

Responsible investment

Sustainable gains



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Responsible investment: sustainable gains

The revolution in how investors are assessing companies is gaining momentum. No longer considered niche, responsible investing is rising in prominence among institutions when making investment judgements.

Indeed, a study carried out by professional services specialist Aon found that 40% of institutions have a responsible investment policy for making buy or sell decisions. A further 14% of the 223 institutional investors Aon spoke to in June are working on implementing such a policy.

More and more institutions are expected to adopt a responsible investment policy with research from State Street, also published in June, showing that 83% of institutional investors and wealth managers expect more money to flow into environmental, social and governance (ESG) ETFs by 2023.

Behind this shift in mindset is growing demand by scheme members for institutional investors to assess the non-financial aspects of a company and its impact on the environment and society

This is partly due to younger people entering the workforce and starting to hand their cash to asset managers to fund their retirement. Many of them wish to make an impact rather than just generate a return.

Regulation has been another driver as research points to the benefits of backing companies that are better governed and work to ensure good practices in their operations could stretch beyond simply lowering risk.

Longer-term gains could be the reward for backing better behaved companies. This is a theory that was backed-up by a notable report by MSCI (*Foundations of ESG Investing*). However, some rightly point out that the findings of one report alone are not enough to change attitudes across the investment industry.

To get to the heart of some of the issues surrounding responsible investment we brought trustees, fund managers and consultants together for a debate on the subject.

You can read the conclusions of our discussion from page four.

Mark Dunne

Editor, *portfolio institutional*

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Tim Manuel

“The great thing about divestment is if you have it as a policy it’s easy to implement. “I’m just not going to invest.” People do acknowledge though that engagement has the potential to have a greater impact.”

Tim Manuel, Aon

PI: What does responsible investment mean to you?

Beatrice Hollond: It goes from screening and exclusion to being an activist through to making a social impact. The whole gamut of that can be considered responsible investing.

Tim Manuel: One of the challenges in this area is that it means different things to different investors. We work with lots of pension schemes and they are on different phases of their journey.

Once you have gone through the awareness and education piece it is important to establish what it means to them and what their motivations are. It is important for an investor to define their objectives and clearly articulate the principles and processes they want to follow. So it means different things to different people.

Karen Shackleton: I’m not sure anybody would say they were an irresponsible investor, but I have heard at least one local authority pension fund saying they love sin because of the financial opportunity that sin stocks present to them. On the whole, pension funds should be responsible investors.

James Brooke Turner: Times are changing. Ten or 20 years ago people would have been quite happy just to make as much money as possible. The zeitgeist is different and it’s no longer acceptable just to make money at any price. The other interesting point is ESG, which is a subset of responsible investment.

PI: What is the difference between responsible investing and ESG?

John William Olsen: ESG is more about the way you do it and the type of topics that you might focus on, while responsible investing is more about behaviour. It's the concept of how you go about investing. Going back to the discussion about defining responsible investment; I'm not sure that we need to. What is important is the objective of the investor and it might be different for a lot of us.

The difficult part about this is when you look at the US, Australian and Asian markets. Their approach to ESG is more from an ethical or a moral perspective. "I don't like this, so I'm going to exclude it." That has been one of the things that some investors feel is detrimental to performance because you are reducing your universe. People and society are changing and what we are seeing become more and more dominant in the discussion about ESG is why is it material for the investment strategy.

The whole discussion about fiduciary duty has been important in the ESG debate and this is now changing, with regulation having an impact on certain sectors. It is becoming important from a financial perspective. Defining 'why' is pretty difficult because we have all been educated in the old way of managing credit and equity risk. Fund managers have been used to price-to-cash-flow and earnings growth, but they are trying to think about how environmental effects are impacting returns and risk. Nobody's educated with this kind of stuff.

We are gradually moving to a space where everybody talks about it, everybody has a feeling about the materiality of it, but we lack the facts to back it up. That is probably one of the biggest issues now in our industry. It is still driven by a belief conviction and there's a lot of work that needs to be done on how you should integrate that into a normal investment process.

