Investment Advisory Committee: Summary minutes

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Attendees:

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Seb Beloe (Head of Research)
Tim Dieppe (Fund Co-Manager)
Ted Franks (Fund Co-Manager)
George Latham (Managing Partner)
Geoff Hall (Chair)
Clare Brook (Adviser)
Kelly Clark (Adviser)
Phineas Glover (Advisor)
David Lloyd-Owen (Adviser)
Nick Robins (Adviser)

Apologies:

Ebba Schmidt (Adviser)

Changes to the Investment Advisory Committee

There have been some changes to the composition of the advisory committee over the past four months. Ebba Schmidt who has served on the Committee for the past three years has very sadly had to step down from the committee due to ill-health. We want to formally record our gratitude to Ebba whose leadership on a wide range of sustainability investment issues has been outstanding. We have been extremely privileged to have had her serve on our committee.

George Latham then introduced Phineas Glover who joined the committee for his first meeting. Phineas is currently a senior advisor at the Investment Forum which was set up to 'contribute to long-term investment performance by promoting cultural change and enhancing shareholder stewardship' in the UK. Phineas joined the Forum in 2014 and was previously a policy advisor at the Association of British Insurers.

George also provided a brief update on the WHEB business highlighting a series of awards that the team has recently won, including achieving a five star rating with 3D Investing – one of only four that received this rating out of 140 funds assessed. The business is also now managing over £110m through the FP WHEB Sustainability Fund and a new segregated mandate, which was awarded to WHEB by Menhaden, a recently listed investment trust focused on investing in the green economy.

Changes to the investment portfolio

The committee reviewed the additions to and sales from the portfolio over the past four months, focusing in particular on whether new holdings represented suitable additions to the fund.

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There have been two additions to the portfolio since the last meeting, both of which are in the Cleaner Energy theme. We have become much more optimistic about the prospects for renewable energy and in particular for solar power. The team completed a theme review over the Summer in which we concluded that solar can expect significant market growth over the next decade at least. With growing scale, more efficient practices and better technology, costs of solar will continue to come down making the technology competitive with all other forms of electricity generation in the coming years in many parts of the world. We have a particular preference for companies with activity in developing solar projects across diverse geographical locations.

Sunpower is a US-based manufacturer of solar photovoltaic modules.[1] The company specialises in high efficiency modules which are used in both ground and roof-mounted applications. The company is also active in project development at utility and commercial scale. Sunpower is well diversified geographically with a strong business in both developed and emerging markets.

[1] For more information on Sunpower see http://us.sunpower.com/

WHEB is participating in efforts by the investment industry to help the UK government develop a more reliable and predictable regulatory environment for… renewable[s].

Hannon Armstrong Sustainable Infrastructure is a speciality finance company that provides debt and equity financing for sustainable infrastructure projects including renewable energy and energy efficiency infrastructure.[2] Their clients include local and state governments as well as private businesses in the US.

Sales from the funds over the period included Constellium (Sustainable Transport), Infinis (Cleaner Energy) and Trimble Navigation with all three being sold because of reduced conviction. The Committee was interested to hear of the increased conviction in solar, but was disappointed about the sale of Infinis a UK-based wind and landfill gas operator. The team explained that Infinis had suffered because of dramatic changes in the level of support for renewable energy in the UK, particularly onshore wind. The Committee was pleased to hear that WHEB is participating in efforts by the investment industry to help the UK government develop a more reliable and predictable regulatory environment for investment in UK-based renewable businesses and projects.

The Committee were also keen to see a full break-down of the fund by investment theme and sub-theme and were interested to hear how the fund is increasing its exposure to cleaner energy and to emission reductions from road vehicles.

What should 'fossil free investing' mean?

Given the size of the oil and gas sector in the modern economy, a high proportion of listed businesses have significant exposure to the fossil fuel industry.

There is substantial and fast growing interest among a wide variety of investors in avoiding investing in fossil fuel-related businesses. This trend is driven both by the commercial risks that are expected to confront these industries and by ethical issues associated with the contribution they make to climate change. Many of these investors are also interested in increasing their investments in funds and companies providing solutions to the problems of climate change.

