The new bottom line

Environmental and Social Goverance Investment (ESGI)

June 2017

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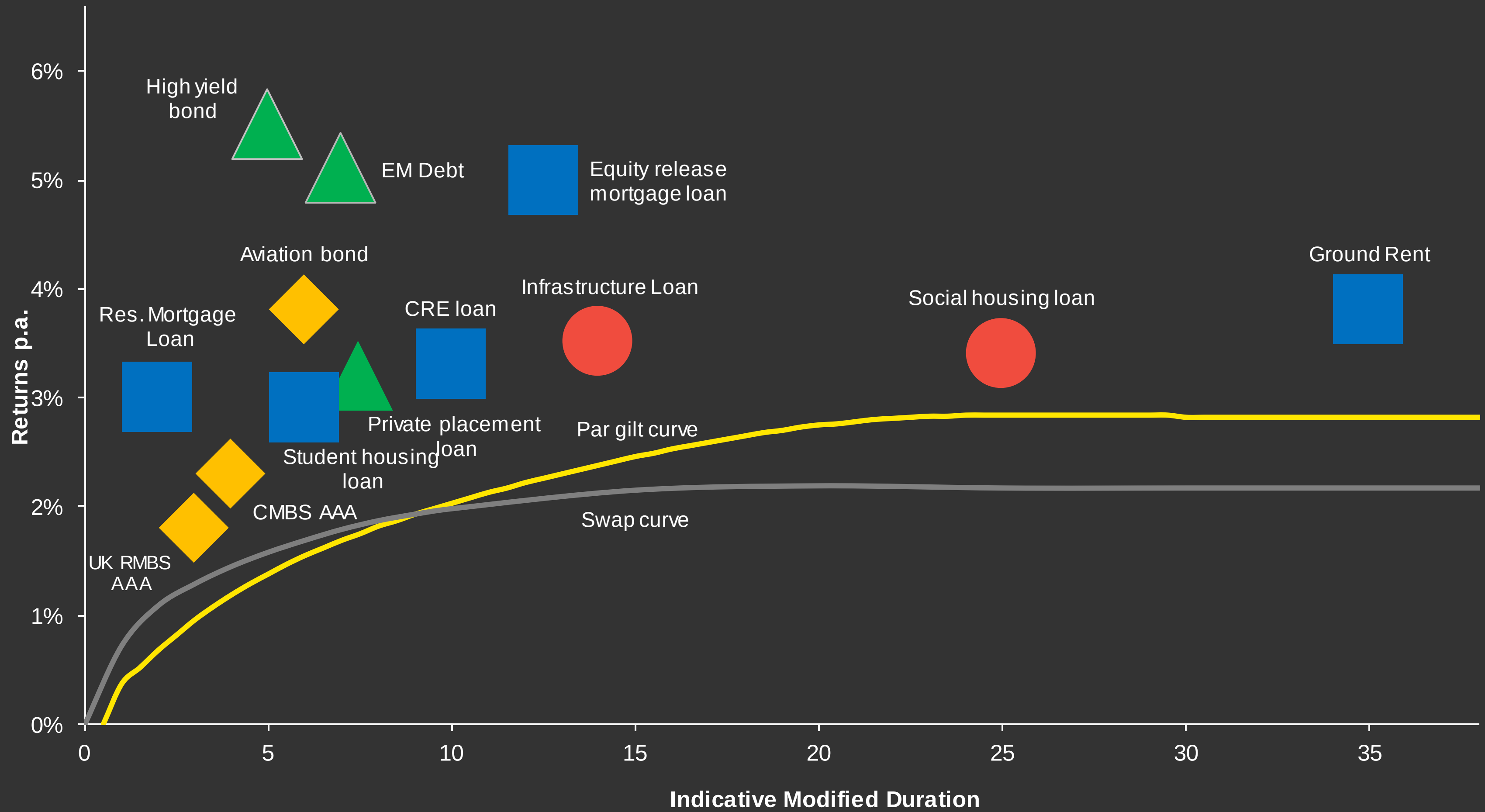
Building a better working world

Introduction



What is Prudential saying?

