



**Testimony of  
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Committee on Banking, Housing and Urban Affairs  
United States Senate

“The Application of Environmental, Social, and Governance Principles in Investing and the Role of Asset Managers, Proxy Advisors, and Other Intermediaries”

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10:00 AM

Chairman Crapo, Ranking Member Brown, and Members of the Committee, thank you for the invitation to testify before you today. My name is John Streur and I am the President and Chief Executive Officer of Calvert Research and Management, an investment management firm based in Washington, DC that invests across global capital markets. Our firm incorporates into our investment decisions information about corporations’ (and other issuers of securities) exposure to, and management of, financially material environmental, societal and governance (“ESG”) factors. Calvert is a subsidiary of Eaton Vance Management, a leading global asset manager based in Boston.<sup>1</sup>

Our firm sponsors one of the largest and most diversified families of responsibly invested mutual funds, encompassing active and passively managed equity, fixed income, alternative and multi-asset strategies. As of February 28, 2019, across our portfolios, we held more than 5,600 securities from over 4,800 issuers in developed and emerging markets. Our primary focus is to generate favorable investment returns for our clients by allocating capital consistent with financially material ESG analysis and through structured engagement with portfolio companies.

As a participant in the global capital markets focused on long-term value creation for our clients, we understand that most corporations and other issuers of securities deliver a strong net benefit to society, through their products and services, creation of jobs and the sum of their behaviors. The world has experienced unmatched

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<sup>1</sup> Calvert Research and Management (“Calvert” or “CRM”) is an investment adviser registered under the Investment Advisers Act of 1940, as amended (“Advisers Act”). Calvert is a Massachusetts business trust formed in August 2016 as a wholly-owned subsidiary of Eaton Vance Management (“EVM”). On December 30, 2016, Calvert completed its purchase of substantially all of the business assets of Calvert Investment Management, Inc. (“CIM”). Calvert’s purchase of the assets of CIM included all technology, know-how, intellectual property and the Calvert Research System and processes. After approval of the Board of Directors/Trustees and shareholders of the Calvert Funds, Calvert also became the successor investment manager to the registered investment management companies that CIM had been manager of prior to the transaction. In addition, Calvert hired the vast majority of the employees that were part of CIM’s sustainability research department. As a result, references related to the activity of CIM prior to the purchase of its assets on December 30, 2016, are deemed herein to be the activity of Calvert.

economic growth over the course of the last century and we recognize that free market capitalism and competition have made a significant contribution in lifting living standards globally.

Today, companies and investors throughout the world are working to better understand how to further the tremendous progress that corporations, competition and capitalism create by conducting a deeper analysis of environmental and societal impacts and of corporate governance systems in place worldwide. As a firm, we are part of a rapidly expanding base of institutional investors and asset owners globally who seek to strengthen corporations and capitalism through improved performance on financially material environmental risk management, job creation, operational efficiency and other factors understood through analysis of environmental and social impact factors.

## **The Evolution of ESG Investment Strategies**

In recent years, interest in corporate exposure to issues such as energy efficiency, water conservation, workplace diversity and human rights has intensified. A heightened awareness of these issues among consumers and investors alike has pushed ESG investing well into the mainstream. In 2018, more than \$12 trillion in the United States was invested in strategies that consider ESG criteria—a 38% increase since 2016. This \$12 trillion represents 26% of professionally managed assets in the United States, which total \$46.6 trillion.<sup>2</sup>

In 2010, there were 281 registered investment companies that incorporated ESG factors into their investment process. Last year, in 2018, that figure had risen to 730—a 2.6x increase in just eight years.<sup>3</sup>

Investors are not the only ones changing their behavior—corporations are also taking action. Many companies in the United States have increased their focus on actively managing and reporting on ESG risks in order to remain competitive in the global market for products and services. Eight years ago, just 20% of the S&P 500 provided any type of reporting on relevant ESG risks. Today, 85% of companies in the S&P 500 actively report on ESG risks factors.<sup>4</sup>

A common misconception about ESG investment strategies is that incorporating environmental, social and governance considerations into an investment process requires the investor to sacrifice returns. Calvert partnered with Professor George Serafeim at Harvard University to conduct research on this topic. Among other findings, we learned that firms in the top quintile of performance on financially material ESG issues significantly outperformed those in the bottom quintile. If an investor had invested \$10,000 in 1993 in a portfolio of stocks performing in the top quintile on relevant ESG factors, by 2014 that portfolio would have returned more than twice that of a portfolio of stocks performing in the bottom quintile on financially material ESG factors.<sup>5</sup>

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<sup>2</sup> US SIF: The Forum for Sustainable and Responsible Investment. *2018 Report on US Sustainable*. Responsible and Impact Investing Trends. Data points are as of December 31 of the preceding year.

<sup>3</sup> Ibid.

