



Integrating ESG  
into Traditional  
Corporate Valuation

# EFFAS C ESG

EFFAS COMMISSION ON ESG



EFFAS THE EUROPEAN FEDERATION  
OF FINANCIAL ANALYSTS SOCIETIES

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## **EFFAS C ESG**

### **EFFAS COMMISSION ON ENVIRONMENTAL, SOCIAL AND GOVERNANCE ISSUES**

#### **- INTEGRATING ESG INTO TRADITIONAL CORPORATE VALUATION**

## **INTRODUCTION**

The emergence of Environmental, Social and Governance issues (ESG) for years has been a prominent phenomenon in international capital markets. Especially in Anglo-Saxon markets the pros and cons of integrating ESG issues into the investment chain has been much discussed, sometimes controversially. Corporates around the globe, nevertheless, produce vast reports about their ESG activities. Typically, these activities are referred to as Corporate Social Responsibility (CSR).

ESG can be defined as issues concerning the risk-related aspects of stocks in the area of environment, social issues such as relationship to workforce and local communities and governance issues comprising Corporate Governance and management systems. Accordingly, CSR may be summarised as the reporting of corporates in response to issues arising out of ESG concerns.

For years, ESG and CSR have been commonly regarded as the special interest of investors with sustainability-driven investment styles. However, in recent years initiatives of political forces and Non-Governmental organisations (NGOs) have managed to gain recognition by capital markets of the importance of ESG and furthered active integration of ESG issues into investment decisions. Prominent campaigns include PRI Principles for Responsible Investments which were developed by invitation of the United Nations Secretary-General by a group of the world's largest institutional investors; Global Compact did bring companies together with UN agencies, labour and civil society to support universal environmental and social principles; the United Nations Environment Programme Finance Initiative (UNEP FI), a global partnership between the United Nations Environment Programme (UNEP) and the private financial sector, working closely with over 160 financial institutions.

By and large equity and bond investors have given greater attention to risks which result from corporate performance in areas traditionally of lesser interest to capital markets such as sustainability management, treatment of human rights or human capital management.

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## **CORPORATE EVALUATION AND ESG**

There is a growing view among investment professionals that mal-treatment of ESG issues by corporate management can affect the performance of investment portfolios. ESG is currently in the process of becoming more and more a part of traditional investment analysis ("mainstreaming"). Investors fulfilling their fiduciary (or equivalent) duty therefore perceive the need to give appropriate consideration to these issues, but to date have lacked a framework for doing so.

Capital markets understand the sensitivity of corporate reputation *en principe*. However, issues arise such as how to measure concepts such as sustainable management, fair treatment of employees or responsible management of greenhouse gas in order to integrate these issues into investment decisions in general and financial analysis in particular. The issue on hand is what is the measure- and benchmarkable impact of good ESG practice on corporate success and how can capital markets model the underlying correlations between good performance in ESG and good performance, bottom line?

There is an urgent need of investment professionals, corporates and political players alike to understand how to handle questions such as:

- What is the contribution of ESG reporting for understanding risk and materiality of investments?
- What are methods, formats and elements of ESG analysis which take into account the needs and requirements of capital markets?
- How to bridge the gap between classic equity valuation and ESG content?

## **TASKS AND OBJECTIVES OF CESG**

EFFAS Commission on ESG (CESG) was founded in October 2007 in Vienna. The objective of CESG is

***Facilitating the integration of non-traditional aspects of corporate performance in the area of ESG into investment processes.***

CESG is a body of investment professionals from leading European and global sell-side and buy-side firms. Members of CESG are predominantly fund managers, financial analysts, equity sector specialists.

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CESG was mandated by EFFAS with the following tasks and objectives:

1. Establishment and coordination of a consistent position by EFFAS on all relevant aspects concerning ESG reporting, measurement and valuation;
2. Bundling of expertise on ESG treatment within the community of European investment professionals;
3. Expand the work on ESG which has been achieved by individual EFFAS member societies to encompass needs of European investment professionals;
4. Serve as a point of reference for and establish a network with current initiatives on ESG both from the political arena, academic field and projects launched by capital market participants;
5. Organise conferences on ESG topics on a European level including corporate presentations from European blue chip companies;
6. Represent EFFAS at international conferences dealing with ESG issues;
7. Represent EFFAS at projects and initiatives which require input and recommendations on the needs of investment professionals.

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## ACTIVITIES

In 2007 and 2008 CESG hosted a conference entitled "Taking ESG into Account" in Frankfurt aimed at enhancing the knowledge of ESG in mainstream capital markets. Taking ESG into Account 2008 attracted more than 150 participants from all over Europe. As integral part of the format Taking ESG into Account also include corporate presentations from Euro-Stoxx and DAX30 companies.



Impressions of Taking ESG into Account Conference Frankfurt, 11 & 12 March 2008

In May 2008 EFFAS EMC gave an unqualified endorsement to specific guidelines for ESG reporting which were defined and authored by a working group of DVFA, the German Society of Investment Professionals, and subsequently identified as one of the key enablers for ESG integration by CESG. "KPIs for ESG" contain 25 key performance indicators for corporate reporting on ESG. These KPIs were surveyed globally with mainstream investment professionals. The guidelines contain precise taxonomies for the reporting as well as ESG management principles. An XBRL (eXtended Business Reporting Language) taxonomy is under preparation.

In the near future, CESG is dedicated to the following deliverables:

- Design and provide a training and qualification workshop on extra-financials for investors and financial analysts.
- Promote adoption of "KPIs for ESG" Guidelines throughout Europe.
- Stage Taking ESG into Account 2009.

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## STRUCTURE AND ORGANISATION



**Chairman:**  
Friedrich Mostboeck, ÖVFA, Austria



**European Coordinator:**  
Ralf Frank, DVFA, Germany

Commission Members from selected international sell-side and buy-side firms as well as leading experts on ESG form the core team of CESG.

Friedrich Mostböck	Erste Bank der österreichischen Sparkassen AG, Austria (Chairman)
Rob Bauer	Universiteit Maastricht, Netherlands
Tommy Borglund	Halvarsson & Halvarsson, Sweden
Christoph Butz	Pictet & Cie, Switzerland
Daniela Carosio	AIAF, Italy
Paul Clements-Hunt	UNEP Finance Initiative, International
Marco Curti	ZKB Zürcher Kantonalbank, Switzerland
Dr. Hendrik Garz	WestLB AG, Germany
Claudia Kruse	JP Morgan, UK
Martine Leonard	CM-CIC Asset Management, France
Felix Schnell	Allianz Global Investors KAG, Germany
Dr. Raj Thamotheram	AXA Investment Managers Ltd, UK

List of members of CESG (21 May 2008)

## FURTHER INFORMATION

Information on CESG's current activities and results can be found on the CIC website on the EFFAS homepage:

<http://www.effas.com/en/commissions.htm>



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