



ESG Investment Return Trends: What Does it Mean for Valuation?

Presented by:

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World's Leading Independent
Valuation Provider



1,427

Professionals

including 160 Managing Directors,
dedicated to Valuation Advisory

In 2021 we performed over **10,667**

engagements for more than **3,618** clients

Kroll professionals:

- Serve on AICPA task forces including: Business Combinations, Goodwill Impairment (Co-Chair) and Private Equity/Venture Capital
- Appointed to The Appraisal Foundation's Appraisal Practices Board
- Principal drafter of U.S. Private Equity Valuation Guidelines
- Provided public commentary to the OECD on base erosion and profit shifting action items impacting transfer pricing
- Served as panelists on IFRS and mark-to-market SEC roundtables
- Appointed to the International Valuation Professional Board by the International Valuation Standards Council (IVSC)
- Numerous involvement in IVSC Boards: Member of the IVSC Business Valuation Board, Financial Instruments Board, Tangible Assets Board, Standards Review Board and IVSC Europe Board
- Participant on the EFRAG Advisory Panel on Intangibles

Our Evolution

In Operation for
Nearly 100 Years

STORIED BRAND 1932-2004

- Duff & Phelps founded as investment research firm

NEW FIRM, EXPANDING CAPABILITIES 2005-2020

- Started as valuation and corporate finance advisor
- Rapid growth into other governance, risk, compliance and complementary solutions
- Acquired 30+ businesses, including Kroll in 2018

ONE TEAM, ONE KROLL 2021-2022

- Duff & Phelps rebrands as Kroll and completes brand unification
- Full business life cycle capabilities across risk, governance and growth
- Serving clients in 140 markets across nearly every industry and sector

Carla S. Nunes, CFA, ABV



Managing Director

Carla S. Nunes is a Managing Director in the Office of Professional Practice of Kroll (previously Duff & Phelps). She has over 25 years of experience. In that role, Carla provides firm-wide technical guidance on a variety of valuation, financial reporting and tax issues. She also co-authors Kroll's annual U.S. and European Goodwill Impairment Studies. In addition, Carla is the Global Leader of Kroll's Valuation Digital Solutions group, which produces cost of capital thought leadership content and data housed in the Cost of Capital Navigator.

- In 2011, Carla completed a one-year rotation in Kroll's London office, where she promoted the firm's IFRS education efforts and marketing initiatives, as well dealing with IFRS implementation issues.
- Prior to this role, Carla was part of the Valuation Advisory Services business unit, performing engagements primarily for financial reporting and tax purposes at Kroll's predecessor firms, PricewaterhouseCoopers, Standard & Poor's, and Duff & Phelps.
- Carla has conducted numerous business and asset valuations for a variety of purposes, including purchase price allocations, goodwill impairment testing, M&A, corporate tax restructuring and debt analysis. She has been involved in multiple valuation assignments for a wide range of industries, including pharma & biotech, healthcare, vitamin retail, specialty chemicals, industrial manufacturing and gaming & hospitality. Carla has substantial experience with cross-border valuations, working with multinational corporations to address complex tax, international cost of capital and foreign exchange issues.
- Carla is one of Kroll's experts addressing valuation issues related to cost of capital. She is a co-author of the "Valuation Handbook" series and is a co-creator of the Kroll Cost of Capital Navigator. Carla is a frequent speaker in webinars and conferences on the topics of cost of capital, goodwill impairment and valuation in general.
- Carla is a Kroll Institute Fellow, a Practitioner Director in the Board of the Financial Management Association (FMA) International, and a member of the Education Committee of the International Institute of Business Valuers (iIBV).
- Carla received her M.B.A. in finance from the University of Rochester's Simon School, an honors degree in business administration from Lisbon's School of Economics and Management (ISEG Lisbon) and completed coursework for a Masters of Taxation from Villanova University School of Law. Additionally, she holds a Chartered Financial Analyst (CFA) designation, an Accredited in Business Valuation (ABV) credential, and has passed the exam and fulfilled all the requirements for the Certified in Entity and Intangibles Valuations (CEIV) credential.

Srividya Gopal, CVA, MRICS



**Managing Director &
Southeast Asia Leader,
Valuation Advisory Services**

- Srividya is Managing Director & Southeast Asia Leader, Valuation Advisory Services at Kroll. She set up American Appraisal Singapore operations in 2012, which later got acquired by Duff & Phelps which has now been rebranded as Kroll. She is the Chair for Kroll's Asia Pacific Management Committee and a member of the firm's Global Leadership Team.
- She has 26 years of experience in valuations, transactions and management consulting. She has advised numerous companies on valuations for the purposes of financial reporting, transaction, restructuring, taxation, dispute resolution and financing.
- She is a member of the Business Valuation Board of the International Valuation Standards Council (IVSC), the global standard setter for valuation. She is a former member of the Institute of Valuers & Appraisers of Singapore (IVAS) Council and chaired their Professional Development Working Group. She is a former member of the global Regulatory Board of the Royal Institution of Chartered Surveyors (RICS). She is a member of the Intangible Asset Disclosure Industry Working Group set up by Singapore Government agencies.
- Srividya has advised several global and Asian alternative investment funds including sovereign wealth funds, private equity, private credit and venture capital investors as well as clients across a variety of sectors such as technology, life sciences, manufacturing, consumer products, energy & resources etc.
- Srividya has published various articles on valuation, PE/VC and M&A, and has been interviewed by several television channels, newspapers and magazines. She is a regular speaker at conferences and seminars.
- Srividya is a registered Chartered Valuer & Appraiser (CVA) with IVAS and Member of the RICS (MRICS). She also has a Post Graduate Diploma in Management (equivalent to MBA), is a Graduate of the Institute of Cost & Works Accountants of India and a Bachelor of Commerce.

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Global Developments in ESG and Climate Disclosures

Three Corporate Reporting Initiatives with Potential Global Reach



International Sustainability Standards Board (ISSB)

- Proposed IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information
- Proposed IFRS S2 Climate-related Disclosures



European Union (EU)

Corporate Sustainability Reporting Directive (CSRD)

Proposed European Sustainability Reporting Standards (ESRS) developed by EFRAG



United States Securities and Exchange Commission (SEC)

2022 Proposal "The Enhancement and Standardization of Climate-Related Disclosures for Investors"

Human capital management disclosures proposal expected in 2023

Three Fund Reporting Initiatives with Potential Global Reach



European Union
(EU)

Sustainable Finance
Disclosure Regulation (SFDR):

- Article 6
- Article 8
- Article 9



United States
Securities and Exchange
Commission (SEC)

