PRI Open Consultation

SUSTAINABLE FINANCIAL SYSTEM, PRINCIPLES, IMPACT

Submission from Norges Bank Investment Management, August 2016

1) Do you agree that these inclusions and exclusions adequately capture the scope of the financial system that the PRI should focus on?

YES NO

Should any elements be added to the scope? Should any elements be removed from the scope?

See some comments later in the questionnaire. We think the scope is explained well in the consultation document and supporting documents. We nevertheless believe that there are important questions of both principle and practice which need to be assessed further before the PRI takes steps to define a role for itself independent of supporting its signatories' efforts under the Principles, or to redirect its focus to potential signatory or PRI contributions to, or responsibility for, sustainable development impacts.

We welcome the PRI's ambition to support research into the sustainability of financial markets. We think a relevant context for such research is the functioning of markets (including governance or principal-agent type challenges). We understand the objective of the PRI's research ambition to be supporting the development of theoretical and empirical analysis to uncover, investigate and assess potential obstacles to achieving a sustainable financial system. Such a research ambition may over time provide a basis for new insights on financial dynamics and implications and thereby provide signatories with knowledge that can inform their own decisions and priorities. The research should not be premised on an assumption that investors can or should necessarily address all obstacles or inefficiencies. Nor that they have a responsibility to do so.

2) Do you agree that this list, and the more detailed list in the supplementary document, adequately captures the causes of risks and challenges to the development of a sustainable financial system that PRI should address?

YES NO

Should any risks, challenges or causes be added to the current list? Should any risks, challenges or causes be removed from the current list?

We would recommend that the PRI prioritises academic research into the functioning of markets and contributions to financial theory. A literature review carried out on our behalf by the University of Oslo earlier in 2016 (see http://www.sv.uio.no/econ/english/research/unpublished-works/working-papers/pdf-files/2016/memo-01-2016.pdf) in the context of climate change indicates a need for further analysis in many areas. Such research could focus on the key premises upon which priorities and strategies for responsible investors and other market actors, including regulators, rest.

3) Do you agree that the drivers of change identified in the paper are the most important to monitor to ensure the PRI's work remains relevant to the financial system of the future?

YES NO

Should any drivers be added to the current list? Should any drivers be removed from the current list?

The indicated geopolitical and other forces are all interesting. The challenge may be to assess the dynamics between these and the financial system. This is nevertheless an area where the development of new theory to complement existing understanding may be required. NBIM has initiated a programme through the Norwegian Finance Initiative on the 'financial economics of climate change' (see https://www.nbim.no/en/investments/research/the-norwegian-finance-initiative-nfi/nfi-research-programme/).

As written above, we would suggest that the objective for looking at these drivers should be to assess their potential implications in the context of the functioning of markets and any implications thereof. In the design of research questions, this could be the underlying premise – rather than a more direct focus on areas where the PRI and signatories can 'intervene'. Over time, such research may nevertheless contribute to the information set that informs signatories' priorities. We think a premise of 'intervention' by investors on systemic challenges inadequately reflects the roles and responsibilities of agents in the economic and political system.

4) How can the PRI better support signatories to align their responsible investment activities with the SDGs?

By outlining the implications of the SDGs to investors. We would recommend a focus on 4) on p. 16. Investors can promote sustainable development through their responsible investment management. We believe it is out of scope to expect all signatories to align their activities to the SDGs other than perhaps at the very high level. We believe it will be very complex to prescribe meaningful, general, definitive, consistent and practical measures for how such alignment could be achieved that are also suitable for reporting and ranking.

The SDGs give a useful indication of the direction of international efforts to address global challenges. Action taken by governments and companies to promote the SDGs may result in potential investment opportunities and changes to investment risk. However, the solutions to many sustainability-related questions depend on adequate policies and regulation across markets, and face global policy coordination challenges. Investors are not responsible for the SDGs and cannot credibly be made accountable for achieving them. Even in coalitions, investors' ability to directly affect fundamental change – as opposed to incremental or marginal improvements in practices or standards over time – is probably very limited in the absence of supportive policies. Other than at a very high level, it is unclear what consistent or meaningful contributions could be expected from investors, let alone how they would be delivered in practice.

With that said, we do see that as a signatory-led initiative, it could be appropriate for the PRI to dedicate resources to supporting the work of interested signatories in relation to the SDGs. One should nevertheless not assume that alignment of investment activities with the SDGs is equally relevant or feasible for all PRI signatories given differences in size, mandates, asset classes, geographic exposures and investment horizons, among other factors.

5) How can the PRI better capture the impacts and outcomes of signatories' responsible investment activities via its Reporting Framework (e.g. signatory contribution to the SDGs)?

We do not believe the PRI should attempt to do this. Our objections concern questions of both principle and practice.

