

# ESG Research Australia Awards 2011

Recognising excellence in ESG research and service



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### WINNING ESG RESEARCH AND SERVICE PROVIDERS

#### Best piece of ESG research by an individual analyst or team

*Equity Strategy: Introducing the Goldman Sachs and Partners Australia Structural Leaders Framework*  
Hamish Tadgell and Jien Goh; Goldman Sachs

#### Highly commended

*Australian Strategy: RBS ESG – Qantas*  
Alva Devoy, Elliot Crane, Mark Williams and Michael Newbold; RBS

#### Best ESG broking firm as voted by investment managers

Citi

# Introduction

The ESG Research Australia Research Awards were created to recognise excellence in ESG research. There are two award categories:

- Best piece of ESG research by an analyst or team
- Best broker service

## **Best piece of ESG research by an analyst or team award**

ESG Research Australia members were invited to submit ESG research produced by brokers in 2010 that they believed added value to their investment processes. A judging panel was formed from a sub-group of ESG Research Australia signatories from the superannuation and funds management industry. This judging panel then assessed the research against:

- Rigour
- Originality
- Reliability
- Integration and useability

More detail on the judging criteria is available on page 9.

## **Best broker service award**

ESG Research Australia members also voted on the award for the best broker service. This was voted on by investment managers and superannuation funds that directly manage Australian equities investments.

Together, the two awards are designed to recognise and promote the important role that brokers can play in identifying and assessing the impact of ESG matters on investments and investment returns.

# Summary

ESG considerations have steadily been gaining traction in the investment community over a number of years and 2010 was no exception. There is genuine interest from investors on the integration of ESG considerations into investment processes. High quality ESG research is vital for investment managers, because best practice approach to ESG integration is becoming an increasingly important factor driving the allocation of capital from investors. To successfully implement ESG considerations into investment processes, investment managers need high quality ESG research which is on par with more traditional financial research.

ESG considerations have steadily been gaining traction in the investment community over a number of years and 2010 was no exception. There is genuine interest from investors on the integration of ESG considerations into investment processes. High quality ESG research is vital for investment managers, because best practice approach to ESG integration is becoming an increasingly important factor driving the allocation of capital from investors. To successfully implement ESG considerations into investment processes, investment managers need high quality ESG research which is on par with more traditional financial research.

The second year of ESG Research Australia saw a substantial improvement in the quality and quantity of ESG research produced by the sell side for the Australian market. In 2010, Colonial First State Global Asset Management (CFSGAM) was pleased to again chair the ESG Research Australia Awards judging panel. These awards were created to encourage brokers to provide quality ESG research and recognise excellence in this area.

The range of ESG research that was shortlisted for judging clearly demonstrated that there isn't a one-size-fits-all approach to ESG research, with a diverse range of papers each having their own strengths and weaknesses. Some research lent itself to be easily integrated, while other research papers would prove challenging, if not impossible, to be integrated into an investment process and were more educational in nature. Some papers were company or sector specific, while others took a

broad thematic approach. Some research examined micro factors, while others took a macro view.

The variety of the research should not be considered negatively. The difference in approach is reflective of the fact that the end users of the research will always have differing needs and utilise the information in different ways. Investment managers are becoming increasingly sophisticated in their information requirements and are wanting research that is most beneficial to their own investment style. There is little consensus in what constitutes superior ESG research. While this presents a challenge to ESG research providers who clearly cannot be all things to all people, it is reflective of the reality that all investment managers take a slightly different approach to ESG integration reflective of the different investment processes.

The differing approach to ESG research in each of the papers made selecting an outright winner challenging. Direct comparisons were not always possible due to the differing approach, aims and outcomes of the research. Further, individual preferences of members on the judging panel was the cause of much debate. Some members felt that integration into the investment process was the most important factor for ESG research, while others favoured originality. As was the case last year, useability was found to often be at odds with originality. Some papers struck a balance between the two, being neither highly original nor highly useable, but good all-rounders.

