committee should be able to engage with investors on these topics.” Boards of directors that are best positioned to engage with investors are those that have formal mandate to oversee sustainability strategy and performance, but also expertise and incentives for sustainability that reinforce one another. These integrated board governance systems allow directors to better understand and make smart decisions on these risks.

# Strategy #1: Formalize sustainable business integration

**Establish management accountability.** [Ceres research](#) highlights the critical importance of management-level accountability structures that incentivize improved sustainability oversight and, ultimately, performance. Among 600 of the largest publicly traded companies in the U.S., those with senior executive accountability for sustainability performance are significantly more likely to strive for improved sustainability performance. Nearly all companies (98 percent) with time-bound and company-wide GHG commitments also hold senior-level executives responsible for sustainability performance. In addition, companies with C-suite accountability for sustainability are nearly three times more likely to proactively engage with investors and are more than seven times more likely to disclose both the risks *and* opportunities of sustainability issues in annual financial disclosures than those without C-suite level oversight.



## Sustainability-Competent Boards

In today's unpredictable business climate of disruption and transformation, corporate boards must be "sustainability competent" to guide companies successfully, and more investors are expecting this. In 2016, the California Public Employees Retirement System (CalPERS) altered its Global Governance Principles by calling on companies in its portfolio to have "expertise and experience in climate change risk management strategies."

A sustainability-competent board displays a fundamental understanding of sustainability issues material to its business sector and integrates these issues into the fabric of board oversight and decision-making on strategy, risk and compensation. A board of directors whose members can assess business risks and growth opportunities in light of evolving ESG factors strengthens corporate resilience. On [Coca-Cola's](#) board, the Public Issues and Diversity Review Committee addresses sustainability issues. Of the three directors on the committee, two also serve on the board's Compensation Committee, while another sits on both the Corporate Governance Committee and the Finance Committee. This cross-pollination of expertise across board committees allows sustainability issues to inform multiple committees and enables integration of these issues into board discussions on risk, governance and compensation.

Ceres' [Lead From the Top](#) report outlines a clear pathway for boards to gain knowledge and awareness of material sustainability issues that can lead to smart, meaningful decisions. The report identifies the skills and experience needed for board members to provide thoughtful oversight of sustainability risks and opportunities, as well as the tools and processes that can help foster deeper engagement at the board level on these issues. The report identifies three main avenues for boards to develop sustainability competence: the nominating process; board education; and board stakeholder engagement.



## RECOMMENDATION



### 2. Develop the sustainability business case.

“It’s all about how you drive long-term success in a business. Value creation is expressed in financial terms, but the drivers of sustainable competitive advantage are beyond purely financial indicators. What we want to hear is what are the long-term drivers of your business? How are you proactively positioning and monitoring them?”

David Blood

Founding Partner, Generation Investment Management

A 2016 Accenture CEO Study found that while 87 percent of CEOs surveyed believe that sustainability impacts their industry, only 59 percent could accurately quantify the business value of their sustainability initiatives.<sup>21</sup> And, based on insights from our investor interviews, far fewer are able to effectively communicate their company’s business case for sustainability to shareholders. Harvard Business School professor Rebecca Henderson, who sits on the corporate boards of Amgen and Idexx, told us, “Investors are always looking for higher returns, but sustainability is handicapped because investors think it’s being led by people who don’t understand the business. This means it is hugely important to demonstrate concrete business cases that deliver real results.”

Ceres’ research finds that 43 percent of the largest companies in the U.S. incorporate sustainability information in investor communications and disclosures.<sup>22</sup> But investors and analysts interviewed for this report observe that environmental and social performance information is rarely presented as financially relevant for the company. Nor is it discussed as an integrated component of the company’s decision-making on strategy, risk and revenue.


**Link financial and sustainability performance metrics.** Presenting the value proposition of sustainability, recognizing both risks and opportunities, is an important first step; and showing direct links between sustainability and financial performance metrics is equally important. An increasing number of companies are communicating to investors about business risks associated with issues such as climate change, water challenges and human rights. For example, Ceres’ 2018 research shows that 51 percent of the largest U.S. companies reported business risks related to climate change in financial filings—up from just 42 percent in 2014.<sup>23</sup> However, while some companies are reporting cost savings from sustainability initiatives—such as energy savings or manufacturing efficiencies—far fewer communicate how sustainability initiatives are driving growth and revenue generation, or improving key metrics, such as employee retention and recruitment.

## Strategy #1: Formalize sustainable business integration

**Communicate long-term value creation.** Mainstream asset managers are increasingly driven by clients who understand that in a world where natural resources are constrained, shortsighted companies will not win out. Although long-term value creation has long been a consistent focus of ESG and impact investors, it has only recently been more widely embraced. A 2017 McKinsey Global Institute report found that from 2001-2014, revenues of long-term focused firms grew on average 47 percent more than the revenues of other firms, and with less volatility. Earnings of long-term firms grew 36 percent more on average over this period than those of other firms, and their economic profits grew by 81 percent more on average.<sup>24</sup> As global industry analyst Evan Hornbuckle, from Wellington Management Company explains, “The companies that we think should win over time are the ones that understand the balanced approach to everything at once, and that profitability and sustainability aren’t mutually exclusive over time.”

For sustainable business leaders who have done the work to integrate sustainability into business strategies—and have the metrics to back it up—failing to communicate this information is a huge missed opportunity. In order for investors to evaluate long-term financial viability, companies must communicate the resilience of their business models in the face of existing and emerging social and environmental risk. Importantly, companies should clearly articulate to investors *why* long-term business strategies matter, how sustainability is a critical component of those strategies and consistently include this information across all investor communication platforms.