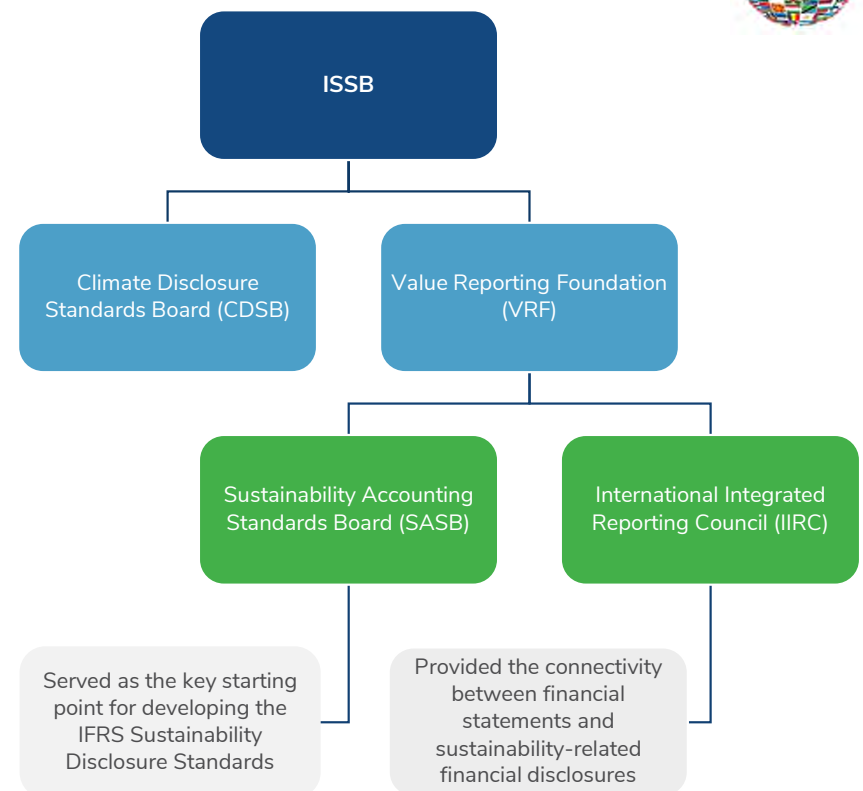
2022 Proposed Amendments
to the Fund "Names Rule"

2022 Proposal on ESG
Disclosures for Investment
Advisers and Investment
Companies

International Sustainability Standards Board (ISSB)



- Created in November 2021, following widespread support during the United Nations Climate Conference (COP27) in Glasgow.
- The IFRS Foundation now oversees two global standard setting boards:
 - (1) the IASB, responsible for international financial reporting standard (IFRS) and
 - (2) the ISSB, tasked with setting IFRS Sustainability Disclosure Standards.
- **In 2022, the IFRS Foundation integrated other independent organizations that had been previously producing voluntary climate, or more broadly ESG and sustainability disclosure standards**
- **ISSB's Objective:** Deliver a comprehensive **global** baseline of sustainability-related (climate and other ESG) disclosure standards that provide investors and other capital market participants with information about companies' sustainability-related risks and opportunities, thereby allowing more informed investment decisions.



International Sustainability Standards Board (ISSB)

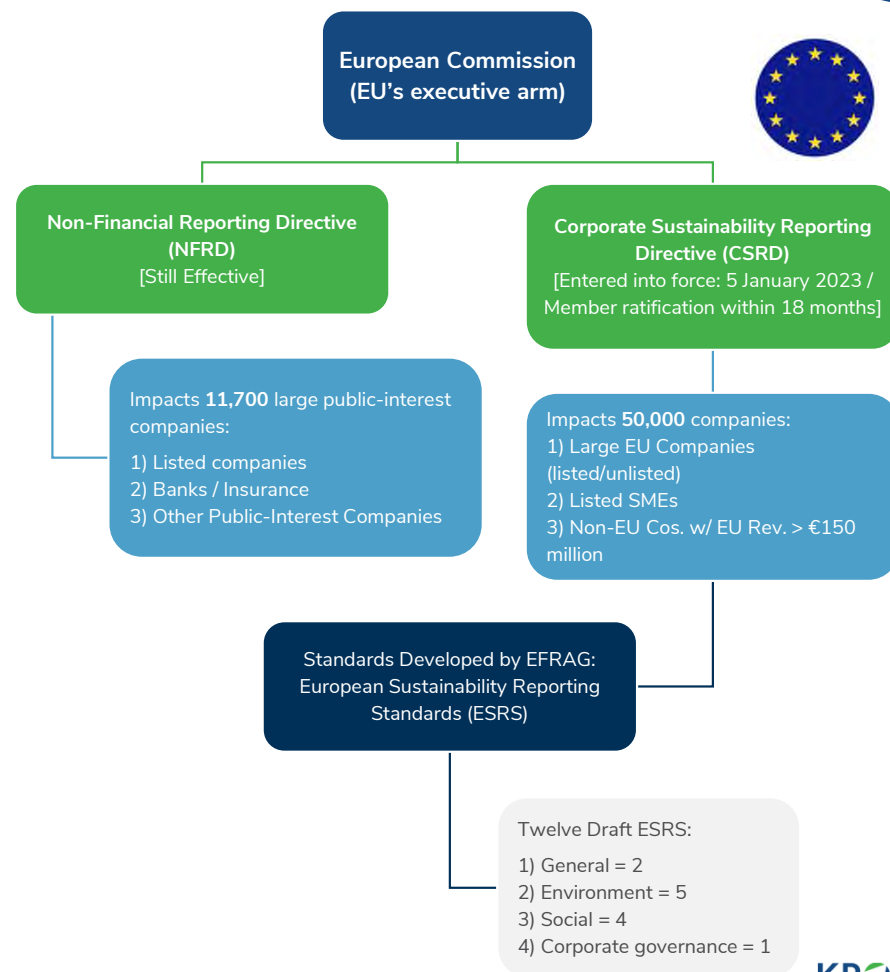


- Published proposed standards in 2022 on:
 - Draft IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information
 - Draft IFRS S2: Climate-related Disclosures
 - Received more than 1,400 comment letters from all over the world and from a wide range of stakeholders.
 - Currently considering feedback and making refinements to the proposals, so that it can start issuing standards this year.
 - The first two standards are expected to be issued in June 2023.
 - Both standards will become effective starting in January 2024 with phased-in dates. This means that an entity would report its first sustainability-related disclosures in 2025, if under scope.
 - Early adoption allowed, but only if an entity applies both IFRS S1 and IFRS S2 at the same time.
 - Additional industry-specific disclosure standards to follow.
- The ISSB is working with a number of jurisdictions to ensure the IFRS Sustainability Disclosure Standards can be adopted and applied effectively around the world.
 - The application of the standards, either voluntary or mandatory, will be predicated on individual jurisdictions' willingness to incorporate them into national laws. Several African, Asian and Latin American countries have expressed interest in adopting.
 - Even if the U.S. or the EU do not adopt these standards domestically, U.S. and EU companies with operations abroad will still have to see to disclosure requirements in jurisdictions where the standards become mandatory.