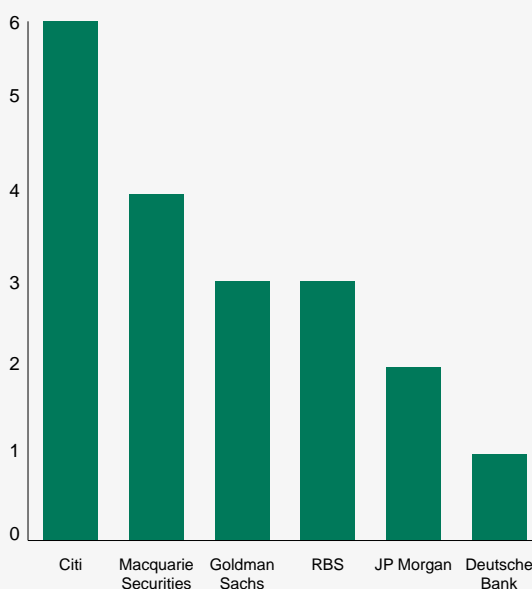
The other two judgement criteria – rigour and reliability – were evident to a high degree in all the shortlisted papers. However, question marks were raised on the reliability of using third party external data which was opaque in its process. Similarly, summarising previously-produced research also caused concerns around reliability.

The judging panel felt that there was a noticeable improvement in the research paper's alignment to investment outcomes, with improved integration between the research and the investment case. However, the panel noted that there is still room for much improvement in this area. The panel felt that there is still a reluctance from the broker community to make a call on the materiality of issues due to potential reputation risk if the call turns out to be incorrect. The judging panel recognised that, while integration is perhaps the most important part of ESG research, it is also the hardest part to get right. Where papers could not be easily integrated, there was still value for the papers to be used in company engagement on ESG issues.

The panel felt that the shortlisted papers' originality was down on last year. This may be as a result of an increased focus on useability and integration, as one typically comes at the expense of the other. Another factor contributing to a lack of originality may be that it is becoming increasingly difficult to come up with new ideas. As research gets more sophisticated and more topics and techniques are used, truly original or groundbreaking pieces will be increasingly difficult to come by. The panel felt that some research was too Australian-centric and didn't sufficiently consider broader, macro and global considerations. Further, there was insufficient consideration of the competitive dimensions of ESG and an absence of strategy pieces. However, the panel felt the overall quality of research was improving and there was an increasing focus on integration and the investment outcome.

The increase in the number of brokers producing ESG research was pleasing, going from two brokers in 2008 to six in 2010, including 'non-traditional' ESG brokers. However, there still remains major broker houses that do not produce ESG research. The number of nominated research pieces from each of the relevant broker houses is shown in the chart below.

Chart 1: Number of nominated research papers by broker



# The nomination process

Members of ESG Research Australia submitted their three most favoured ESG research pieces from a total of six brokers. A total of 19 papers were nominated and a list of these papers is included on page 11. From these papers a shortlist of nine papers, shown below, were submitted for the Best piece of ESG research by an individual analyst or team award.

## Shortlisted research

| Author(s)   | Broker firm          | Research title  |
|---|----------------------|---|
| Elaine Prior & Felipe Faria                                   | Citi                 | ESG: ASX100 Remuneration analysis. Analyzing Incentive Structures; Seeking Remuneration Anomalies   |
| Elaine Prior & Felipe Faria                                   | Citi                 | Safety Spotlight: ASX 100 Companies & More Injury & Fatalities Data FY05 to FY10 Presented & Interpreted  |
| Elaine Prior, Felipe Faria, Craig Woolford & Michael Goltsman | Citi                 | ESG: ASX-Listed Retailers – Risk Management Labour & Human Rights in International Supply Chains  |
| Andrew Gray   | Goldman Sachs        | Carbon Disclosure Project 2010. ASX100 Companies Are Showing A Strategic And Financially Oriented Climate Change Response Against An Uncertain Policy Backdrop. |
| Hamish Tadgell & Jien Goh                                     | Goldman Sachs        | Equity strategy: Introducing the GS&PA Structural Leaders Framework   |
| Sam Ferraro, Matthew Ross, Alain Lebel & Alistaire Paterson   | Goldman Sachs        | Corporate Governance and Agency Costs: Does Firm Complexity Matter  |
| Garry Sherrif, Benjamin Wilson & Jason Steed                  | JP Morgan            | ESG and the Energy sector: Water concerns: QLD Coal Seam Gas Developments   |
| Aimee Kaye & Cindy Dowling                                    | Macquarie Securities | ESG The insurance climate   |
| Alva DeVoy, Elliott Crane, Mark Williams & Michael Newbold    | RBS                  | Australia strategy: RBS ESG – Qantas  |