Shackleton: The Environment Agency is a classic one who tried to make sure that their beliefs were reflected in their investment portfolios. Increasingly, they have become more and more intentional in their investments, saying: "Right, rather than this screening process, let's invest intentionally to achieve the impact that we want which reflects our beliefs." This is a journey and the labels that we put on some of these things mean you can get caught up in differences of opinion over what a definition actually means.

Brooke Turner: Is it important that the ESG values are your own or can you use somebody else's?

Shackleton: This has been an interesting discussion for the local authority pension funds who are pooling. They have to come up with a common ESG policy that applies across all their member funds, which is quite complex because they all have slightly different takes on it.

PI: What is driving responsible investment as a strategy?

Holland: It's driven by what's happening in the world, including serious issues with climate change. The world is changing and we need to figure out how we're going help fix it. As shareholders in large companies, if one can be slightly more activist and convince people that companies need to pay attention, that's a useful role to play.

Also younger people are much more interested in environment or social issues and over time that is being picked up. For example, through the university investment portfolios there's been quite a bit of agitation about what they should or shouldn't be invested in. So that is flowing through as well. We are not going to change back. It is here to stay.

Manuel: You are right. What we've seen is an acknowledgement of a need for collective action to try and achieve these goals that most people recognise need to happen in order to have a more sustainable future. We've existed in that cycle where it's always been someone else's fault or it's easy to point and say: "They are the person who needs to initiate this change." What Paris did was start that ball rolling and there's been that obvious acceleration over the last few years of greater policy intervention as governments are looking to try and deliver on some of those promises and the commitments they have made.

Olsen: The tipping point was probably COP 21 and the United Nations' millennium development goals in 2015 which created a wave of regulation on top of what already existed in the investment market. Regulation, certainly in the European Union now with their action plan, becoming more pronounced on ESG is going to have a huge impact on the investment community and the financial industry.

Wim Van Hyfte: It has to a large part been driven by institutional investors, starting a long time ago with the church and purpose driven exclusion investing. The move into sustainability and ESG, although it

can be quite complex to understand, is actually an intuitive and easy-to-understand proposition. You are making an investment to make money, but you are also doing something good at the same time. The two are not mutually exclusive. And I think that notion is becoming more widely recognised and accepted, and rightly so.

ESG is both about managing risk or mitigating or avoiding exposures to some areas of the market that you don't like, and also seizing sustainability opportunities. This is very much an inclusive way of investing. You are only investing in the good things and can have an impact on society and the issues that we all know are out there. They are getting a lot more exposure through social media. So there's a lot more exposure to private investors than you saw five years ago.

Brooke Turner: It has come about partly through globalisation. Supply chains are so enormous and companies are so exposed and vulnerable in a way that they haven't been before.

Manuel: I was with a pension scheme yesterday – they are in the food industry – and we got onto this topic. The organisation sponsoring this pension fund has a statement which says that one of their goals is to build a sustainable supply network with responsible sourcing. All the people in the room agreed that this is something they pursue to lead to better outcomes. What that does is let you move on to a discussion which is: "Well, if we're investing in companies shouldn't we look to understand what their goals are in relation to sustainability? If that leads to better outcomes for all the companies we're investing in that will lead to better outcomes for investors".

Brooke Turner: MSCI's research on companies with better ESG perform better makes sense. Companies that invest in safety would probably be better run.

Hollond: The Environment Agency's track record over the last 12 years has been pretty good.

Shackleton: It demonstrates that there is some value in responsible investing.

Hollond: That's the first proof we have that it's worthwhile and working rather than having to give up return in order to invest like that.

Manuel: Because there is this angle of responsible investment there's a collective need to all work together. What you see today is a niche of pension schemes or investors that are pursuing this, but it is often driven because there is a natural alignment or a set of beliefs that come from their stakeholders.

