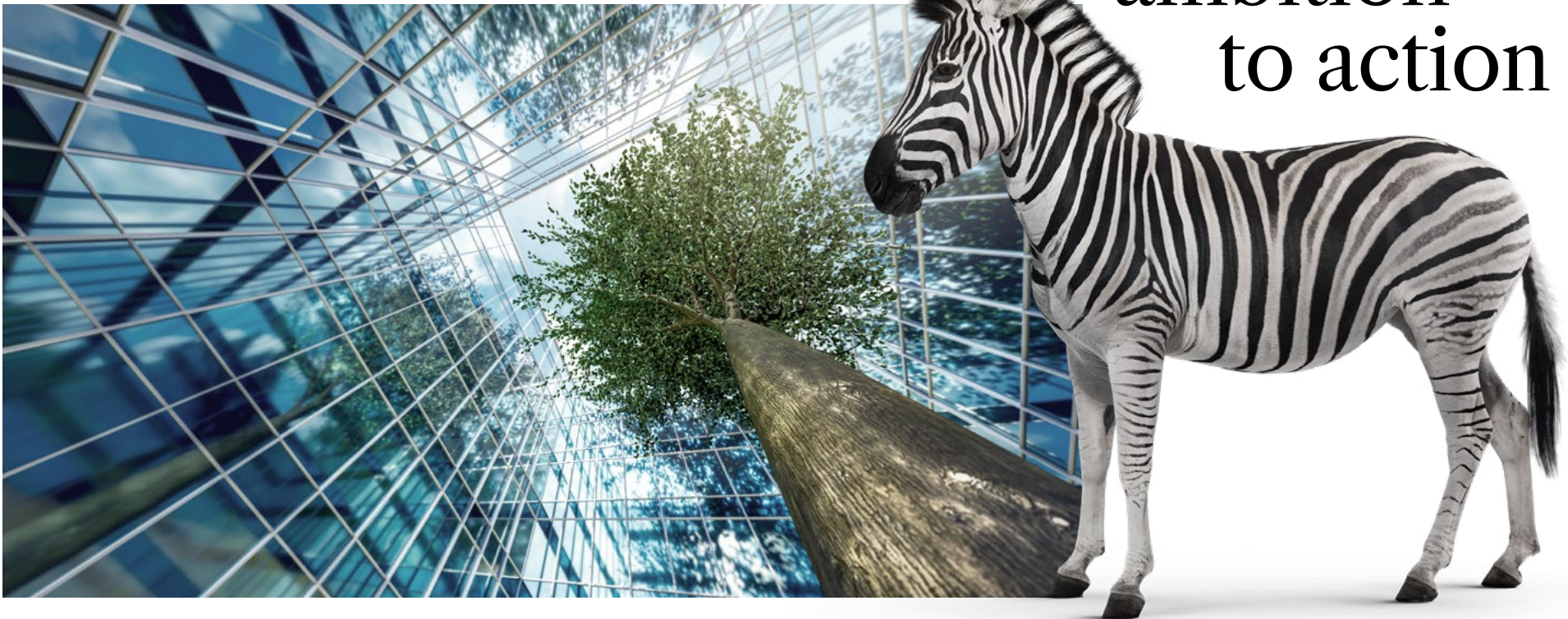


Sustainability:

Report 1 - October 2023

ambition
to action



For mid-market companies with limited resources, how can ESG make a material difference to their growth and long-term viability?



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Foreword

Corporations are now occupied with the task of integrating sustainability and associated ESG considerations into their core commercial strategies. This task has emerged as companies take up their role as responsible corporate citizens and seek to play an appropriate part in addressing the existential challenges we face as human beings. They are also motivated by the fact that such a move will increasingly attract both capital and top talent, as well as be required from a regulatory and governance perspective in the future.

Against this backdrop we surveyed 500 UK company leaders to gain a deeper understanding of the approach they are taking towards sustainability. These companies remain an underserved and overlooked category of the UK economy – a major engine for future growth.

The findings show that mid-market companies are on the right path to incorporate sustainability into their business models, turning their ambitions into action.

Investec's purpose is "to create enduring worth." And one of its core values is to "live in society, not off it." These cultural ideas call on us to regard sustainability as an integral part of our business rather than ancillary to

“ Investec's purpose is “to create enduring worth.” And one of its core values is to “live in society, not off it.”

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it. For over two decades, Investec has been on a journey to understand sustainability in all its complexity and identify how we can have a lasting positive impact on people and the planet, because we've always seen it as the right thing to do.

Sharing these learnings among our network is one way we can make a difference. My colleagues across a range of lending, advisory and treasury teams have been very encouraged by this research and how we help to turn sustainability ambitions into action.

I would like to thank all participants who took part in the survey, and particularly these clients, Banner, Foodspeed, geo (Green Energy Options), Mindera, Morley Glass & Glazing, Piglet's Pantry and RH Amar who have added a rich and pragmatic perspective to the research.

I hope you find this report to be insightful, and we are enthusiastic to continue the conversations about your sustainability journey with you.

Marc Kahn,
Chief Strategy and Sustainability
Officer at Investec Bank plc



Executive summary

With this research, we want to add some depth to an important conversation about Environmental, Social and Governance (ESG) strategies. In a fast-changing landscape, how are the UK's mid-market businesses approaching ESG?