### COMPANY IN ACTION



In 2018, **The Coca-Cola Company** took steps to align its sustainability and annual reports and demonstrate clearly the company’s vision for long-term value creation, inclusive of sustainability. One of the key ways the company demonstrates integration across these two reports is through leadership and communication from its board of directors. Each of the reports features a letter authored by the Coca-Cola board of directors and signed by its board chair, Muhtar Kent. Each describes Coca-Cola’s vision for long-term value creation. In the company’s sustainability report, the board representatives describe sustainability as key to its long-term value creation strategy, stating that this “expansive and inclusive view of value creation helps maximize our potential as a business to grow, create economic value...” The letter goes on to explain the board’s responsibility for providing oversight to the company’s sustainability progress, describing this as part of their fiduciary duty: “At Coca-Cola, the Board of Directors is elected by our shareowners to oversee their interests in the long-term health and the overall success of the business and its financial strength,” and explains “Our sustainability efforts, therefore, are not separate from our business but actually foundational to the way we do business. As essential components of the long-term growth strategy of The Coca-Cola Company, our sustainability initiatives benefit our business and the communities we serve.”<sup>26</sup>

# Strategy #1: Formalize sustainable business integration

## RECOMMENDATION



### 3. Cultivate collaboration between sustainability, investor relations and governance teams.

“Often investors get channeled to the CSR experts for dialogue, those are the folks that live and breathe these issues. They should be part of the conversation. But in many companies, they may not have a direct channel to the CFO. Investors also want information from executives with a common understanding of ESG and financial performance who can speak to how integrating sustainability efforts into business practices can enhance long-term profitability.”

Tim Smith

Director of ESG Shareowner Engagement, Boston Trust & Investment Management Company

The shift from reactive to proactive investor engagement on a company's sustainable business strategy will require closer partnerships between a company's sustainability team and those responsible for traditional investor communications, including investor relations and corporate governance staff. As an analyst from a major U.S. asset manager explains, “Companies should be talking about these issues in a business performance context, but many people in finance have preconceived notions that these conversations have to happen with the company's ESG experts.”

An effective investor relations (IR) team acts as a key translator between the company and its investors. With the goals of maintaining a loyal shareholder and debt-holder base, enhancing long-term shareholder value, lowering costs of capital and building credibility, collaboration with company ESG experts on the sustainability team is increasingly a win-win for IR teams.

**Build fluency between IR and sustainability.** While the investors we interviewed were measured in their expectations for IR representatives to handle expert-level sustainability related questions, they did place value on IR teams that are able to effectively make the connection between sustainability and business performance. If, for example, the head of IR is able to speak fluently with mainstream investors about how sustainability efforts positively influence risk mitigation and revenue growth—and similarly, if the head of sustainability can articulate to investors how sustainability improves the bottom line—this can be a unique differentiator. As an investment manager at a European asset management firm explained, “If the IR team is unable to answer questions, then the message sent is that the company is missing something or isn't committed.”

## Strategy #1: Formalize sustainable business integration

Building stronger relationships with IR, however, requires demystifying both sustainability and financial terms. Sustainability teams should develop their own financial acumen. As one Ceres member company said, “I hear too often from fellow Chief Sustainability Officers that they are afraid to speak with those in the finance function.” Finding comfort in discussing financial performance and the business context will lead to building bridges, using shared language and developing a common business case and messaging for investors.

**Collaborate with the corporate secretary.** A key role of the corporate secretary is advising the board on how they can discharge their responsibilities toward shareholders, which is why the corporate secretary and IR departments work closely together. Intel has proactively engaged with investors on sustainability for nearly two decades. It identifies internal alignment and collaboration between key decision-makers in corporate responsibility, corporate governance and investor relations as a critical ingredient for success. Representatives from these three teams regularly travel together to engage directly with shareholders, outline sustainability strategies and gather investor feedback, which further informs strategies and disclosure.

Ultimately, coordinated efforts between the sustainability, investor relations, corporate governance, public reporting, legal and finance teams will determine the success or failure of a company as it moves to effectively communicate its sustainable business strategy to investors.

### COMPANY IN ACTION

Companies that effectively coordinate across internal teams—including sustainability, IR and governance—often find greater success when communicating sustainable business priorities and progress to investors. For many years, **Microsoft** has been engaging its investors on relevant ESG issues. What once began as engagement to a small number of interested SRIs has expanded to include proactive engagement with more than 50 of its top institutional investors representing nearly half of the company’s ownership. “Early on, Microsoft tended to hear about environmental and social issues from smaller, mission-driven investors,” Steve Lippman, director of ESG engagement at Microsoft explains. “Over time, that expanded to include European pension fund investors, then pension funds in the U.S. But at this point, mainstream Wall Street firms are coming to us with interest in understanding our ESG strategy and how we are addressing key risks.”

In response to this heightened level of investor interest—and in an effort to ensure quality of communication to a breadth and diversity of investors—the company has formalized its internal alignment and collaboration across teams. In spring 2018, Microsoft established a new position of ESG Engagement Director within the Office of the Corporate Secretary. This new role allows the Director to manage the company’s shareholder engagement activities on ESG issues. Through direct partnership between the company’s ESG experts, IR team and Corporate Secretary’s office, the company is able to integrate ESG topics across its investor outreach and communications, and better provide institutional investors with insights on sustainability strategies, policies and performance.



## Strategy #2: Identify what to disclose and where to disclose it



1. Focus investor-directed disclosures on what is material, but don't ignore emerging trends.



2. Disclose decision-useful information, both quantitatively *and* qualitatively.



3. Disclose sustainability information consistently where investors are already looking.

“BlackRock’s engagements with companies focus on the financially material sustainability topics most relevant to their business and long-term economic value. Sound practices around ESG factors inherent to a company’s business model can be a signal of operational excellence and management quality.”

**Michelle Edkins**

Managing Director, Global Head of Investment Stewardship, BlackRock

Robust and comparable disclosure gives investors the information they need to make better investment decisions. And, more than ever, investors are looking for more transparency on growing financial implications from issues such as climate change, resource scarcity, data privacy violations and human rights abuses.

Investors need information that helps them assess risk management and resilience. They also need to understand business priorities, key trends and strategic direction. And they need to see this information disclosed in financial terms that can be easily integrated into their assessment processes. The recommendations below shine a light on investor expectations for meaningful ESG disclosure. They respond to the question Ceres most commonly hears from the companies we work with: “What does meaningful ESG disclosure look like to the investor community, and where do they want to see it?”

### Disclose what matters

A recent Ceres report, [Disclose What Matters](#), shows that companies generally fall into one of three phases in the maturity of their sustainability disclosure systems: Comparability, Integration, Reliability. In Phase 1 (Comparability), companies adopt commonly accepted disclosure frameworks in response to market demands for comparability. Ceres’ research finds that most large global companies are in this phase, with 70 percent of major global corporations using the GRI standards in their disclosure. In Phase 2 (Integration), companies show how they are integrating sustainability into strategies and bottom-line business performance. This integration is shown through key systems such as board oversight of sustainability, materiality assessments and stakeholder engagement. While most global companies have these systems in place, the quality of disclosures and connections back to company strategies are still mediocre. In Phase 3 (Reliability), companies show that their sustainability disclosures are as reliable as financial disclosures due to external approvals of their disclosures. Most large global companies do not externally assure their sustainability disclosures.