European Union – Corporate Disclosures

EFRAG

- The rules introduced by the NFRD remain in force until companies have to apply the new rules of the CSRD. Under the NFRD, large companies have to publish information related to: environmental matters, social matters and treatment of employees, respect for human rights, anti-corruption and bribery, and board diversity.
- CSRD introduces more detailed reporting requirements on companies' impact on the environment, human rights and social standards
- The European Commission (EC) will adopt the first set of mandatory standards by June 2023.
- Disclosures subject to independent auditing and certification.
- The rules will start applying between 2024 and 2028:
 - From 1 January 2024 for large public-interest companies (with over 500 employees) already subject to NFRD, with reports due in 2025;
 - From 1 January 2025 for large companies not currently subject to NFRD (with more than 250 employees and/or €40 million in revenue and/or €20 million in total assets), with reports due in 2026;
 - From 1 January 2026 for listed SMEs and other undertakings, with reports due in 2027. SMEs can opt-out until 2028.



United States – Corporate Disclosures

Securities and Exchange Commission (SEC)



- In 2022, the SEC proposed for public comment, “The Enhancement and Standardization of Climate-Related Disclosures for Investors,” amending rules that would require registrants to provide certain climate-related information in their registration statements (e.g., S-1, S-4) and annual reports (e.g., 10-K, 20-F).
- The SEC indicated plans for further rulemaking on human capital management disclosures, with a proposal expected in 2023.
- By the end of the climate proposal’s comment period, the SEC had received more than 11,000 comment letters—a significantly higher volume than it typically receives—from a broad range of constituents, both in favor and against various aspects of the proposal.
- The SEC expects to issue the final climate rules sometime in the fall of 2023.
- The proposed rules would be phased in for all companies, with the compliance date dependent upon the status of the company (e.g., large accelerated filer) and the content of the item of disclosure. As originally proposed, the earliest impact of the new rules would begin to be felt and seen in 2023-2024. However, given that the final rulemaking has been pushed out by several months, the timeline for compliance could also be extended.
- Some attestation would be required.

Scenario Analyses and the Taskforce on Climate-Related Financial Disclosures (TCFD)

- All of the three major disclosure initiatives based their proposed standards in part on the TCFD recommendations.
- An essential recommendation of TCFD is to undertake climate-related scenario analyses to assess companies' resilience to climate change
- Both the CSRD (based on the proposed ESRS) and the ISSB will require companies to use scenario analysis in some form to assess their climate resilience.
- Unclear if the SEC will make it mandatory in some circumstances.
- To the extent a company is subject to either the CSRD or the ISSB, it would have to develop a system to conduct climate-related scenario analyses to meet the associated disclosure requirements.

16%

of Companies disclosed the use of climate-related scenario analyses in **2021**

6%

of Companies disclosed the use of climate-related scenario analyses in **2019**

Based on an AI (artificial intelligence) review of reports from over 1,400 public companies from five geographic regions over a three-year period (fiscal years 2019, 2020 and 2021). Source: "2022 Status Report: Task Force on Climate-related Financial Disclosures", Financial Stability Board, 13 October 2022.

Extra Resources

Global Developments in ESG Disclosures May Have a Significant Impact on U.S. Companies

Valuation Insights First Quarter 2023

By Carla Nunes and Marianna Todorova

<https://www.kroll.com/en/insights/publications/valuation/valuation-insights-first-quarter-2023/global-developments-in-esg-disclosures>

Kroll ESG and Global Investor Returns Study

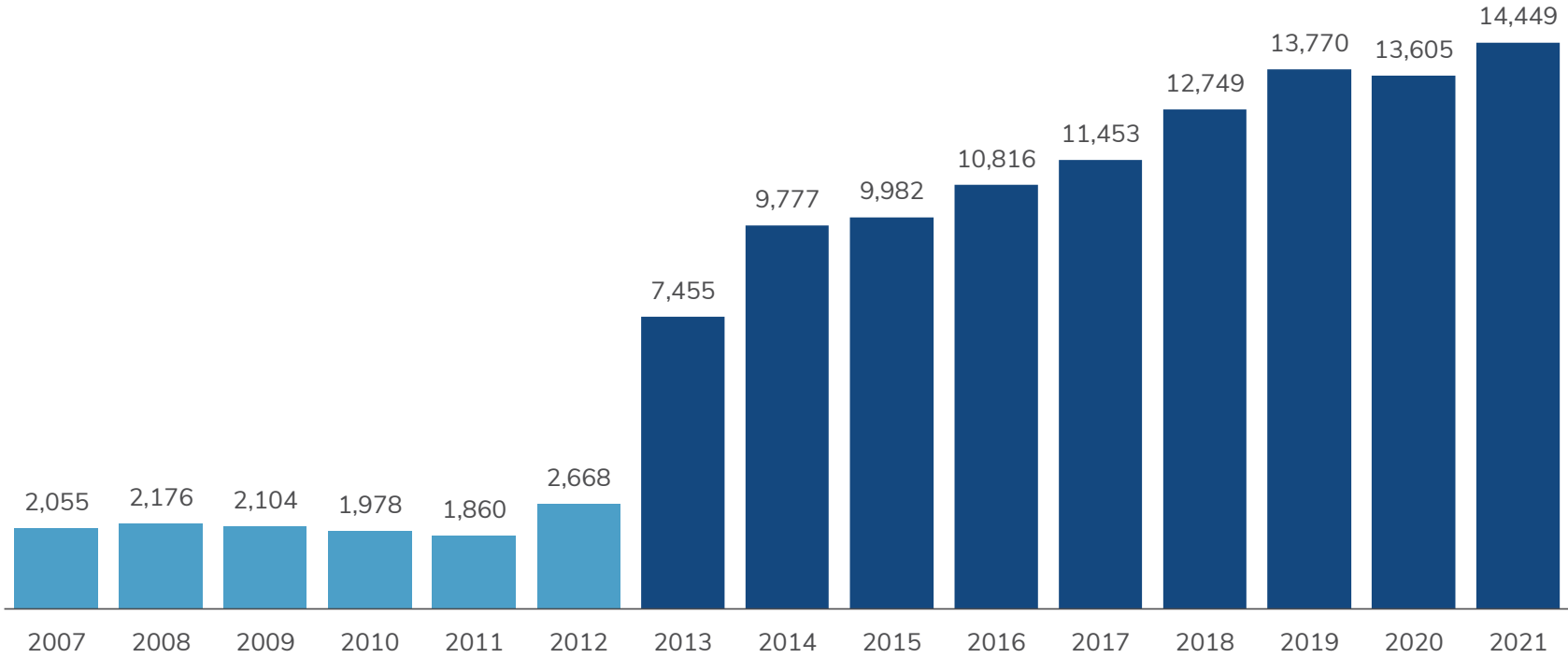
Kroll ESG and Global Investment Returns Study