As the only full-service bank for the mid-market, we're familiar with the ESG progress that our clients are making every day. However, we've noticed that in comparison with larger businesses, there is less of a consensus among smaller ones on the solutions to ESG-related challenges, for the smaller ones.

To address this gap, in part one of this two-part series, we have focused on common questions and challenges that are facing the UK's mid-market companies on the topic of ESG.

First, we asked mid-market businesses how they think about the commercial benefits of embracing ESG.

Encouragingly, we found that 70% of respondents are planning or implementing their ESG strategy. Most of the respondents also agree that strong ESG performance will make their companies more attractive: to potential investors, acquirers, partners. It will also help them with financing and re-financing in the future. But how can companies capitalise on a market that increasingly rewards tangible progress on sustainability?

Second, we wanted to learn how mid-market corporates assign responsibility for ESG strategy.

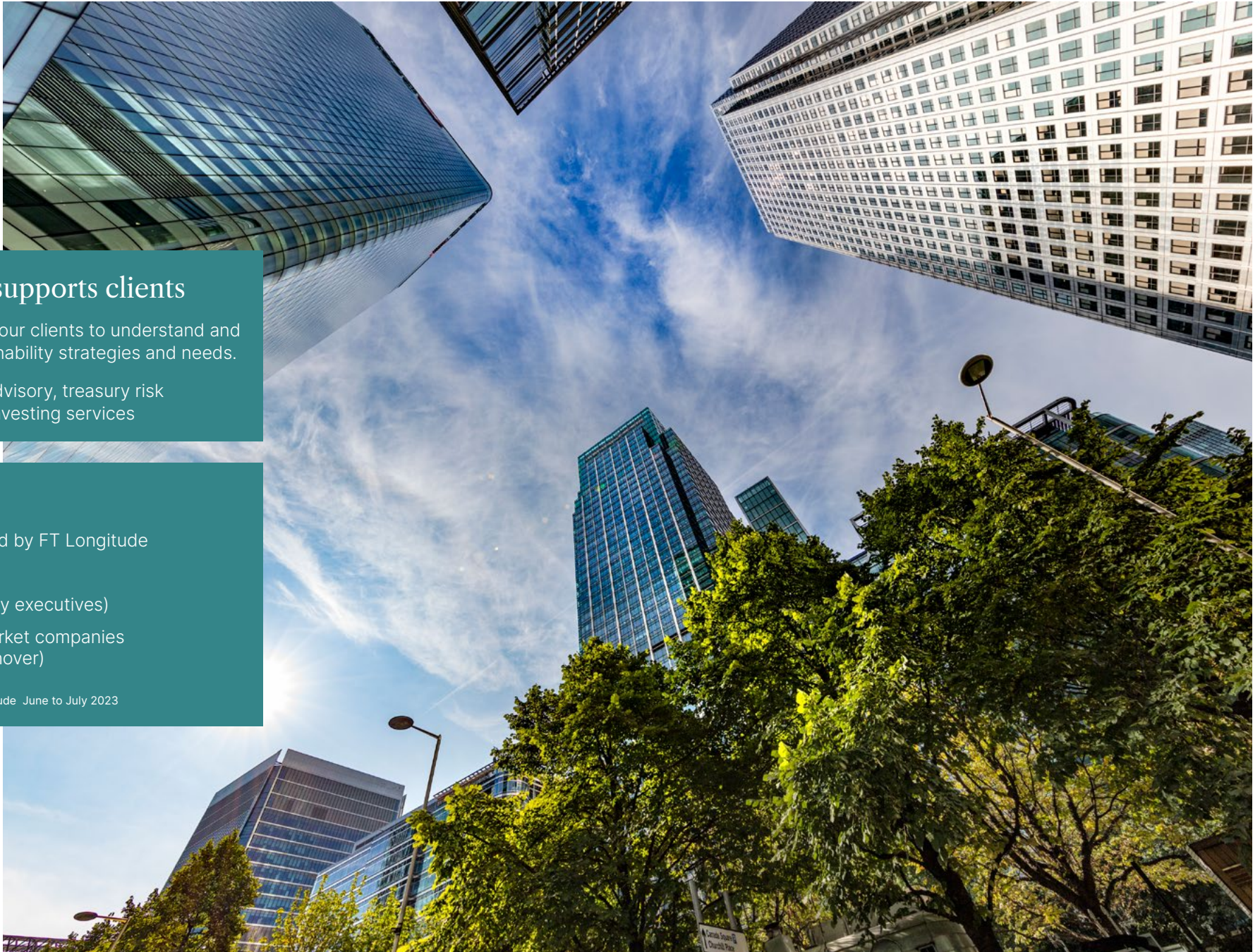
If ESG strategy is not led by the CEO, can it be central to the day-to-day performance of a company? Our research suggests it can. However, it also shows that companies have different approaches – with 24% of respondents saying that responsibility should be shared across the C-suite. We have also looked at the rise of the chief sustainability officer and their influence on strategic decision-making, as well as the benefit of bottom-up, crowdsourced ESG strategies.