Our approach to ESG

Prudential's purpose is to help people de-risk their lives and deal with their biggest financial concerns. We use our capabilities, footprint and scale to meet the long-term savings and protection needs of an increasingly self-reliant middle class, creating value for both our customers and our shareholders.

Our relationships with our customers are long-term, so it is vital that our strategy and its execution ensure that we are a sustainable business. Our success in delivering for our customers and shareholders depends on effective engagement with our stakeholders.

Managing a sustainable business means managing a wide range of ESG issues. Every one of these areas is integral to our performance and sustainability and we approach them accordingly.

Polling question # 1

ESG risks are material financial risks?

A. Agree

B. Disagree

C. What are ESG risks?

Polling question # 2

I should be considering ESG risks within my work?

A. Agree

B. Disagree

C. What are ESG risks?

Polling question # 3

Do you think that climate change will significantly affect how the life industry operates a) before 2025?; b) before 2035?

A. Yes

B. No

What we will cover

1. **What is ESGI?**
2. Responsible investment – “why not” rather than “why”?
3. The role of actuaries - takeaways and action points

The better the question.
The better the answer.
The better the world works.

What is ESGI?

ESGI is also know as Responsible investment

It is defined as "*an approach to investing that aims to incorporate environmental, social and governance (ESG) factors into investment decisions, to better manage risk and generate sustainable, long-term returns*." (Principles for Responsible Investment).

Environmental factors

We have set out below our perception of the types of climate change risks with examples of each of them. These risks are only a starting point and it is expected that many physical impacts of climate change are self-reinforcing.

Physical

Damage to land, buildings, stock or infrastructure owing to physical effects of climate-related factors, such as:

- Heat waves
- Drought
- Rising sea levels
- Ocean acidification
- Storms or flooding.

Secondary

Knock-on effects of physical risks, such as:

- Falling crop yields
- Resource shortages
- Supply chain disruption
- Migration
- Political instability and conflict.

Policy

Financial impairment arising from local, national or international policy responses to climate change, such as:

- Carbon pricing or levies
- Emission caps
- Subsidy withdrawal.

Liability

Financial liabilities, such as insurance liabilities and legal claims, arising under the law of contract, tort or negligence due to other climate-related risks.

Transition

Financial losses arising from disorderly or volatile adjustments to the value of listed and unlisted securities, assets and liabilities in response to other climate-related risks.

Reputational

Risks affecting businesses engaging in, or connected with, activities that some stakeholders consider to be inconsistent with addressing climate change.

Social factors

Social Factors

Diversity

- Gender
- Culture

Human Rights

- Freedom of speech
- Freedom of thought

Consumer protection

- Mis-selling

Animal Welfare

- Pharmaceutical companies

Governance factors

What is ESGI?

Responsible investment activities are often categorised into three elements:

Engage – Active ownership

Exercising shareholder rights, and engaging with companies on ESG topics to encourage them to adapt certain behaviour.

Invest – ESG in investment analysis

Integrating ESG factors in investment decision making and analysis; identify thematic ESG opportunities.

Avoid – Negative screening

Avoiding undesired investments altogether, through screening or reallocation for financial risk.

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Waiting for climate change

Time to act…

ESG related discussions kicked off long ago, dating back to 1987.

