EDMOND DE ROTHSCHILD

THE SRI CHRONICLES

N° 29 - March 2022

News | p.3

"ONE OCEAN SUMMIT": A NEW DRIVER IN THE PRESERVATION OF OUR OCEANS?

From an academic point of view | p.4 et 5

SHAREHOLDERS AND THE ENVIRONMENT: A REVIEW OF FOUR DECADES OF ACADEMIC RESEARCH

JEAN-PHILIPPE DESMARTIN
Head of the Responsible Investment Team

WHAT CAN RESPONSIBLE INVESTORS DO RELATIVE TO THE WAR IN UKRAINE?

Responsible investors in Europe have long considered sensitive issues such as war zones or serious violations of human rights from a distance as part of "peripheral" investment components in Africa, Asia or Latin America. But when a war of a scale unseen since 1945 breaks out in Europe, what can responsible investors do?

Many European institutional investors – including the leader in terms of assets under management, the Norwegian sovereign fund – reacted initially, both swiftly and across the board, by excluding Russian assets from all their investments, including shares and corporate/sovereign debt. Divesting from the Russian economy can be ascribed to risk management and support for the economic and financial sanctions introduced by the European Union and other Western countries including Switzerland, the United Kingdom and the United States. But removing these assets from portfolios can also be explained by a sense of moral duty.

Regarding this exclusion-based approach, and its highly welcome ethical aspect, the war in Ukraine underscores the importance for the European economy of two environmental themes: energy efficiency and renewable energies. As the dictum goes, the best energy is the one that is not consumed. With the surge in the prices of fossil fuels such as natural gas and oil, energy efficiency is more important than ever, in all of its guises, including smart grids, electrification, building insulation and public transport. Renewable energies are another vital investment theme for Europe as it looks to master its energy destiny, from wind, solar and geothermal to biomass, biomethane and green hydrogen.

The war in Ukraine is also fuelling debate over the role of civil nuclear energy, liquefied natural gas, access to rare earths, and the eligibility of conventional arms players. These topics deserve more than a few sentences in an editorial.

Enjoy reading.

Sustainable Finance and Responsible Investment Chair

Edmond de Rothschild Asset Management is a co-sponsor of the Sustainable Finance and Responsible Investment Chair which is co-managed by Ecole Polytechnique and the Toulouse School of Economics, and is a co-sponsor of the FIR - PRI european research awards.

FORUM POUR L'INVESTISSEMENT RESPONSABLE

PRI Principles for Responsible Investment

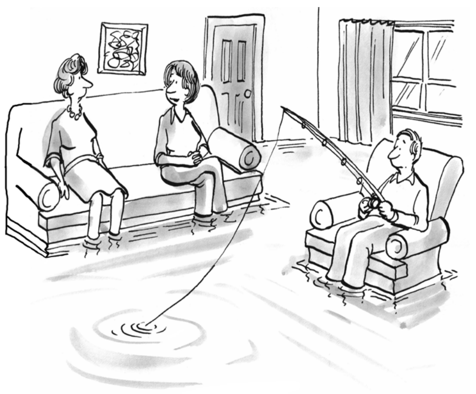
NEWS

“ONE OCEAN SUMMIT”: A NEW DRIVER IN THE PRESERVATION OF OUR OCEANS?

The first “One Ocean Summit” (OOS) was held from 9 to 11 February 2022 in Brest and brought together some forty heads of state and government leaders. This summit was designed in the same vein as the “One Planet Summit”, conceived for climate issues. It should serve as a political impetus to raise awareness among all stakeholders of the importance of preserving marine resources.

AN EMERGENCY FOR THE PLANET

The oceans cover more than 70% of our planet, i.e. 362 million km², and store almost 93% of its carbon. They regulate major environmental balances, particularly the climate, provide multiple resources, and are a key vector of economic and human exchanges. Today, our oceans are threatened by numerous pressures, such as the effects of climate change, the overexploitation of marine resources, and pollution, particularly that caused by plastic, which has a considerable impact on biodiversity. According to a recent report by the World Wildlife Fund (WWF) on the impact of plastic pollution on oceans, seas and marine ecosystems, between 86 and 150 million tonnes of plastic are already present in the oceans, equivalent to the weight of 3 to 5 million whales! Between 60% and 90% of this is single-use plastics that degrade over time into “nanoplastics”, which are harmful to the marine ecosystem. The number of microplastics could double (even if all plastic emissions cease now) or even quadruple by 2050 according to projections.