Finally, we asked respondents how their ESG strategies are linked to company purpose.

Companies that have implemented ESG strategies are more likely to say that their approach to ESG is aligned with the business principles of their organisation. In fact, our research reveals that 44% of mid-market companies believe that ESG policies and practices can only be implemented when an organisation's purpose is clearly defined.

The importance of a defined organisational purpose appears to be a key success factor for a successful ESG strategy. So, how can leaders ensure that ESG is embedded in day-to-day performance and culture?

We hope that the findings of our research serve as a useful addition to the important conversations that you are already having in your businesses. And stay tuned for part two of our research in early 2024, which will feature case studies from businesses that have implemented ESG strategies.



How Investec supports clients

- We work alongside our clients to understand and align to their sustainability strategies and needs.
- We offer lending, advisory, treasury risk management and investing services

Methodology

- Research conducted by FT Longitude
- 500 respondents
- All C-suite (company executives)
- All from UK mid-market companies (£10m-£250m turnover)

Research conducted by FT Longitude June to July 2023

01

The ESG premium might be more valuable than you realise

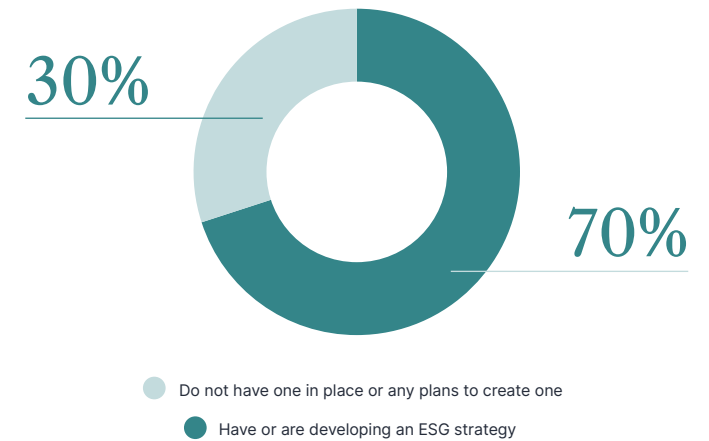
More than half (61%) of respondents also say that without an ESG strategy, they are in a weaker position when it comes to negotiating or renegotiating finance.

According to our research, a majority of UK mid-market businesses say that strong ESG performance will make their companies more attractive to potential investors, acquirers and partners. And more than half (61%) say that without an ESG strategy they are in a weaker position when it comes to negotiating or renegotiating finance. So, are companies doing enough to wide ranging sustainability into tangible value

The survey finds that most companies (70%) are currently planning, implementing or have implemented an ESG strategy. The vast majority of companies that already have an ESG strategy in place expect to see a positive impact on revenue growth as a result.

Joanna Hunter, Founder of food producer Piglet's Pantry, says that a focus on sustainability is significant to her business. "It can only add value to the company," she says. "It goes on the balance sheet in terms of profit and loss. It goes side by side with brand value. It's one of the most important things we talk about nearly every day."

ESG strategies already in place



In the research, those who are implementing, or have implemented, a strategy report a number of tangible benefits:

- 44% say they experienced improved brand reputation
- 39% report operational improvements and efficiencies
- 37% cite a stronger risk management strategy

ESG can open doors to finance

As expectations from banks and investors continue to grow, companies that are ahead on ESG could find it easier to secure funding.

Rishi Madlani, UK Head of sustainability at Investec Bank plc, says that many large UK banks have pledged for their balance sheets to reach net zero by 2050. For some, this involves meeting interim targets by 2030, meaning they will want to work with companies that take their wide sustainability goals seriously.

“There is currently significant finance available for green-labelled assets,” he says. “As we get closer to 2030, there will be more competition for these assets and finance will need to be funding the transition. If banks are going to meet their net zero commitments, they’re only going to be able to finance customers that have similar goals. Access to finance will be predicated on progress.”

One survey of UK-based lenders has shown that 93% expect ESG-related lending in the mid-market to increase in the next few years. A big majority also said that a firm’s ESG status, or its ability to transition to net zero, influences credit risk assessments.¹

For many banks, such as Investec, ESG is a key factor in credit decision-making. In certain areas of lending we use screening processes, such as management and due diligence questionnaires, to understand where a business is on the ESG spectrum, which is then factored in to credit decision-making. Furthermore, margin incentives can be offered to encourage behaviour change. Banks also consider how serious the management team is about sustainability.

Showing that it is a priority is not just important to lenders, but to potential partners too. James Amar, Strategy and CSR Director of food importer RH Amar, says that this means sustainability is no longer an afterthought. “Some of the new business we’ve taken on in the last couple of years is from more ethical brand partners,” he says. “Within the context of a client or partner PowerPoint presentation, the subject of ESG is now at the start of the presentation — not the end. It sets out the stall in terms of talking about our values and how we like to do business.”



