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ESG is Dead, Long Live ESG

Webinar Transcript

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Robert McConnaughey (00:00:10:11 - 00:11:01:02)

Good afternoon, everyone, and welcome to our webinar, for today's The Big So What™ discussion our topic is ESG is dead, long live ESG. I appreciate everyone taking time out of their busy days to join us. I'm Robert McConaughey. I head up Corbin's Investor Relations Advisory and Sustainability work. For the next 45 minutes, our panelists and I are going to discuss the state of the state of ESG for public companies and their equity investors.

There's been plenty of noise around ESG recently, but we believe that the ESG backlash has led to a lot of healthy conversation and reexamination of the future role of ESG in public company strategy. I've been with Corbin for three years but have spent my career on the buy side. Before that, places like Fidelity Equity and Columbia Threadneedle, where, as the Head of Equity, I helped build their global sustainable investing business, so not only working on this as an advisor to public companies today but come to that with the experience of an ESG investor.

With me today to discuss and debate these issues, we're thrilled to have a distinguished panel representing the investment community as well as in-house corporate sustainability officers. First, my friend and former colleague Katherine Collins is the Head of Sustainable Investing at Putnam Investments and portfolio manager for Putnam Sustainable Equity Strategies with over $8 billion in assets under management. In addition to her investment roles, Ms. Collins is an author and beekeeper, holding degrees from Harvard Divinity School and Wellesley College. She serves on several nonprofit boards, including the Santa Fe Institute, Harvard Divinity School's Dean's Council, and Wellesley Center for Women. In 2021, she was named to the inaugural Forbes 50 over 50 list of leaders who are shaping the future of finance.

Catherine Sheehy leads the ESG work at United Therapeutics Corporation, a pioneering $11 billion market cap biotechnology company, as well as serving as the company's public benefit corporation Transparency Director. Before joining United Therapeutics, Catherine worked at UL Solutions, a global leader in applied safety science, where she focused on customer sustainability efforts. Previous work included working at Accenture in Management Consulting and at the Human Rights Campaign, where she helped advanced LGBTQ+ workplace diversity issues for several years. For several years before that, Catherine worked at the Investor Responsibility Research Center.

Richard Brasher leads the sustainability effort at LKQ Corporation, a $14 billion market cap provider of alternative and specialty parts to repair and accessorize automobiles and other vehicles in North America and across Europe. LKQ is also the world's largest recycler of automobiles, effectively dismantling and reusing or remanufacturing nearly three quarters of a million vehicles annually. Prior to LKQ, Richard has held various finance roles around the globe.

Before we dive into our discussion, I'm going to share a few slides of Corbin research and perspective to set the stage.

So, we've all witnessed the loud backlash against ESG out in the popular press, and we don't want to diminish that. This is a real phenomenon, even if we believe that it is really amplified by some of the polarized politics of our day, his backlash is real, and we want to really think about what it represents. Now, in our opinion, a large percentage of this is anti-ESG as part of a broader anti-woke, anti-political correctness approach. Also, there's a faction of anti-ESG work that is really a function of defending the fossil fuel industry. There are other sub issues of folks that have concerns about ESG as regulatory overreach or an undue administrative burden on lots of companies, particularly smaller companies, or questions around the relevance of all aspects of ESG for all companies.

There's also thoughts of, you know, some critics would say ESG is just a window dressing exercise versus really authentic action. You know, well-funded companies can go through that exercise report on all this data, which is a lot tougher for smaller companies where it is less core to their business. So, this is a real issue, and we take it seriously.

That said, according to our research spanning over a decade, ESG continues overall to grow in importance as an investment factor for the investors that we're speaking to over this period of time, and again, we started doing that, collecting this data back in 2010. We've steadily seen ESG grow up to our data last year, where 55% of those polled viewed ESG as very important or critical as an investment factor, with less than 3% saying it really didn't matter.

Building on that, investors belief that ESG is a factor in creating Alpha, excess performance, increased to almost 30% last year from just 8% only two years prior in 2021. And ultimately, at the end of the day, there is a huge pool of capital that is either directly sustainable or influenced by ESG and sustainability issues. So, let's, you know, fast forward to the present.

You know, this is sort of hot off the presses data based on the polling from our audience here today from registrants for this webinar. In asking our audience, has this backlash impacted your organization's core commitments to ESG or sustainability, 90% said that they have maintained those core commitments. 7% said they're actually increasing. And it was a very spare, you know, 2% said that they were reducing their commitments.

In fairness, if we cut through this to some of the qualitative open-ended questions, there is an underlying theme within that maintained bucket of reconsidering how we're maintaining our core commitments. And the common theme around that was gravitation toward things that were clearly economically material to the business.