“Climate change has allowed him to do his fishing inside the house.”

FIRST COMMITMENTS MADE

At the end of the summit, several commitments were made on each of the four major themes addressed: the protection of marine ecosystems and the promotion of sustainable fishing, the fight against pollution, the fight against climate change, and ocean governance. Here are some examples: reaching the target of 30% of marine space protected by 2030; ending overfishing and verifying, controlling and sanctioning illegal, unreported and unregulated fishing; continuing the discussion on the adoption of a legally binding treaty on plastic pollution; preserving marine ecosystems by mitigating and adapting to climate change; supporting the transition toward low-carbon industries; mapping 80% of the ocean floor by 2030; and launching the High Ambition Coalition for a High Seas Treaty for biodiversity in an international area beyond national jurisdiction that covers 60% of the world’s seas and oceans.

THE RESPONSIBILITY OF FINANCIAL INVESTORS

Holding this first “One Ocean Summit” is in itself a first step forward because, too often, the oceans remain on the sidelines of major international talks on climate and biodiversity. Yet, the intrinsic links between oceans, climate and biodiversity are indisputable and call for an integrated governance of environmental issues. Investors cannot ignore this, as illustrated by Article 29 of the Energy-Climate Law in France, which requires financial investors to report on biodiversity from 2022 onwards (measurement of the biodiversity footprint and contribution to reducing impacts on biodiversity). Biodiversity and our oceans are one and the same: protecting our oceans means protecting a source of biodiversity and a climate regulator.

SHAREHOLDERS AND THE ENVIRONMENT: A REVIEW OF FOUR DECADES OF ACADEMIC RESEARCH

GUNTHER CAPELLE-BLANCARD

Gunther Capelle-Blancard is Professor at the University of Paris 1 Panthéon-Sorbonne and at the Paris School of Business. He received his PhD in 2001 and was awarded the Prix de l'Association Française de Finance and the Prix de la Chancellerie des Universités de Paris. From 2007 to 2015, he directed the Master's degree in Money-Banking-Finance-Insurance at the University of Paris 1, before being elected Deputy Director of the Sorbonne School of Economics from 2015 to 2018.

His research focuses on ethical finance, the financialisation of the economy, the transformations that affect financial systems and the way they are regulated. Author of more than forty academic articles in international journals (*The Journal of Business Ethics, The Journal of Banking & Finance, The Journal of Environmental Economics & Management, The Review of Finance*, etc.), he has also written several academic books.

The aim of this paper is to question the place and the role of financial markets today in the framing of environmental policies. In this regard, the authors review four decades of academic research regarding the reaction of shareholders to environmental events. To set the stage, the authors first provide an account of the Brumadinho ecological disaster in Brazil that occurred in 2019. They then provide a critical review of over 100 event studies, covering a set of events relating to environmental issues such as industrial accidents, public disclosure programs, changes in environmental regulation, environmental news and corporate initiatives.

THE BRUMADINHO DISASTER AS A STARTING POINT

The Brumadinho ecological and human disaster is one of the last examples of the problematic relationship between corporations, shareholders and the environment. The rupture of this Brazilian mining dam led in 2019 to a tide of toxic mud, equivalent to 5,000 Olympic-sized swimming pools, spreading at a speed of 70 km/h and killing more than 250 people. The Brumadinho tragedy was not natural, as it was the result of the mining activities of the Vale group, the world's largest producer of iron ore. Vale has denied the toxic nature of this devastating spill, even though it was not the first time that this multinational company has been involved in accidents, and has reached an agreement with the government for a fine of around $1.8 billion. On the NYSE, Vale's stock lost 8% the day after the disaster and 18% three days later. The losses for the shareholders were estimated at 60 billion reis and supposed to take into account the costs that the company will incur. Only seven months later, Vale's stock price returned to the same price range as before the disaster.

The Brumadinho dam disaster highlights how financial markets actually value environmental damage. A multinational, complying with the highest standards and committed to social responsibility, faces a major accident. The authorities impose a fine; the shareholders face a temporary loss on their wealth. However, after a couple of months, it is business as usual.

CRITICAL REVIEW OF EVENT STUDIES

In a second step, the paper focuses on event studies of the past forty years to detail the relationship between environmental events and the response from shareholders. These events are collected mainly through newspaper articles, official publications and NGOs. The methodology for assessing the costs and benefits to shareholders is based on the event study methodology, i.e. a statistical method to assess the impact of an event on the value of a firm, by evaluating the abnormal return (AB) which is the difference between the actual return of a security and the expected return.