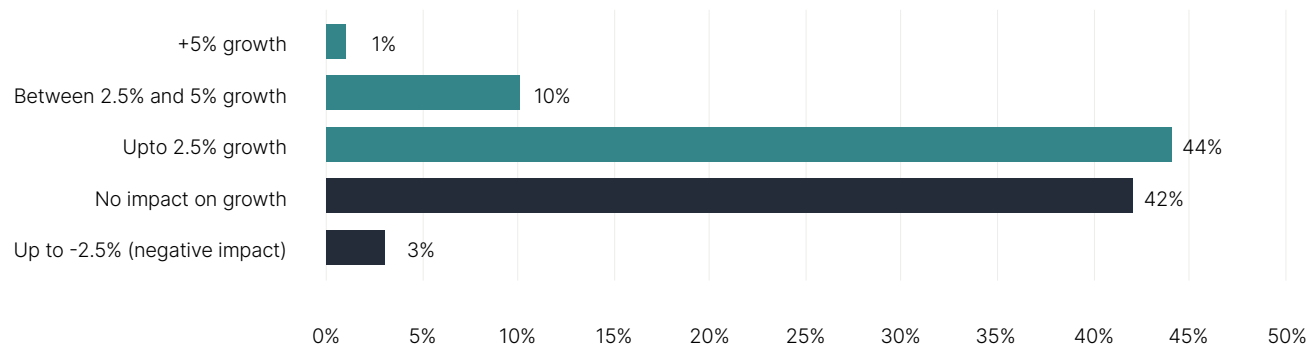
“ Access to finance will be predicated on progress.



Rishi Madlani, UK Head of sustainability at Investec Bank plc

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If fully implemented, what do you perceive as the revenue opportunity of your ESG strategy?



1. <https://www.grantthornton.co.uk/insights/esg-lending-momentum-is-building-for-the-mid-market/>

Investors are looking at ESG

Institutional investors are also increasing their focus on ESG. They are more likely to see companies with strong ESG performance as less risky, better prepared for uncertainty and more successful in the long term.²

In PwC's 2022 Global Investor Survey, more than a quarter of the investors said they were willing to accept a lower rate of return on investment from a company that undertakes activities that have a beneficial impact on society or the environment.³ They also placed ESG-related outcomes, such as effective corporate governance and reduction of greenhouse gas emissions, among their top five priorities for businesses. Another survey by PwC of private equity firms found similar sentiments, and also revealed that an assessment of ESG factors is now standard practice as part of the deal process.⁴

What ESG data are investors looking for? There is no uniform approach, but according to EY analysis, it should be relevant and related to the primary activities of the company and be detailed enough to be comparable to peers.⁵

Steve Cunningham, CEO of Consumer engagement company geo (Green Energy Options), says that embedding ESG reporting into day-to-day operations is crucial to doing it well. "If you're running the process of

reporting separately to what you do in your day-to-day, you'll always fail," he says. "When it's an embedded part of the business, the reporting aspects of achieving and maintaining B Corp, or any other standard, should be no more onerous than other internal processes."

Is it crunch time for mid-market companies?

ESG regulation is developing rapidly in the UK and Europe, and it can be difficult for businesses to navigate multiple requirements - especially the divergence between different markets.⁶

This regulatory pressure can persuade companies to move more quickly on their sustainability strategies, but our research shows that access to finance and attractiveness to investors are also important reasons to press on.

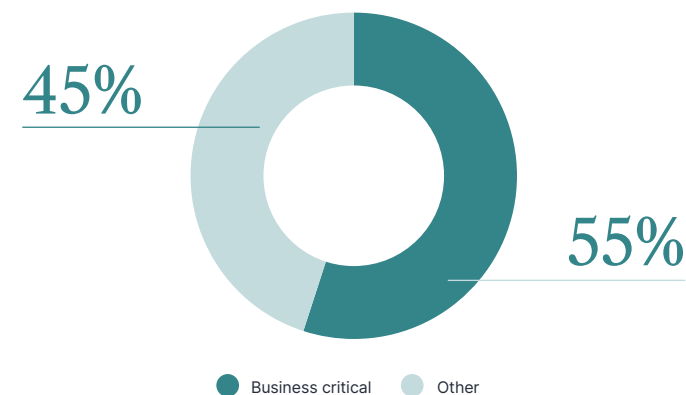
Many mid-market companies already recognise the significance of ESG: 24% see ESG as a sizeable business opportunity, 55% say it is business critical and a similar number say it is fundamental to how a business should operate.

Ian Webb, CFO of schoolwear company Banner, says that leaders should wake up to the fact that ESG progress can be profitable. "Banks and debt providers

Nearly a quarter (24%) see ESG as a business opportunity, while over half (55%) say it is business critical and a similar number saying it is fundamental to how a business should operate.

are starting to write covenants around achievement of ESG objectives," he says. "So it's encouraging that there is cheaper money out there for organisations that do this well. This should obliterate the scepticism around ESG, because there are tangible examples of ESG developments turning into real money and cheaper debt."