Year	Event
1987	The World Commission on Environment and Development Issues report "Our Common Future" with most commonly accepted definition of sustainability as: "sustainable development that meets the needs of the present without compromising the ability of future generations to meet their own needs".
1990	UN General Assembly negotiations on a Framework Convention begin in December Intergovernmental Negotiating Committee (INC) held five sessions, where more than 150 states discussed binding commitments, targets and timetables for emissions reductions, financial mechanisms, technology transfer and" common but differentiated" responsibilities of developed and developing countries.
1991	The UN Framework Convention on Climate Change (UNFCCC) opens for signatures at Rio Earth Summit in June, bringing the world together to curb greenhouse gas emissions and adapt to climate change.
1997	Kyoto Protocol is adopted in December 1997, establishing for the first time in history global commitment to reducing carbon emissions and to fight climate change
2001	The 7th Conference of Parties (COP7,) held in Marrakesh in November 2001, formalised the agreement on operational rules for International Emissions Trading Association (IETA), the Clean Development Mechanism (CDM) and Joint Implementation (JI) along with a compliance regime and accounting procedures.
2002	The Global Reporting Initiative (GRI) and the Extractive Industry Transparency Initiative (EITI) are launched, increasing corporate transparency, allowing stakeholders to hold them accountable for their contributions to sustainable development.
2005	The UN-backed Principles for Responsible Investment (PRI) are launched, a catalyst for financial markets to adopt responsible investment approaches.

Time to act… (cont'd)

In recent years, discussions and actions have accelerated.

Year	Event
2005	EU Emissions Trading launches in January 2005 – the first and largest emissions trading scheme in the world, launches as a major pillar of EU climate policy. Installations regulated by the scheme are collectively responsible for close to half of the EU's emissions of CO_2.
2006	The Stern Review concludes that climate change damages global CDP by up to 20% if left unchecked, and climate change emerges on the global business agenda.
2010	The Cancun Agreements stablishes the Green Climate Fund in December 2010.
2014	The European Union issues a new directive on non-financial entities with more than 500 employees to report on policies, risks and outcomes related to environmental, social, and governance (ESG) matters.
2014	The Intergovernmental Panel on Climate Change (IPCC) release the synthesis report of its 5th assessment report, which underlined the urgency of climate action in March 2014.
2015	In December 2015, the 21st Conference of Parties (COP21) convenes countries and forms an agreement to limit temperature rise to two degrees. This may mean that far-reaching measures must be taken, such as limiting fossil fuel extraction, implementing carbon pricing mechanisms on a global level, and company disclosure on emissions intensity of asset portfolios.
2016	The landmark Paris Agreement in October 2016, requiring 55 countries representing 55% of global emissions of greenhouse gases, is ratified after 10 more countries finally endorse the deal.
2017	Trump confirms withdrawal from the Paris Agreement in June 2017.

What are we hearing?

Climate Change: Managing Risk and Uncertainty
Policy Briefing

Guardian sustainable business

Climate change and resource scarcity may wipe out pensions industry
Jo Confino

New report from Anglia Ruskin University shows that actuaries, charged with risk management in the financial sector, have ignored the greatest risk of all time

theguardian

Carney warns of risks from climate change 'tragedy of the horizon'

Bank of England governor tells Lloyd's insurers that 'challenges currently posed by climate change pale in significance compared with what might come'

Donald J. Trump
@realDonaldTrump

The concept of global warming was created by and for the Chinese in order to make U.S. manufacturing non-competitive.

20,565 11,642

China and California sign deal to work on climate change without Trump

Governor Jerry Brown says president's decision to pull the US out of the Paris agreement will be only a temporary setback

CNBC

Obama unveils clean energy plan, amid legal threats

Everett Rosenfeld | @Ev_Rosenfeld

The Telegraph

HOME » FINANCE » ECONOMICS

Paris climate deal to ignite a $90 trillion energy revolution

The old fossil order is on borrowed time as China and even India join the drive for dramatic cuts in CO2 emissions

BloombergBusiness

News Markets Insights Video

Americans Have Never Been So Sure About Climate Change—Even Republicans

Look at the massive shift among Republicans on the issue this year.