We saw lots of quotes of “We perhaps have gotten less aggressive talking about DEI issues in our public work, but our decarbonization business opportunities are so great that we're reinvesting there. Thus, our core remains intact.” Along the way, almost 50% (49% of our respondents) said their organization, as a function of some of these changes, has made adjustments to where they're using the term ESG, largely converting from ESG to sustainability.

It's an issue that we'll talk about with our panel later. Switching to our polls of corporates as to how they think about ESG in their business strategy. Again, the data here, the blue column is 2019, the black column of 2023. We've seen just in that four years ESG go from 36% saying it was critical or very important to 62% viewing ESG as critical or very important to their company's long-term success.

Backing up some of that ESG versus sustainability terminology work, what you're seeing here is a word scrape of earnings transcripts, earnings presentations, and investor presentations. Over time, we have clearly seen a steady drumbeat of sustainability not diminishing, but the external use of the term ESG has seen a noticeable drop. So again, we think those core commitments, the overall direction of travel, hasn't changed; some sensitivity to how we talk about it has. And again, we think lots of that is healthy.

On this page, we're talking about the Corbin Critical Five Investment Factors. In our work over 16 years and close to 25,000 investor interviews, five things have risen to the top that we consistently hear from investors are the most important aspects as to how they assess a company’s leadership quality, sound long-term strategy, execution, track record, sustainable competitive advantages, and effective capital allocation.

Being a leader in trying to manage all those things is tricky. We think that managing sustainability as a function of all those is relevant and important. Stakeholder relationships for long-term positive impact, relationships with customers, suppliers, employers, regulators, and shareholders all have really complex needs related to changes in society around us, regulatory changes, and environmental changes. Those are all creating risks and opportunities. And investors are looking for leaders that are capable of incorporating these complex issues into their strategy. How do we, if we say we're going to deal with those issues, execute it effectively? How do we use those to build competitive advantage in our business? If we can solve complex sustainability issues for a customer while delivering reliability, low cost, that can deepen our competitive moats.

And how do we think about capital allocation in the context of conservation and efficiency? Sustainability is relevant to these things. So done right and again done right is an important caveat. Sustainability can reinforce a company's value proposition to a broad investor audience. A few key takeaways before we get to the panel. One ESG isn't going away. It remains an influential investment factor, with 90%+ of investors placing importance on ESG while making investment decisions. Two, corporates are increasingly integrating ESG deeply into their long-term business strategies. More than half view it as very important to their company's long-term success, and that's doubled since 2019. Importantly, ESG is seen as both risk mitigation and increasingly as an opportunity to build competitive advantage.

And we'll talk a lot about this today about how do we make sure that ESG is something that we can play offense with and build into our strategy, not just a "We'll do less bad stuff in the course of doing business." And finally, as ESG is increasingly adopted by more and more corporates, investors are finding it more important to discern a holistic, competitive edge, not just screening out the negative outliers, but looking at companies that are authentic and targeted to cut through the noise. And those companies that can do so are accessing much larger pools of capital.

So that's our quick summary of our data and findings. Now let's turn to our panel for a broader discussion.

So, Katherine Collins, you know, if we if we cut through some of these polarized politics of the ESG backlash, you know, the crux of that anti-ESG argument is that ESG considerations conflict with fiduciary duty. You know, I've always enjoyed hearing you talk about new investment ideas. You have that find tremendous value creation opportunities through a sustainability lens. So, what do you say to those that see ESG in conflict with shareholder goals and things?

Katherine Collins (00:11:01:02 - 00:13:42:24)

Thanks, Robert, it's a great place to start, and I think maybe to orient us as we dive in, it is helpful to reflect on where we've come from. For many folks who have been practitioners in the field for a long time, it wasn't that long ago that we were laboring in obscurity. You know, no one was too sure what we were working on.

Nobody really wanted to engage in topics around ESG or sustainability. ESG wasn't even a term until relatively recently. That first phase was followed, it seems quickly now by what I call the everything everywhere, all at once phase, you know, lots of investment, product development, lots of new nomenclature, lots of new regulatory requirements, lots of people saying lots of things very quickly.

This is the phase where you go home for Thanksgiving and your cousins suddenly have very strong opinions on ESG regulatory process, needs to kind of out of the blue. So, it's not too surprising that after a very active period like that, we now have entered the third phase, which I would call the phase of refinement, you know, the phase where we get the chance to really focus a little more strategically.

In many cases, we're getting to better questions kind of next level questions. And I see this across all the different contexts that we're working within, both with operating companies and with investors, and with our own clients. So, I think that arc of development is really important to reflect upon, it's the same arc that we see for almost every other innovation wave.