# Strategy #2: Identify what to disclose and where to disclose it

## RECOMMENDATION



### 1. Focus investor-directed disclosures on what is material, but don't ignore emerging trends.

“Our focus is on materiality. We don't have a long list of perhaps 80 things, but seven to ten instead. What is important to that business, what's an opportunity, and what's a risk? Has the company taken the time to map its material issues, disclose what it believes is material and how it is managing these?”

David Sheasby

Head of Stewardship & ESG, Martin Currie Investment Management Ltd

As a Ceres Company Network member put it, “At some point, there is so much information that there is no information.” The investors and analysts we interviewed agree. To be effective in communicating with investors, companies must focus disclosure and engagement on issues that have—or may have in the future—a financial impact on the company.

Ceres' recent research shows the number of companies conducting materiality assessments of environmental and social issues has grown to 32 percent of the 600 largest publicly traded companies in the U.S.—compared with just seven percent in 2014.<sup>26</sup> This growth is driven in part by calls from investors to focus disclosures on the most business-critical issues. Another factor is new and evolving reporting frameworks helping companies identify material issues, such as the Sustainable Accounting Standards Board (SASB) and Global Reporting Initiative (GRI).

**Disclose material ESG issues.** Despite this growing investor consensus for more focused communications, the definition of material ESG issues and how that definition guides assessment of corporate disclosures still varies within the investment community. Some investors we interviewed strongly encourage using SASB sector guidance; others prefer more inclusive approaches outlined by the GRI guidance, which guides disclosure of significant economic, environmental and social impacts. Still other investors, especially those explicitly focused on ESG or impact investment, use their own priority issue lists that guide evaluation of and engagement with companies. Companies can navigate this variance by transparently disclosing their own approaches for determining material environmental and social issues, including details on significant audiences and issues considered in the prioritization process, as well as details of how prioritized issues were then considered in strategies and decision-making.

“I am looking at the changing risk context because I want to try to ensure my fundamental research doesn't get derailed because of an ESG factor I didn't unearth.”

Evan Hornbuckle, Global Industry Analyst, Wellington Management Company

## Strategy #2: Identify what to disclose and where to disclose it

**Include emerging risks and opportunities.** Another important takeaway from our conversations with investors and analysts is that more focused disclosures should also include discussion of *emerging* risks and opportunities. Robust materiality assessment processes should identify risks within varied time frames, both short- and long-term, and as a result, evaluate and identify emerging issues. Disclosure of these emerging trends helps investors understand issues that may *become* material in the future and illuminates how the company is responding. Among the emerging trends that investors identified most commonly in our interviews: automation and artificial intelligence, water variability, traceability in supply chains, just transition to the low carbon economy, the *gig* economy, and shifts towards more global consumption.

### Water “Emerges” Into the Spotlight

Not long ago, financial risks related to droughts, flooding and water quality were considered “emerging issues.” This has clearly changed. Growing financial risks associated with increasing water competition, weak regulations, population growth, aging infrastructure, water contamination and climate change impacts are quickly grabbing the attention of investors. In just two years the Investor Water Hub—a working group of the Ceres Investor Network founded in 2016—grew to include more than 100 investors with more than \$20 trillion in assets under management.

*“This is really a critical determination for anyone working in the investment space at this time. If they have not already developed a set of internal metrics and risk evaluation procedures around the water risk that their portfolio companies face, they are behind.”* — Ken Locklin, Director, Impax Asset Management

As more investors clamor to understand water-related risks in their portfolios, they are calling on companies to disclose more decision-useful information, including their strategies for handling these risks. [The Ceres Investor Water Toolkit](#), released in 2017, is a tool developed by investors for investors. It offers a how-to guide for understanding water risks and for identifying companies and securities with high and low water exposure. Companies in water-dependent sectors can also use the toolkit to gather valuable insights in how investors are assessing water risks.

### COMPANY IN ACTION

For a company like **PepsiCo**, water is its lifeblood. In its 2018 annual financial filing, PepsiCo identifies the potential adverse effects of water scarcity in its supply chains and potential consequences for its business operations. Higher production costs and investments in water-efficient technologies could compromise the company’s business and financial performance. Further, failing to maintain high ethical, social, and environmental practices (such as failing to act responsibly with respect to water use, human rights in the supply chain, public health or community impacts) could also hurt the company’s reputation and brand image. Water scarcity thus poses a double risk: not only can a lack of water negatively affect the company’s business operations and finances, a failure to be water efficient can also adversely affect consumer perceptions of its brands.



# Strategy #2: Identify what to disclose and where to disclose it

## RECOMMENDATION



### 2. Disclose decision-useful information, both quantitatively *and* qualitatively

“It’s not reasonable to ask that complex and diverse sustainability information be distilled into just three key metrics regardless of company context. You wouldn’t look at only five metrics on a Bloomberg terminal before making an investment decision. We want companies to report more openly about their long-term value creation stories and provide useful information that gives investors insights into what they’ve identified as long-term sustainable investment risks and opportunities that they need to manage—be it workforce transition planning or climate resilience—and how they see these topics affecting their bottom-line over the long-term.”

**Beth Richtman**

Managing Investment Director, Sustainable Investments Program,  
California Public Employees Retirement System (CalPERS)

Today’s conversations aren’t about *whether* companies should provide sustainability disclosure; but rather what constitutes good disclosure and how companies can be incentivized to provide it. The elements of good disclosure are generally understood to be the following: consistency over time; trended performance data; comparability between companies and industries; comprehensiveness of the scope of information provided; reliability; accuracy; and inclusion of relevant and material sustainability issues. Reporting that meets these criteria is considered “decision-useful” to investors and other users of corporate reports.

Most importantly, investors want to better understand the links between sustainability and financial performance. Quantifying the impacts—within the context of risk and revenue—will enable investors to integrate this information into financial modeling and valuations. As the executive director of research at a major U.S. asset manager put it, “The average portfolio manager doesn’t know what raw data looks like—they view trends and correlations, so create a chart that shows long term ESG performance and shareholder price—that will catch their attention.”