Executive Summary



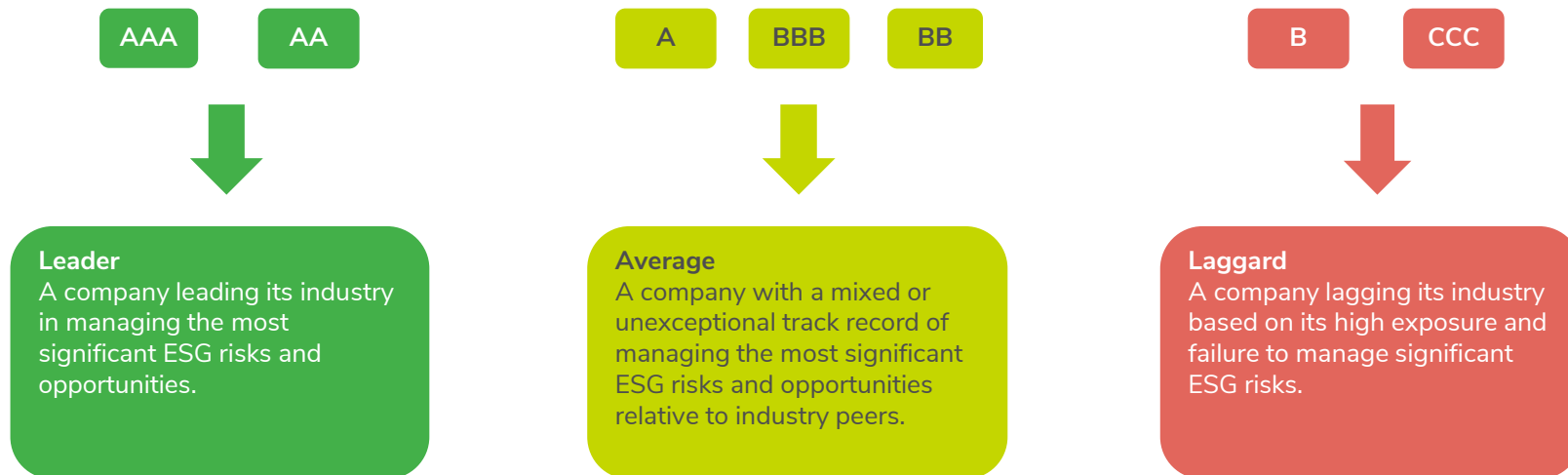
- **Expected Release: July 2023**
- Universe of over **13,000+** publicly-traded companies across a variety of geographies and industries around the globe.
- Investigated the relationship between a company's total stock returns (dividends plus capital appreciation) and its MSCI ESG rating over the **2013-2021 period**.
- Examined **four geographic regions** (World, North America, Western Europe, and Asia Pacific) and **12 countries/markets** (Australia, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Japan, South Korea, United Kingdom, and United States).
- Within some of these geographies, we further scrutinized the results for **11 industries** (as defined by the GICS): Energy, Materials, Industrials, Consumer Discretionary, Consumer Staples, Health Care, Financials, Information Technology, Communications Services, Utilities and Real Estate.

Monthly Average Number of Issuers Included in the MSCI ESG Ratings Time Series



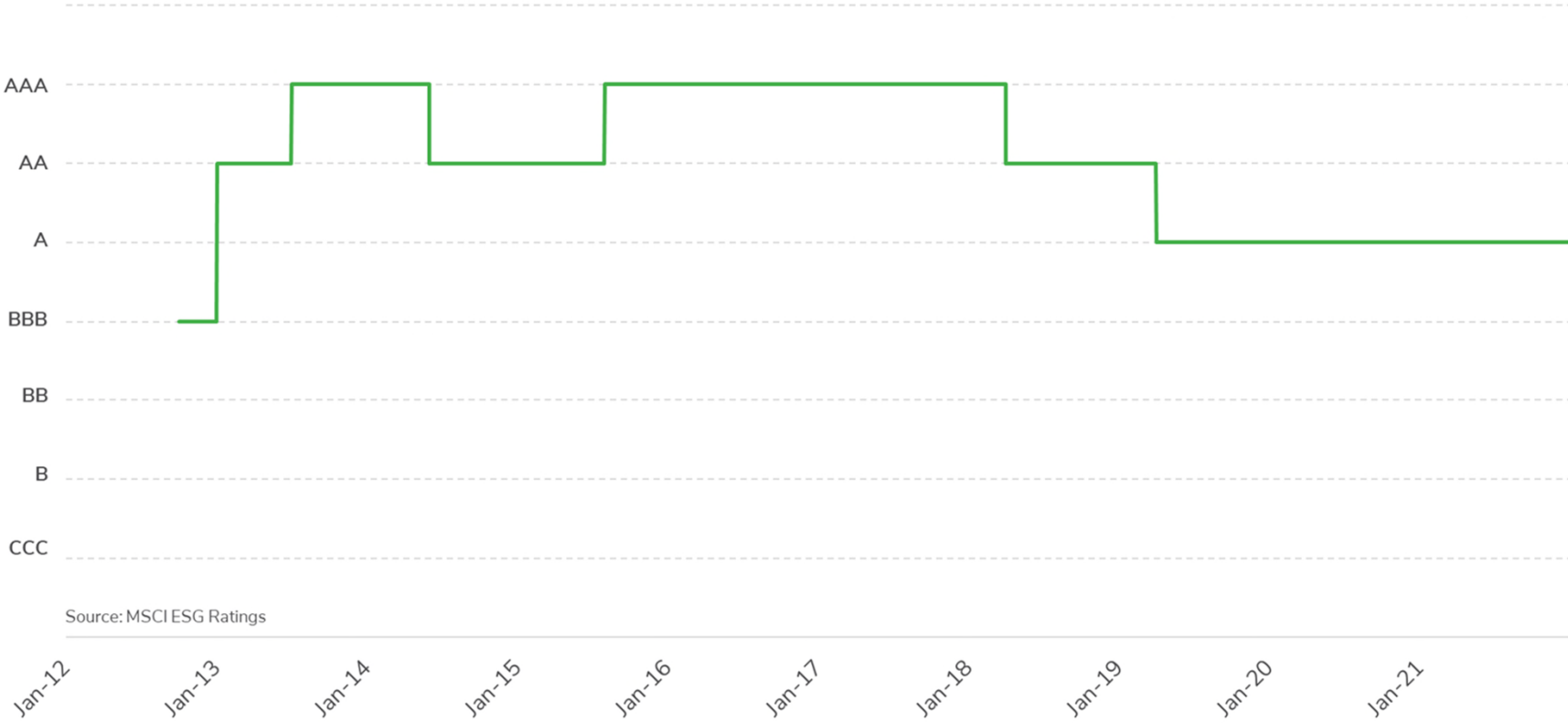
MSCI ESG Ratings System

Not the same as Credit Ratings



MSCI ESG Ratings Over Time

Example: Tesla



Source: MSCI ESG Ratings

Kroll ESG and Global Investment Returns Study

Methodology Summary



- Created portfolios (or indexes) comprised of companies rated in each of MSCI's ESG rating categories and rebalanced them each month over the study period.
- Computed **total returns** (= dividend + capital appreciation) on a monthly basis for each index:
 - Calculated what the cumulative return was for each index since January 2013 through December 2021 (i.e., what would \$1 invested in December 2012 would grow to be at the end of December 2021).
 - Annualized the cumulative returns for easy comparison of one rating category relative to another.
- Index returns are **market-cap weighted** based on the individual companies' total returns in each rating category.
- Returns are denominated in **USD** to allow for comparison across geographies.