It is useful and appropriate for investors to set goals, communicate priorities, and as relevant, report on passed milestones or results from their responsible investment management. Activities related to integration of ESG-issues in risk management, investment decisions and ownership activities, as outlined in the Principles, are examples of activities investors may be expected to report on at a given level of detail.

We understand the PRI sees a need for greater accountability from signatories and clearer demonstration of their strategies and activities as responsible investors. However, we question whether assessing and rating 'positive impacts', in the form of signatory contributions to the SDGs or other metrics, is an appropriate role for the PRI/PRI reporting.

The objective of most responsible financial investors is to maximise returns according to their investment mandates. Conceptually, it should be possible to be a responsible investor without linking outcomes of activities to SDGs or other policy goals. All 'SDG-related activities' will not be financially relevant to all investors. Accordingly, using 'SDG-impacts' as a benchmark for measuring responsible investment achievements may give rise to unclear or multiple management objectives.

Steward Redqueen points out that 'the reports and their underlying questions seem to be too detailed and technical.' Attempts to capture impact will add further complexity. We believe it would be challenging to define relevant and consistent reporting metrics across strategies, asset classes and investor types. Investors also engage in other activities not directly linked to the actual investment process. For example, how should one assess the impact of standard setting activities or broader ownership initiatives?

The nature of the financial markets make it difficult to attribute outcomes to individual investors' specific activities. How does one, for example, account for the impact of a listed equity investment? Should the underlying rationale for an investment be taken into account in an impact assessment? Upon making the investment, the investor provides liquidity by accepting the terms of an exchange; also marginally affecting the issuer's cost of capital. If the aim is to measure the impact of an investor's active choices, this could involve a number of assumptions and variables – the appropriate baseline for the investor's choice; the size of the holding relative to other holdings; a deviation vis-a-vis a benchmark.

6) Should the Principles be updated to include a clear reference to the need for signatories to take steps to address broader financial system risks and promote a sustainable financial system that benefits society as a whole, as stated in the PRI's Mission? This could be achieved by adding a seventh Principle, for example.

YES **NO**

Additional comments:

We understand the PRI's reasons for considering such a principle. We nevertheless believe that the argument for amending the Principles works better as a rationale for acting as a responsible investor, in line with the original six Principles to which signatories have committed their support.

It is in our view relevant that long-term investors have a clear interest in well-functioning markets and market outcomes, which over time contribute to sustainable economic, social and environmental development. Many investors may seek ways to address relevant obstacles, and where they deem suitable, promote sustainability more broadly. Investors do not – and are not supposed to – assume responsibility or account for the functioning of markets or market outcomes in a broad sense.

Should the PRI nevertheless conclude that the further consideration of such an additional principle is appropriate, we recommend a thorough process of asset owner consultation, in line with the process preceding the agreement on the original Principles.

7) Can you identify any other revisions that may need to be made to the existing six Principles to ensure they better reflect the responsible investment activities and priorities of signatories?

YES **NO**

8) How would you define success for the PRI in 10 years' time? What metrics should the organisation use to determine whether it has achieved this and what targets should it set for itself?

As noted in the Steward Redqueen report, '[…] it is difficult to be effective and efficient and deliver high quality across so many areas, and concerns were expressed about the breadth of the PRI's activities and the negative impact this can have on quality'. The PRI should maintain its role as a signatory-based and asset owner led initiative promoting the Principles and supporting investors and other relevant actors in their responsible investment activities.

Given this role, the PRI's success should not be viewed or measured on a stand-alone basis independent from the signatories' own work to integrating ESG and other tenets of responsible and sustainable investment in their investment management.

The PRI should be measured on how it fulfils its support, knowledge-sharing and educational tasks, not in terms of any direct or indirect potential impact the PRI organisation itself may have on sustainability issues. In this context, success for the PRI in 10 years could mean maintaining its signatory base and making sure that the organisation provides a platform for signatories to gain access to knowledge, resources and tools to help facilitate the achievement of their own responsible investment goals. Such a primary focus seems aligned with the signatory survey results presented in the Steward Redqueen report.

9) Should the PRI partner with other established reporting organisations (e.g. GRI, IIRC) to develop investor reporting supplements for their sustainability reporting frameworks (as per Steward Redqueen's recommendation)?

YES **NO**

Additional comments:

We think the relevant organisations should develop these frameworks themselves, in consultation with the industry and relevant stakeholders and other partners of their choice. The PRI is one such stakeholder, but we believe the PRI should maintain its present role and focus on promoting the Principles and supporting signatories. As established reporting organisations develop reporting supplements targeted at investors, the PRI reporting framework may, as appropriate, be updated and over time harmonised with, prevailing standards.