**Quantify cost savings and increased revenue.** Many analysts and investors emphasized the importance of quantifying how environmental and social performance impacts financial performance. For example, in 2017 technology company HPE reported leveraging its superior sustainability performance and product energy efficiency to land \$700 million in new revenue (based on contracts or sales in which sustainability factors were a known consideration).<sup>27</sup> In 2018, Nike Inc.’s CFO shared with investors that since the launch of the company’s sustainably innovated FlyKnit technology, the product has generated over \$1 billion, and is quickly approaching \$2 billion, in revenue growth for the company.<sup>28</sup>

**Put data into context.** Even in cases where robust quantitative information is disclosed, it is the qualitative information that puts that data into context, helping investors to understand current and potential impacts for operational costs and future growth. Qualitative information was cited

## Strategy #2: Identify what to disclose and where to disclose it

in our interviews as a key way to understand a company's commitment for integrating sustainability across the business and its long-term strategy. As Tim Goodman, director of engagement at Hermes Investment Management put it, "This year's carbon emissions versus last year's doesn't actually tell you a lot, but the fact that a company is saying 'we want a business with lower emissions and this is how we are planning to do that'—it says a lot more than the actual data."

### COMPANY IN ACTION



In late 2018, **Citi** became the first U.S. bank to issue a formal climate risk report—*Finance for a Climate-Resilient Future*—detailing its progress on implementation of the TCFD recommendations. The report outlines the company's efforts to conduct climate scenario analysis designed to understand the potential financial impacts of climate change on its lending portfolios in the oil & gas and utilities sectors. The report identifies climate change as "one of today's most critical issues [which] presents risks that must be carefully managed....these changes will disrupt supply chains, damage infrastructure, reduce crop yields and lead to a decline in biodiversity...."<sup>30</sup> The company describes a cross-organizational process that led to the development of the report, in which representatives from Banking, Risk, Quantitative Analysis, Corporate Sustainability and Environmental and Social Risk Management worked together to complete the analysis that identified the company's climate risks, as well as the opportunities, it will face now and into the future. By adopting the TCFD framework, Citi hopes to minimize future risks and position the company for success in the emerging low-carbon energy future.<sup>31</sup>

### Investors Demand Quantitative and Qualitative Disclosure on Climate Change

In the eight years since the Securities and Exchange Commission (SEC) issued guidance on disclosing climate change-related business risks, the number of companies mentioning this risk in financial filings has grown. Ceres' research finds that 51 percent of 600 largest publicly traded U.S. companies mention climate-related risks in their financial filings, up from 42 percent in 2014. The vast majority of companies, however, only disclose climate-related risks as a regulatory risk (68 percent) or as a physical risk (55 percent), with a smaller percentage citing reputational risks. Boilerplate language about future carbon-reducing regulations has become commonplace, but this language does not give investors the information they need to understand the complexities of industry or company-specific risk.

Backed by more than 360 investors with more than \$19 trillion in assets, the 2017 recommendations from the Task Force on Climate-related Financial Disclosures (TCFD) were a significant development in pushing for more meaningful disclosure of material climate risks across all sectors. The release of the TCFD recommendations was supported by more than 100 companies; just over a year later the TCFD public support grew to more than 500 firms with nearly \$8 trillion in market capitalizations, including financial firms responsible for assets of nearly **\$100 trillion**.<sup>29</sup>

The tactical and comprehensive TCFD recommendations—including guidance to describe the resilience of the organization's strategy, analyzing climate-related scenarios aligned with the most current science, and metrics for measuring performance and progress—provide companies with much needed guidance for more meaningful and useful disclosures to investors. The TCFD framework helps facilitate investment decision-making that considers both the physical risks posed by climate change, as well as the risks and opportunities of shifts to cleaner technologies.

## Strategy #2: Identify what to disclose and where to disclose it

### RECOMMENDATION

### 3. Include decision-useful ESG information where investors are already looking.

“ On our public equity investment team, we look at the 10-k and how they describe the risks for the business. Then we look at how risks are described in the sustainability report. We are looking for consistency.”

Lila Preston

Partner, Generation Investment Management

ESG performance metrics are now being integrated into assessments and decision-making processes at the largest asset managers and owners in the world. In 2017, Caisse de dépôt et placement du Québec (CDPQ)—Canada’s second largest pension fund with over C\$285 billion in assets under management—announced a new investment strategy to support Paris Agreement targets and the transition to a low-carbon global economy. This strategy means that CDPQ will factor climate change in all investment decisions across its entire portfolio. It aims to increase its low carbon investments 50 percent by 2020 and reduce the carbon intensity of its portfolio 25 percent by 2020. Importantly, CDPQ portfolio managers are incentivized to meet these targets and to achieve their KPIs each year.

**Increase accessibility of ESG information.** As more investors prioritize ESG factors, the accessibility of relevant sustainability information gains importance. A 2017 CFA Institute survey found that 66 percent of respondents, including portfolio managers and research analysts, pull ESG information and data from third party research.<sup>32</sup> In particular, passive investors depend upon provider ratings in comparing traditional index and ESG ratings. The prevalence of third-party research underscores the importance of increasing accessibility to ESG information and data.

Yet in the end, whether it is the investors themselves or a research provider analyst seeking the information, they can only assess what they can locate. And when companies proactively include decision-useful ESG information within investor-focused disclosures they are better able to control the narrative, demonstrate how their strategies differentiate them from peers, and clearly communicate the added business value that in turn creates a competitive edge.

While all of the investors and analysts Ceres interviewed use some type of third-party research provider, they emphasized that this type of analysis was one of many sources they reviewed.

***So, where should companies disclose this information so that investors are more likely to find and use it?***

→ **Sustainability reports and websites.** Both mainstream and ESG-focused investors interviewed revealed they routinely examine company sustainability reports and websites to get information on ESG performance and strategy. Importantly, however, they said they use these sources because that is where they *expect* to get the most complete information, not because that is necessarily where they want to see it.