Types of Securities Included and Excluded in the Study

Source: Refinitiv

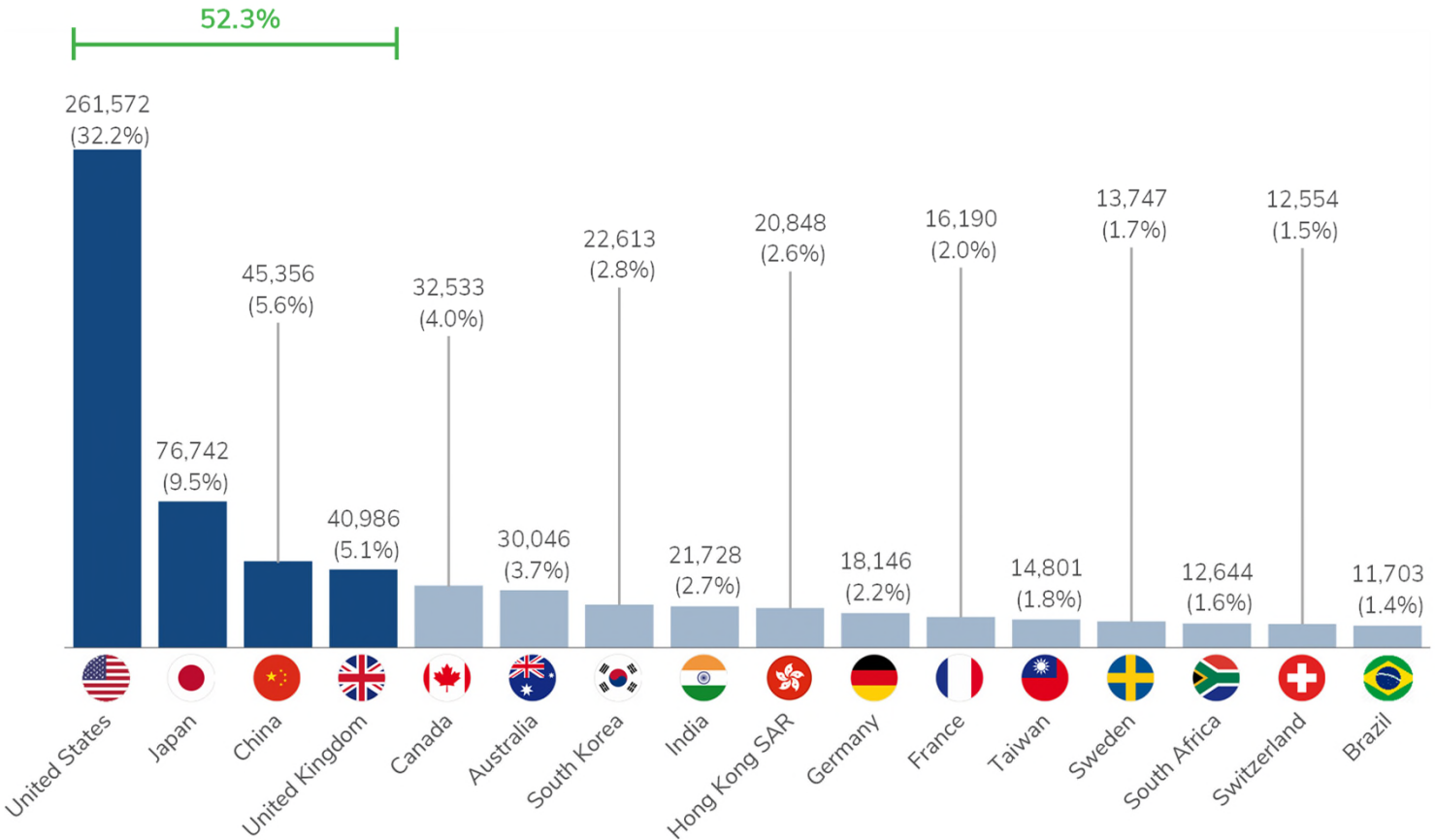


Included	
TRCS Code	Description of TRCS Code
BDR	Brazilian Depository Receipts
CEDEAR	Argentinian Depository Receipts
CHESS	CHESS Depository Interests
DEPOSITSHS	Depository Shares
FULLPAID	Fully Paid Ordinary Shares
ORD	Ordinary Shares
STAPLED	Stapled Securities
ADR	American Depository Receipts
DEPOSITSHS	Depository Shares

Excluded	
TRCS Code	Description of TRCS Code
NA	NA
CAPSEC	Capital Securities (NYSE)
CEF	Closed-Ended Fund
CPR	Convertible Preference Shares
CRTGUA	Guarantee Certificates
CUM	Cumulative Preference Shares
DEBENT	Debenture
DEFER	Deferred Shares
DRC	Depository Receipt
DVR	Differential Voting Rights Shares
ELN	Equity-linked Note
ENHTRUST	Enhanced Trust Preferred Securities(NYSE)
GENUS	Genussscheine
INVCERT	Investment Certificates
ORDSUBR	Ordinary Subscription Receipts
PART	Participation
PARTPRF	Participating Preference Shares
PREFERRED	Preferred Shares
PRF	Preference Shares
REDEEM	Redeemable Preference Shares
RTS	Rights
SAVE	Savings Shares
UNT	Unit