<sup>4</sup> Governance & Accountability Institute, Inc. *FLASH REPORT: 85% of the S&P 500 Companies Published Corporate Sustainability Reports in 2017*. March 20, 2018.

<sup>5</sup> George Serafeim. *The Role of the Corporation in Society: Implications for Investors*. September 2015. Source: Adapted from Khan, Mozaffar and Serafeim, George and Yoon, Aaron S., “Corporate Sustainability: First Evidence on Materiality,” (November 9, 2016). “The Accounting Review,” Vol. 91, No. 6, pp. 1697-1724. Available at SSRN: <https://ssrn.com/abstract=2575912> or <https://dx.doi.org/10.2139/ssrn.2575912>.

## Exhibit. Firms with strong ESG scores significantly outperform those with weak scores



Source: Adapted from Khan, Mozaffar and Serafeim, George and Yoon, Aaron S., “Corporate Sustainability: First Evidence on Materiality,” (November 9, 2016). “The Accounting Review,” Vol. 91, No. 6, pp. 1697-1724. Available at SSRN: <https://ssrn.com/abstract=2575912> or <https://dx.doi.org/10.2139/ssrn.2575912>.

Notes: The chart above illustrates the author's analysis of a large number of U.S. stocks from 1993 to 2014, ranked on the strength of their ESG commitments. The stocks were grouped into the top 20% of the universe (top ESG score) versus the bottom 20% (bottom ESG score). Past performance is no guarantee of future results. Data is for illustrative purposes only.

The business case for incorporating ESG considerations into the investment process is well grounded in empirical evidence. A recent study that aggregated the results of 2,200 studies on the topic concluded that the vast majority found positive correlations between corporate financial performance and ESG considerations that are financially material to that business.<sup>6</sup> Associated financial benefits included lower costs of capital, improved operating performance, and stronger free cash flow.

The rapidly growing action being taken to incorporate ESG factors into the business practices of U.S. corporations and the investment processes of U.S. investment management firms is a conscious attempt by these entities to strengthen our capitalist system and ensure U.S. firms maintain a competitive position globally. The Principles for Responsible Investment (“PRI”), an international network of firms incorporating ESG factors into their investment and ownership decisions that launched at the U.S.’s own New York Stock Exchange in 2006, now include over 2,300 investment firms globally as signatories.<sup>7</sup>

All too often, a genuine focus on ESG considerations by corporate entities and financial firms is associated with a narrow set of politicized issues, and the potential withholding of capital access or other financial products and services from lawful and legitimate businesses. Our firm seeks to inclusively invest in issuers that are positioned to capitalize on what we see as a long-term macroeconomic trend toward a more sustainable future. It is critical that the U.S. capital markets’ infrastructure and regulatory policy keep pace with these global trends in order to maintain our economic competitiveness.

<sup>6</sup> Gunnar Friede & Timo Busch. *ESG and Financial Performance: Aggregated evidence from more than 2000 empirical studies*. 2015. available at: <https://www.tandfonline.com/doi/full/10.1080/20430795.2015.1118917>

<sup>7</sup> Principles for Responsible Investment, “About”, 2018, available at: <https://www.unpri.org/pri/about-the-pri>

## Disclosure Standardization of Environmental, Social, and Governance Risk Factors

Corporate disclosure standards have evolved over time to reflect changing industry trends as well as regulatory and judicial developments. Undoubtedly, there has been a great deal of discussion and debate amongst the investment community, regulatory authorities, and members of this Committee as to the need or degree to which particular environmental, social or governance data should be disclosed by public issuers of securities. Rather than address specific proposals or existing petitions for actions on rulemaking, I would like to briefly speak to this issue's relevance as it pertains to the benefits of standardization and the competitiveness of U.S. capital markets.

In the United States, we are fortunate to have the deepest, most liquid and most developed capital market in the world. Our financial economy has proven to be a strategic competitive advantage for the nation. The efficient flow of capital that it provides has enabled companies of all sizes to innovate, create jobs, and contribute to an enhanced quality of life for Americans. Yet, when it comes to the issue of standardizing disclosures related to ESG risk factors, we are behind many other developed economies around the globe.

