

INVESTOR BRIEFING NO. 20

AUGUST 2015

HOW ARE INVESTORS USING THE BUSINESS BENCHMARK ON FARM ANIMAL WELFARE? REFLECTIONS

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Introduction

The third Business Benchmark on Farm Animal Welfare (BBFAW)¹ was launched in London in February 2015. Following the launch of the Benchmark, we surveyed investors on how they have used the Benchmark to date, on how they plan to use the Benchmark in the future and on how the Benchmark might be made more useful to investors².

Our Survey of Investor Opinion

We canvassed investor opinion in four ways:

- We participated in two investor events, a seminar hosted by Morgan Stanley in London on 2 March 2015 and a roundtable hosted by UKSIF and Standard Life Investments in Edinburgh on 25 June 2015. In both cases, we presented the key findings of the Benchmark and we sought participants' views on the relevance of the Benchmark to their investment activities.
- We presented the key findings from the third Benchmark as part of a panel discussion on emerging issues for the food industry at the RI Europe 2015 Conference in London on 2-3 June 2015³.

¹ Nicky Amos and Rory Sullivan (2015), *The Business Benchmark on Farm Animal Welfare: 2014 Report* (BBFAW, London), http://www.bbfaaw.com/wp-content/uploads/2015/02/BBFAW_2014_Report.pdf

² We conducted similar surveys following the release of the first and second benchmarks. See: Rory Sullivan and Nicky Amos, N. (2013), *How Are Investors using the 2012 Business Benchmark on Farm Animal Welfare?* BBFAW Investor Briefing No. 10 (BBFAW, London), http://www.bbfaaw.com/wp-content/uploads/2010/08/Briefing_No10_How_are_investors_using_the_2012_Benchmark.pdf and Nicky Amos and Rory Sullivan (2014), *How Are Companies Using the Business Benchmark on Farm Animal Welfare?* BBFAW Investor Briefing No. 16 (BBFAW, London), http://www.bbfaaw.com/wp-content/uploads/2010/08/Investor-Briefing-No-16_How-are-Companies-using-the-Benchmark.pdf respectively.

³ <http://www.cvent.com/events/ri-europe-2015/event-summary-9e50e57e0c4c4456915b735470f0fa63.aspx>

- We conducted an online survey of the organisations and individuals that have registered on the BBFAW website. In total, we received 15 responses: ten asset managers (Allianz Global Investors, Aviva Investors, BlueBay Asset Management LLP, BNP Paribas Investment Partners, F&C, LGT Capital Management, NEI Investments, Newton, Rathbones, Schrodgers), three service providers (ESG Communications, GES, Stratcom) and two investor networks (ICCR, SHARE).
- As part of the process of developing a collaborative engagement programme on farm animal welfare (see Box 1), we had extensive discussions with the participating organisations about how they use the Benchmark and how they might use the results of the engagement initiative.

We acknowledge that this approach may not provide a completely representative picture of current practice, given that many of the individuals that participated in the events and the survey already had some interest in the issue of farm animal welfare. Therefore, the following findings are best seen as providing a general picture of current activity rather than a completely comprehensive assessment.

Box 1: 2015 Collaborative Engagement on Farm Animal Welfare

In May 2015, seven institutional investors – Aviva Investors, BNP Paribas Investment Partners, Collier Capital, EdenTree Investment Management, NEI Investments, Rathbone Greenbank Investments and Schrodgers – announced that they intended to work with the BBFAW Secretariat to encourage major global food companies to strengthen their management systems and processes on farm animal welfare. In August 2015, the BBFAW Secretariat announced that three additional investor organisations – the Central Finance Board of the Methodist Church, Epworth Investment Management and Triodos – had joined the initiative.

The engagement programme has two objectives:

- To encourage low ranking companies in the Benchmark to adopt robust policies on farm animal welfare, to strengthen their management systems and processes, and to start reporting on their practices and performance.
- To commend the high ranking companies for their performance in the Benchmark, and to provide a clear signal that investors are supportive of good performance on this issue.

