Transcript of *bluenotes* podcast interview with ANZ CEO Shayne Elliott and Ethical Partners Co-founder and Investment Director Nathan Parkin

Shayne Elliott

Well as you know, I've been Chief Executive of ANZ for a little over five years and before that I was the Chief Financial Officer for three. And so I've spent eight years really thinking about bank strategy but also talking to a lot of our investors over that period of time. And, you know, there's been a lot of change in eight years but one of the most fundamental changes has been the rise of interest in the whole area of ESG. Eight years ago, it was something people were vaguely interested in, it might come up at the end of the meeting. Today, I would say that most of our meetings start on ESG. And that's why ANZ thinks deeply about ESG and the way it fits in with our own business strategy.

But one of the most respected voices in the market around this whole area of ESG and investment is Nathan Parkin who I'm speaking with today. Well known in the market, in particular for a really successful 12-year stint at Perpetual where, amongst other responsibilities, he had carriage of the Ethical SRI Fund which is recognised by the market with a number of awards. Nathan has operated across the spectrum of the equities market and in late-2017 he and a colleague established Ethical Partners Funds. And I'm really fortunate to have Nathan with me here today. Welcome, Nathan.

Nathan Parkin

Thanks Shayne, I really appreciate the chance to be here and thanks for the introduction.

Shayne Elliott

The whole ESG area has really increased in visibility in the last couple of years. I think in many ways we almost just take that for granted now but it has grown and broadened. It's a broader definition in my mind anyway.

The conversation is far more widespread, it's broken out of the corporate world and it's really mainstream now. Whether that is around diversity, climate change obviously, human rights, and increasingly talking about things like biodiversity. Why do you think that trajectory has escalated so much and so quickly?

Nathan Parkin

Good question Shayne. I really think that the events of the past few years have exposed the cracks. So we're looking at the pandemic, we're looking at various political movements around the world, we're looking at the Black Lives Matter movement and even the recent IPCC report. I think it just became increasingly clear that the pendulum swung way too far in one direction in regards to inequality, opportunity, depletion of resources, financial disparity and a whole bunch of other things. In some ways, that move was way overdue.

I think there is a sense out there that this massive disruption that we've had has given the people around the world this chance to reimagine a different perspective and probably this idea of building back better. A better appreciation for nature, health and also the risks of mistreating those things.

I think the voices of youth are out there particularly loudly at the moment and that's a great thing. You see a whole bunch of other generations listening to the youth and being conscious of leaving a better world for our kids. There's been tremendous technological change and advances here as well that allow us to solve some of these issues. So you know a reliance on fossil fuels that's been around for 50 or 100 years, there are now technologies to solve some of that.

So it's becoming increasingly important I think that businesses incorporate ESG into their normal business planning. it's no longer a side issue that people think about, you know, after work and it would be a nice thing to do. We just think it's increasingly going to be in the middle of a business. And that idea that ESG is philanthropy or something else has moved well into the core of business and saying, "well, how can I use my core business to run things more responsibly or create opportunities or indeed avoid risk". The other aspect of that argument, of course, is that global capital flows are moving out of areas now more quickly than ever before. And this idea that government policy, I mean, we have got a very rapidly changing regulatory regime. But the idea that government policy can, you know, stick a finger in the dike and stop the dam bursting on some of these issues is really being you know, it's probably past that idea. And so capital flows have moved and in some respects, government policies are racing to catch up with that. So we think that the other reason these things have bubbled to the surface so much is that global capital flows are, and have, moved more rapidly than what people thought they might.

Shayne Elliott it's interesting you say that. I mean, there are still those out there - and I get a few emails with this them - that sort of see this as a binary choice. We're either running a business or we're doing ESG and caring about the community and that somehow one comes at the cost of the other.

Now, of course, ESG principles are at the heart of your investment framework. So how do you guys marry up a strong decent returns focus - because you've got to generate returns for your funds holders - with your ESG framework? And how do you how you make sense of that?

Nathan Parkin Well, it's a really good point. We think it's really the same thing. So when we started Ethical Partners, we deliberately made the decision to put ESG factors into our investment process. We think that the companies that are very conscious of being responsible in a social way, in human rights way, in an environmental sense usually have good governance to back that and they're really the same thing. So why wouldn't a more responsible and socially aware business have more success?