As I mentioned earlier, 85% of companies in the S&P 500 already actively report on ESG risk factors voluntarily, through corporate sustainability reports or other corporate disclosures. However, much of the information provided through voluntary disclosures is difficult to compare and inconsistent across issuers, resulting in considerable costs and resource expenditure for investors. While it is impossible to discern the amount of expense incurred by investors attempting to discern ESG data, one estimate suggests that by 2020, \$745 million will be spent globally on ESG data alone.<sup>8</sup>

The PRI,<sup>9</sup> along with MSCI, a global data and investment research provider, recently identified 300 policy initiatives that promoted sustainable finance in 50 of the largest economies around the globe. Two hundred of those initiatives were corporate reporting requirements covering ESG factors.<sup>10</sup> There are now seven stock exchanges—in Australia, Brazil, India, Malaysia, Norway, South Africa, and the United Kingdom—where companies must have some degree of environmental or social disclosure in order to meet the exchanges' requirements to list. In 2018, the China Securities Regulatory Commission introduced requirements that will mandate all listed companies and bond issuers in China disclose environmental, social, and governance risks associated with their operations.<sup>11</sup>

These nations recognize that the competition for capital and investment is fiercely competitive and global in nature. Of course, the United States should always act in the best interests of its own citizens and balance concerns from a variety of constituencies. However, failing to take action to standardize ESG disclosures may afford other nations the opportunity to shape global standards that ultimately impact U.S. capital markets and our nation's economic competitiveness.

Finally, Calvert recognizes that as investors, our success is intrinsically linked to the success of the companies and issuers in which we are invested. We would advocate that any rulemaking or action regarding disclosure be done in a deliberate and fair process that balances the need for reliable and complete information on ESG considerations along with limiting any unnecessary regulatory burden.

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<sup>8</sup> ESG Data: Mainstream Consumption, Bigger Spending, January 9, 2019, *available at*: [www.optimas.com/research/428/detail/](http://www.optimas.com/research/428/detail/)

<sup>9</sup> Principles for Responsible Investment, "About", 2018, *available at*: <https://www.unpri.org/pri/about-the-pri>

<sup>10</sup> PRI and MSCI, *Global Guide to Responsible Investment Regulation*, 2016, *available at* <https://www.unpri.org/page/responsible-investment-regulation>.

<sup>11</sup> Latham & Watkins LLP, *China Mandates ESG Disclosures for Listed Companies and Bond Issuers*, 2018, *available at* <https://www.globalelr.com/2018/02/china-mandates-esg-disclosures-for-listed-companies-and-bond-issuers/>.

## **Structured Engagement and the Role of Proxy Advisory Firms**

Given that the title of today's hearing explicitly addresses the role of proxy advisory firms, I would like to take this opportunity to share how our firm utilizes those services. A core part of Calvert's investment approach is structured engagement with companies and management teams in an attempt to improve both the enterprise value of the firms in which we are invested and address their environmental and social impact. We believe that active ownership is essential for improving one's position as a shareowner and that including engagement as a key element of our process is our duty as responsible stewards of our client's capital.

ESG strategies have often been characterized by the exclusion of certain companies from a portfolio because of either controversial events or objectionable products or practices. At Calvert, we believe it is best to invest as inclusively as possible and work with companies strategically to drive positive change and long-term shareholder value.

Proxy advisory firms, the two most predominant firms being Institutional Shareholder Services (ISS) and Glass, Lewis & Co. (Glass Lewis), play an important role in the institutional investment ecosystem. We are aware that ISS and Glass Lewis provide ESG-related voting recommendations and that these organizations have taken positions related to shareholder proposals on ESG topics.

Calvert views its relationship with proxy advisory firms as one that can be accurately defined as just that—an advisor. We have developed our own customized set of Global Proxy Voting Guidelines, which are publicly available on our website<sup>12</sup>, and outline our approach to voting on critical issues facing corporations. In addition to using a proxy advisory firm to assist in vote execution, we subscribe to custom research services so that our proxy advisor can perform the research necessary to make voting recommendations based on our Global Proxy Voting Guidelines. That said, the decisions on how and when to vote are solely Calvert's.

In an effort to remain as transparent as possible, we also post votes to the Calvert website within 72 hours of being cast and, in almost all cases, in advance of the meeting so that Calvert's clients and the general public can see how we voted on behalf of our clients. During the 2018 Proxy Season, which ran from July 1, 2017 to June 30, 2018, we voted at 4,425 meetings on issues ranging from climate change and energy to board diversity and sustainability reporting.

We believe proxy advisors serve a valuable role in providing research services to the investment industry. Further, the actual process of properly casting votes and maintaining records is transaction intensive and the ability to outsource these functions to specialized service providers provides operational efficiency to the U.S. asset management industry.

Much of the criticism that is directed toward proxy advisory firms in today's policy debate often appears from sources other than the institutional investors that voluntarily choose to utilize the services of proxy advisory firms. Ultimately, we would not favor any additional actions that would compromise the independence of the research and advice we receive from these vendors or impose unnecessary costs or burdens on investment firms.

## **Conclusion**

I would like to again thank the Committee for allowing me the opportunity to share my perspectives on these important topics. My sincere hope is that this forum provides an opportunity for constructive dialogue on how to balance the ongoing competitiveness of U.S. capital markets, investment management firms, and corporations with the need to ensure that our capitalist system achieves the most sustainable future possible.

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<sup>12</sup> <https://www.calvert.com/Proxy-Voting.php>