The engagement involves the participants formally writing to each of these companies and, subject to resource availability, following up with some further engagement with the companies. The BBFAW Secretariat will track changes in company performance in 2015 and the 2016 Benchmarks.

Key Findings

1. The Benchmark is being used by investors

Most of the investors that responded to our survey have considered how the Benchmark might be used in their investment research. A smaller proportion (approximately half of those surveyed) has used the Benchmark in their company engagement.

In relation to investment research, the Benchmark has been used to:

- Assess the business risks and opportunities of farm animal welfare for companies.
- Provide insights into how companies are identifying and managing risks in their supply chains. One respondent to our survey commented that farm animal welfare can act as a proxy indicator for the overall strength of a company's supply chain management, where poor policies and practices can indicate a higher level of supply chain risk, or indicate that a company is not well-positioned to take advantage of opportunities associated with higher welfare products.
- Cross-check investors' own assessments of companies' sustainability approaches and strategies. It is, however, interesting that a number of investors do analyse company performance on farm animal welfare but do not use the Benchmark in this process. For example, one respondent to our survey commented that they do not use any third party research or indices such as the Benchmark in their investment research, as they prefer to conduct their own research on ESG issues.
- Understand the evolution of farm animal welfare as an investment subject and as a corporate management priority.
- Communicate with internal investment research teams on the investment relevance of farm animal welfare issues.

In relation to engagement, the Benchmark has been used to:

- Prioritise companies for engagement. Investors have used the Benchmark both to identify laggards (i.e. poor performers) and leaders (to understand what has enabled these companies to become leaders).

- Inform investors' engagement with companies, whether on the specific subject of farm animal welfare or as part of wider discussions on sustainability strategy and governance. In 2015, BBFAW produced a short guide on how investors could use the Benchmark in their engagement with companies⁴.
- Underpin the collaborative engagement on farm animal welfare described in Box 1.
- Inform questions at company AGMs, with ShareAction raising the question of Greggs' and Whitbread's performance in the Benchmark at their respective AGMs.

Box 2: Rathbone Greenbank Investment's Approach to Farm Animal Welfare

The core aim of our investment process is to identify companies that are aware of their wider responsibilities and the opportunities that will arise from the need for a more sustainable society. We also seek to understand the social, environmental and ethical issues which are of concern or interest to our clients. Animal welfare, and farm animal welfare in particular, sits at the intersection of these.

As investors, we see a company's management of farm animal welfare as a proxy for how well it is managing overall risk across often complex, global supply chains. A failure to manage these risks can lead to costly product recalls, reputational damage and the threat of tightened regulation should voluntary codes and self-regulation fail. Intensive farming may help to lower prices in the short-term, but the long-term impacts on human health - for example through increased use of antibiotics and growth hormones in livestock, or higher incidence of food-borne pathogens - and associated costs to society are likely to be greater than any short-term benefits.

At the same time, 87% of our clients who have expressed a view on this issue have indicated they would wish to avoid investing in companies with poor animal welfare standards, and a similar proportion are interested in supporting companies which demonstrate good practice. As consumer attitudes change and regulation is tightened, companies are adapting their business models to include higher animal welfare standards, resulting in a wider investible universe for investors concerned about animal welfare.

However, while there has been a marked increase in the number of companies reporting on farm animal welfare issues, there is still significant disparity in the quality of information provided. In particular, there is often a failure by companies to back-up high level statements with specific details. This makes it difficult for investors to properly assess the risks and opportunities associated with individual companies' farm animal welfare practices.