Mid-market companies already recognise the significance of ESG



2. https://www.ey.com/en_uk/assurance/why-esg-performance-is-growing-in-importance-for-investors

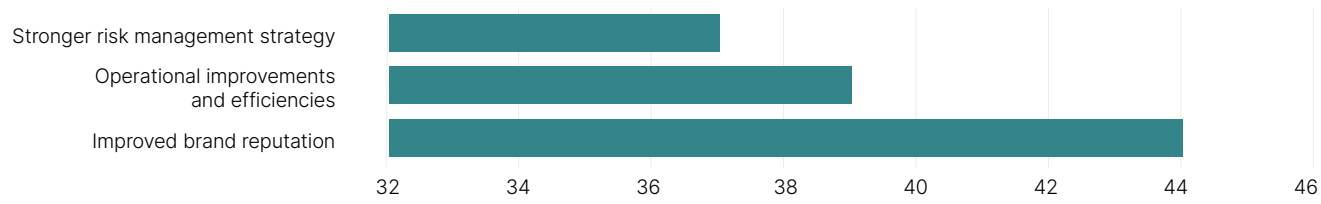
3. <https://www.pwc.com/gx/en/global-investor-survey/PwC-Global-Investor-Survey-2022.pdf>

4. <https://www.pwc.com/gx/en/services/sustainability/publications/private-equity-and-the-responsible-investment-survey.html>

5. https://www.ey.com/en_us/climate-change-sustainability-services/meeting-the-esg-data-needs-of-institutional-investors

6. <https://www.thomsonreuters.com/en-us/posts/esg/2023-esg-outlook-europe/>

In the research, those who are implementing, or have implemented, a strategy report a number of tangible benefits

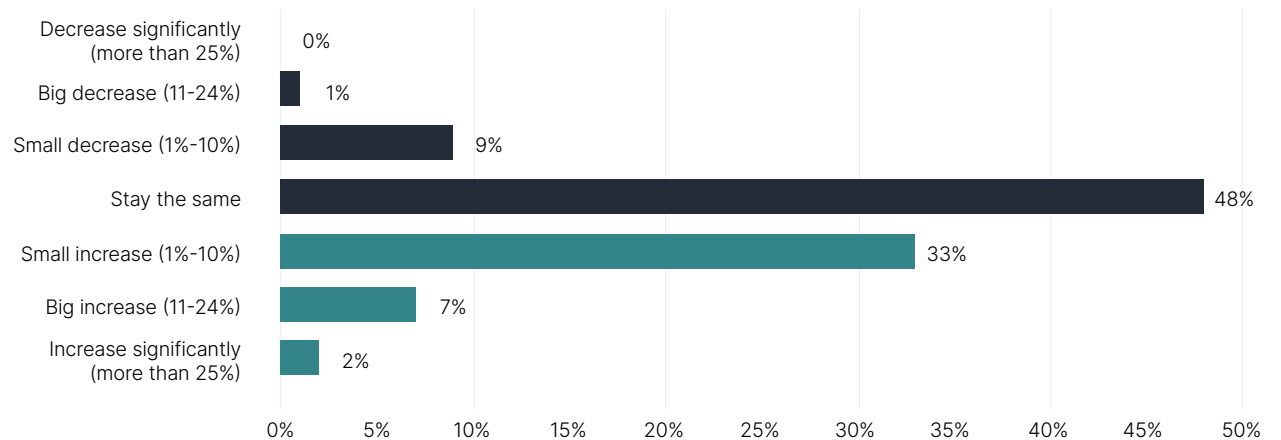


02

Who's really in charge of ESG?

For those (24%) companies that say responsibility is shared across the C-suite, ESG is more likely to be seen as business critical and fundamental to how business should operate compared to those where only the CEO or CSO is in charge.

How do you expect your investment in ESG strategy or implementation to change over the next 12 months?



If ESG performance is fundamental to a company's long-term value, who should ultimately be charged with its success — and who is accountable if it fails?

Regulatory updates such as the tightening of the UK Corporate Governance Code⁷ and mandatory reporting on Scope 3 greenhouse gas emissions⁸ mean there is increasing pressure on mid-market companies to embed ESG into their business models.

Yet there is little consensus about who should be responsible for meeting this challenge. According to our research, CEOs, CSOs and a C-suite collective are most likely to lead on ESG.

For those companies that say responsibility is shared across the C-suite (24% of those surveyed), ESG is more likely to be seen as business critical and fundamental to how business should operate than companies where the CEO or CSO is in charge.

So, is there a right - and wrong - candidate for the job? Or is the task of embedding sustainability too complex and costly for a single person?

7. <https://www.grantthornton.co.uk/insights/the-corporate-governance-code-and-financial-services/>
8. <https://www.edie.net/british-companies-not-ready-for-eus-scope-3-emissions-reporting-mandate/>

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Being in charge of finance and sustainability means we can take a balanced view of the two, which is hugely helpful to the organisation.

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Ian Webb, CFO, Banner

Pooling resources

Given that ESG affects financial performance and influences supply chain and reputational risk, the CFO - who leads strategy at just 7% of organisations surveyed - can play a pivotal role.

Concepción Galdón, Vice-dean for business with purpose at IE Business School, says that companies should consider combining responsibilities. “As a medium-sized company, you need to be very pragmatic and use existing resources and channels,” she says. “Combining a sustainability role with the role of finance chief, for example, is smart because you can use existing processes to capture financial data. You are adding new variables to existing budget conversations.”