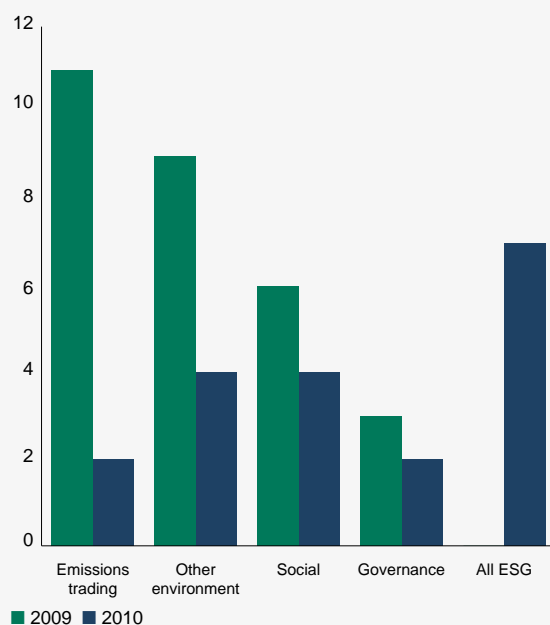
# Research topics

As shown in the chart below, the types of research were markedly different from the previous year. This reflects the dynamic nature of ESG research, the changing demands from clients and the macro environment which drives the nature of the research.

The number of research papers on emissions trading, which featured heavily in 2009, fell sharply from eleven to two papers as it fell off the political agenda. Conversely, the number of papers covering the spectrum of all ESG lifted from zero in 2009, to seven papers in 2010, reflecting the broadening consideration of ESG issues that brokers are providing.

There were 29 papers submitted in 2009 compared to 19 in 2010, so proportionally, papers covering the topics of 'Other environment', 'Social' and 'Governance' remained largely in line with the previous year.

Chart 2: Types of research submitted



## Research topics for future consideration

The judging panel would recommend an increase in the following areas of research to help enhance the breadth and usefulness of ESG research:

- consumer and public health issues
- supply chain stewardship issues
- related party transactions and independence of the Board
- consumer debts for the financial services and retail sector
- executive remuneration
- board quality
- geo-political and security risk
- macro and strategy pieces
- global consideration of Australian companies, and
- increased consideration of externalities

## *Equity Strategy: Introducing the Goldman Sachs and Partners Australia Structural Leaders Framework*

Hamish Tadgell and Jien Goh; Goldman Sachs

### **Synopsis**

The Goldman Sachs and Partners Australia Structural Leaders Framework paper identifies Australian and New Zealand companies that Goldman Sachs believes are well positioned to sustain competitive advantage and superior return on capital over the next three to five years and beyond.

The cornerstones of the framework, which form the three pillars of analysis for scoring companies, comprise of: return on capital, industry positioning and ESG management. The 26 companies that rank above median on all three pillars of the framework are considered Structural Leaders. From this list, 13 Focus List stocks are identified. These are the Structural Leaders that Goldman Sachs believe are best placed to sustain superior returns based on their competitive positioning and management of ESG issues. The framework was designed to assist investors by incorporating ESG considerations in an investment analysis, given the linkage between ESG factors, returns and share price performance.

### **Overview**

This paper was praised as the most easily integrated into an investment process, although some committee members felt it lacked originality. However Goldman Sachs was acknowledged for having three people undertaking ESG research which was seen to encourage originality within the team. Integration of ESG is perhaps the most challenging aspect of ESG research, and the useability of this research in an investment process was this paper's key strength and led to the paper winning the award.

### **Judge's comments**

"The paper illustrates that if ESG factors are integrated it does create alpha"

"Simply highlights what is most expensive, rather than providing insight into ESG risks"

"Integration has been prioritised above all else"

"Without question this paper is the most able to be integrated"

"This paper wins on integration and useability"

# Highly commended

## *Australian Strategy: RBS ESG – Qantas*

Alva DeVoy, Elliot Crane, Mark Williams and Michael Newbold; RBS

### **Synopsis**

RBS evaluated Qantas against its key performance indicators (KPIs) for ESG. The paper measured Qantas' ability to reduce emissions, energy and water use and the opportunities for the company to reduce its greenhouse gas footprint through the introduction of new aircraft and sustainable aviation fuel. RBS screened Qantas on its social, governance and viability KPIs, and commended the company on significant year-on-year reductions in its lost time injury frequency rate. RBS also examined Qantas on employee satisfaction and other viability KPIs such as on-time arrivals trends and the long-term business model sustainability. The paper concluded that Qantas has displayed excellent ability to both monitor and act on ESG factors.