China to announce carbon trading plans

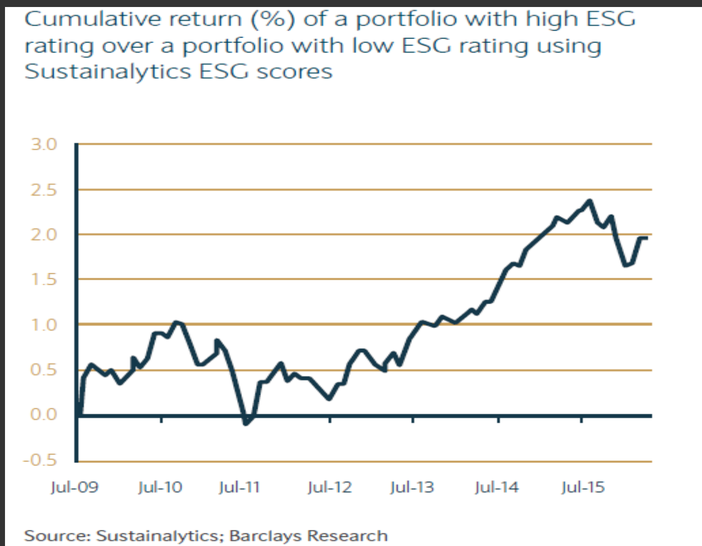
Xi Jinping to unveil cap-and-trade system in Washington that will affect businesses around the world

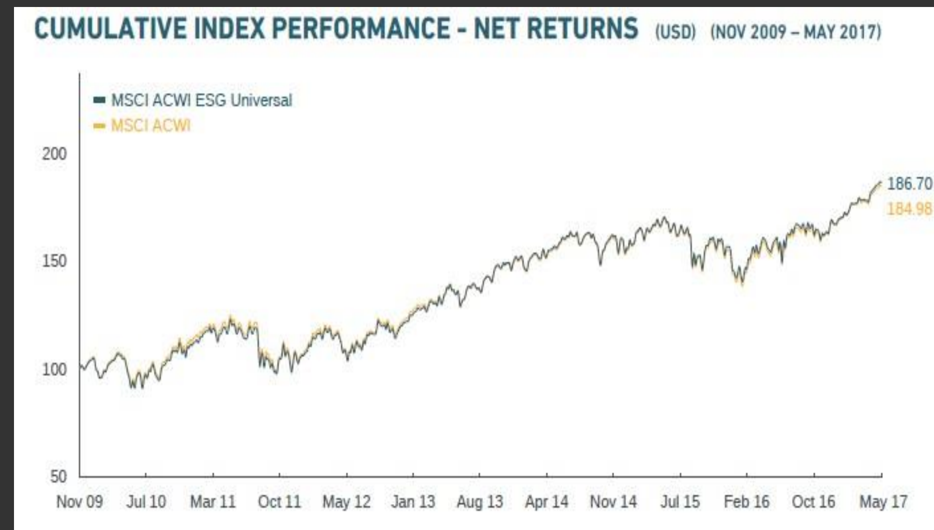
Investors move to limit impact of climate change on their portfolios

COP21 · CMP11
PARIS 2015
UN CLIMATE CHANGE CONFERENCE

What are the drivers for financial services firms?

- ESG and performance – how do they compare?





INDEX RISK AND RETURN CHARACTERISTICS (NOV 30, 2009 – MAY 31, 2017)

				ANNUALIZED STD DEV (%) [2]			SHARPE RATIO [2, 3]				
	Beta	Tracking Error (%)	Turnover (%) [1]	3 Yr	5 Yr	10 Yr	3 Yr	5 Yr	10 Yr	Since Nov 30, 2009	(%)
MSCI ACWI ESG Universal	0.99	1.01	13.72	10.91	10.20	na	0.51	1.13	na	0.67	18.40
MSCI ACWI	1.00	0.00	2.74	10.81	10.13	na	0.50	1.10	na	0.65	19.20

[1] Last 12 months [2] Based on monthly net returns data [3] Based on ICE LIBOR 1M

What are the drivers for financial services firms? (cont'd)

Pension scheme trustee's guidance

Diversification of return / green investment

Corporate governance…

Risk of inaction - stranded assets

Marketing / brand strengthening

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Addressing climate change – the route forward

Climate change agenda	How actuaries can help
There has been an increased in interest in climate change related issues in recent times as seen by the Paris Agreement signed during the 21st Annual Conference of the Parties (COP21) in October 2016.	?
Climate change is on the global agenda and is likely to impact businesses across the globe. Inevitably, some regions will have better understanding relative to the rest.	
Being a relatively new topic, it is unlikely that businesses have the required insights and expertise to address these issues.	
One of the key ways of understanding climate change related issues may lie in the advancement of technology.	
There is a need for actuaries to pay greater attention to climate change related issues as part of their daily work, including those in the investment space.	

