2020 AUSTRALIAN IPO REVIEW: MARKETING IN THE ESG ERA

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Guides – By **Timothy Stutt**

Environmental, social and governance (ESG) issues continued to gain traction at both the institutional and retail investor level during 2020, in some cases impacting on the type of ESG information included in prospectuses and other disclosure documents for companies' public offerings.

Historically, it has been relatively common for companies to include high level commitments to corporate social responsibility (CSR) in their prospectuses or disclosure documents, along with more granular information regarding compliance with the recommendations of the ASX Corporate Governance Council's Principles and Recommendations (ASX Principles).

During 2020, we saw increased expectations regarding ESG matters driving certain companies to enhance marketability by improving the quality and quantity of their ESG disclosure. In some cases this included a more "holistic" consideration of ESG opportunities, risks and governance than would be typical in previous years, and it is a trend we expect to continue and accelerate over the course of 2021.

GROWING INFORMATIONAL DEMANDS REGARDING ESG

For a number of years, statements from BlackRock and others, have made it clear that institutional investors expect listed companies to proactively consider, manage and disclose ESG risk exposures on issues like climate, human rights and labour practices.

Increasingly, however, it has also become apparent that many institutional investors are themselves under pressure to better integrate ESG considerations into the way they build their portfolios, manage risk and generate returns. Examples include:

- recent European regulation seeking to prevent “greenwashing” by requiring asset managers to disclose the percentage alignment of their portfolio with a taxonomy of “environmentally sustainable” activities; or
- recent proceedings brought against REST Super in relation to its diligence and disclosure of climate risk in its portfolio (settled in December 2020).

Growing appetite for ESG and “sustainable” investments (including at the retail level), has also encouraged greater levels of ESG information being published by portfolio companies to assist with screening, diligence and alignment with investment mandates.

ENHANCING DISCLOSURE IN AN IPO CONTEXT

The listing requirements of ASX have, over the past decade years, supported the provision of significant information to potential investors on company governance. This information has, however, been centred on the governance charters and policies recommended under the ASX Principles, with relatively little information on companies’ broader approach to ESG.

As companies seek to enhance the information they provide to potential investors, we are seeing increased focus in the following areas:

Disclosure of material risks	Outlining the company’s approach to ESG	ESG policies and processes
Many companies’ understanding of, and response to, ESG risks is rapidly evolving. In this context, an increased focus on ESG risks may be warranted when formulating disclosure of material risks related to the investment. Examples could include the risk of “loss of market” due to rapid decarbonisation or reputational risks flowing from human rights practices in the company’s supply chain.	In the same way companies have historically outlined their approach to governance in IPO documents, companies could include greater disclosure in relation to ESG risk management. This is likely to extend beyond high level “CSR” statements to provide greater on companies’ mechanisms for considering and escalating specific ESG risks in the business (eg Board or Committee accountabilities, whistleblowing policies, etc).	The recent Fourth Edition of the ASX Principles included additional recommendations for certain ESG policies, including whistleblowing and anti-bribery and corruption. However, in some cases, where companies have specific ESG risk exposures, we have also seen the adoption of additional targeted policies at listing. Recent examples have included ESG investment policies, environmental policies and ethical sourcing policies.

FORWARD THINKING ON ESG

While carefully considered policies and disclosure on ESG may enhance the marketability of some companies, at this stage it is not a uniform market expectation and practices continue to be varied.

However, having regard to the intensity of many institutional investors focus on ESG – including the effect of “feedback loops” (created by the expectations of their own investors in turn) – it is clear that there is shifting ground in this area and this will continue to change over time.

For this reason, we are also increasingly engaging with private equity and asset owners on ESG diligence and risk management projects, with a view to enhancing the marketability of companies at the exit stage.

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KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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