So, for anyone who's invested in or operated an enterprise for a long time, this is actually a pretty familiar pattern. So, in this phase of our assignment, I'm really happy to say that in most settings we're seeing a real focus, not a diminishing, not a backtracking, but again, over refinement, a real focus on the issues that are most strategic for any given setting.

And so, it's not a cookie cutter approach. It's very context specific. If you're an investor, this is kind of a dream come true. We all want to focus on what's most important for any given investment decision, and that means understanding for any given company, any given region or any given industry, taking all of that into consideration, and making those issues, the primary issues. Almost everyone on this call is probably familiar at this point with the concept of materiality and in particular financial materiality.

That is sort of the bridge between the issues that are important generically in the world and the issues that are important in a given specific context. And so, for anyone who's taking that that notion of materiality as their North Star, I think we're standing on really solid ground in that. And that goes for the relationship with fiduciary duty as well.

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If you're focused on what's important, that's your job as a fiduciary. It doesn't matter what category that importance falls into.

Robert McConnaughey (00:13:43:01 - 00:14:07:24)

That's great. Turning to our other Catherine, Catherine Sheehy, United Therapeutics has gone several steps farther than even most mission driven companies and is now a registered public benefit corporation that hasn't seemed to have weighed on your financial success in any way. So how would you summarize for a skeptical investor the ways in which the focus on sustainability actually benefits the business?

Catherine Sheehy (00:14:08:01 - 00:17:58:00)

So, you're correct, being a PBC hasn't affected our financial success. What it does is it codifies our obligation to serve and report to multiple stakeholders, including investors. So, let me give you some background before answering your question. UT was founded in 1996 by parents Martine and Bina Rothblatt, trying to save the life of their kid who was diagnosed with a rare disease called pulmonary arterial hypertension, or PAH. It's a type of high blood pressure that affects the blood vessels in the lungs and the right side of the heart. And it causes the heart to work harder, ultimately leads to failure and ultimately death.

Now, there were no good therapies at the time. The only known cure remains lung transplantation. And when I say terminal, I mean that these parents were told that their child had, at best, about five years.

So, our PBC purpose today draws from that founding history. Our purpose is to provide a brighter future for patients through the development of novel pharmaceutical therapies and technologies that expand the availability of tolerable, transplantable organs. And because I suspect that a lot of people might wonder about this, I'm really pleased to report that Martin and Binion's daughter, Genesis, who got that diagnosis in the nineties, works for the company today.

She's our inspirational founder and ambassador. Now we see our PBC strategy is the flip side of our ESG strategy, and it's all underneath our overarching sustainability approach. So, we align our PBC objectives with our three core stakeholders. Patient outcomes is our North Star, our people, and we have a goal to be a destination employer because we need to attract the most innovative, tenacious people to do this work.

And then the last one is a big one. It's all of humankind. And that's where our objective to operate sustainability lives. And we've made significant investments in mitigating our environmental footprint because we've seen the science linking patient health to environmental factors, including climate related impacts, and specifically as a company working on solutions to address diseases that affect the lungs.

It's kind of a no brainer, right, to address our own environmental impacts. And that's why we have a long-standing commitment to, say, net zero energy facilities where feasible. Fast forward to today, we've got, you know, seven megawatts of onsite solar capacity to power own operations. About 16% of our portfolio operates assignment zero energy facilities, and about 26% of our portfolio maintains fleet certifications.

So, when we get to that question about the level of investment in our environmental footprint and we do get that question about how environmental sustainability benefits the business, I have three responses. The first one is about energy. Greener buildings use less fossil fuel energy, and with onsite solar, less energy from the grid, and that translates into lower cost to operate overall. But it also makes our buildings more resilient to potential energy outages that can happen during peak demand, let alone during dramatic weather events.

Now let's talk about people. I think we've all seen studies telling us that Gen Z and millennials, which together account for almost half the global population, want to make a positive impact on society and the communities that they live and work in.

And they want to work for companies that are doing the right thing. And so, we want to hire those people. And then the final point that I make is that other stakeholders value this work. So, all sorts of stakeholders, from local community members, elected officials and, of course, certain investors are really interested in how we address these issues.

Robert McConnaughey (00:17:58:02 - 00:18:23:02)

Great. Thank you; it's an inspiring story. Richard, similar question for you. You know, theoretically, if you were asked to respond to a grouchy board member, not that any of your board members are actually grouchy, but if you were theoretically asked to respond to a grouchy board member asking, you know, how does this sustainability stuff create value for LKQ, you know, what would you say?

Richard Brasher (00:18:23:04 - 00:22:07:18)

First of all, I agree with you, our board members tend not to be grouchy, but should they be grouchy. I think that's definitely, you know, an important thing to think about. I'd like to go back firstly to something that you said earlier. You talked about sort of the overall backlash against ESG. And I think the first point I would make is that I don't really see it as a backlash so much as a maturing of understanding.