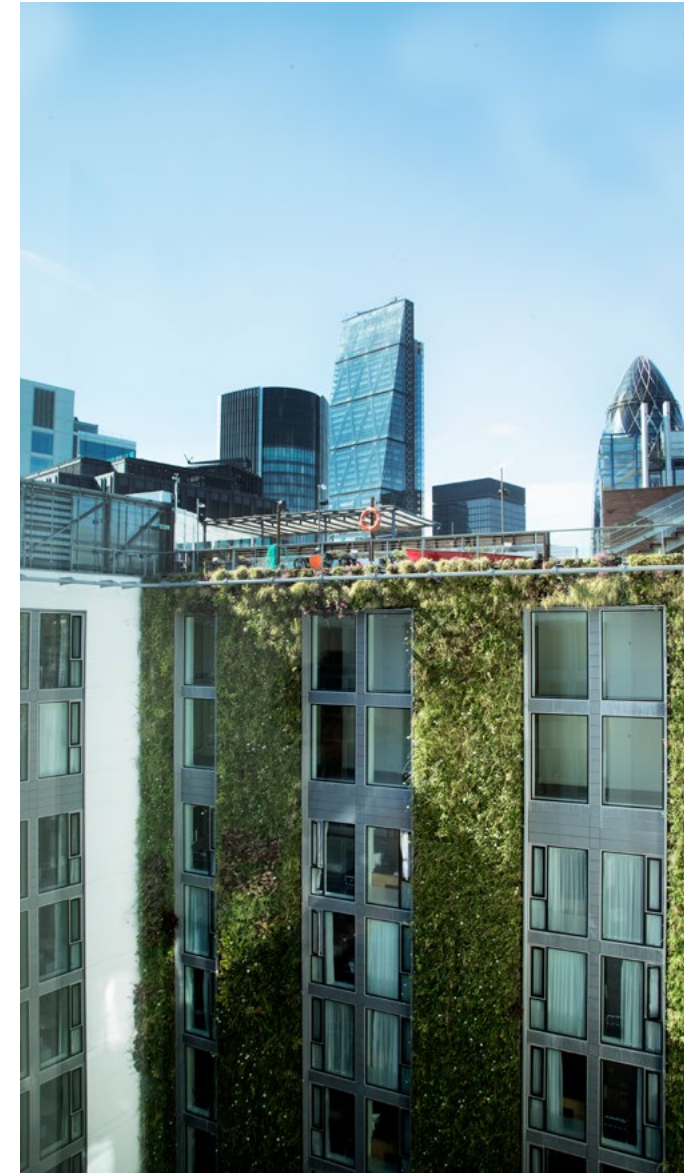
For Banner, combining roles helps to avoid strategic and operational conflict. “Being in charge of finance and sustainability means we can take a balanced view of the two, which is hugely helpful to the organisation,” explains CFO Webb. “It drives out any binary views that it’s one versus the other.”

Should companies appoint a sustainability chief?

In our research, 18% of mid-market companies say the CSO takes responsibility for ESG. This compares with 37% of large companies that have a CSO.⁹

Appointing a CSO is becoming more commonplace. In the US, 81% of Fortune 1000 companies have one within their leadership hierarchy,¹⁰ which could be because stakeholders are starting to expect it.¹¹

But should mid-market companies follow this lead? In a Deloitte study of financial services firms, some respondents thought they were ‘too small’ to appoint a CSO, implying that the role may be required as the firm grows.¹²



9. <https://www.pwc.co.uk/press-room/press-releases/uk-firms-turning-to-chief-sustainability-officers-as-board-level.html>

10. https://www.ey.com/en_us/sustainability/sustainability-and-esg-trends-index

11. <https://www.pwc.com/gx/en/corporate-reporting/assets/pwc-global-investor-survey-2021.pdf>

12. <https://www2.deloitte.com/content/dam/Deloitte/bg/Documents/financial-services/gx-fsi-future-of-the-cso-report.pdf>

Direction from the CEO is a must

When a business appoints a CSO or combines roles, it should consider reporting lines. When the CSO reports directly to the CEO, it tells regulators and investors that the company considers its sustainability goals to be a strategic imperative.¹³

For a quarter (26%) of the companies in the research that are pursuing an ESG strategy, the chief executive is ultimately responsible.

Callum Bell, Head of lending and co-head of private equity at Investec, says that the CEO can influence adoption of sustainability across an organisation. “The chief executive should be leading,” he says. “The buy-in of the chief executive is key. “Like any strategy, when it has buy-in from the top it has better prioritisation and focus to enable a successful implementation and to best capture the growth opportunities. There will be an increasing trend of hiring chief executives who can point to a proven track record of embedding ESG into their strategy.”

“ Like any strategy, when it has buy-in from the top it has better prioritisation and focus to enable a successful implementation and to best capture the growth opportunities. There will be an increasing trend of hiring chief executives who can point to a proven track record of embedding ESG into their strategy. ”

Callum Bell, head of direct lending and co-head of private equity client group at Investec Bank

What is the role of the board?

The company board is ultimately responsible for long-term success, so it needs to have oversight of ESG strategy and play an active role, ensuring that sustainability objectives are an integral part of discussions with the CEO and executive team.