What will make a difference is if the mainstream starts incorporating these topics and themes into the way they make decisions. The mainstream often doesn't have that connection with a set of values. The best way to progress the discussion is to focus on the risk and return because often that's the first hurdle you need to overcome.

Olsen: That's a complex discussion. You've talked about environmental, social and governance issues, but having that type of discussion – why it is material from the risk/return side – can be complex for an investor to understand and that's not an easy job for us.

Manuel: When is any part of our job easy?

Olsen: True. You mentioned that young people are probably not going to approach it from a risk/return perspective; it's more about beliefs and conviction. They want to invest with a purpose and they want to have some return, but they want to make sure that it's not detrimental to whatever they think is important. The whole debate about climate change obviously can be idealistic and dogmatic about divestment but it also creates a lot of opportunities, whether it's imposed by regulation or whether it's created by market opportunities via changing customer spending. How you materialise that, how do you bring that to life for a pension fund is not always easy. Probably the biggest challenge for the ESG market is to become fully mainstream.

Manuel: There's a huge body of academic work out there. You see examples of meta-studies that combine all of those, and more often than not most of those studies demonstrate that there is a positive connection between ESG and financial outcomes. So why isn't that body sufficient to prove the case?

Olsen: Everybody realises that good governance contributes to good returns because nobody wants to be investing in companies that are not managed properly. Then there are aspects of gender diversity, some research has been done there. If you start thinking about how we have been taught in terms of risk modelling and return generation, there's no academic research on sustainability, and that's surprising. So our students, whether it's economics or engineering, are still taught with the old principles of investing.



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Brooke Turner: I'm quite interested in the developments at MSCI on their ESG and passive indices and how they construct them. This goes to the taxonomy point. They have a set of criteria for E, S and G and then they score all the companies in their universe against that and the bottom 5% drop out. That is similar to the credit markets. The bottom 5% become junk and therefore, the junk ESG, will find it harder to attract capital. Returns would be higher, but companies will be motivated if MSCI's ESG indices become a flagship in same way as for investment-grade credit. What this nascent industry is missing is a benchmark.

Shackleton: Asset owners will be the people who drive this agenda and make it mainstream. I see it starting to happen. If you look at the profile of asset owners who have signed up to Pensions for Purpose, some of them are clearly the sort that you were talking about where there's an alignment of interest. A lot of these members are local authority pension funds which are aware of social needs and want to try and address those. What I find interesting is that a number of people sign up and say they don't want a public profile. "We're not sure about impact investment, but we'd like to find out more, but we don't want people to know that we are looking at it." So they are interested, they are intrigued and that's the start of movement.

Brooke Turner: For me, that's particularly difficult to do well. That's where outsourcing those decisions, like you outsource credit ratings, becomes quite attractive. You just have to say: "I don't really mind, I'm going to have MSCI's values for this in the same way as having S&P's values for credit ratings."

Manuel: I saw some analysis that was looking at two index providers who calculate ESG scores. When their scores were plotted against each other there didn't seem to be any correlation. So in a way your outcomes could be completely different, depending on which index provider you buy into.

Olsen: You are also putting too much emphasis on the scoring and less on the actual work. In equities we have a strong culture of doing the fundamental deep research ourselves; we don't just follow the buy and sell recommendations by Morgan Stanley. In many cases it's a lot better than what's being produced by the rating agencies. So it's okay to have a benchmark, but it doesn't liberate you from doing the work yourself.

Brooke Turner: A good bond manager wouldn't outsource their analysis. They would do it themselves.

Van Hyfte: They will probably look at the credit rating but when getting to the point of investing they will do their own analysis to come to the final decision. Those kinds of data providers are important but it still remains a tick-box exercise. You need to have an overall policy or a strategy.

Olsen: The ratings are only about ESG risk so they don't take into account culture or sustainability.