⁴ Rory Sullivan, Nicky Amos and Abigail Herron (2015), *Engagement on Farm Animal Welfare: A User's Guide*. Investor Briefing No. 19 (BBFAW, London). <http://www.bbfaw.com/wp-content/uploads/2015/05/Investor-Briefing-No-19-Engagement-on-Farm-Animal-Welfare-A-Users-Guide.pdf>

The Business Benchmark on Farm Animal Welfare (BBFAW) has proved to be a valuable tool to support this analysis. We incorporate BBFAW's company rankings into our assessment of a company's performance with regard to animal welfare, both from a positive and negative perspective, and also use it to inform our overall evaluation of that company's supply chain risk management. BBFAW's additional commentary on particular sub-issues, such as long-distance livestock transportation, is also helpful in framing discussions with companies and ensuring that we are able to ask the most pertinent questions in meetings.

We frequently make companies aware that we use the BBFAW ranking in our assessment of them and have recently joined a collaborative engagement project utilising the results of the Benchmark. This has seen a group of seven institutional investors write to companies ranked in the bottom two tiers of the index to encourage improved farm animal welfare policies, practices and reporting. The group has also written to top-ranking companies to commend their performance and highlight continued investor interest in this important issue.

Kate Elliot, Ethical Researcher, Rathbone Greenbank Investments

Finally, in relation to client and stakeholder engagement, investors have reported on the Benchmark in the news and reports they provide to clients. Some share this information with those clients with a particular interest in farm animal welfare (and related issues around the food industry). Others distribute the information more widely using the Benchmark and/or their engagement with the BBFAW Secretariat to illustrate their processes for identifying and tracking new and emerging ESG issues.

2. Many investors have yet to use the Benchmark

We are very aware that many investors have yet to take significant account of farm animal welfare in their investment processes or in their engagement with companies. There are various reasons:

- For many investors, farm animal welfare continues to be seen as an 'ethical' rather than a mainstream investment issue. Over the past three years, investors have asked us about the financial significance of farm animal welfare to companies. They have asked, for example, about the costs associated with regulatory compliance, the scale of the opportunities that may result from the adoption of higher standards, and how higher welfare standards translate into higher carcass yields or improved efficiency. We have also been asked about whether investors can deliver investment value through a focus on farm animal welfare (as opposed to ESG issues more generally).

- There is relatively little demand from asset owners for investment organisations to explicitly consider farm animal welfare in their investment processes. A number of investors have commented to us that they would look at farm animal welfare in their investment research and their engagement if they saw demand from their clients to do so. We have received similar comments from ESG research providers who have noted that they rarely get asked about farm animal welfare by their asset owner or asset manager clients.
- The universe of companies covered by the Benchmark is not relevant to all investors.

Suggestions for Strengthening the Benchmark

In response to previous surveys of how investors use the Benchmark, we have made a series of changes. We have changed the structure and content of the main Benchmark report, we have produced two-page company summary documents setting out each company's strengths, weaknesses and areas for improvement and, in 2015, we produced a short guide on how investors might use the Benchmark in their company engagement⁵.

These changes have been welcomed by investors, but we continue to receive further suggestions for improvement. In this year's survey of investor opinion, the most common suggestions were that we:

- Provide a more detailed account of each company's performance.
 - **BBFAW Comment:** *We will seek to improve the two-page company summaries by providing more contextual information on each company's performance. We hope that these changes, together with the short guide to investor engagement, will enhance the usefulness of the information being provided.*
- Make the company profile information more readily available (e.g. through a login on the BBFAW website rather on request as at present).
 - **BBFAW Comment:** *We are planning to upgrade the BBFAW website in late 2015/early 2016. As part of this process, we will explore the feasibility of establishing a section of the website that can only be accessed by investors.*
- Broaden the number and geographic scope of the companies covered by the Benchmark.
 - **BBFAW Comment:** *We have increased the number of companies covered by the Benchmark from approximately 70 in the first two Benchmarks, to 80 in the third Benchmark and to the 90 proposed for the fourth Benchmark. Our expectation is that the Benchmark will eventually cover 100 companies.*

⁵ Sullivan, Amos and Herron (2015) (Note 4).

