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Globally consistent ESG policies are indispensable for international finance

Undoubtedly, sustainable finance is accelerating as investor demand is rising. In order to meet the demand, asset managers and financial institutions are increasingly incorporating ESG criteria into the investment and distribution process. In parallel, corporates are working to provide greater transparency through non-financial reporting. Fidelity International developed an in-house proprietary ESG rating tool launched in 2019, evaluating its investee companies on ESG metrics. This approach is a key building block for enhanced corporate engagement on non-financial factors with investee companies, and in response to investor client demand as well as policy expectations. Recent data evidence confirms a correlation between financial and non-financial factors, as companies with robust ESG scores have on average suffered less financial loss and outperformed.

To continue the journey from here, the work of policy makers in the area of sustainable finance is indispensable for the success of the financial sector and corporates to transition towards a greener financial system and economy. ESG policies provide guidance for asset owners, managers and corporates on the definition of sustainable economic activities and their application in practice. It is imperative that ESG standards converge at international level so to prevent regulatory arbitrage across global jurisdictions, as capital flows are international and corporates operate across global supply chains.

At the heart of the success lies an improved and standardised approach to corporate disclosure. In the EU, corporate transparency is driven by a revised EU Non-Financial Reporting Directive (NFRD), which is expected to result in more comparable and meaningful disclosures. Consequently, investors may have better quality data in future when engaging with the investee companies on sustainable corporate governance. However, investors are already valuing corporates on both their financial and non-financial performance today, since the EU's Sustainable Finance Disclosure Regulation (SFDR) entered into force in March 2021.

Therefore, it is essential that corporates swiftly disclose non-financial data based on international frameworks existing today, developed already by SASB, the Sustainability Accounting Standards Board, and the FSB's TCFD, the Financial Stability Board's Task Force on Climate-related Financial Disclosures created in December 2015. EU sustainable policy initiatives ideally would build on these frameworks and develop them further as envisaged through the double materiality concept embedded in the future, revised EU NFRD.

Likewise, it is welcomed that EFRAG, the European Financial Reporting Advisory Group, aims to ensure that IFRS - International Financial Reporting Standards - takes into account European needs. Consequently, the investor community is hopeful that globally consistent minimum sustainable reporting standards are developed by policy makers and existing frameworks applied today by the corporate community, responsive to regional needs. IOSCO's urgent call for globally consistent, comparable and reliability disclosure standards in February 2021 and commitment towards working with the IFRS to develop an SSB - Sustainability Standards Board - is highly encouraging to achieve global convergence.

The EU's efforts to establish a dialogue through the International Platform on Sustainable Finance (IPSF) could be the critical path towards achieving global convergence of ESG standards and already includes major countries in the Americas and Asia Pacific. Hence, asset managers welcomed that the United Kingdom joint the IPSF at the beginning of 2021 and encourage also the United States becoming a member, as they are indispensable in successfully achieving the global convergence of ESG standards. COP26 this year will also represent a key opportunity to align international sustainable finance policies.

Most importantly, in the interest of investor protection - both retail and institutional investors - international convergence of ESG standards including eco-labels for financial products will be vital. Ideally these in future will be built on global, not just on regional policy initiatives such as the EU Taxonomy, corporate disclosure and SFDR ESG product classification. Hence, international ESG policy convergence will ultimately benefit the end investor.