So, I think there's two points there. First of all, ESG is relatively new-say about ten, ten years, maybe 20 years old in terms of the concept. And I think the public debate on climate is absolutely valid and very important to have both sides of the debate. But I think backlashes put a bit too to too strong a term for it.

So, I kind of call it getting wiser to the facts, and the second point I would make is I think we've gone from what was a voluntary world into a mandatory world. So, I remember the days back in the early 2000s when the European Union introduced the IFRS accounting standards. And that was a big change for a lot of corporations to deal with.

And I still like the ESG, or sustainability disclosures that are coming from CSR in Europe, the estimates out of the SEC and California. So, it's very similar to that big change from a very voluntary, fragmented reporting environment into one which is much more regulated. So, I think first of all, the grouchy board member is going to ask those questions, and I'm going to give him two answers or two answers around that sort of development, the public debate, debate and development of reporting environment.

So, I think in terms of value, the way I would describe it is that I think there are two types of value. There's real value. And when I talk about real value, I mean real economic financial value that comes out of changing the way you behave. Catherine talked about buildings becoming more efficient. I mean, just think about driving an electric vehicle. If you drive an electric vehicle for 100 miles, that might cost you $6 in electricity. If you drive an internal combustion engine vehicle for 100 miles, that might cost you $18 in gas. And so, when you're thinking about how do you transport, how do you operate your business, I think there are real values to the uptake.

And I think secondly, there's a potential cost of doing nothing. Catherine mentioned that Catherine, she mentioned it earlier on in terms of the Gen Z expectations, if you do nothing, there's a big potential cost and that's not just around talent, attraction and retention of the social impact and stakeholder management, but I think there's a potential for that cost to be manifested in real financial terms.

I was speaking with an economist this morning, and we mentioned that sort of three letter word, tax, in relation to well, what happens if you do nothing? Does that mean that you end up being taxed for emitting carbon? So, I think I think there's a very dangerous world that we're sort of going into. And there are two really important elements. What's the potential value that you could be gaining by embracing sustainability, and what are the potential costs that you are not avoiding if you do nothing? I think that's very important. So, yeah, long answer. But it's a very, very complicated area.

Robert McConnaughey (00:22:07:20 - 00:24:05:17)

No, and I appreciate your perspective on the long term. That again it's lots of these issues are big; they're not easy to work on. And so, if you only start on them when you're absolutely forced to, you may be, you know, trying to play a lot of catch up. One question that we actually get from our audience that we hear frequently is, "You know, hey, I just never get questions from my investors on ESG. So, does this stuff really matter?" And, you know, my perspective on that is that perhaps you're not framing it correctly. Now, some of the audience members might say, "Hey, it's great to hear you're doing organ replacement work, or hey, you're doing circular economy work. But, you know, we're just a retailer. We sell people stuff, and we want to be responsible in the world. But you know people aren't really focused on the fourth decimal point of our emissions." Our general answer to that is perhaps you're not thinking about defining your sustainability program in the right authentic material ways and playing offense with it. In describing why it's important to you, how do you stand out for your with your customers, with your stakeholders and coloring perhaps a little bit outside the lines if you view it just as no one asks me about the data, it's kind of like saying, Well, hey, no one really asks me about page 47 of my 10-K.

You need to go out and say, here's our strategy and why those numbers matter. It's the same thing here. So again, our general answer to that question is sustainability matters in some way and perhaps in different flavors to all companies, and it's contingent on the leaders within the company to embrace it and make it part of their strategy so that it is it is authentic and material on all levels.

So again, I'll throw it out to the panel. Any thoughts on that? Hey, I just I just don't get questions on it. How does it matter to me?

Katherine Collins (00:24:05:19 - 00:26:26:20)

Yeah, I can start on that, Robert. Maybe to illustrate your point with a little anecdote, one of our first meetings when I started my work at Putnam with the team was with a big life sciences company. And so we talked for a long time in preparation, thinking about where the fundamental strategy of the company intersected with key sustainability questions.

And we focused about half meaning talking about their product pipeline, how it was going to help effectiveness in developing solutions, ultimately improved patient outcomes. So, kind of the impact-oriented side of sustainability, we talked about half the meeting about their own team development and how they were developing the management processes, procedures, capacity to support this really tremendous growth that they anticipated over the long term for the company.

We got to the end and asked the CFO if there is any other major sustainability topic that he wanted to make sure we included, and he just rolled his eyes, exasperated. "That ESG stuff, I hate it. I can't stand that." And we said, "Well, this was our ESG meeting. Look, you like that?" And he busted out laughing.