And so we felt that marrying up those traditional, fundamental things that investors normally look at like cash flow and balance sheets and interviewing management teams and Boards with some ESG components in the process on how we assess companies was going to deliver good risk-adjusted returns over the longer term. And that's certainly how we've seen that develop. So what are the broad reasons we do that? We think it's about identifying those risks and opportunities, systematically talking to people about their approach to capital and people management. It's those companies that are more aware of future trends in their business decisions, understanding what their customers want and need. And it's understanding the regulatory and legal landscape to incorporate that before there's some radical policy shift that maybe business gets caught off guard.

We think that the successful businesses will do this and increasingly be aware of it. There are so many examples now of those companies that are managing things really well, in this respect, that have created good value for shareholders. And of course, we're all aware of those companies out there that haven't done that, failed that character test and it usually follows through in financial performance and shareholder returns ultimately. It may not do that in the immediate short term, but ultimately, those businesses that haven't paid heed to their customers, the wider community, their employees, their supply chains usually come unstuck over a period of time.

Shayne Elliott In your line of work, I guess there are some industries that you literally just put a line and say they're not for us, right? Without getting into the details necessarily but it would be interesting just to understand the framework you have for how would you make those decisions and what are the kinds of things you look at in determining "hey that industry's just not for us"?

Nathan Parkin Yes, it's a critical area. Not everyone’s ethics are going to be the same so to rule things out on that basis is sometimes a tough choice. But we're looking at what our clients want to invest in. But a lot of our clients don't want their capital invested in some specific industries. They don't want their capital to be supporting growth in those industries, they don't necessarily want to receive dividends from those industries. And everyone's ethics are going to be slightly different but we usually have a pretty good crossover.

So, you know, the industries that we're generally avoiding include fossil fuels and gambling and alcohol and weapons and tobacco and things like that. And we also look at country risks. So we exclude the bottom 30 per cent in our wholesale fund of companies operating in countries where there's a really high level of bribery and corruption risk. We think those things are important for transparency, we think they're important for human rights practice but they'll ultimately be important for shareholder returns at the same time. We think that it's possible - and we've shown this - that you can generate good risk-adjusted returns without supporting some of those industries that our clients are saying, "well, we'd just rather... if we can generate those returns without investing in those areas, we're OK with that". We have funds that will rule some industries off at zero per cent. We've got clients that will rule some things off at 10 per cent of revenue.

But what we do try and do is not take a wholesale approach to things like mining and agriculture. These are some of the hard to abate emissions, high emissions industries in Australia in particular. Ethical Partners has half a billion dollars invested in mining companies and their transition commodities and others that may well be able to mine at net zero emissions. And they are producing really critical commodities for electrifying the world. Agriculture as well. So that is a debate within ethical investing circles, it's a hard to abate area, it's bad but some of those companies are going to be key to solving these issues on a much broader basis than just ruling them out. Some of the companies that we're investing in the agri space are developing technologies and programs that will solve some of the emissions problems for that whole sector ultimately. And so that's really exciting. And for us, it's about that opportunity set as well.

Shayne Elliott Now, of course, one of the beauties of taking a purely financial perspective on investing is it's kind of easy, right? You can get out your spreadsheet, get out your Excel spreadsheet, pump in the numbers and it's transparent, you can apply filters and all sorts of relatively simple numeric analysis.

When you get into this whole area of ESG, it's hard right? It's complicated. And I take the point about industry but even in a good industry, you can have good and bad players to your point about ethics or the way they run. So how do you do that? And then, in terms of disclosures, how do you know? And do you have any views on where you think companies can do a better job with disclosures?

Nathan Parkin Yes. So we have a systematic way of looking at some issues across all the spectrum of ASX companies that that we consider appropriate for investment. We will look at country risk on every business, at human rights risk. And we're thinking about things like modern slavery risks, and so we're looking at transparency around supply chains, we're looking at grievance mechanisms. All of the things that encompass human rights and give consideration to the business. We'll look at environmental - just transition, carbon emissions, targets around some of this. We try to normalise some of those things right across all industries and then we interrogate boards and management teams around, "well, what do you really think? The report says this, what have you done, where are you going with it, what's your understanding of it, how many people on the Board have had sustainability training as one measure?"

I guess the way we try to cut through what might otherwise be called "greenwashing" is to see where people really believe what they say. To the extent that we can marry our practice with policy and reporting, that's critical in how we assess that and how we get to the bottom of some of those areas might just look really great. There have been a number of times where we've sat in front of people and said "your report says this" and they said, "does it?" And it's clear that they haven't really bought into it. Maybe someone in the business has written that, maybe they don't really own the outcomes. So we think that's where traditional meetings with management teams and ESG can really be very, very useful. It's likely the people running a business and a Board will know about the balance sheet and how much debt you have and what your exposures are in a lending sense. But they may not be up to speed on some of the ESG initiatives in the business. And we often see there's some disconnect.