### **Overview**

This paper was considered by the judging panel as being the best all-rounder, striking a good balance between useability and originality. The judging panel felt the paper made a genuine attempt to integrate ESG considerations into the investment process. However, it was felt that the paper could have taken into account more ESG externalities and macro factors, such as fuel prices and international industry comparisons. The paper's focus on a single company was commended for its originality and refreshing approach.

### **Judge's comments**

"The best all rounder."

"It was all micro considerations, with no macro or external factors considered"

"This paper has at least tried to integrate ESG into decision making"

"As a global business, global comparisons with other airlines would have been useful"

"Top score on originality taking a single company-specific view"

# Best ESG broking firm award

## Summary

Best ESG Broking Firm as voted by investment managers is awarded by ESG Research Australia to the broking firm rated highest for overall service and provision of ESG research on Australian equities.

This award is based on investment managers' opinions as to which broking firm is providing, in their view, the most valuable ESG research and support. Different investment managers will have different views on what is most valuable, and so this award recognises the variety of ways in which ESG can be incorporated into the investment process. The award is intentionally subjective in nature as it reflects investment managers' opinions of value and service in ESG.

The award encapsulates the views of all investment managers that are ESG Research Australia members. The broad and representative cross-section of investment managers will help to achieve a key aim of this award, which is to acknowledge the broking firm with the best ESG capabilities and service.

## Winning broking firm

Citi was again voted 'Best Broking Firm as Voted by Investment Managers'. Citi had six papers nominated for the 'Best piece of ESG research by an analyst or team award', with three papers making the final shortlist. It is also pleasing that research from six brokers were nominated, up from two brokers two years ago.

Elaine Prior from Citi once again got particular recognition from the judging panel for her work in the field of ESG research. The paper 'Safety Spotlight: ASX 100 companies and more injury and fatalities data FY05 to FY10 presented and interpreted', written by Elaine Prior and Felipe Faria was highly regarded by the judging panel.

## Judges' comments

"Elaine undertakes very thorough groundwork"

"Elaine does great work although it can be difficult to integrate"

"Citi understands the subtleties of ESG research more than any other"

"A lot of detail on the topic, but relevance and implications are not clear"

"Elaine's work has strong education value"

# Award criteria

The following factors were considered by the ESG Research Australia judging panel in assessing research produced by the sell side for their clients and asset owners for the award of 'Best piece of ESG research by an analyst or team'.

## Integration and useability

The panel looked to test the ease with which analysts could incorporate the research into their stock analysis by gauging its practicality and whether there is a framework underlying the analysis. Ideally, the research should contribute to the further integration of ESG into investment analysis. The panel looked for:

- analysis of ESG impacts on company-specific investment value drivers
- integration into securities valuation, and
- integration of ESG analysis into securities recommendations

## Rigour

The panel examined whether the research was rigorous, including the approach taken in the analysis and to the development of a framework to assess the issues. The panel also looked for the issues to be clearly identified in a timely manner. Clarity of thought and expression was also important. Data was required to be expressed in a way that allowed key issues to be incorporated into company valuations.

## Reliability

The panel looked to test the investment relevance of sector and issue analysis, specifically:

- the significance of top-down and thematic analysis for decision-making
- identification of sector themes and impacts, and
- differentiation of long- and short-term horizon impacts

## Originality

The panel looked to see if the research contained any new information and insights, although the general topic may have covered an existing issue. This would include an assessment of the reasoning applied in the analysis and transparency of research outputs. The panel also looked to see if the research was sufficiently differentiated from other material available in the market place.

## How the research scored against the criteria

As shown in the chart on the next page, the category of Rigour was the area where the nominated papers scored most highly. It was evident that brokers are undertaking work to get an increasing amount of detail for their research papers. There was evidence of back-testing information to ensure reliability and site visits to operations to get the full picture. Brokers are improving their work in analysing and normalising data, however the panel would like to see more rigour in the consideration of externalities in ESG research.