## Strategy #2: Identify what to disclose and where to disclose it

- **Proxy statements, 10-Ks and annual reports.** Investors emphasized that in order to reach a broad audience (including investors and analysts not primarily focused on ESG), ESG information should be integrated into sources that all investors reference—specifically, the 10-k, proxy statement and annual report. Driven by investor demands for more quality information on board governance, proxy statements are an increasingly important vehicle for communicating with investors. The National Association for Corporate Directors (NACD) recently guided companies on this topic, saying, “To facilitate investor understanding, proxy filers should craft engaging narratives and offer clear visibility into their organization’s board governance approach and emerging investor priorities—from human-capital management and boardroom diversity to environmental, social, and governance (ESG) issues.”<sup>33</sup>
- **Investor Relations websites.** The biggest missed opportunity identified by investors and analysts is the failure of companies to showcase customized, streamlined sustainability disclosures in the investor relations pages of their websites. Investor-backed tools, including the Sustainability Accounting Standards Board (SASB) guidance and TCFD recommendations, can guide more abbreviated disclosures for investors. In 2018, for example, Nike Inc. added a SASB reference guide on its IR website, while still providing an opportunity for investors to access additional content and context via its Sustainable Business Report. The IR website is also a platform to feature business relevant sustainability content such as sustainable product innovations, cost savings through investments in efficiency and sustainability-driven revenue growth.

**Create consistency.** One challenge cited by investors and analysts is the lack of consistency in sustainability information disclosed across communication platforms. Investors interviewed revealed their strategies to seek out discrepancies across disclosures in order to identify red flags, specifically assessing how risks for the business are described in the 10-k, sustainability report and proxy statements. In instances when a company’s disclosure seems unbalanced and inconsistent, some investors will gather additional insights by conducting site visits, engaging with unions and reaching out to NGOs to gain a more comprehensive understanding of the company’s performance.

### COMPANY IN ACTION

In 2017, **JetBlue** was one of the first U.S. publicly traded companies to publish disclosures aligned to the SASB guidance and, in 2018, was again among the first companies to release a joint SASB and TCFD report. In this report, which is easily accessible from the company’s investor relations website, JetBlue highlights the financial risks presented by a changing climate and steps taken to prepare: “Climate issues are of particular interest since the extremely active 2017 Atlantic hurricane season. For an airline like JetBlue with a significant focus in the Caribbean, the prospect of more extreme storms raises a legitimate concern: How prepared is JetBlue to deal with changing weather patterns that may be caused by climate change? Our experience with Hurricanes Harvey, Irma, and Maria shows that JetBlue is well positioned among major airlines to deal with the impacts of a changing climate.”<sup>34</sup> The company’s disclosure goes on to describe how JetBlue’s attention to and integration of ESG issues into its business helps the company not only protect, but also increase, financial returns. This reporting is complemented by the company’s disclosure in its 2018 proxy statement, which specifically identifies the top three environmental issues discussed by the board of directors in 2017, and the 2017 10-k, where climate change is specifically cited as a financial risk for the company.

## Strategy #3: Implement a proactive investor engagement strategy

### RECOMMENDATIONS



1. Use language that investors understand and value.



2. Leverage the C-suite and board of directors as key messengers.



3. Diversify investor engagement strategies.

“More and more companies are making their board members available to us for discussions around ESG issues where we have questions. Some are even proactively making directors available to discuss the board’s approach to managing risks and opportunities. Letting investors into your thinking and strategy should not be limited to times of crisis. Making a company’s position known on a sunny day means that when things are complex or there is opposition, there is no last-minute panic of trying to socialize how the company thinks about risks and opportunities.”

**Danielle Sugarman**, Vice President, Investment Stewardship, BlackRock

Investor driven engagement, via direct dialogue, shareholder resolutions and collective campaigns is a rising trend, and for good reason: it’s working. Evidence from collaborative dialogues involving 225 investment organizations from 2007-2017 shows that after “successful” engagements (as defined by a set of predetermined criteria and scorecards), target companies experience improved profitability (as measured by return on assets).<sup>35</sup>

The ESG and long-term focused asset managers we interviewed identified direct company engagement as a critical component in their assessment of corporate strategies and performance. Due to staff and resource limitations, however, they also look for efficiencies through collaboration. Among smaller socially responsible investment and impact investment firms, there is a significant amount of coordination around direct company engagement. As one socially responsible investor put it, “Although you may be only hearing from one of us on a particular topic, you can be sure that others support that action and engagement—we just have to find ways to divide and conquer.”

Larger mainstream asset managers also recognize the importance of direct engagement, but similarly cite resource constraints. Unless proactively engaged by a company, many mainstream investors limit direct contact to companies deemed to be poor performers on sustainability criteria, noting factors of higher risk or greater potential for impact/influence within their sector.

This nuanced dynamic is one reason many companies believe investors just don’t care. But as every investor we interviewed pointed out: a lack of engagement doesn’t mean they aren’t paying attention.

## Strategy #3: Implement a proactive investor engagement strategy

Whether they're fielding few or many investor requests for engagement or ESG information, companies that do the hard work of developing a compelling sustainability business case have an opportunity to take control of the narrative and capture competitive advantage. A consistent refrain Ceres hears from investors is that if a company is not talking about its sustainability strategy and performance, they may conclude the company does not have a story to tell or, even worse, it's hiding something.

The recommendations included in this engagement-focused strategy can guide companies to build on the foundation of improved business integration and alignment, and more robust and targeted ESG disclosure, to shift investor ESG engagement strategies from reactive to proactive. By speaking in the language investors value, positioning leadership as key messengers and diversifying investor engagement strategies, companies can leverage their sustainable business strategy to differentiate from peers and effectively position sustainability as an important driver of business value.

### RECOMMENDATION



#### 1. Use language that investors understand and value.

“ We need to see corporate sustainability managers operating as business partners and leaders. We also need to hear from CFOs regarding how they perceive value creation around sustainability and what that means for systemic business results.”

**Candace Hewitt**

Responsible Investing Senior Analyst at Nuveen, a TIAA Company

A core function of the IR team is to understand investor expectations and to then communicate the company's values and strategies using language that investors understand, including profit margins, projected goals, earnings per share (EPS) and dividends.<sup>36</sup> Not surprisingly, analysts and investors emphasized the importance of language choice and the value of positioning these issues in the business performance context. As Evan Hornbuckle, a global industry analyst at Wellington Management Company described, “The potential impacts of climate change can make it into specific stock decisions—seasonal exposure, supply chain disruptions, long-duration supply chains (guessing inventory levels nine months out). Business models can be pressured by changing weather patterns over time.”

While it is important for companies to recognize who within the investment firm they are engaging and consider how this might affect the ESG information shared, these observations underscore the important role companies can play in increasing investor understanding of the financial importance of operating more sustainably. Consistent communication on sustainability issues, using language



## Strategy #3: Implement a proactive investor engagement strategy

investors can understand and integrate in their evaluations—with an emphasis on risk mitigation, cost avoidance, revenue growth and competitive differentiation—will increase investor comfort on these topics, resulting in competitive advantages for companies that are proactive.