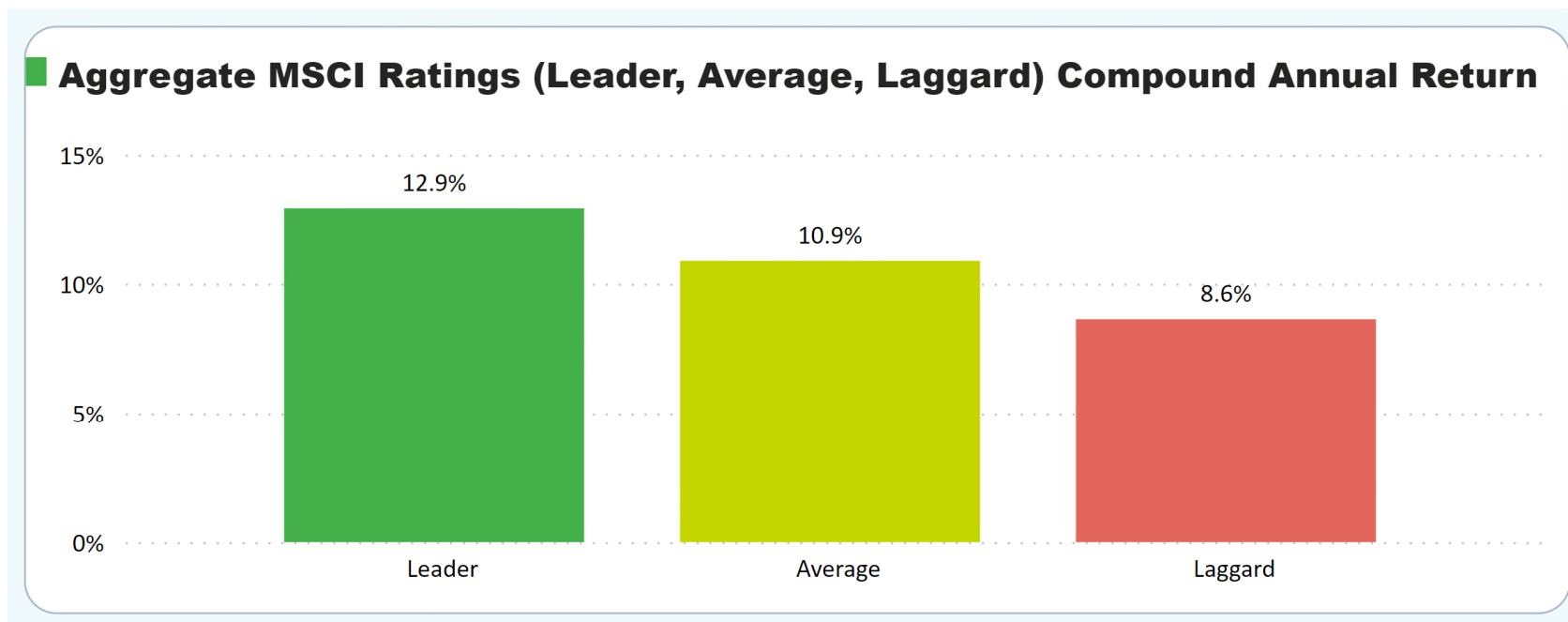
Top 16 Countries/Markets Included in the World Indexes

Number of Firm-Month Observations (January 2013–December 2021)



Kroll Study

High Level Results – World Portfolio



ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is World)

Kroll Study

High Level Results – World Portfolio



Company Count by MSCI Rating (Leader, Average, Laggard)

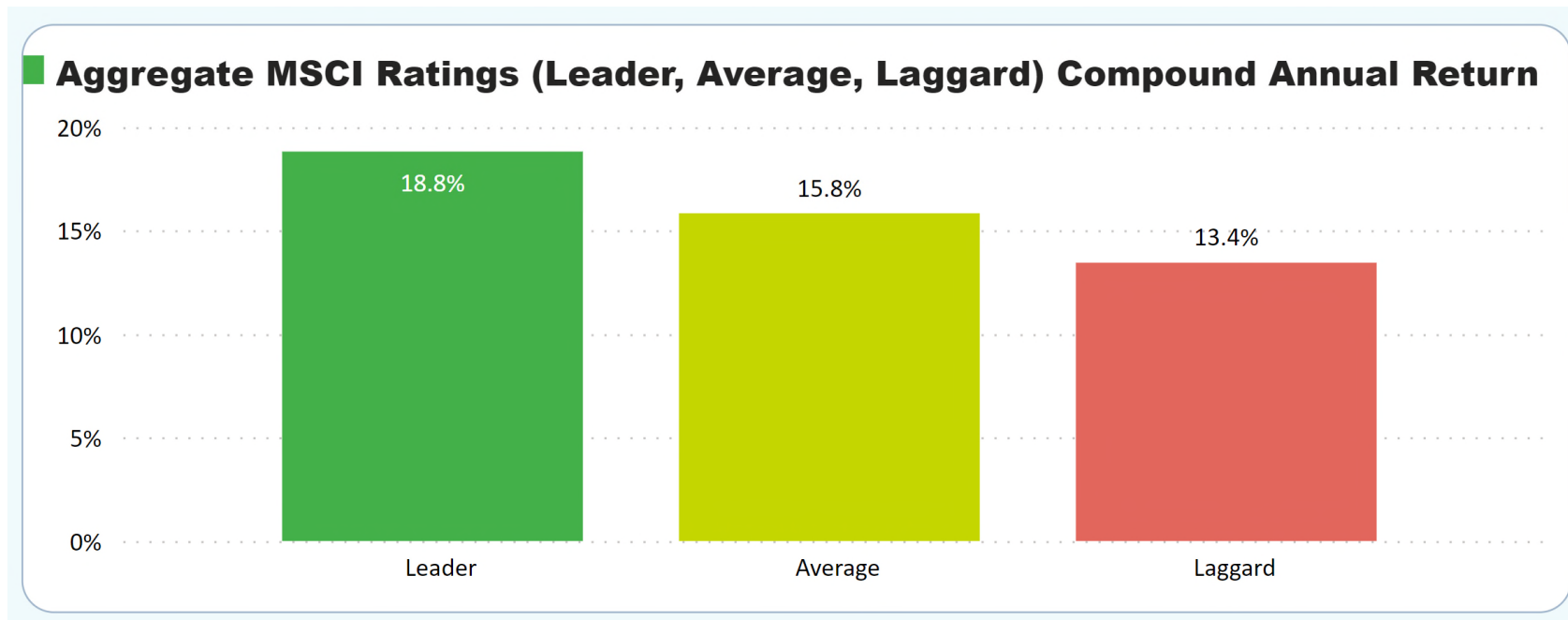
Rating	Company Count (Mo. Avg. 2013–2021)	Company Count (Dec 2021)
Leader	941	1,486
Average	4,780	6,621
Laggard	1,791	2,563

ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is World)

Kroll Study

High Level Results – North America



ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is North America)

Kroll Study

High Level Results – North America



Company Count by MSCI Rating (Leader, Average, Laggard)