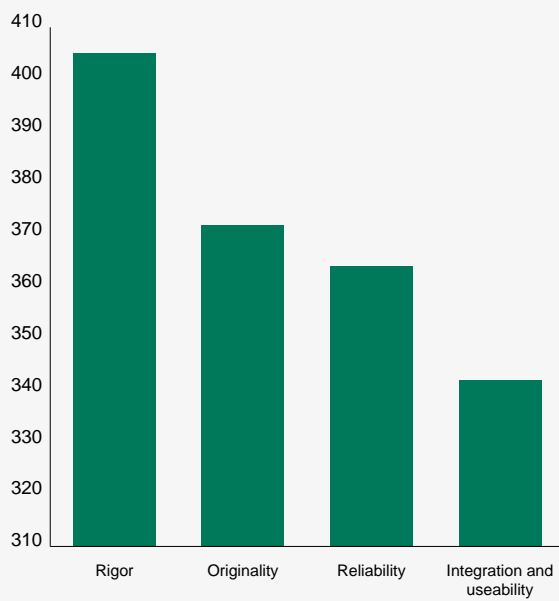
Integration and useability scored the lowest, which may be the result of every fund manager wanting something different from ESG research, depending on their needs and investment style. It may also be found to be lacking because it is the most difficult criteria to satisfy. Some panel members felt that it was up to the investment analysts to use the information to intellectually integrate it into their investment process rather than the brokers to make this leap themselves. Also, the value of papers that can be used as a basis for engagement, rather than necessarily integration alone, was highlighted as important and useful for satisfying the Principles for Responsible Investment.

# Award criteria

continued

On the whole, the panel felt that originality was down on last year, when a broader approach to ESG research was taken.

Chart 3: How the research scored



# Nominated papers

All members of ESG Research Australia were invited to submit a maximum of three pieces of research they thought was worthy of consideration by the research assessment committee. The following pieces were submitted:

| Author(s)  | Broker firm              | Research title  |
|--|--------------------------|---|
| Elaine Prior & Felipe Faria                                    | Citi                     | Safety Spotlight: ASX 100 Companies & More Injury & Fatalities Data FY05 to FY10 Presented & Interpreted  |
| Elaine Prior & Felipe Faria                                    | Citi                     | ESG: ASX100 Remuneration analysis. Analyzing Incentive Structures; Seeking Remuneration Anomalies   |
| Elaine Prior & Felipe Faria                                    | Citi                     | ASX100 ESG Compendium (series)<br>Discussing New ESG Issues; Highlighting Key ESG Issues  |
| Elaine Prior & Felipe Faria                                    | Citi                     | ASX-listed Office Trusts: Does 'green' pay?   |
| Elaine Prior & Felipe Faria                                    | Citi                     | Murray Darling Basin Plan Flags Water Cuts Company impacts via agricultural output and water quality risks  |
| Elaine Prior, Felipe Faria, Craig Woolford & Michael Goltsman  | Citi                     | ESG: ASX-Listed Retailers – Risk Management Labour & Human Rights in International Supply Chains  |
| Tim Jordon, Timothy King & Emily Behncke                       | Deutsche Bank            | ESG Dashboard: ESG in the Australian building materials sector: Carbon is key   |
| Andrew Gray  | Goldman Sachs            | Carbon Disclosure Project 2010. ASX100 Companies Are Showing A Strategic And Financially Oriented Climate Change Response Against An Uncertain Policy Backdrop. |
| Hamish Tadgell & Jien Goh                                      | Goldman Sachs            | Equity strategy: Introducing the GS&PA Structural Leaders Framework   |
| Sam Ferraro, Matthew Ross, Alain Lebel & Alistaire Paterson    | Goldman Sachs            | Corporate Governance and Agency Costs: Does Firm Complexity Matter  |
| Garry Sherrif, Benjamin Wilson & Jason Steed                   | JP Morgan                | ESG and the Energy sector: Water concerns: QLD Coal Seam Gas Developments   |
| Garry Sherriff, Fraser Jamieson, Mark Busuttill & Joseph J Kim | JP Morgan                | ESG and the Resources Sector: Social Analysis: Safety, Workforce, Community   |
| Aimee Kaye, Gavin Maher & Shai Hill                            | Macquarie Securities     | ESG Late Renewal for Renewables   |
| Aimee Kaye   | Macquarie Securities     | ESG Innovation: It isn't Easy being green   |
| Aimee Kaye   | Macquarie Securities     | ESG - Industrial Relations  |
| Aimee Kaye & Cindy Dowling                                     | Macquarie Securities     | ESG The insurance climate   |
| Alva DeVoy, Elliott Crane, Mark Williams & Michael Newbold     | RBS                      | Australia strategy: RBS ESG – Qantas  |
| Alva DeVoy & Elliott Crane                                     | RBS Equities (Australia) | Australian Strategy: RBS ESG  |
| Alva DeVoy, Luke Macnab, Michael Newbold & Elliott Crane       | RBS Equities (Australia) | Australian Strategy: RBS ESG - Transurban   |