More than half (54%) of FTSE 500 companies now have a board-level committee focused on ESG.¹⁴ This approach allows ESG considerations to be overseen by a smaller group of board members who have relevant knowledge and skills. This pooling of knowledge and best practice can come from other sources, too. For smaller companies, it may not be non-executive directors who provide this counsel, but industry groups, local networks and peer organisations.

The chief executive, finance chief and CSO are all sensible candidates to lead on ESG, depending on the company’s needs and size. But even with a single leader

in place to lead progress, each senior manager will need to play an active role in embedding sustainability throughout the organisation.

Banner’s Webb agrees that every part of the organisation should focus on ESG. “One of the most impactful parts of driving our agenda forward is having a team of colleagues who are advocates for green initiatives,” he says. “Every manager in our organisation has a sustainability goal in their annual objectives and appraisal, so it’s woven into what we do.”

Ruth Leas, CEO of Investec Bank plc, notes that we make ESG part of the ‘exercise’ of daily activity, whether that’s liquidity requirements or return on equity. “It’s integrated into the way of thinking,” she says. “This behaviour has been paid forward across the leadership team and is reflected in the nature of the leaders we look to hire.”



13. <https://www.gartner.com/en/articles/does-your-organization-need-a-chief-sustainability-officer>

14. <https://www.thecorporategovernanceinstitute.com/insights/news-analysis/over-half-of-ftse-100-firms-have-esg-board-committees/#:~:text=What%20is%20the%20role%20of,and%20increase%20their%20stock%20price.>

There is no blueprint

Software development company Mindera promotes “a self-organisation and experiment-driven environment” with ‘bubbles’ of expertise instead of a traditional organisational structure and hierarchy. This philosophy extends to ESG.

“We have a collective approach,” says Pedro Teixeira, who is the People Lead at Mindera. “I am leading a group of 60 people who focus on policies and carbon sprint actions. And the group is divided into three smaller working groups focused on different priorities, including education and emissions reduction.”

There is no single path, but mid-market companies can build on existing infrastructure and operations to give themselves the best chance of success.

“The approach will differ depending on the company,” says IE Business School’s Galdón. “But you should use what you already have wherever possible. ESG needs to be connected to the nature of who you are, and it needs to travel right through your business model and value chain.”



03

Why mission matters to ESG

Companies need a clear purpose if their ESG strategy is going to meet rising expectations — both inside and outside their organisation.

Our research finds that most companies are either developing, implementing or have implemented an ESG strategy. And the biggest motivating factor for doing it is to enhance their brand and reputation.

Done well, an ESG strategy weaves sustainability into the DNA of the business so it is reflected in everything from product innovation to talent retention.

“Sustainability is very important to the buying decisions of many of our clients — if you don’t have a plan, it’s a non-starter,” says Hunter, founder of food producer Piglet’s Pantry. “Building a culture internally is also incredibly important if conscious practices are going to be instilled across the business.”

It all starts with purpose

Our data shows that 44% of mid-market companies agree that ESG policies and practices can only be implemented when the organisation’s purpose is clearly defined.

For Cunningham, CEO of geo (Green Energy Options), defining a strong company purpose has made ESG an integral part of the company. “Deciding what our mission should be and understanding where ESG was crucial was really important,” he says. “For any business, your legacy is critical to understanding why you have ESG goals and why you should fit your business around them.”

Cunningham explains that attitudes to reporting on ESG have changed since geo defined its purpose. “We were running a good business, but we didn’t know where

44% of mid-market companies believe that ESG policies and practices can only be implemented when the organisation’s purpose is clearly defined.

we wanted it to go,” he says. “If you’re only reporting on ESG because you think your investors or customers want you to, people will always hate reporting on it because it’s not what your business really believes in. Your supply chain and customers won’t buy into it.”

Amar adds: “Some of the new business we’ve taken on in the last couple of years has been from far more ethical brand partners, so there has to be much closer alignment in supplier values.

Hunter adds that Piglet’s Pantry is making more active choices in its supply chain. “We are lobbying them to make better conscious decisions,” she says. But she adds that instead of refusing to work with the organisations that do not adopt the same practices, education and collaboration come first. “If you want to work with people you must work in true partnership, and sharing best practice and knowledge is the best way to do that.”

The research highlights how important partners, customers and suppliers are to the process:

42%

of surveyed companies say ESG has a critical role in reducing supply chain risk

45%

agree that ESG credentials are an increasingly important factor in the procurement/tender process

41%

agree that customer buying decisions are increasingly influenced by ESG policies and practices

Weave sustainability into the fabric of the business

Establishing a company mission can be a good first step in implementing an ESG strategy, and ensuring that the mission is strongly tied to sustainability goals can help focus minds. In our research, “competing strategic priorities” is identified as one of the biggest barriers to ESG adoption. But if company purpose dictates strategy, it should prevent this kind of clash.

Linking sustainability goals with company purpose will make it easier for employees and customers to buy into ESG. The research reveals that the vast majority of businesses (90%) say that their ESG principles are aligned with engaging employees at all levels.

For Webb, tying sustainability goals to its mission of giving every child a chance to shine has galvanised employees. “As an organisation, it says this is what school uniform is about, but it’s also a service delivery and a sustainability message,” he says. “It is helpful for our culture, and it helps with recruitment and retention.”