And so, and his comment, I thought was really telling. The comment was like, "but you were asking about our business strategy." And he was genuinely perplexed. And so that showed me two things. One is that for a lot of folks and in a lot of settings, these still are two different conversations. And maybe we're not yet fully uniting ESG and core strategy, which again, is what I was getting to in this this age of refinement, kind of this next phase that Richard was alluding to as well.

I think these things are coming together in a much clearer way, but I don't really mind if it's not labeled ESG. I would much rather have a substantial conversation about strategy that touched on all the major ESG issues and have an ESG conversation. That's what that was-somehow separate, and off to the side, and lesser. And so, it is a real challenge for companies that are working on how to communicate this information effectively.

There are a lot of things that are required at this point and not optional to Richard's point, and I don't want to skip over that. That's a monumental effort, but that can be diminished in terms of its importance or complexity. But the strategic link to most investors, I think, is the part where it all kind of comes together in a way that is actionable and really usable. And so, we're seeing those ties more and more closely, but I'm not sure labels help us in this regard.

Robert McConnaughey (00:26:26:22 – 00:27:12:15)

I love your story. We've had the same experience here where we'll do discovery calls with the CEO and be talking about, you know, their innovation program to develop new products for their customers. And they'll be like, "Well, when are we getting to the ESG stuff?" I'm like, "You guys make engines, and there's a lot of questions about how those engines are going to evolve over time."

This is their sustainability part of the program, and they sort of expect it to be again, "Well, tell me about your emissions goals or a diversity ratio." Or very much that disclosure regime as opposed to something linked to strategy. So, I love that story and find it right on point. Katherine, Richard, or Catherine Sheehy any thoughts on this? How do we make it matter? How do we help investors know why this is important?

Richard Brasher (00:27:12:17 - 00:28:32:20)

I think, yeah, I would add something here as well. I think that's absolutely right. She mentioned sort of I think cutting through the noise or making sure that it was clear. I think there's been a huge amount of what I would classify as a sort of noise. Now, I started my career as an accountant, but being an auditor for over 20 years.

So, I sort of come to this topic with a very accounting head on me. And that accounting had sort of is asking, well, is this number the correct number? Is this a number that I can rely on that I can look at and say, I know where that comes from. But I think investors have gotten used to looking at 10-Ks and 10-Qs in the US.

They've been used to looking at financial statements in Europe, and they've been used to looking at numbers and saying, "Well, I know where those numbers come from, and I know I can rely on them, whether they're in a US GAAP, or whether in a different GAAP." And I think the sustainability world is kind of going in that direction. I don't think we're there yet. So, when it comes to it, does it matter? I think the answer is it definitely will matter, and it will matter more the clearer the data gets and the more reliance that can be placed upon the needs being disclosed.

Robert McConnaughey (00:28:32:22 - 00:28:46:03)

How do you think about balancing those more traditional, quantifiable ESG as largely negative externality reduction versus a sort of more holistic view of stakeholder care?

Katherine Collins (00:28:46:05 - 00:31:38:01)

Now, Robert, I'm glad you asked. So, one thing we haven't mentioned about the investment context at Putnam is that Putnam is an active investor, and that means that we're proactively choosing the individual securities that are going into our portfolios. That's a very different starting point than a passive investor that's starting with a big universe of an index and deciding what to screen out.

So, I love starting with the starting point-blank sheet of paper. What do you want to fill up your portfolio, as opposed to what do you want to subtract? It's a much more generative starting point for me. It's why I have stayed in active management my whole career. So that's important in terms of context. Because of that, for all our investment processes at Putnam, we're aiming for this holistic understanding of what is the way to make better decisions over time, it's to understand the companies you're investing in as completely as possible and to make more accurate assessments about the future value of that company. And so, we really do always start with a really simple question. Why does this company exist in the first place? What is this company doing that is of use and a value in the world, and what might that look like as we project into the future?

So, the exact same process applies when we think about sustainability. So, some of this work is very quantitative in nature, some of it's very qualitative, that's the nature seeing things for our sustainability considerations. But that idea of focusing on what's relevant and also taking that forward looking use, those are the two ingredients that we're looking for.

And I'll say with that in mind, it is really important, I think, to discern between a couple elements that have already come up in today's discussion. There is a fair amount of ESG work that is a little bit more compliance oriented. It's a little bit more focused on establishing that floor of responsibility, credibility or, you know, acceptable behavior.

