Wespath
INSTITUTIONAL INVESTMENTS

Wespath Benefits and Investments (Wespath) implements the Sustainable Investment Strategies for investment funds made available through it and its subsidiaries, including Wespath Institutional Investments (WII).

Wespath 'Transition Ready' Strategy—Investing for a Low-Carbon Future

In 2018, Wespath partnered with BlackRock, the world's largest asset manager, to develop a new way of investing for the low-carbon transition. This is a sector neutral strategy that seeks to improve investment performance by tilting toward 'Transition Ready' companies—those preparing now for a low-carbon future. The strategy evaluates companies across all sectors based on their current and planned core business involvement and natural resource management. It recommends investing in companies using natural resources more efficiently, investing in carbon-efficient technologies and adopting strategies to reduce carbon emissions.

The world is changing, and we are investing in the companies that are changing with it.

Kaitlin Bergan, Vice President in BlackRock's Institutional Product Group, interviews Wespath's **Juan Lois**, Manager, Impact Investments, about Wespath's approach to the low-carbon transition and the development of this market-leading strategy.

Juan Lois
Manager, Impact Investments

KAITLIN: Tell us about your role and Wespath's history with sustainable investing?

JUAN: My role at Wespath is to ensure we invest all our assets in a manner that promotes the long-term development of a sustainable economy. To do so, we use a range of tools, including corporate engagement, ESG integration, thematic mandates and negative screening. While these tools have changed over time, sustainable investing is not new for Wespath. Some of our corporate engagements—specifically those related to climate change—date back over 20 years. This stems from the culture at Wespath, where we believe the intentional integration of environmental, social and governance issues into the investment process enhances returns over the long term, and is essential to fulfilling our fiduciary duty.

KAITLIN: What you said about taking ESG into account as a fiduciary on behalf of your clients is so important. Wespath has taken a very proactive stance on ESG integration. In 2017, you published your low-carbon investment belief, which was very market-leading in the industry. How did that come about?

JUAN: Wespath has viewed climate change as a material investment risk for over two decades, and we've been engaging with companies ever since. In 2015, we started to realize that the ability to systematically capture the risks and the opportunities associated with climate change had fundamentally changed. There was now more and better data than ever before. There was more scientific literature, better disclosure and greater investor sophistication in measuring climate risk and identifying investable opportunities.

We realized a more strategic and holistic approach to the low-carbon transition would ultimately enhance the long-term resiliency of our funds. We worked internally with senior leadership and our board of directors to define what the low-carbon transition meant to us and to the funds we manage on behalf of our participants and all our stakeholders.

This belief essentially states that a global transition to a low-carbon economy is underway, and the public policies, emerging technologies and physical impacts associated with climate change are creating winners and losers across companies, industries and countries, impacting investment returns. As prudent fiduciaries, we must assess these risks and opportunities in the management of our funds.

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KAITLIN: What impact did the establishment of the *Low-carbon Transition Investment Belief* have on the management of Wespath funds?

JUAN: Once we established the belief, we analyzed the extent to which Wespath's funds aligned with the belief. The majority of our funds are actively managed. Therefore, we have a series of tools we can use, like manager or corporate engagement, to ensure the analysis of climate risks are incorporated into the investment process.

For passively-managed assets, however, the same tools do not exist. On the passive side, we believed that the risks and opportunities associated with the low-carbon transition were not being properly incorporated into traditional benchmarks. We saw inefficiency in how the market was pricing transition risk.

We wanted to know if there were investment products in the market that were trying to capture this mispricing so we issued a request for information (RFI) to a range of ESG data and index providers and asset managers. We wanted to know if they were thinking about the risks and opportunities of the low-carbon transition in the same ways that we were.

KAITLIN: What were the initial responses?

JUAN: The RFI was based on the hypothesis that companies preparing for the transition to the low-carbon economy by adapting their business lines would be more resilient over the long-term and ultimately better investments. Additionally, we expected a structural shift to occur in energy and resource consumption, where companies with better environmental performance would not only be streamlining the company's operations, but would also be rewarded by the market. To us, that means that a company's progress toward the transition, or its transition-readiness, might indicate future profitability.

When we issued the RFI, we were looking for three things. First, we wanted to gather ESG and climate-related data from a wide range of sources. Second, we wanted the strategy to indicate a company's future preparedness for the transition to a low carbon economy. Third, we wanted a 'transition readiness' framework focused on generating alpha.

The responses we received validated that there was a tremendous amount of data out there. However, the data differed drastically from vendor to vendor, it was often backward looking, and ultimately, it did not capture our fundamental investment thesis around transition-readiness. We needed to partner with an asset manager to build something new.

KAITLIN: How did the partnership with BlackRock evolve to create a custom framework that aligned with your views?

> "A more strategic and holistic approach to the low-carbon transition would enhance the long-term resiliency of our funds."

JUAN: From the beginning, there was very strong alignment in how we were both thinking about the risk and opportunities associated with the transition to a low-carbon economy BlackRock made it very clear that they were focused on both mitigating material financial risk and increasing exposure to climate-related investment opportunities in order to generate alpha.

Throughout the process, there was an exchange of ideas that allowed the strategy to develop in a manner that not only met our three requirements, but significantly enhanced the product along the way. The key to this open and collaborative dialogue was the trust we both established over the long history of our institutions working together.

KAITLIN: Looking ahead, what do you see as the most exciting opportunity in sustainable investing over the next five to ten years?

JUAN: This framework identifies companies that are looking at the world around them and adapting their business models to better align with the future. In doing this, these companies are not only reducing their long-term risk and taking advantage of the various market opportunities, but are also actively driving the change that we need to see in order to solve the many issues we face as a global society. As long term investors and fiduciaries, we all have a responsibility to create and support the development of a sustainable economy.

Doing so will enhance long term prosperity, will invest in the people that make up the global economy and ultimately protect the environment in which we operate.

To learn more about the Wespath Transition Ready Strategy, please read our Press Release at **wespath.com/transitionready/news/**, or contact us at **1-847-866-4100**.

Additional Resources at Wespath.com

- **WII's Investment Beliefs, including our Low-carbon Transition Investment Belief**
- **WII's Climate Change page**

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