Incorporating ESG and broader sustainability goals into the company mission will also help to increase transparency and satisfaction for employees.¹⁵ A Deloitte study, for instance, has revealed that 39% of Gen Z workers have turned down employers that do not align with their values.¹⁶



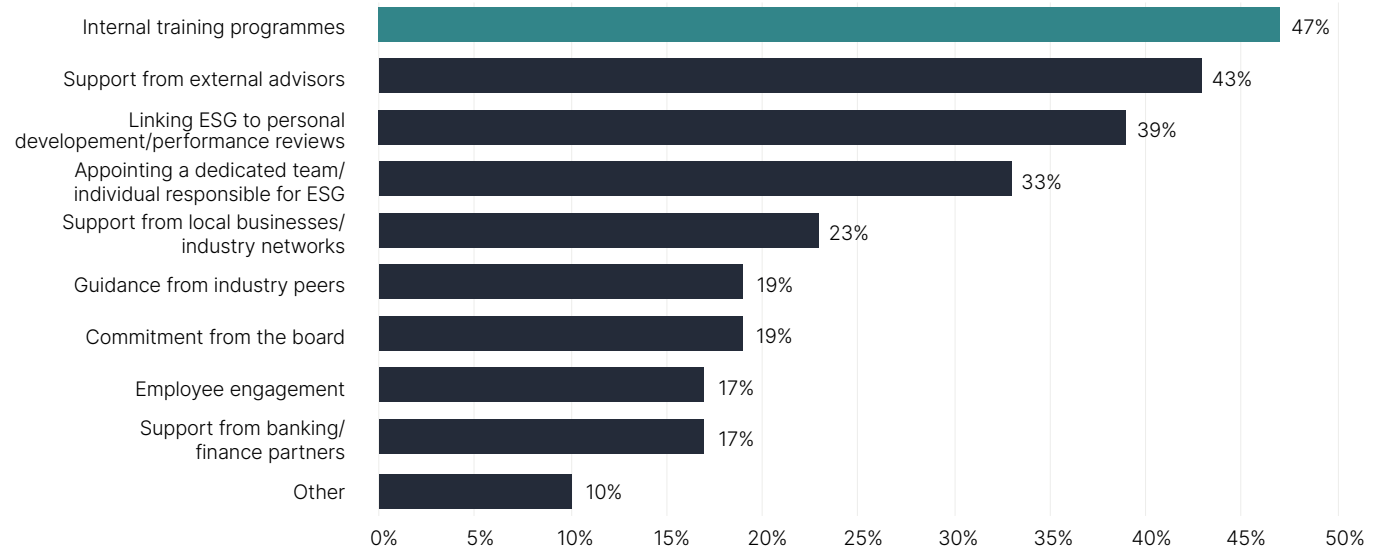
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People need to understand your longer-term vision and strategy, not all the specifics of it, but they want to be striving for something and be inspired. That’s how you get the best performance out of people. It’s not going to be long before you get to that point; even as a smaller company you will start thinking about purpose.

Ruth Leas, CEO of Investec Bank plc

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What has had the greatest impact on the success of your ESG strategy so far?



15. <https://www.mckinsey.com/capabilities/strategy-and-corporate-finance/our-insights/five-ways-that-esg-creates-value>

16. <https://www.deloitte.com/global/en/issues/work/content/genzmillennialsurvey.html>

Nearly half (47%) of businesses that have an ESG strategy in place say that internal training and education have had the most significant impact on its success.

To attract and retain employees, businesses must demonstrate how they will be able to influence and shape strategies not policy. One way to do this is through education on ESG and company purpose. Nearly half of businesses we surveyed (47%) that have an ESG strategy in place say that internal training and education have had the most significant impact on the strategy's success.

Amar explains that when his company formulated its three-year strategy, a critical element was its CSR programme, Doing Business Better (DBB). And employee education on the programme was essential. "We conducted several workshops as part of our strategy process, and DBB was covered over and over again — from product packaging and customer interactions to IT solutions," he says. "People now think about it day to day. When it comes to overall business decision-making, it is front and centre."

A sustainable business speaks a different language

Galdón, vice-dean for business with purpose at IE Business School, explains that when you move from treating ESG as a box-ticking exercise to incorporating it into your wider company mission, there is a marked change in how the business operates.

"It becomes the core of what you do," she says. "It needs to be built into supply chain management, into product and service design. It needs to be built into hiring and promotion policies. The activity changes. It's a different language that we're speaking."

“

Companies often get started in two areas, for listed companies it's where they have already been gathering data. One is in reporting carbon emissions, because even those who don't have to now are going to have to very soon. And the second is diversity and inclusion, because it's not hard to understand conceptually that you will attract better talent if you've got better policies and practices.

”

Alicia Forry
UK Equity ESG, Investec





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Ian Webb
CFO, Banner



Pedro Teixeira
People Lead, Mindera



Steve Cunningham
CEO, geo (Green Energy Options)



Concepción Galdón
Vice-dean for business with purpose, IE Business School

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Let's talk

Our team of specialists are on hand to assist.

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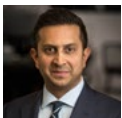
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