We deal with compliance in every aspect of investing, and so does every operating company we deal with. We all want to be standing on a stronger, better floor. However, that's a very different function than the strategic functions we've all been alluding to, where you're looking at not just the floor of what's acceptable, but the sky of what's possible. And, you know, if you're an equity investor, that's what you wake up excited about in the morning. What's the greatest thing we could do, and how could we do it in the best possible way? So, I do think that when it comes to investment philosophy, if you're only looking at the risk-oriented parts of ESG, you tend to be looking down at the floor.

Again, I don't want to dismiss that. That's a really important piece of the puzzle. But if you're really looking for that strategic upside, for that long term value creation, kind of expanding that to this more expansive, sometimes more qualitative, but definitely more strategic, more Alpha-oriented within the investment world realm is really essential. We want to get that entire picture of the floor and the sky within our investment process.

Robert McConnaughey ((00:31:38:03 - 00:32:05:15)

One of the questions that we asked our audience was around naming conventions, where we saw basically half of our respondents say that they were actively working internally on the mix of ESG versus sustainability or other language. So maybe just, you know, turning to you all in terms of just language labeling, how you think about the term ESG versus sustainability or impact, or other terminology.

Catherine Sheehy (00:32:05:17 - 00:34:52:04)

You know, it's an important conversation, I'll admit. But I will confess to that. It's a little tiresome to me, and I'll explain why. So, I started this journey into whatever we want to call it today. Back in the 1990s, I worked in what we then called the socially responsible investing industry. It's different from what we're talking about today that we're in, although it's inclusive of that.

There were a fair number of religious investors who were doing at the time, what's called negative screening. That means screening out companies involved in industries like alcohol, tobacco, or gambling. And there was even a backlash at that time, I might say. Someone created a sin index. It didn't perform very well. And then there was another reaction from some conservative investors to other investors who are using the issue of nondiscrimination based on sexual orientation.

They wanted that data point to screen companies in that had that kind of inclusive policy. But some of the conservative investors that we were working with at the time they didn't screen the same way. And so, the preferred term that they used at the time was values-based investing, not to be confused with value-based investing.

And so, I think that’s still here, but it's been dropped because of the confusion. And then you use this term, impact investing. I actually started to hear about ESG in the late 1990s, that was coming from mainstream investors who saw the value of this content in making investment decisions. I think, as Katherine has so well stated, but they wanted to distinguish themselves from and distance themselves from the religious investors who are approaching these issues in a specific way.

So, what does all that mean? I mean, as far as I'm concerned, we could call it Ned. I mean, I don't care, or we call it just, you know, risk analysis and opportunity analysis for investing decisions, as you sort of talked about here. Personally, I do default to using the term sustainability, even though I know that that's confusing and off putting to some.

And I agree with Katherine that our language sometimes doesn't serve us. But when I use that term, I mean that vision of the world where there's enough for everyone forever. Because to me, that's what this word is about. But the backlash, just in terms of what we're doing here, hasn't changed our approach, for sure. We have actually discussed the language, we're tracking it. We're seeking advice from our expert advisors about how to navigate the world. Fundamentally, though, we're continuing to do all the things that we've been doing because it makes sense for our business, because it makes business sense.

Richard Brasher (00:34:52:06 - 00:36:07:05)

So, I completely agree with Catherine now that the whole discussion is the word you used was tiresome, I agree with that word. I think it's tiresome, and you could call it anything. Ned. Bob. George. It doesn't matter. I kind of consider it to be the new normal. It's going to become a little bit like if you run a business, you run a company, and you get those companies listed, and you have to issue a set of financial statements every year.

It's just going to become normal. Every company will issue a set of financial statements attached to those, which will end up being a lot of data or other things that those companies are doing. So, I think that's kind of the way from a reporting perspective. And I'll just add one other thought, which is that the sustainable the word sustainable has been used a lot, even in the non-sustainability world, over the last ten years.

Certainly, in my experience, I always used to say the old auditor in me would say a sustainable business is a business that's here tomorrow. And so, really, sustainability is kind of an extension of that. Sustainability means we're still going to be here writing tomorrow. If you don't get behind it, you might not be. And I think that's the rest.

Katherine Collins (00:36:07:07 - 00:38:08:17)

I would just add that I think the throughline I see in both Catherine and Richards remarks is the same throughline I see from my perspective, which is we are seeing, I'd say, more precision in terms of a lot of conversation as ESG became a kind of lazy shorthand for a whole lot of other things, you know, diversity of functions, a diversity of information, a diversity of viewpoints.

And we're getting a little more specific, again, a little more refined, which is, I think, a very positive development. One test that we use internally for our own communication at our research and in language is a really simple question like, “Does this need a new label?” This thing we're talking about or not, like, “Do we already have a home for this conversation?”