IFoA Risk Bulletin

"Actuaries should ensure that they understand, and are clear in communicating, the extent to which they have taken account of climate-related risks in any relevant decisions, calculations or advice"

The IFoA referred its members to the report published by the Task Force on Climate-related Financial Disclosures (TCFD), specifically page 16 of the report which contains risks identified under each of the headings of Governance, Strategy, Risk Management and Metrics and Targets.

The IFoA urged actuaries to consider how climate change risks would affect the advice they give. For example, they should take into account the:

I. implications of climate risk on invested assets
II. implications of extreme weather on firms with short term liabilities (e.g. general insurers and reinsurers)
III. implications of changing patterns of temperature and disease on mortality for firms with long term liabilities (e.g. life insurers, reinsurers and pensions funds).

Types of risk highlighted in the risk bulletin includes:

I. Physical risks – arising from potential degradation to physical assets
II. Transition risks – arising from the speed of implementation of government policies, for example rapid transition to low carbon economy leading to "stranded assets"
III. Liability risks – arising from damage suffered by third parties due to climate change

EY

IFoA ESG Investment Working Party

- Environmental, social and corporate governance (ESG) issues are increasingly acknowledged as important investment considerations. ESG encompasses a wide range of topics including climate change and water scarcity; working conditions and human rights; board diversity and executive remuneration.
- Reporting to the Resource and Environment (R&E) Board and the Finance and Investment (F&I) Board, the ESG Investment Working Party will work to co-ordinate and expand the IFoA's ESG-related investment activities and advance actuarial capacity in this field.
- The working party will cover ESG considerations in relation to assets in a broad sense, including their financial impact and their incorporation in investment processes.

IFoA initiatives

Engagement – practical guide for ESG	Working party acknowledges a gap around literature/support for members ► professionalism CPD videos / CPD sessions could be a route into ESG, discussing the ethical dilemmas it present ► a number of investment managers do webinars on these topics which could be leveraged as an easy route forward ► lots of ESG material exists; we need to make the link between actuaries and ESG ► hard to get attention of actuarial community without numbers – e.g. an order of magnitude on climate impact on pension scheme funding to inform the way we think about this.
IFoA as PRI Network supporter	Principles for Responsible Investment (PRI) is the leading global organisation advocating responsible investment. Though supported by the United Nations, it is an independent organisation. There are around 1500 signatories of the PRI. These are asset owners, investment managers and professional service providers who pay a fee to be signatories. ► Open to non-profit organisations which commit to actively supporting the PRI within their spheres of influence. Requires promotion of responsible investment and the PRI, at least one speaking slot for the PRI each year, and to reporting annually on PRI activities. ► Proposal going to PPAC (Policy & Public Affairs Committee). Expectation is that it will be approved and meeting held with PRI to discuss how to collaborate and support each other. ► PRI is developing its reporting process. One of key changes is introducing reporting for service providers on a trial basis currently and becoming compulsory next year None of the current network supporters appear to be professional bodies, so the IFoA would be the first to sign up. This is consistent with our growing involvement in ESG work and demonstrates a broad approach to professionalism, including taking long-term views and going beyond narrow self interest.
ESGI as part of exam curriculum	The IFoA's new curriculum will first be examined in April 2019. ESG will be incorporated into core reading for the new advanced specialist investment paper (SA7).

Breakout session
The role of actuaries

BREAK OUT (3 groups)

- Should insurers (and pension funds) as asset owners be considering environmental social and governance (ESG) factors as part of their investment framework?
- What opportunities does ESG investment present?
- Is Solvency II ignoring one of the biggest long term risks to global economic markets?