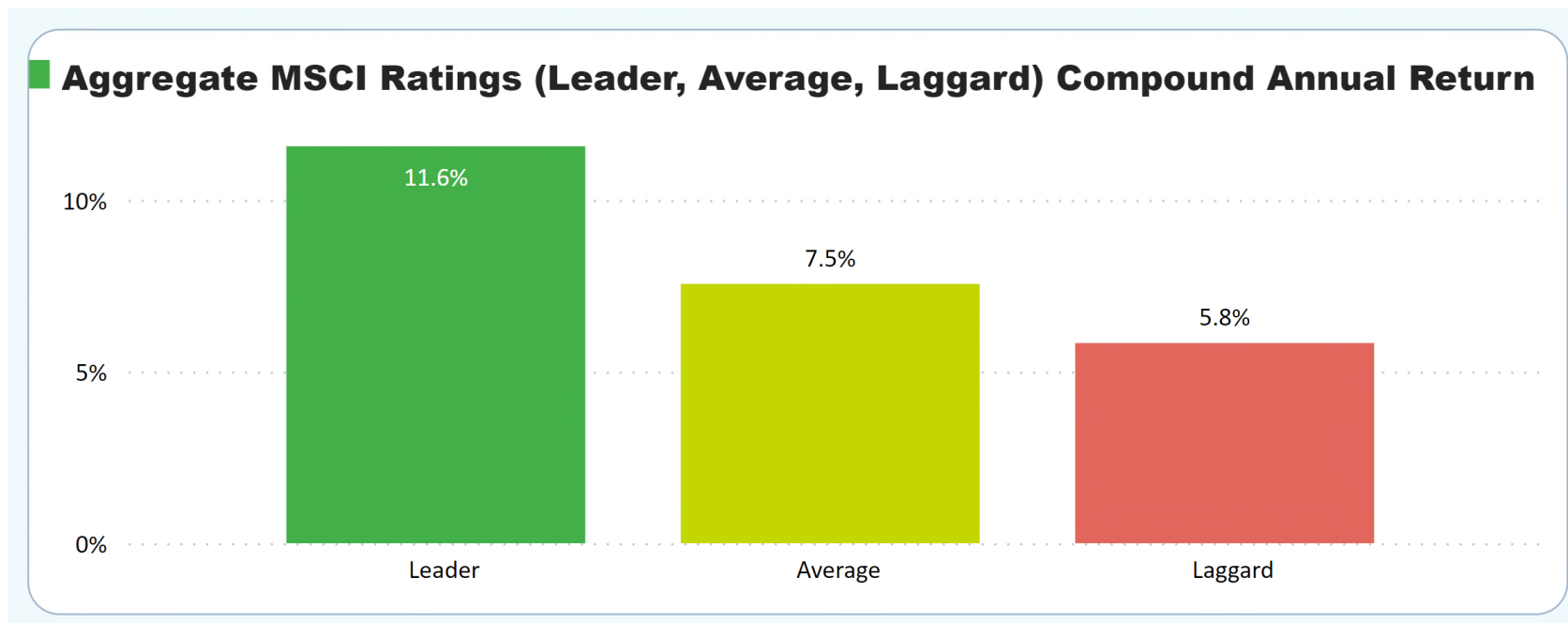
Rating	Company Count (Mo. Avg. 2013–2021)	Company Count (Dec 2021)
Leader	181	312
Average	1,904	2,198
Laggard	639	523

ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is North America)

Kroll Study

High Level Results – Asia Pacific



ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is Asia Pacific)

Kroll Study

High Level Results – Asia Pacific



Company Count by MSCI Rating (Leader, Average, Laggard)

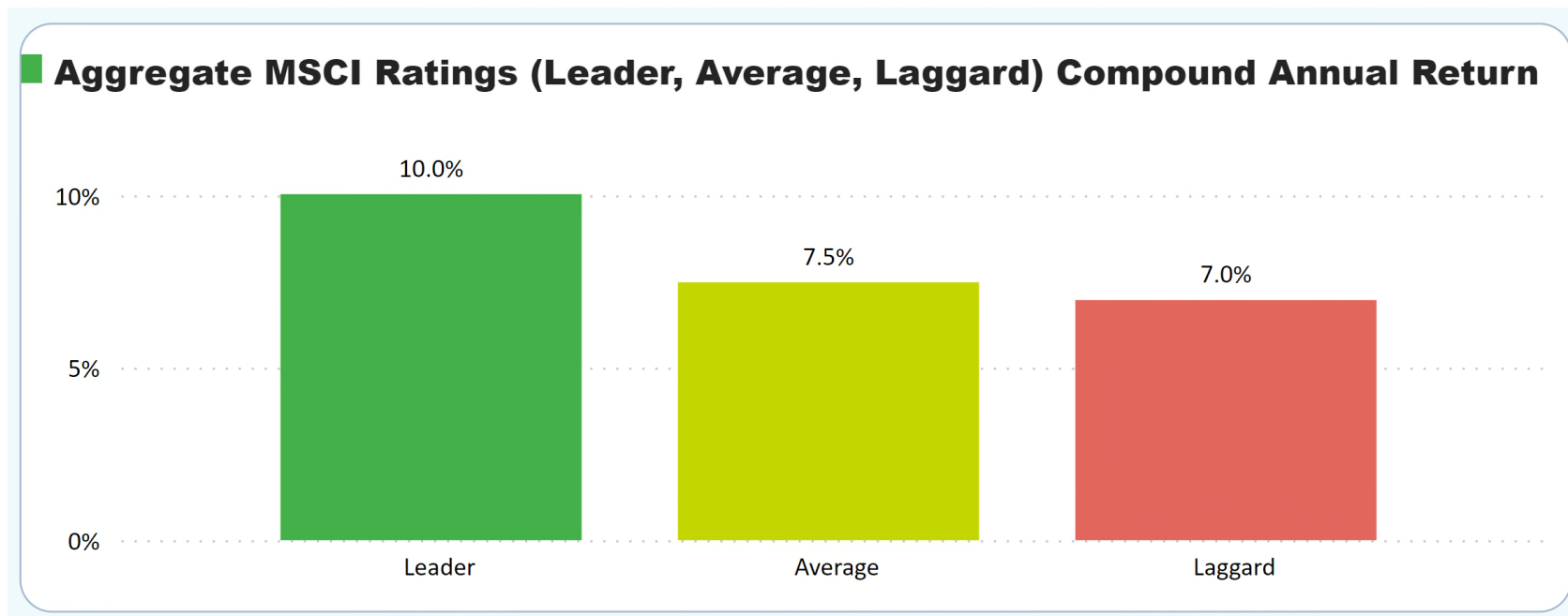
Rating	Company Count (Mo. Avg. 2013–2021)	Company Count (Dec 2021)
Leader	181	266
Average	1,283	2,340
Laggard	769	1,591

ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is Asia Pacific)

Kroll Study

High Level Results – Western Europe



ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is Western Europe)

Kroll Study

High Level Results – Western Europe



Company Count by MSCI Rating (Leader, Average, Laggard)