Companies considered to be sustainable business leaders often fall into the trap of positioning sustainability as the “right thing to do,” without making the connection to the business case. While sustainability reports provide opportunities to discuss wide-ranging sustainability benefits, investor-directed messaging should focus on how these investments are strengthening the company and its bottom line. Speaking about material environmental and social issues—through the prism of supply chain resilience, stranded asset avoidance, cost savings and efficiency, improved product performance, consumer acquisition and increased employee retention—allows investors to consider these issues in terms they understand and can integrate in their valuations. As one major U.S. asset manager explained, “Language choices are important. Investors think about climate risk—not climate change. It is a small thing, but it matters.”

While companies often share frustrations that IR teams and other executives are not receiving questions related to sustainability issues, those we interviewed emphasized that as investors continue to develop their understanding of these risks and opportunities, ESG queries will increasingly look like traditional investor questions. Specifically, the larger asset managers we interviewed shared that their questions may not be positioned as “sustainability questions” at all, but instead will be placed in terms of relevant financial issues: supply chain stability, natural resource availability, talent retention, operational efficiencies, etc. Greater collaboration between sustainability experts, investor relations, corporate secretaries’ offices and those in finance functions will help identify when these less noticeable shifts in investor questioning take place—a clear sign, in other words, that boundaries between financial and ESG performance are disappearing.

### COMPANY IN ACTION

During its 17 years of engaging shareholders on ESG issues, **Intel** has found success by diversifying its investor engagement and using consistent messaging across its investor communications. In the opening statement to shareholders at its 2017 AGM, the company explained to investors how it integrates sustainability in strategies, management systems and goals across its supply chains; and at its 2018 AGM, the CEO highlighted the company’s commitment to improve diversity across its employees and board of directors.

Throughout the year, Intel convenes smaller, ESG-focused investor engagement sessions across the country. Intel’s investor outreach team—a collaborative effort of the corporate responsibility, IR and corporate governance teams—leverages these engagements to capture feedback on its strategy and disclosure, stay apprised of evolving investor expectations and build critical relationships with shareowners and debt holders. Director of Corporate Responsibility at Intel, Suzanne Fallender reflects, “We have found that our integrated and year-round approach to investor outreach and reporting has resulted in improved insights into our investors’ ESG strategies and has also further strengthened our internal collaboration and integrated thinking.”

# Strategy #3: Implement a proactive investor engagement strategy

## RECOMMENDATION



### 2. Leverage the C-suite and board of directors as key messengers.

“ If the CEO says it’s important, it carries more weight than any other. Wall Street cares about what the person in charge has to say— otherwise how important can this be if the CEO is not willing to take the time to speak about it?”

Executive Director of Research, Major U.S. Asset Manager

Direct engagement is one of the most effective strategies investors have for assessing management’s commitment to a sustainable business strategy. But a key factor in this engagement is who companies send as representatives, and *how prepared* those representatives are to respond to ESG-related questions and concerns. Recent research by Ceres makes clear that including a company representative with decision-making authority is a critical element for a successful corporate/investor engagement;<sup>37</sup> this view was further bolstered by our investor interviews. Quite simply, the messenger matters.

**Deploy the C-suite.** While IR departments are the usual first stop for interested investors, companies send a powerful message when the CEO, CFO and other members of leadership can speak knowledgeably about the business value of sustainability. As the primary spokespeople at major investor forums, including annual meetings, investor days and quarterly earnings calls, C-suite members set the tone for what is and is not important to a company’s current and future success. As one major U.S. asset manager put it, “Wall Street cares about what the person in charge has to say, otherwise how important can this be if the CEO is not willing to take the time to speak about it.”

While the importance of CEO buy-in cannot be overstated, investors interviewed also highlighted the untapped potential of CFOs as key spokespeople on sustainability issues. This sentiment was echoed in a recent study from FM Global arguing that CFOs must get prepared for the very real financial impacts of climate change. “Board members, shareholders, investors and analysts during quarterly earnings calls will increasingly want credible information on the company’s preparedness for the next big [storm],” observes FM Global CFO Kevin Ingram, “And that requires the CFO to ask tough questions and undertake thoughtful cost-benefit and return-on-investment analyses for capital allocation purposes.”<sup>38</sup> CFOs are uniquely positioned to demonstrate to interested stakeholders, especially investors, how a company is integrating ESG considerations in decision-making related to risks, revenues and strategy. Such communication can attract new investment and lower capital costs. And as Lila Preston, a partner at Generation Investment Management affirmed, “The CFO being knowledgeable is important. CFO training is a huge opportunity for companies to better quantify the impact of these issues and integrate them into their strategy.”

## Strategy #3: Implement a proactive investor engagement strategy

For companies with comprehensive sustainable business strategies, mobilizing C-suite members to discuss these issues authoritatively can be a competitive advantage. By using language that resonates with investors, they have a unique opportunity to present the business case for sustainability to broad and diverse investor audiences.

**Leverage the Board of Directors.** Many investors we interviewed expressed strong interest in hearing more from board members. As company fiduciaries, directors have a unique perspective and ability to demonstrate how material sustainability issues are considered as part of their governance role. In fact, organizations such as the National Association for Corporate Directors (NACD) are now mobilizing to educate members on critical sustainability issues, including climate change. Investors are also increasingly calling on companies to demonstrate board competence on material sustainability issues. In 2016, the California Public Employees Retirement System (CalPERS) revised its Global Governance Principles by calling on companies to have “expertise and experience in climate change risk management strategies.”<sup>39</sup> By proactively mobilizing board members, companies with formal oversight at this level can effectively demonstrate “sustainability competence” to interested investors. Ceres’ research finds a third of the largest U.S. publicly traded companies have formalized board oversight for sustainability strategy and performance. And as one investor observed, “If these risks are critical enough that your board is looking at them, they should be talking about these risks with investors.”