ESG – what is the actuarial angle?

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ESG – what is the actuarial angle?

1. Understanding the implications for specific asset classes
2. Translating qualitative views on ESG into quantitative framework
3. Implementing ESG considerations into investment strategy and decisions
4. Modelling impacts of ESG factors
5. Understanding the different implications of E vs S vs G

EY

What should actuaries be aware of?

Understanding of responsible investment

- Related concepts and terminology, including sustainability, SRI, ethical investment and impact investment; differing emphases on financial and environmental/social/ethical objectives
- List of example ESG factors
- Evidence for the relevance of ESG to financial performance
- Importance of long-term perspective, but relevant over short-term too
- Relevant at all stages of the investment process: asset allocation, manager selection and monitoring, stock selection and monitoring, exercise of ownership rights, reporting
- Example approaches: integration, negative screening, positive screening, ESG-related indices (including tilting), themed investments. Note: all asset classes, not just equities
- Climate change as an environmental and social factor, including distinction between physical, transition and liability risks, and concept of stranded assets
- Corporate governance codes, complemented by stewardship codes

Legislative requirements and regulatory expectations

- Fiduciary duty of pension scheme trustees (eg Law Commission guidance in the UK)
- UK Pensions Regulator's guidance for DB and DC schemes
- Amended EU directives: IORP and shareholder rights
- Bank of England's September 2015 report to Defra about climate change implications for the insurance industry (and Mark Carney's accompanying speech)
- Task Force on Climate-Related Financial Disclosures

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Appendix

A. Points of view

Point of views

EY is recognised worldwide for our insightful and well-rounded analysis of a vast range of topics of interest for today's business community. Below are examples of recent points of view published by EY on the nexus of climate change and the finance sector.

Climate Change: The investment perspective

Drawing from EY's involvement as one of the four project managers on the Taskforce on Climate-related Financial Disclosures (TCFD) providing recommendations across sectors on how companies can identify, manage and evaluate climate change risks and opportunities, this report explores the many ways in which climate change and stranded assets are impacting the investment community. Find it here

Shifting the carbon pricing debate

This EY-commissioned study, based on a survey of more than 100 executives from around the world conducted in 2015, explores the prevailing views of businesses around the world toward carbon pricing, as both a regulatory necessity and strategic corporate priority. Find it here.

2017 Global PE Equity Survey

Drawing on EY's extensive network, this report surveyed over a hundred private equity funds to analyse how PE firms are staying competitive in the face of new regulation and reporting expectations. The study shows that improving management reporting has been the key area of focus for PE firms. Forward looking CFOs have been keen to produce information more accurately and expeditiously. Indeed, developing investor communications should lead to a more streamlined process and the ability to report additional factors such as ESG while ensuring that investor portals are being used to their full potential. Find it here.

Sustainable Investing: How the millennial generation invests its wealth.

Adapting to a sustainable investment environment will be a challenge for firms and will require changes to the existing culture, technology and processes. Our view is that firms must prioritize advisor awareness of millennial values and assure advisors are fully trained and equipped with the tools required to have meaningful discussions around sustainable investing. Find it here.

Tomorrow's Investment Rules 2.0

For a second year, EY surveyed a global sample of more than 200 institutional investors, including portfolio managers, equity analysts, chief investment officers and managing directors. We explored their views on the availability and quality of corporate nonfinancial information, and on whether they used this information when making investment decisions. Find it here.

Is your nonfinancial performance revealing the true value of your business to investors

This report provides insights into the views of institutional investors on nonfinancial reporting and the role ESG analysis plays in their investment decision making. The Paris Climate Conference agreement will lead to an increase in disclosures about companies' climate practices and risk management strategies, say investors. Nonfinancial performance plays a pivotal role in the investment decisions for most of the surveyed investors, and for a greater percentage of investors than in previous years. Find it here.

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