RPIA
Global Fixed Income Experts

ESG Engagement Example
Q4 2023

BACKGROUND

Back in November 2022, MSCI marked a German automaker with a "red flag" in its social issue category due to allegations of forced labour related to Uyghur employees at a joint venture manufacturing plant in Xinjiang, China. The automaker commissioned an independent audit performed by a Berlin-based auditor, which published results on December 6, 2023, confirming that they found no indication of forced labour.

On December 12, 2023, MSCI upgraded the red flag on labour rights and supply chain issues to an orange flag, in response to the positive audit. However, the following day, senior staff at the auditor distanced themselves from the audit, posting on LinkedIn that very few team members within their firm "participated, supported, or backed this projected." The Founder and CEO of the auditing firm, has stood by the results of this audit, stating that his assessment as project director of this audit remains unchanged.

ENGAGEMENT FOCUS

We met with members of the automaker's Investor Relations team and Management Board following these updates in December 2023. During our discussion, we asked about the recent audit and the subsequent distancing by members of the auditing team. The company confirmed that MSCI is pleased with the audit process, and the automaker was in dialogue with MSCI prior to the audit and ensured all required materials were included in the audit process.

In addition to the social issue category upgrade, the company was also upgraded from fail to watchlist on the MSCI UN Global Compact Alignment assessment, which makes them eligible for certain ESG indices that screen for these scores. Barclays has calculated that being on the fail list is worth 6 basis points (bps) and the watchlist, 2bps. Barclays also believes the greenium is ~3bps on average for the green bond market, but much higher at 10bps in the auto sector due to scarcity.

PROGRESS & MONITORING

This engagement increased our confidence in the company's credit profile and the MSCI rating upgrades regarding the labour issue helped improve demand, with investors bidding up the automaker's secondary bonds following the MSCI update. Our increased conviction allowed us to continue holding our 3.875% Hybrids from this issuer which performed well post-upgrade, as well as invest in the new 4.75-year and 7.75-year bonds the company brought to market in Europe.

We will continue to monitor the company's governance oversight and labour rights practices. The automaker also has carbon netural and carbon emission reduction goals on the environmental side, which we are also monitoring as we wait for updated reporting on their progress.