Like, don't call it ESG. If it's a governance issue, just say it's a governance issue. Let's talk about the issue. So maybe just to pull from the last couple of days of meetings internally, you know, we talked with a consumer company about the integrity of the quality of their ingredients. We talked with an industrial company about the importance of their employee incentive programs. We talked to the technology company about the security of their energy supply. We talked with a health care company about the importance of access to their new products. Those are the issues that I don't actually want to wrap them up in a more abstract label on them. And I find that this cuts through a lot of the polarization as well.

You know, if you ask any given CEO these days their views on climate policy or ESG disclosure, you're going to get a very ranting answer in either direction, any which direction. But if you ask something more precise, like, “Hey, your biggest facility flooded twice last year, what are you doing to mitigate that ongoing risk?”, or “I see your employee turnover has really improved the last couple of years, and that's not so intuitive. It's been a very competitive labor market. How are you doing that?” You know, that's a real conversation, and, you know, much more proximate, much more strategic, much more useful. And so, we're trying to get to that next layer down when you get to the substance as opposed to the labels.

Robert McConnaughey (00:38:08:19 - 00:39:12:12)

Yeah, and I like that. And I think the thing I think about this is that I don't want the industry to retreat from ESG because ESG is associated with, has built enemies. So, let's just avoid it because it has its set of enemies and call it something different to change the names to protect the innocent. I do think to your point, Katherine Collins, and what everybody's touched on is let's just talk specifically in plain English about what we're talking about and make it relevant to people if they associate ESG with some sort of just broad wokeness, let's cut through this to say, "No, we're really talking about this aspect of what you're doing", and I think that helps to change the temperature in the room as to why this is relevant and important to me. So again, I appreciate the spectrum of answers here.

Coming down the homestretch here. You know, Catherine and Richard, you know, how do you aim to stand out from your peers? You've touched on aspects of this, but how do you aim to stand out when it comes to ESG and sustainability? And maybe more importantly, where are you on that journey today?

Richard Brasher (00:39:12:14 - 00:40:24:09)

I mentioned it earlier on, and I mentioned again that our business, the LKQ Corporation, was founded 25 years or so ago. Out of that philosophy of turning what is effectively scrap into really, really useful things that humankind needs and wants every day, 300 acquisitions later, just over 300 acquisitions later, we're still doing the same thing. So, if you ever wondered where your vehicle goes at the end of its life, well, now you know, it's kind of interesting to me looking at it and looking at where we are today.

We talked so much about the circular economy. Quite a lot of the circular economy is partially circular. So, things get mixed, things get perhaps recycled, mixed with virgin materials or new materials. For us, the circular economy of being recyclers is just in our DNA. I think that sort of I think the point is not necessarily how do we make that stand out, it's how we just tell that story, because that is the story to tell. I think that in itself will make us stand out.

Robert McConnaughey (00:40:24:15 - 00:40:25:22)

Catherine Sheehy?

Catherine Sheehy (00:40:25:24 - 00:42:58:15)

You know, in terms of standing out, I think we've touched on a couple things that say some of this is going to be table stakes. And I really think that's important, and I applaud that. But where I'd like to see us really stand out from our peers and we're on this journey is where the nexus issue is, where the E and the S, even the financial issues converge.

So, you know, I've heard some people call this a handprint that a net-positive contribution organization can make. And the things that I'm talking about, our actions that benefit our patients, that help us attract and retain amazing, diverse talent that benefits our communities around us and beyond, and even touch on fundamentals like cost. And that's hard that, that kind of analysis is complex. It's not short term, it's long term, but it's really exciting. And I'll give one example. In June of last year, we opened up a site, net zero cold storage, good manufacturing practice cold storage warehouse for our pharmaceuticals so that we can store inventory. We have a commitment to store two years of inventory to ensure that no patient gets left behind in accessing the medicines and therapies we offer.

That's extraordinary by itself. But this site net zero building has solar. We have the geo exchange wells underneath to manage our energy use. We have backup battery storage, Tesla MEGAPACK on site. I mean it's really a feat, so it touches that that commitment to patients. It is super energy efficient. It's right next door to our day care on site. So, we are absolutely committed to safety of operations and inside, you know, fully electronic, all sorts of things. And so that affects or, you know, your need for labor to support a building of this size. And also, you know, we're anticipating that it also reduces potential hazards around workplace safety and health issues because you're just managing it differently.

And so that's what I get really super excited about. It's the combination of those things. And how do we measure that? How do we talk about it? I think there's you know, the language isn't really kind of there for us yet on all those things. But that's, I think, where I think companies can make a difference.

Robert McConnaughey (00:42:58:17 - 00:44:35:19)

Some of the most gratifying work that we do touches on the story that you just told Catherine about, you know, helping people to say, "What are you doing for your patients in this case? What are you doing for customers? Why is your turnover going down?" to Katherine Collins's earlier story and pulling out those things that are important and real that oftentimes got left on the cutting room floor because they didn't fit neatly into an ESG disclosure box.