### COMPANY IN ACTION



Throughout 2017 and 2018, **Nike Inc.** leveraged its C-suite to bring sustainability front and center to its investors. At its 2017 Investor Day, Nike informed shareholders of the company’s expectations that 50 percent of its growth in the next five years would be driven by innovation. And in a 2018 video on its IR website, Nike’s CFO Andy Campion explains how sustainable innovation is a core part of that strategy. Campion describes how the company is realizing shareholder value through investments in sustainability. He discusses how sustainability is unlocking product innovations that are high-performing, both in terms of athlete experience and revenue growth—highlighting that since the launch of the company’s sustainably innovated FlyKnit technology, the product has generated over \$1 billion, and is quickly approaching \$2 billion, in revenue growth for the company.<sup>40</sup> The website also features easy access to Nike’s Sustainable Business Report and focused disclosures on its most material issues, as identified by the Sustainable Accounting Standards Board (SASB) guidance. Nike’s Sustainable Business Report includes a more detailed Global Reporting Initiative (GRI) index, and a map of the company’s strategy to the UN Sustainable Development Goals.



# Strategy #3: Implement a proactive investor engagement strategy

## RECOMMENDATION



### 3. Diversify investor engagement strategies.

“Disclosure is useful, but to get a better sense of commitment from a company, you have to interact with them. No matter how good their intentions are, you need to see words line up with actions.”

Tim Goodman, Director of Engagement, Hermes Investment Management

Ceres' 2018 research finds that among the 600 largest publicly traded U.S. companies, 43 percent are now actively engaging investors through forums including earnings calls, annual general meetings, and investor days. But how those companies are engaging on ESG issues, and the depth and value of that engagement, varies widely.

Not all investors are created equal; depending upon the type of investor, and their level of interest in ESG strategies and performance, preferences on where companies present their information differ. As Jamie Martin, executive director of global sustainable finance at Morgan Stanley describes, “ESG investing is not just one thing. It could be integrating ESG into the entire analysis process, the portfolio manager trying to figure out best in class, or momentum stories of companies just starting to get into sustainability, etc. It’s important for investor relations teams to understand that dynamic. There is no one-size-fits-all approach.”

Despite this, the most consistent piece of advice offered was a call for companies to include decision-useful ESG information across engagement platforms. Both mainstream and ESG-focused investors affirmed [Ceres' expectation](#) that if the company believes environmental and social issues are financial issues—and, in particular, if there is an identified business case—this information should be integrated into priority investor meetings, including annual meetings, investor days and even quarterly earnings calls. Importantly, though, companies should recognize that within each of these forums there is a variance in the benefits gained from proactively sharing ESG information.

In using these venues, investors emphasized three main criteria for success:

- 1) focus on presenting sustainability in a business case frame**, emphasizing its influence on risk mitigation, resilience and business growth;
- 2) include company representatives with decision-making authority**, in addition to internal ESG experts; and
- 3) use consistent messaging across all venues.**

# Strategy #3: Implement a proactive investor engagement strategy

## INVESTOR ENGAGEMENT STRATEGIES

### ANNUAL GENERAL MEETINGS

The AGM represents an under-utilized opportunity for presenting sustainability as a strategic priority to large and diverse investors. The format of the traditional AGM is not conducive to in-depth engagement, and the trend toward virtual AGMs is even less so, but it is a critical venue for demonstrating how sustainability is driving business value through both proactive risk mitigation and growth. The AGM is perhaps the biggest opportunity for educating a broad cross-section of investors and positioning the company's leadership as informed messengers of the sustainable business strategy. A small, but growing, number of companies are now integrating sustainability commitments and progress into AGMs, but the vast majority still fail to present the information as financially relevant, strategic investments.

### EARNINGS CALLS

Investors we interviewed were mixed in their opinions as to the value of integrating ESG information in quarterly earnings calls. Some noted the value of complementing the short-term nature of earnings calls with details on longer-term business strategies, including insights on ESG factors relating to corporate resilience. As one European asset manager describes, "There is a big job for [companies] to educate investors. Including a couple of slides on a quarterly earnings call can help educate and engage a fund manager who might be interested."

### ROADSHOWS

ESG-focused company roadshows enable more in-depth dialogues with interested investors, including valuable feedback related to strategies, performance and disclosure. These dialogues often illuminate emerging issues of concern from investors attuned to the environmental and social impacts a company may face. To further maximize these opportunities, however, companies should broaden invitations to include participation by both SRIs and mainstream investors. As an analyst from a major U.S. asset management firm shared, "I have never been invited to a sustainability-focused event hosted by a company, but I would like to be."

### INVESTOR DAYS

A large number of investors we interviewed cited Investor Days as excellent forums for presenting sustainable business strategies in a more substantive way. Investor Days can foster dialogue between investors and the company, and given the breadth of investors that attend, can be an opportunity for educating mainstream investors on the business case for sustainability.

### PRIVATE DIRECT DIALOGUES

One of the most common, and effective, strategies for investor engagement is private direct dialogue. These engagements enable constructive discussion on sensitive issues, facilitate sharing of investor insights and can improve investor understanding of a company's culture, strategy and performance.<sup>41</sup> Direct engagements promote relationship building, and, when done proactively, can deliver the message that the company is willing to invest time and resources to demonstrate sustainability as a competitive advantage. These engagements can also provide a valuable forum for proactively engaging mainstream investors who often prioritize ESG-focused engagement on poor performers or who may be disinclined to participate in ESG directed roadshows. As corporate-driven investor engagement increases, however, investor capacity for these more resource intensive engagements may be challenged. This reinforces the need for companies to diversify engagement strategies and integrate decision-useful ESG information into all investor communications and engagements.

### INVESTOR-FOCUSED CONFERENCES

While sustainable business leaders are often speaking at sustainability-focused conferences, very few target investor-focused events. These forums provide unique opportunities to engage and speak directly with interested investors, and to proactively present sustainable business strategies. These events can also be leveraged to encourage greater collaboration and shared learning across sustainability, IR and governance teams, providing a lower-risk opportunity to jointly meet with investors.



Sustainability is now an inextricable component of **NRG Energy's** future strategy and core messaging to its investors, and the company has diversified its strategy to reach a breadth of investors. Vice President of Sustainability at NRG Energy Bruno Sarda explains:

“At NRG, sustainability is more than a single target or objective, it is foundational to our business and how we serve our customers. Sustainability is fully integrated into all parts of the organization. For this reason, we engage with our investor audience on ESG and sustainability in a holistic, integrated manner. This year we organized investor meetings with NRG’s leadership, from Investor Relations, to Sustainability, to our Corporate Secretary. This allowed us to share and discuss key ESG issues such as governance, including executive compensation and board composition, as well as sustainability alongside our overall company strategy and transformation plan. This holistic approach encouraged our investors to bring ESG analysts, proxy and governance experts, and sometimes sector analysts to meetings, resulting in our ability to address and unify these topics and demonstrate their importance to the overall company strategy.”

