Oil & gas companies create environmental and safety risks every day, and properly evaluating a company’s ability to manage these risks is part of analysts’ job in developing a robust investment thesis. While reporting on these issues improves almost daily, its usefulness unfortunately has not, as methodology, availability and formats vary wildly.

A standardized framework enables financial estimations and potentially creates a self-governing regime. Additionally, the inclusion of this data in investor decks creates the opportunity for a conversation around environmental and safety risks. In addition to our traditional ongoing engagements in the Energy sector, we recently sent letters to upstream oil & gas companies and refiners to request relevant environmental and safety metrics. We expect this data will enhance our evaluation of companies in both absolute and relative terms, not only assessing competitive positioning today but also the ability to create value tomorrow.

**QUALITY CULTURES ARE PERVASIVE**

Financial and extra-financial performance metrics are inextricably linked, with the latter providing important insights on the former. We prefer to invest in companies whose management teams and cultural behavior are less likely to lead to financial injury. Therefore, we look for quality management teams who are responsible corporate stewards of capital. Leadership reinforces culture, inspires execution and creates identity. We believe the definition of quality management includes experienced management teams that make prudent decisions, healthy balance sheets with comfortably more assets than liabilities, and brands free from negative associations. Environmental and safety performance metrics provide critical insights into these characteristics. Integrating this data into our research process enables us to accurately assign a value to a company’s stock, both in absolute and peer-relative terms. We expect the best-run, strategic-minded, resource-efficient companies to outperform over time. We want to reward those companies with higher enterprise valuations.
SMALL ASK, BIG IMPACT

In our open letter, we requested that U.S. energy companies include standardized environmental and safety performance metrics in investor presentation decks, not buried in website links. In other words, our message is: “Don't tell us—show us!”

Specifically, we requested the following:

- Data displayed in investor presentation decks so that it is easily found. These decks are typically the starting point for conversations with stakeholders and have ample, appropriate room for this dialogue.

- Standardized metrics so we can make peer comparisons. We requested carbon emissions intensity, water usage intensity, greenhouse gas emissions and safety performance data from upstream, refinery and integrated companies, as appropriate.

- Data reported over time so that we can see changes.

Most investors would agree that reporting on environmental and safety data instead of financial data would be detrimental. We request companies to provide the data in the investor deck where we learn what a company does and how it operates; it is an easy way to make it available to investors. Additionally, we ask for the information in a standardized format or with explanatory footnotes, just like other data.

Sustainability and corporate citizenship reports are proliferating. Good stewards are likely to attract better business partners and receive preferential consideration to enter communities where they wish to operate. Moreover, shares often see a valuation lift from investors who place a premium on companies that may minimize their industry investment risk. We find this trend extremely encouraging and have been inspired by these reports. However, challenges of access and comparability remain.

FEWER INJURIES, FEWER ACCIDENTS, FEWER LIABILITIES

As investors, we understand we have a fiduciary duty to our clients to be good stewards of capital. To that end, we invest in companies we believe will generate above-market returns over time. From a research perspective, companies with better performance on extra-financial metrics like environmental stewardship and safety will often produce peer-superior financial returns. We choose to incorporate analysis that may be predictive of those returns; the better the safety and environmental records are, the lower the costs of remediation will be. If the goal is a comprehensive review of an investment’s risk/reward profile, analysis of environmental and safety performance should be included, particularly in the Energy sector.

“Thank you for asking about these metrics. We are very proud of our reporting and disclosure, and in fact, we win awards for it!”
- Major U.S. E&P Company CEO

“Frankly, we’ve asked investors about their interest in these metrics, but they seem only to ask and care about the financials, the business case.”
- Major U.S. Oil Company Investor Relations Manager

“It’s nice to be concerned about the environment, but my prospects and clients are sophisticated investors only prioritizing financial returns, not feel-good stuff.”
- Asset Management Salesperson

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THE CONVERSATION HAS STARTED

We believe this information is important, and we are asking. In time, we hope disclosure and discussion of environmental and safety metrics become far more robust. In the meantime, we have started the conversation with companies in our coverage universe. As the world becomes more conscious of environmental impacts, metrics like emissions and water are increasingly becoming critical areas of exposure and risk. Given the physicality and industrialization of these sectors, safety is also a top priority.

The challenge of what data is included and its format won’t be solved overnight. Our initial request for standardized environmental and safety metrics provides a framework for useful analysis and continued dialogue. In time, whether through investor request or government mandate, we anticipate the expansion of environmental and safety data reporting. Our intent is to provide an efficient, meaningful way to start this process.

“How do I get management teams to talk about this unless analysts ask? How do I get analysts to ask about this unless management teams talk about its importance?”

- Chief Sustainability Officer at an S&P 500 Company
RISKS

All investments involve risk, including loss of principal. Certain investments involve greater or unique risks that should be considered along with the objectives, fees, and expenses before investing. The natural resources sector can be affected by events occurring in nature, inflation, and domestic and international politics. Interest rates, commodity prices, economic, tax, and energy developments, and government regulations may affect the natural resources sector and the share prices of the companies in the sector.

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