We try to pull that out. Part of what we've tried to add around, you know, our work, is communicating in ways in addition to traditional data tables. How do you, you know, write a compelling story? How do you condense that down to what really is material to your core audience and things that, you know, we often talk about it as, what could you explain to, you know, an 11-year-old niece or nephew sitting at the dining room table as to why our work is important?

And if it doesn't pass that test, you know, people, ultimately the non ESG geeks in the room, aren't going to pay attention and read it anyway. So, we need to again simplify, make it really clear, and call out that broader stakeholder care. So, I get I appreciate the stories that we're told that bring that to light.

So again, wrapping it all up, Katherine Collins, just as a long-time student of success in this field, you know, what do you see as those key ingredients–the characteristics–key actions of the companies that have driven the most improvement over time–not necessarily the ones that are at the top, but the ones that have seen the biggest delta in their work. What are those key characteristics that you would recommend to the audience?

Katherine Collins (00:44:35:21 - 00:47:56:04)

Yeah, I think if I think about what extraordinary looks like to us, I guess there are a few points of reference, and I'm so glad we have two great examples here with Catherine and Richard of two totally different business models and how this shows up differently in different settings than it should. So that idea of all this work being context-specific context relevant, I think, has really shone through today. From Putnam's standpoint, we use a framework for identifying leadership that is really matter of fact, but I think it can apply across a lot of different settings. You can look for activity that's again focused on relevant material issues. That's proactive in nature, not just checking the box, but doing something really strategically interesting and additive, something that has influence across the company in terms of its results and effectiveness.

But ideally, beyond the company's borders, extending outwards to customers, employees, and maybe backwards into supply networks, and then effective, you know, does it actually work? Is it is it producing the benefit we think? It is a very straightforward kind of qualitative framework, but easy to plug in both quantitative and qualitative analysis to answer those questions. And when I translate that to more general conversations with companies, it's all the descriptors you would think, you know, alignment, authenticity, go hand in hand. If I'm talking to a company that is all about risk management, say a big financial company, and none of this shows up in any of their risk commentary, like, that's a little weird. If I'm talking to a company that really prides itself on its engineering excellence and this isn't somehow showing up within their discussion of their engineer, that's a little weird.

So, looking for the existing strengths in the company and seeing how this is influencing or relevant to those strengths is really key. And then the second component we've touched on a lot today, which is the idea of, you know, is it serious, is it strategic, and is it candid? Well, that's what we're hearing and observing over time.

I'll give an example here. A very large tech company had a very serious commitment to expanding diversity amongst their technical engineering team, and they were monitoring it over a multi-year period, really crucial to the company's long-term success that this that this capacity continue to improve and expand at the company. They made some really great progress, but from a pretty low base. And what stood out to me in their reporting that year, they noted the progress, but they could have easily gotten a headline and said, "Look this metric has doubled," and they didn't. They chose to say, "Here's the metric, here's what happened. It's still unacceptably low," which was true. And so, you know, I do look a lot at how companies choose to present the information.

It's fine to put a positive wrapper around things, but there's a difference between a positive wrapper and a deceptive wrapper. And any company that is extra candid about the challenges, we kind of give extra points to. You know, there's no use pretending that this isn't hard. And so, I really extra appreciate the companies who are candid about the challenges and think it helps investors make better decisions.

And just as importantly, it sort of sets a standard for candor amongst your peers, competitors, customers, and suppliers. You know, I think the more that this can be a real conversation and not an exercise in trying to turn a strategic conversation into a marketing conversation, the better off we'll all be.

Robert McConnaughey (00:47:56:06 - 00:49:09:10)

That's a great place to wrap it up. I think, you know, just trying to summarize a lot of what we heard that came out of that at the end is, you know, getting that honest baseline of data but harnessing it in a clear way that attaches to real strategy, to issues that matter to whatever the audience and stakeholders we're talking about, whether that be shareholders, employees, customers, suppliers, or regulators. How do we use that baseline-all the work that goes into some of the nuts and bolts of ESG-to make it relevant, real? We think that when that's done correctly, it's a revelation to people that it is truly powerful, but it does see a hierarchy, and we think that our data suggests that it's only going to grow. So again, I really want to thank each of you on the panel for taking the time to join us today.

I also really want to thank our audience. I know everybody in your world is incredibly busy, but I appreciate the opportunity to share our thoughts and findings with you. We didn't have the time to hit all the questions that were received during registration. We will be sending out both a summary of this event and some additional responses to specific questions to all our attendees.

So, thank you all once again. Until next time, that's The Big So What™.

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