Van Hyfte: Just one last point on the benchmark. During a period where I managed for a pretty big asset owner, I found it a little frustrating but intriguing that I was always benchmarked against a normal equity benchmark. I had to do performance attribution every quarter or every year and I got frustrated. We agreed on a philosophy: sustainability. Yet every year I had to do a full report on why I underperformed, where I outperformed? Why?" I see what happened in my portfolio and felt the impact of short-term movements in the market but that's not really relevant from the way I'm investing because you keep that long-term focus. That benchmarking issue is definitely a big problem in this industry.

Holland: So what would you do?

Van Hyfte: It's difficult. In Canada there was a pension fund that got rid of all its benchmarking and said we have only one benchmark; inflation. It is simple. The only thing you would want to beat is that benchmark. That changed the whole scope of investing because it was about reflecting your beliefs and convictions in your portfolio. You don't benchmark yourself anymore against a market cap-weighted index, which are, from my humble perspective, not efficient. You have a different framework. It's about beliefs, you keep a long-term focus. You want to address climate change, you want to integrate social issues in the supply chain into your investment strategy, and that's the way you invest. It is not about the MSCI World anymore where if you are not invested in Apple and Facebook you underperform. It reduces the whole discussion of sustainability to maybe two or three stocks, which is not fair from a sustainability perspective. So the whole benchmarking discussion is an important topic for the ESG space.

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Shackleton: There is an education process that is required to get to that point. The problem is that for many investors making that first step on their ESG journey, they are comparing it to what they would have done if they hadn't have moved in the first place. It is almost like they want to check that there's no regret risk in their decision.

Manuel: I'd say that this shift to a more responsible approach goes hand-in-hand with a rebalance of the way we think about short term and long term. We are all guilty of focusing too much on what's just happened. Any report you open, anything you read about, any discussion you have always starts with "What were last quarter's returns?" rather than "What are the returns since inception or longer?"

Hollond: As a fund manager, if you underperform for three years the trustees are going to chuck you out because they have an obligation to think about. So even though you want to be long term it's difficult for the decision-makers on the trustee board to be like that because they know that there's a tolerance cycle.

Shackleton: Nobody has mentioned the sustainable development goals (SDGs) yet. I see a real trend towards trying to assess the impact in a portfolio, even in a regular portfolio, but I see a real trend towards trying to measure that against the SDGs for better or for worse.

Manuel: I'd agree to seeing a trend of trying. I'm yet to recognise someone finding a good way of doing that which is comprehensive, looks under the surface and yet is not so complicated that it's unworkable.

Olsen: Obviously impact investors have to measure the outcomes. You can do it on a project basis or a company basis if you have access to the data, but doing it on a portfolio level is next to impossible because you're dealing with so many different sectors and business models.

Shackleton: There are managers who are trying to do that now.

Olsen: You can have a company like Unilever, where you have a CEO that has a strong sustainability drive, a strong culture, and, arguably, have more impact than a lot of typical impact companies, but none of their revenues go towards the SDGs. Frameworks are good, but should allow us to use common sense and make decisions that we believe best fit the goals of our investors.

Brooke Turner: There's a great framework phrase: "Once you set a target you miss the point because you introduce so many extraneous factors."

PI: So measuring the effectiveness of the non-financial aspects of these investments is a challenge?

Shackleton: You need a way to assess a manager. As an adviser, I need to assess whether they are first of all actually doing what they promised they would do in terms of their intentionality, in terms of what impact they're trying to achieve. Then, over time, you want to see whether they are improving that impact. It's a question of how do you assess that and there is not an easy solution to that question. It probably varies from manager to manager as well.

Olsen: Most consultants and institutional investors know they need to do the due diligence on fund managers. We need to sit down with the CEO, look them in the eye and ask questions to figure out whether or not he means what he says and whether or not he's on top of what's going on in his company. It's the same with the manager selection.

Brooke Turner: There are codes like UK PRI (Principles for Responsible Investment) so you can venture into that world of a set of criteria which people can apply.



Beatrice Hollond



Wim Van Hyfte

“It’s more a question of how do you align yourself with the fact that you have so many members, with so many different objectives and you need to get that into an investment philosophy which reflects sustainability?”