Shayne Elliott I mean, that's the difference with financials, financial reporting is supported by a whole bunch of standards and audits and robustness. Whether companies want to disclose things or not, they're sort of compelled to and to think about things in a certain way, right? And there's standardisation. Now clearly there's been quite a big move around climate disclosures. And we're not there yet but that's clearly taking shape as a more standardised, acceptable way of disclosing. Any thoughts on other... outside climate change or emissions? Gender - I guess we've got some generally accepted ways. Any thoughts on what might be next in that area? Where you think there might or there should be more standardisation around disclosures?

Nathan Parkin Yeah, we think about the future trends and the future areas of ESG that might become more important over time. I mean, diversity within a business - not just gender - but other forms of diversity. We think that will be an important area of disclosure and practice. A number of leading companies listed on the ASX already do that.

We think biodiversity is going to be really critical as well. And whilst that sounds complicated, it's just how you draw on nature to run your business and how does nature affect you. But how do you effect nature? That is going to be an enormous area of growth. And we think, in particular, water risk and use of water. How you affect that, that's going to be an increasing trend as well. And as you say, the climate disclosures and TCFD and other things that may well become standard. Regulation, practice and various boards are rating towards standardisation of some of those things. But the area continues to evolve probably more quickly than any other that we deal with in terms of financial and other types of reporting. This is an area that keeps moving.

Shayne Elliott You personally do a bit across the not-for-profit space and so that idea of giving back is clearly really important to you as an individual - and I imagine, to your firm. How does your work in that space and what that exposes you to? How does that impact your day job as an ethical investor with the Ethical Partners?

Nathan Parkin An important part of setting this business up was setting up your vehicle to give back as we grew from zero. And, you know, the business is well established now, the Giving Fund that we set up - the Tatrai Giving Fund - named after a small Cambodian village that we built a school in many years ago. And that was a really important part of giving back. And it's donated to some tremendous causes. So on youth mental health, malnutrition, domestic violence, child aid, education, human rights, healthcare and family support are some of the areas that we've been able to support.

And just meeting with and interviewing... and we put some of the interviews in the latest annual report that we did for the giving fund. We were able to interview five different people who just spend their life giving to others and doing something really great in the world. And so that's inspiring. It's also personally rewarding to read those and hear from those people and see what they're doing out there. There's a tremendous amount of human spirit in those stories. We've also set up an Ethical Partners "Good Investing" podcast. We interview people ourselves that are good in business and give back in some way and we find that an inspiring thing to do. It's great to meet those people, they continue to drive you and their stories drive us. The way that we will advocate for ESG practices and policies in businesses that we invest in.

So we've taken that idea and it is part of our core business as well. And so, the wight of the money that we manage and we're very privileged to do so can sometimes influence how responsible businesses can be and some of the practices that get introduced. So in a number of ways, we've tried to have that in the business and have it in the giving fund that we launched early on and we plan to grow that every year.

Shayne Elliott Great. Well, that's a great way to finish up Nathan. And I think it really speaks well of your firm, obviously, in the sense of purpose and alignment that you have. And it's great to hear the way you think about these issues. Because in our conversations with our own customers, many of which would be people you invest in I'm sure, this has become an area of great interest to many companies about how they can have a bigger impact in a positive way on the community in which they operate.

And I think in my life as an executive and just in work, it's become much more prevalent and not just acceptable, but actually expected that people do consider their impact on the broader environment and the community etc. And I guess for ANZ it was partly what brought about this whole sense of running a company that is purpose-driven. And we've really seen the benefits of that with our own people and I think we're trying to do a better job in showing exactly what you said - that this is not another thing we do, it's just embedded into our day-to-day business practices. And we're not there yet, we've still got some work to do but I think that's what's really exciting about it.

I love the fact that you talked about - because I say the same thing here - that it's not just about all the things we won't to do. That's actually kind of the easy actually, it's all the things we could do and will do in terms of actually the positive influence we can have through the allocation of capital and our own resources as an organisation to solve meaningful problems for the community.

Thanks very much for your time. It was a great discussion and good luck and I'd love to catch up at some point in the future and talk again.

Nathan Parkin Yeah, that'd be great Shayne. Thanks very much for your time today.

For investor enquiries contact:

Jill Campbell; +61 412 047 448