# About ESG Research Australia

To encourage brokers to provide ESG research, HESTA, UniSuper and VicSuper initiated ESG Research Australia in 2009. A number of superannuation funds and fund managers have subsequently joined ESG Research Australia to work towards the common objective of increasing the quantity, quality and scope of ESG research produced on Australian companies.

ESG Research Australia is an association of Australian superannuation funds, fund managers and asset consultants which has the single objective of increasing the amount and quality of broker and other equity research in Australia that includes consideration of ESG issues. ESG Research Australia is an association incorporated under Australian law (incorporated 2009) and is governed by an Executive Committee comprised of fund managers and superannuation funds and is currently Chaired by Rob Fowler from HESTA Super Fund. Membership currently represents 42 institutions managing over \$100 billion in Australian equities, including some of Australia's largest fund managers and superannuation funds.

## The judging panel

The Judging Panel for the award Best Piece of ESG Research by an Individual Analyst or Team comprised of the following members.

|                                 |  |
|---------------------------------|--|
| <b>Amanda McCluskey (Chair)</b> | Colonial First State Global Asset Management |
| <b>Azhar Abidi</b>              | IFM  |
| <b>Ben Sturzenegger</b>         | Christian Super                              |
| <b>Don Hamson</b>               | Plato Investment Management Limited          |
| <b>Graeme Rough</b>             | UCA Funds Management                         |
| <b>Matt Picone</b>              | Acadian Asset Management                     |
| <b>Richard Fuller</b>           | HESTA  |
| <b>Rob Fowler</b>               | HESTA  |
| <b>Sam Dyson</b>                | Maple-Brown Abbott                           |
| <b>Talieh Bentley</b>           | UniSuper                                     |
| <b>Tim Macready</b>             | Christian Super                              |
| <b>Tom Gillespie</b>            | ARIA   |

With additional feedback from **Dinusha Peiris**, Head of Research, RIAA

## ESG Research Australia members

### Investment managers

|  |
|--|
| Acadian Asset Management (Australia) Ltd           |
| Ankura Capital                                     |
| Ausbil Dexia Limited                               |
| Aviva Investors Australia Limited                  |
| BlackRock  |
| Colonial First State Global Asset Management       |
| Eley Griffiths Group Pty Ltd                       |
| Fortis Investment Partners Pty Ltd                 |
| Goldman Sachs JBWere Investment Management Pty Ltd |
| Greencape Capital                                  |
| Hyperion Asset Management Limited                  |
| Industry Fund Management                           |
| ING Investment Management                          |
| Investors Mutual Limited                           |
| JF Capital Partners Ltd                            |
| Maple-Brown Abbott                                 |
| Northcape Capital Pty Ltd                          |
| Northward Capital                                  |
| Orbis Australia                                    |
| Paradice Investments                               |
| Perennial Growth Management                        |
| Plato Investment Management Ltd                    |
| PM Capital Limited                                 |
| Queensland Investment Corporation                  |
| Renaissance Smaller Companies                      |
| Tyndall Investment Management                      |
| UCA Funds Management                               |

### Super funds

|  |
|--|
| AustralianSuper Pty Ltd                      |
| CareSuper                                    |
| Catholic Superannuation & Retirement Fund    |
| Catholic Superannuation Fund                 |
| Cbus   |
| Christian Super                              |
| Austra Health Super                          |
| HESTA Super Fund                             |
| Statewide Superannuation Trust               |
| Unisuper Management Pty Ltd                  |
| VicSuper                                     |
| Vision Super                                 |
| Australian Reward Investment Alliance (ARIA) |

### Asset consultants

|                                |
|--------------------------------|
| Frontier Investment Consulting |
|--------------------------------|

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