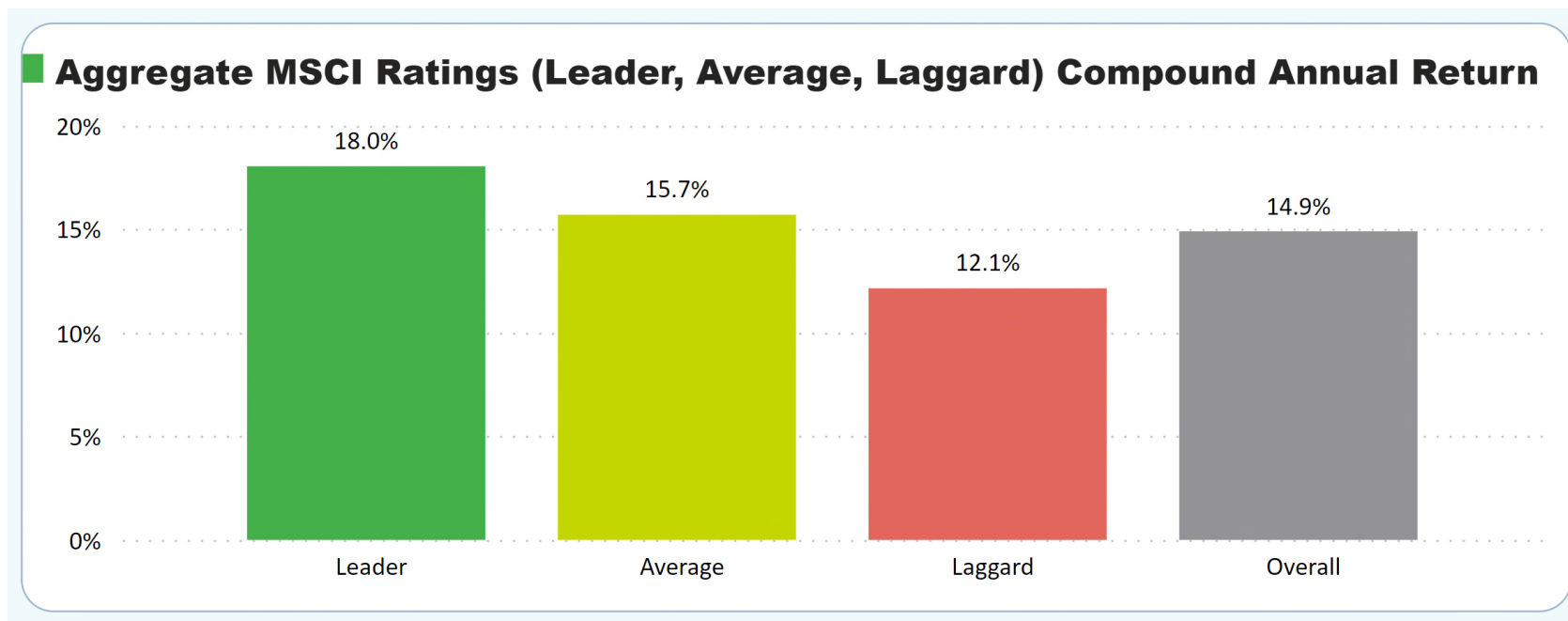
Rating	Company Count (Mo. Avg. 2013–2021)	Company Count (Dec 2021)
Leader	409	655
Average	897	1,152
Laggard	126	122

ESG and Global Investment Returns Study

Filtered by Rating (is Leader, Average, Laggard, or Overall), Industry (is Overall), Region (is Western Europe)

Kroll Study

High Level Results – U.S. Industry Example: Financials



ESG and Global Investment Returns Study

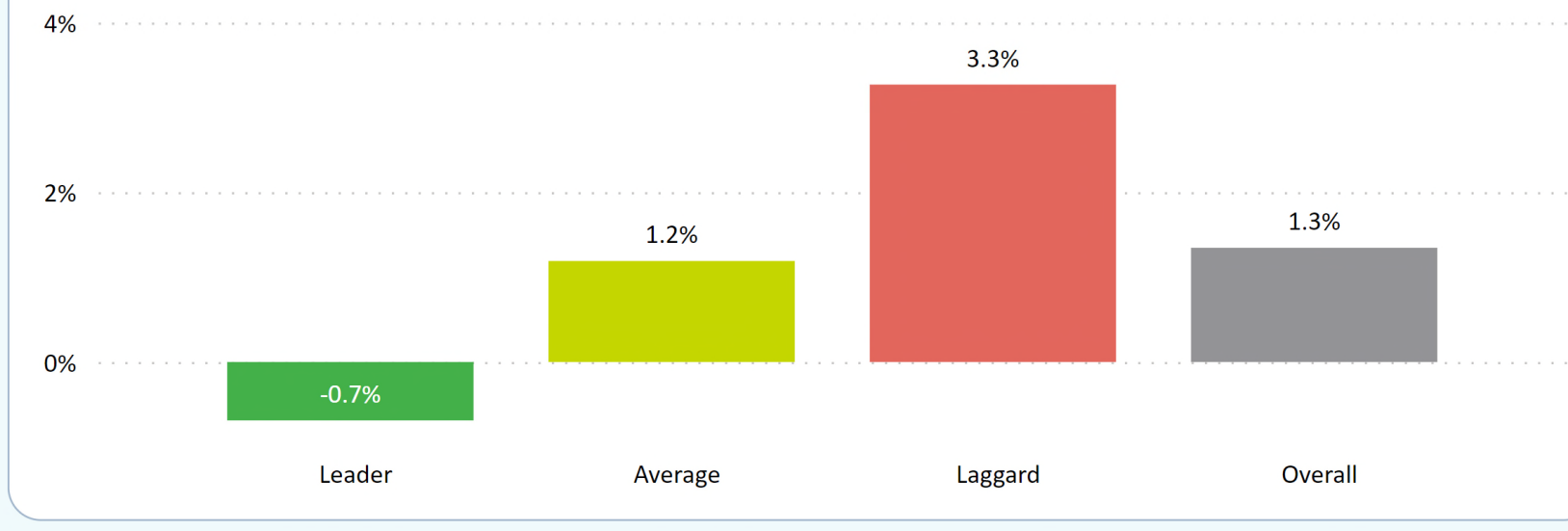
Filtered by **Rating** (is Leader, Average, Laggard, or Overall), **Industry** (is Financials), **Region** (is United States)

Kroll Study

High Level Results – U.S. Industry Example: Energy



■ Aggregate MSCI Ratings (Leader, Average, Laggard) Compound Annual Return



ESG and Global Investment Returns Study

Filtered by **Rating** (is Leader, Average, Laggard, or Overall), **Industry** (is Energy), **Region** (is United States)

Kroll ESG and Global Investment Returns Study

Main Takeaways



- The idea behind ESG investing is that if significant capital is flowing to companies that are considered “good” ESG citizens, they should be able to raise capital at a lower cost (when compared to “bad” ESG citizens).
- From an investor perspective, a lower cost of capital means that investors should expect lower returns from companies with better ESG credentials. However, the Kroll study reveals that companies with better ESG ratings generally outperformed those with lower ratings over the 2013-2021 period, the opposite that theory would predict.
- This relationship holds generally for all the major geographic regions and for most countries in the study. While we have not shared the graphs in this presentation, there are two notable exceptions: Brazil and Germany.
- Focusing on U.S. industries, the best ESG rated companies do not always come out on top. ESG Leaders outperformed Average and Laggard-rated companies in only five out of the 11 industries examined. Leaders still outperformed Laggards in all but three industries: Energy, Healthcare and Communications Services. Outperformance is not limited to the Tech sector, contrary to popular perception.
- **Bottom line:** making an adjustment to Cost of Capital (discount rates) for ESG is not a straightforward exercise – it could vary by industry and country as well as over time.

Kroll ESG and Global Investment Returns Study

Caveats



- As more scrutiny is placed on what constitutes an ESG-focused investment, capital allocations may change the relationship observed in our study.
- Because there are fewer companies with an ESG rating in some countries/industries, the results may not be as meaningful as for broader geographic regions. This is also the case with the more granular results for the seven individual ESG rating categories (i.e., AAA, AA, A, BBB, BB, B, and CCC).
- The study only covers companies that had an ESG rating assigned by MSCI and therefore does not cover the entire universe of publicly traded companies around the world.