

***UKSIF Consultation Lunch:
Influencing the UK operating environment for investment and finance
in the aftermath of the current crisis***

Held on Tuesday 16 December 2008 chaired by UKSIF Chair Steve Waygood and kindly hosted by UKSIF Board Member Helen Wildsmith at CCLA.

Attendees

Steve	Waygood (Chair)	Aviva Investors
Sagarika	Chatterjee	F&C
Melissa	Epperly	Goldman Sachs
Jane	Goodland	Watson Wyatt
Aled	Jones	PPF
My-Linh	Ngo	Henderson
Nick	Robbins	HSBC
David	Russell	USS
Penny	Shepherd	UKSIF
Richard	Stathers	Schroders
Rory	Sullivan	Insight
Helen	Wildsmith	CCLA
Clarence	Yang	BGI

All participants attended in a personal capacity and organisational affiliations are given for information only. There were some additional late cancellations due to sickness. The meeting was held under the Chatham House rule but all attendees have given permission for their names to be listed.

Purpose

The purpose of the meeting was to discuss and comment on:

- UKSIF plans for **influencing financial services regulation and public policy** in 2009
- **Preliminary research** that UKSIF has been doing in the previous few months to support this

This work is being undertaken in support of UKSIF's strategic aim to "**Ensure that the Operating Environment for the UK Finance Sector encourages and enables leadership in Sustainable and Responsible Finance**". It is complementary to other UKSIF activities such as the UKSIF information clearing house, the UKSIF Analyst Seminar Programme, the Sustainable Pensions Project and National Ethical Investment Week that support of the organisation's other aims to "Grow Customer Demand" and "Ensure Access to High Quality Supply".

The research was undertaken by UKSIF's temporary research assistant Camila Yamahaki, whose work has been kindly funded by Aviva Investors, together with pro bono support from Helen Wildsmith in a personal capacity as part of her PhD research.

Steve introduced the proceedings by highlighting that the topic for discussion was not the current crisis but "how to fix the next problem".

The diagram "Multi-level analysis of the impediments to SRI" in "Identifying impediments to SRI in Europe: a review of the practitioner and academic literature" (Juravle & Lewis 2008, in Business Ethics: A European Review, 17:3, Page 303) was used as a stimulus to thinking but it was highlighted that the topic was the much broader issue of a sustainable financial system rather than "SRI".

The list below records points made in the discussion. In the spirit of brainstorming, participants were encouraged to build on the contribution of others rather than to identify where they disagreed. The points noted therefore do not necessarily have the unanimous support of those present.

It was agreed that the discussion would be written up for circulation to participants as a “menu” of items that could be taken forward. This aims both to stimulate continuing discussion and to inform the further development of UKSIF’s plans.

Points Made

Contributions to the discussion have been clustered by topic. They included:

“Framing” Messages

- **The future will not be like the past:** The system/market will be radically different in 10-20 years time. The market is a reflection of society. Societal values are changing. Ed Milliband has called for a social movement around climate change. Pension system will be structurally different in 20 years time due to DC; individual pots more important over the long term; changes in asset allocation that are income related not risk related; and need to build LTRI into these changes.
- Our agenda offers an **opportunity to rehabilitate the financial sector** and address sustainable development eg. “we have moved a long way but most finance still does not support sustainable development”; “yes, the finance sector needs to change its ways; we have good ideas linking decent returns with social objectives”; “now is an opportunity to enable asset prices to reflect climate change”.

Key Problems to be Addressed

- **Dominant values and norms within the industry and within society:** This includes the values and norms affecting individual behaviour at work.
- **Short-termism:** Danger that the long-termism for pension funds means LDI = derivatives and swaps – this is too far from the real economy but the industry may come up with more of these instruments in response. Problems with valuation models and short term performance reviews. Focus on costs not benefits of RI.
- **Conflicts of interest:** broker conflicts of interest in relation to corporate access; insurance company conflicts of interest eg re corporate partnerships.

Key Solutions to be Championed

- **Leadership, ownership and accountability:** license to operate, values, universal owners, cultural issues (need more “brave” leaders willing to step outside the norm), better informed and educated trustees, engaged beneficiaries, insurance companies behaving as asset owners; potential to create replacement “investment beliefs”; stronger demands and better success measures from owners; shifting the focus from trading to owning; techniques to motivate cultural change and improved quality of ownership; the potential for major asset owners with passive investment strategies to be the driver for addressing systemic risk; in the long term, close the accountability loop so that transparency drives change – the pensions disclosure regulation did not achieve this but PRI learned from that experience and did.
- **Transparency:** Address information asymmetries; mandatory disclosure on climate change in listing rules won’t be resisted.
- **Improved incentives in the supply chain:** better KPIs; measures of how well asset managers are improving companies; greater focus on what the short term focus costs in the long term; taking account of the impact of new regulation; board directors could have ESG as part of their remuneration; owners of companies could put pressure on corporate investor relations teams (facilitated by PRI or UKSIF).

Tactics and Leverage

- Restrict ourselves to **two major “battlegrounds”** eg. (a) climate change and (b) the pensions review. Climate change integration into the markets is very winnable. Pensions are our territory.
- Tactical opportunities for intervention include (1) 1-2 big asks to the **G20** (but there is a risk that our asks may get lost there) (2) Investment Governance Group / Newly revised **Myners Principles** (3) **WWF’s campaign** to get the middle classes concerned about pensions and climate change (4) connecting with the **ABI** agenda and feeding suggested key questions to them (5) encouraging active ownership by **insurance companies**.
- Some practitioners can have most influence acting through the **collective power** of a forum like UKSIF. Look at where we might want to make **alliances** eg. Tomorrow’s Company.
- Be loud but be smart. Have the courage of our convictions and **speak loudly** – but also pick interventions that have **the most potential impact for the least cost**. Establish our relevance to

the credit crunch and get involved in substantial debates but at the same time decide the appropriate level of involvement – framing the debate or detailed nitty-gritty? Consider whether we are likely to be able to impact regulators or whether our effects would be more effective elsewhere.

- In the long term, need to build solid demand through financial literacy but **currently accept the case for tougher regulation** - beneficiary understanding would be better but is too long term.

Further Actions Identified

- An investor focus on **supporting companies to survive the downturn with integrity** (eg. outsourcing, retraining, impacts on supply chains eg. CDP supply chain projects); supporting and championing leaders rather than just challenging laggards
- Focus on outcomes as well as process – need a **clearer vision of a sustainable economy** that goes beyond climate change
- A short **paper on finance for sustainable development** that deconstructs the City based on NGO critiques of FDI but addressing allocation of capital by portfolio investors. Include the lack of a UK development bank. “NGOs are doing a bad job of deconstructing the City but a good job of deconstructing corporate activity”.
- Explore the proposal that financial institutions should be required to make a **market risk forecast**, looking externally not internally, and report what they are doing to address the risks identified. Would effective implementation of the enhanced business review achieve this or is it a distinct regulatory proposal?
- Promote debate on **what are valid financial instruments** – when do financial instruments that support the operation of the real economy tip over into supporting a counter-productive “casino economy”?

Written up by Penny Shepherd
January 2009