### Unintended Consequences of the virtual AGM.

Virtual-only annual general meetings (AGMs) increased from 21 in 2011 to 155 in 2016 to over 212 in 2017.<sup>42</sup> Touted as a strategy for democratizing investor attendance—removing potential time and resource barriers so more investors might participate in these often low-attendance events—the virtual AGM has raised investor concerns that these meetings impinge on shareholder rights to directly access and engage management, both critical elements of good governance.

In response, some of the country’s largest investors are speaking out. In a 2017 letter to dozens of S&P 500 companies, the New York City Comptroller Scott Stringer argues virtual meetings are affecting investor ability to hold management accountable, stating “It’s one of the great markers of American enterprise—whether you own one share or 1 million, you can speak at a company’s annual meeting.”<sup>43</sup> The Comptroller’s Office also announced it would vote against directors at any company with a virtual-only AGM. In response to Duke Energy’s move toward virtual meetings, the California State Teachers Retirement System—a pension fund that at the time held \$143 million in Duke shares and more than \$44 million in Duke bonds—sent a letter to the company observing “...the annual in-person meeting often represents the only time that shareholders, particularly small shareholders, have the opportunity to interact with management and board members.”<sup>44</sup>

Shareholder concerns spurred the Council for Institutional Investors to issue a formal position on virtual meetings, which encourages companies to “use virtual meetings only as a supplement to traditional in-person shareowner meetings, not as a substitute,” and continues “Companies incorporating virtual technology into their shareowner meeting should use it as a tool for broadening, not limiting, shareowner meeting participation.....Any bona fide shareholder who desires to be in the physical room from which the chair conducts a virtual-meeting should have the choice to do so...”<sup>45</sup>

In response to investor pressure and shareholder resolutions, companies including ConocoPhillips and Union Pacific announced they would return to an in-person annual meeting format in 2018.

“Annual meetings can be an effective town hall where investors have a chance to ask questions, the board responds and both sides have a meaningful experience—sometimes the CEO or board is out informally shaking hands with shareholders,” Tim Smith, director of ESG engagement at Walden Asset Management said. “The gold standard is a hybrid, where you allow people to come to a meeting, but also allow them to participate online.”





# A Two-Way Street: A Call for Increased Investor Transparency

When we asked investors to consider the future of ESG investing, many first looked back. Changes in the past decade, particularly in the past few years, left investors we interviewed with very little uncertainty about the future of ESG and its growing importance in investment decision-making.

Increasingly, major investment firms are stepping out to make their position very public. In October 2018, BlackRock CEO Larry Fink told global CEOs of the firm's intention to become a leader in sustainable investing. "We are going to see evidence over the long term that sustainable investing is going to be at least equivalent to core investments. I believe personally it will be higher," Fink wrote in his annual letter to CEOs.<sup>46</sup> Two months later, UBS Global Wealth Management announced plans to grade managers on its platform on their integration of ESG factors in investment processes. As Greg Trinks, head of Investment Management Research for the Americas at UBS Global Wealth Management, explained, "You see products that are labeled as [ESG] and are not. It's difficult for clients to gauge those assessments—the degree to which ESG approaches are employed. [W]e need to provide solutions and guidance that help clients understand the differences."<sup>47</sup>

These are positive market signals that will continue to reinforce the need for improved corporate communication of the business value of sustainability. Yet, investor calls for increased corporate transparency must also be met with improved clarity from investors on how strong ESG performance will be rewarded. Specifically, investors have an opportunity to:

1. Transparently communicate priorities for corporate performance and disclosure;
2. Demonstrate how ESG considerations are integrated in investment decision-making;
3. Build expertise on the business value of sustainability; and
4. Increase the sophistication of corporate engagement on ESG by asking questions that demonstrate an understanding that ESG issues are material financial issues, and by demanding that companies communicate this link.

As one socially responsible investment manager put it, "The investment community needs to up their game by connecting the dots between sustainability and financial performance. We can't get away with the same type of questions we did 5-6 years ago; we need to ask tougher questions that drive companies to communicate the business case for sustainability."

Ceres understands that sustainability is the bottom line. We are committed to a future where sustainability is not a separate work stream, but an integral component of business planning and execution that investors routinely assess and reward. **By elevating sustainability as a key driver of business value, companies and investors *must and can* change the conversation.**

# Appendix: Methodology

The methodology for this report consisted of a review of themes presented throughout Ceres-led investor and corporate dialogues, individual interviews with investment professionals and corporate sustainability executives and a review of the most recent literature and research.

## Ceres-led Investor and Company Dialogues

For 30 years, Ceres has partnered with the world's largest corporations and investors to better integrate environmental and social considerations into the way they do business—effectively working together to redefine business as usual. Through our convenings we provide forums for investors to gain insights into companies' current and emerging challenges, risks and opportunities—and for companies to access valuable insights into evolving investor expectations for environmental and social performance. As active advocates in thousands of these corporate and investor dialogues, Ceres has gained unique insight into the expectations investors have of the companies they own, the evolution of those expectations and engagement strategies, and the common threads that have emerged from these dialogues.

## Interviews

Informed by the literature review and themes from Ceres corporate and investor dialogues, we conducted more than 30 interviews with investment professionals and corporate executives to gain deeper insights into the research topic.

The investors we interviewed were a mix of those located in the U.S. and Europe. We conducted semi-structured interviews, covering the following key themes:

- What does meaningful ESG disclosure look like to the investor community, and where do they want to see it?
- In what timeframe are investors interested: short or long-term?
- How do investors define sustainable business leadership?
- How, in an increasingly crowded space of companies claiming to be sustainable, can companies stand out and be rewarded by investors for their leadership?

The corporate sustainability professionals we interviewed represented U.S.-headquartered, publicly traded companies. We conducted semi-structured interviews, covering the following key themes:

- Drivers of ESG integration into investor engagement;
- The evolution of investor engagement on ESG topics—what's worked and what hasn't; and
- Internal engagement and alignment of key corporate decision-makers and representatives.

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**Ceres**

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Headquarters  
99 Chauncy Street, 6th Floor  
Boston, MA 02111  
[www.ceres.org](http://www.ceres.org)