WHEB is both a supporter and beneficiary of these trends and wanted to get the committee's views on where boundaries should lie on what constitutes a fossil free fund. The complexity in this question comes with the wide range of businesses that are not directly involved in extracting and selling fossil fuels, but have some involvement in the value chain of these industries. Given the size of the oil and gas sector in the modern economy, a surprising number of listed businesses have significant exposure to the fossil fuel industry. Furthermore there are other businesses that while clearly 'in transition' to a focus on lower carbon activities, still have some legacy exposure to fossil fuels.

Committee members stressed the importance of clear communication as to where WHEB draws the line [on fossil fuel exposure].

The committee was sympathetic to this issue, agreeing that being entirely fossil free is not a practical proposition in today's economy which is so highly dependent on fossil fuels. Several committee members felt that the 'intentionality' and motivation to invest in low carbon solutions was central, and that it was also important to guard against an overly strict definition that would lead to very narrowly focused funds. 'Being too purist and reductionist will not work' was the view of one member.

Having said that, committee members also believed that it was important to ensure that direct exposure to fossil fuel production should be essentially zero. Furthermore, businesses with exposure to fossil fuel activities should be able to demonstrate that their activities either mitigate the negative impacts of fossil fuel activity or, where activities aren't focused on mitigating negative impacts, that they are a small part of their overall business and that they are on a clear trajectory to reducing this exposure over time.

Above all, committee members stressed the importance of clear communication as to where WHEB draws the line and that this should as far as possible be based on sound science and objective analysis. Given the lack of informed debate in this area, committee members suggested that WHEB might want to convene an expert group to help agree some clear parameters on what 'fossil free' should mean in practice.

[2] For more information about Hannon Armstrong see http://www.bloomberg.com/news/videos/2015-07-17/efficiency-is-impactful-way-to-reduce-emissions-eckel

Large asset owners are increasingly asking for asset managers to demonstrate how they take environmental, social and governance (ESG) issues into account.

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What is the future for ESG investing?

Asset owners, in particular, large asset owners are increasingly asking for asset managers to demonstrate how they take environmental, social and governance (ESG) issues into account in their investment decisions.[3] On the surface this is clearly a very welcome development and should encourage asset managers to do a better job at addressing these issues. However, in practice, many asset owners use company ESG 'scores' that are generated by research providers as a key tool in measuring how and whether asset managers take account of ESG in their investment process.

We summarised these developments for the Advisory Committee and during the discussion the following points were raised:

- Most managers that claim to do integrated analysis are not, in the view of the Committee, undertaking sophisticated analysis but simply 'ticking a box on ESG integration'.
- A fully integrated approach that uses ESG analysis as an input to the investment process may be inadvertently penalised because ESG issues are not as 'visible' because they are not scored separately. Some SRI labels actively penalise approaches that do not have ESG issues measured separately.
- ESG analysis in isolation is fundamentally flawed as an approach, because the products and services that are produced by the business are typically excluded from this analysis, which instead focuses almost entirely on the company's own policies and processes.
- Furthermore, ESG ratings are of highly variable quality with company research often out of date and undertaken by inexperienced analysts with little agreement on what constitutes the basis for analysis between firms.
- Ultimately ESG issues are just one part of the picture and assessing the total 'impact' of a company – including an assessment of product impact – is the critical issue. "ESG issues are just the ingredients, impact is the recipe" as one member put it.

The Committee suggested that WHEB organise a seminar with leading practitioners of ESG integration and impact investing to better articulate the limitations and challenges of ESG integration in investment decision-making.

[3] For more information about Hannon Armstrong see http://www.bloomberg.com/news/videos/2015-07-17/efficiency-is-impactful-way-to-reduce-emissions-eckel

Investment Advisory Committee Members

Clare Brook:
CEO, Blue Marine Foundation

Nick Robins:
Co-Director of a UNEP Inquiry into the Design of a Sustainable Financial System

Geoff Hall:
Chairman of WHEB Asset Management. Former CIO at Allianz Insurance Plc

Phineas Glover:
Senior Adviser, The Investor Forum, Investment Association

Kelly Clark:
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David Lloyd Owen:
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