INDUSTRIAL ACCIDENTS WITH ENVIRONMENTAL CONCERNS

Through these studies, some accidents with harmful environmental fallout are more present than others, such as the Chernobyl and Fukushima nuclear disasters, the Bhopal chemical explosion or the BP Deepwater Horizon spill. In several cases, the market value of the firm involved in the accident experienced a significant drop. However, it is not clear whether such a drop always persists.

Indeed, after the Bhopal explosion on December 3, 1984, which released 27 tons of the highly poisonous methyl isocyanate, killing more than 4,000 people and injuring 200,000 others, Union Carbide's market value dropped from 3.5 to 2.5 billion dollars and in the first month after the accident, the AR was -31.5%. However, a year later, the cumulative AR (CAR) had become insignificant and in March 1986, the CAR was +31% after a restructuring and a recapitalization of the company.

The authors find that, through major events, which occurred between 1990 and 2005, on average, the market capitalization of the companies involved in these events decreased by 1.3% two days after the disaster and that the financial loss was related to the number of deaths and pollution. Thus, the market reaction appeared limited.

Nevertheless, accidents with social and environmental impacts are not the only events that affect the AR. Different studies have been conducted to investigate market reactions to environmental regulations.

PUBLIC DISCLOSURE PROGRAMS RELATING TO ENVIRONMENTAL ISSUES

Indeed, the study first finds the effect of public disclosures. These announcements can have a positive effect because the company becomes more transparent, which reduces the risk for the company and the shareholders. However, this transparency can also be risky if the information disclosed leads to losses. An example of such a disclosure policy is the Toxics Release Inventory promoted in the US in 1986. It is the most important case of environmental policy based on public disclosure. After the promotion, the market value of manufacturing firms listed at the NYSE or AMEX, which reported TRI releases, dropped by $4.1 million the first day with an AR of -0.284%.

Secondly, the focus is on legal actions taken against companies because of environmental violations. Possible fines obviously have a negative impact on the value of the company. However, the loss of company value can be attributed primarily to media coverage, the expectation of subsequent litigation, and the defendant's willingness to settle. Finally, market reactions to regulations negatively affect the AR in most cases. However, most of these effects are small, meaning that they do not seem to result in sufficient financial incentives for firms to improve their environmental performance.

ENVIRONMENTAL NEWS AND CORPORATE INITIATIVES

Concerning the environmental news, the authors refer to studies conducted on the ESG ratings of companies. If they are negative, this leads to a fall in the AR of 0.1%, but conversely, a positive rating does not necessarily lead to an increase. Here we find the phenomenon of media coverage and the loss is linked to the proximity between shareholders and the controversies.

Some companies make corporate initiatives by being proactive and by aiming to limit their negative impacts and reduce their ecological footprint through CSR strategic behaviors and corporate environmentalism. These firms can be rewarded for these voluntary corporate disclosures with Environmental Awards and Certifications or with ratings and rankings delivered by third parties. These rewards can affect the AR but third parties must be careful about greenwashing practices through these strategies and behaviors.

To conclude, many environmental events confirm that there is a response from the stock market, which affects the value of the firm. This is particularly the case with environmentally damaging events. The mean abnormal returns (AARs) are -2% and the median is 0.6%. However, for environmentally friendly events, the ARRs are modest, at +0.2%.

In light of this research, it appears that financial market reactions are limited to translating environmental concerns into financial consequences.

"Shareholders and the environment: a review of four decades of academic research", *Environmental Research Letters, Volume 16, Number 12,* Gunther Capelle-Blancard, Adrien Desroziers and Bert Scholtens, published by IOP Publishing Ltd

COMPANY MEETINGS

CELLNEX

Founded in 2000 under the name of Abertis Telecom in Spain, Cellnex is a wireless telecommunications infrastructure operator in Europe, particularly based in Spain, Italy and France. The group has announced the launch of its ESG Master Plan for 2021-2025, which will have a direct impact on infrastructure services, which represent 80% of its turnover in 2020. Cellnex contributes globally to bridging the digital divide.

The internal results of the Environmental Management System over the period 2016-2020 through its 100,000 sites are satisfying, primarily regarding the group's energy intensity (-31%) as well as the carbon intensity which was divided by two. Cellnex's objectives have been validated by SBTi in 2021 and have a major ambition through its ESG Master plan: use 100% renewable energy by 2025.