- **BBFAW Comment:** *In relation to geographic coverage, we started by focusing primarily on companies with a significant presence in Europe. We have progressively extended our coverage of US-based companies and, in the fourth Benchmark, we will cover the three largest food companies in Australia and New Zealand. We then intend turning our attention to the emerging markets and adding to the four emerging market companies currently covered by the Benchmark. We will, as we have done since the inception of the Benchmark, consult with investors on the universe of companies to ensure that we are focusing on companies and geographies that are relevant to them.*

- Provide more information on the business case for farm animal welfare.
 - **BBFAW Comment:** *This is a priority for us. We have received an increasing number of questions about the business case for companies to focus on farm animal welfare. Over the past two years we have produced a number of briefings on elements of the business case (e.g. on the scale of consumer demand for higher welfare products). We have also encouraged the sell-side to produce research on the investment case for farm animal welfare. We have seen some signs of progress, with Morgan Stanley discussing the third Benchmark report in one of its weekly client updates and Natixis covering farm animal welfare as part of a wider report on responsible purchasing in beef, milk and leather.*

 - **BBFAW Comment:** *We have been reluctant to comment on how farm animal welfare issues affect companies' financial performance. We see this as analysis that is best done by the sell-side. Where the sell-side does produce such research, we do reference it in our work and look to bring it to the attention of investors and other stakeholders.*

- Provide more information on key farm animal welfare and investment issues.
 - **BBFAW Comment:** *We regularly produce briefings and other materials in response to requests from investors. Examples include the briefings we have produced on antibiotics, on cloning and on genetic engineering, and a forthcoming briefing on finfish. We actively seek feedback from investors on potential topics, as we want to ensure that the materials that we produce are relevant to investors.*

Strengthening the Benchmark: An Investor Perspective

The Benchmark is evolving into a tool which is of increasing potential value for investors, in instances where the issue of farm animal welfare management are key reputational and supply chain risks for specific companies. The ever expanding universe of companies covered means it is potentially more relevant to a wider set of investors and the larger peer group analysis makes the insights gained more valid. Whilst it is understandable that the Benchmark has initially focused on assessing management practices, the progressive inclusion of the performance component is welcomed and much needed as it is critical for a balanced evaluation.

The reporting of the Benchmark analysis – the summary report as well as individual company data has also been improving – all help to improve investor awareness and understanding of the issue as a potential investment risk, and encourage investors to consider the Benchmark as a tool for measuring corporate practice and performance.

There are some areas where the Benchmark could be made more useful to investors:

- **Accessibility:** by making it easier for investors to access company profile data online, rather than needing to route such requests via the BBFAW Secretariat,
- **Issue materiality:** by adding some background information to the company two-pagers on the scale of companies' exposure to farm animal welfare (e.g. the percentage of their revenues and costs associated with dairy, poultry, cattle etc.), on specific aspects of their exposure (e.g. the location of processing sites) and the company's position in previous Benchmarks.
- **Engagement areas:** by providing more company-specific engagement questions.

My-Linh Ngo, Senior ESG Analyst, BlueBay Asset Management LLP

Concluding Comments

We are encouraged by the feedback we have received. We are pleased that the robustness and credibility of the Benchmark is recognised by investors and we are pleased that more investors are starting to use the Benchmark in their investment research and decision-making and in their engagement with companies. We do, however, recognise that farm animal welfare remains a relatively immature investment issue and that we have a long way to go, even among those investors that are aware of and supportive of our work.

The investor survey has been hugely valuable and we are grateful to all of the organisations that have taken the time to provide us with such useful feedback. It has provided important insights into how the Benchmark is being used by investors, and into how the Benchmark might be made more useful to investors. We intend to repeat the survey again in 2016 following the publication of the fourth Benchmark report.

Authors' Details

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The **Business Benchmark on Farm Animal Welfare** is designed to help drive higher farm animal welfare standards in the world's leading food businesses. It is the first global measure of animal welfare standards in food companies and is designed for use by investors, companies, NGOs and other interested stakeholders.

For more information, go to www.bbfaw.com or contact the Programme Director, Nicky Amos: nicky@nicky-amos.co.uk.