Employee safety is a major concern for the group with the maintenance of the towers, which is an outsourced activity for Cellnex. Moreover, customer satisfaction and data protection are key elements in the industry. To this regard, the group's ambitions are to deploy ISO 9001 (Quality Management) and 27001 (Information Security Management) from 2020.

Regarding governance, Cellnex benefits from the presence of its CEO, Tobias Martinez, who joined in 2015 and was formerly CEO of Abertis Infrastructures. Remuneration of the group's directors is aligned with the company's long-term performance.

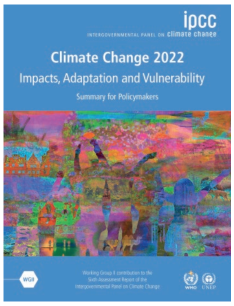
Source of data: Edmond de Rothschild Asset Management (France).

The information about the companies cannot be assimilated to an opinion of Edmond de Rothschild Asset Management (France) on the expected evolution of the securities and on the foreseeable evolution of the price of the financial instruments they issue. This information cannot be interpreted as a recommendation to buy or sell such securities.

RECOMMENDED READING

HALF MEASURES ARE NO LONGER POSSIBLE

The contribution of Working Group II to the 6th Assessment Report of the IPCC (International Panel on Climate Change), entitled "Climate Change 2022: Impacts, Adaptation and Vulnerability", was published in late February. This report, to which 270 authors from 67 countries contributed, is even more alarming than the IPCC's previous work in terms of the threat that climate change poses to human well-being and the health of the planet. It stresses the urgency of taking immediate, far-reaching action if we are to avoid climate catastrophe. If this is a global challenge, it requires local solutions, particularly within cities, which are essential to the solution. Beyond the voice of the experts, this is a call to each and every one of us to be concerned.



Read the report: https://www.ipcc.ch/report/ar6/wg2/

150 million tons

The amount of plastic waste in the oceans. It could increase fivefold by 2050 and represent the mass of fish in all the world's seas.

Source: UN, 2021.

57%

of the world's population fully vaccinated against Covid-19, for a total of 10.9 billion doses administered.

Source: Our World in Data; March 13, 2022.

INTENSIFYING DIALOGUE AND ENGAGEMENT WITH THE NURSING HOME SECTOR

The nursing home sector has been under a lot of pressure in the media and on the stock market in recent weeks. Korian and especially Orpea have been the subject of serious allegations concerning working conditions and the well-being of residents.

The difficult social context of Orpea's sector (working conditions, risks of abuse, etc.), whether we are talking about public or private actors or associations, is unfortunately nothing new. For example, this sector is rated lower than other healthcare businesses (pharmaceutical companies, biotechs and medical equipment) in our proprietary ESG analysis model called EDR BUILD. For this reason, Orpea is one of the companies with which we conduct a policy of dialogue/engagement on social issues.

The Covid-19 crisis has shown the importance of the nursing home sector and its role in the health and well-being of the elderly. It has also highlighted the complexity of the sector's working conditions (staff turnover, accidents at work, difficulties in recruiting and retaining talent, training/permanent employment, etc.). Let us not forget that this is one of the three major sectors affected by the "Great Resignation" in the United States (1-construction, 2-hospitality/restaurants and 3-health services).

AN INCREASED NEED TO BUILD CONFIDENCE

The allegations against Orpea also concern governance issues, which has raised questions about other operators in the sector. As soon as the Responsible Investment team became aware of the controversies highlighted by this news, it placed the company under negative watch. Following the controversies affecting Orpea, we updated the company's ESG rating on 26 January 2022 based on the limited information available to us. This rating will be finalised after publication of the results of the independent audit commissioned by the Board of Directors, and the administrative and financial investigations.

Through the *Investor Statement of Expectations for the Nursing Home Sector* coordinated by UNI Global Union, which we joined in 2021, 95 institutions representing $3.34 trillion in combined assets under management are calling on companies in the sector to implement ambitious policies on quality of care, employee health and safety, staffing levels, and the level of the lowest pay grades. This commitment is an opportunity to strengthen the confidence of investors and public opinion in an essential sector and in particular the management team of Orpea, which we met several times. During these discussions, we broached the subject of understaffing with the group, along with many other issues which were revealed in the book "The Gravediggers" by Victor Castanet. We will maintain and intensify this dialogue throughout 2022.

EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)
47, rue du Faubourg Saint-Honoré, 75401 Paris Cedex 08
Société anonyme governed by an executive board and a supervisory board with capital of 11,033,769 euros
AMF Registration No. GP 04000015 - 332.652.536 R.C.S. Paris
www.edram.fr