Wim Van Hyfte, Candriam

Olsen: Fund managers have some of the responsibility. We’re not used to being super-transparent about everything we do. There’s no reason why we shouldn’t put a two-pager for each company that we hold on the website so people can read about the impact or sustainability or the engagements we’ve had with management. That is probably the right way to do it. It is just giving the information to people so that they can access it. We have all the digital media that we didn’t have 10 years ago, so it’s a lot easier to reach the end customers.

PI: Are trustees more informed on this topic than they were a few years ago?

Olsen: Yeah, much better. In some cases it’s the pure negative screen, so they are concerned about not investing in industries such as thermal coal. It differs in each European country; in some cases they don’t like nuclear, while in France, where they have a lot of nuclear, they are more concerned about thermal energy.

Some countries, especially in Europe, are more focused on screenings, while in the UK the drive has been much more towards engagement. You see that with some companies like Shell. Coming from Scandinavia, the British are much better at getting together and working on specific projects, trying to change things and push change through. That is a key strength of the UK as a management industry.



PI: Why are the British more into engagement than screening and divestment?

Holland: We are the second largest manager of assets in the world. We should be further ahead than a lot of other people.

Shackleton: The local authority pension funds realised their potential quite some time ago and set up a collective forum, the Local Authority Pension Fund Forum (LAPFF), to maximise their shareholder power as a group.

PI: How effective is this engagement?

Van Hyfte: You need the threat of divestment to have impact on engagement because otherwise it's not going to be effective. It is easy to say you will engage to achieve something, but how do you measure whether you have achieved your objective. Regarding climate change, engagement can have impact.

The whole debate about divestment is a little misguided in terms of fossil fuels. In the UK I had a debate with a university student about divesting from fossil fuels. The argument I made was could we switch on the lights again if you divest now? The impact and the disruption are going to be huge. If you look at the predominant uses it's heating, transportation, power generation and we don't have a viable alternative for most of these issues at the scale that is required today.

Innovation is important, but simply divesting from fossil fuels I'm not sure will achieve what we want to achieve. Divestment is definitely a tool when there is a viable alternative. Most will agree that there's a decent alternative to thermal coal in terms of power generation, but for others there isn't for fossil fuels.



It's not only about energy use. Don't forget that it's about other types of chemical industry. You see it in pharmaceuticals and fertilisers also. Fossil fuels have many purposes. So the divestment trend from fossil energy is a little tricky. We need to realise where it's used, why it's used and do we have a decent alternative that won't create disruption in society.

Shackleton: Friends of the Earth had an effective targeted campaign with local authority pension funds. They sent their local campaign groups along to committee meetings to present their case to the local authority committee.

It was a well thought-through presentation of the facts and obviously they are keen for pension funds to divest. Actually, it meant that the committee then had quite an informed and engaging debate. One or two have gone with divestment, but most of them are sticking with engagement as being the right way forward.

Holland: The other thing you can say about engagement is – and it may be a softer thing – if you have collective and active engagement over time it might make corporate boards say: “We need to think about these things because we are going to have this engagement issue coming through.” So it might just put that on their agenda on a more regular basis.

Olsen: That is definitely the case. We can see that from the leading companies across the world. In Europe, where you've had this trend for much longer, the focus from company boards is much better.

Manuel: The great thing about divestment is if you have it as a policy it's easy to implement. “I'm just not going to invest.” People do acknowledge though that engagement has the potential to have a greater impact.



John William Olsen

“People and society are changing and what we are seeing become more and more dominant in the discussion about ESG is why is it material for the investment strategy.”

John William Olsen, M&G

I've seen an example of a set of objectives for an investor that is making that transition, and the wording was along the lines of: “Our objective is to divest from companies that are involved in fossil fuel extraction and be a major international partner in the development of renewable energy.” You can see that a conflict exists because the divestment part is blunt. There's no discretion around it, you just divest from all companies involved in fossil fuels. The second part of that objective is much more nuanced around impact and outcomes. You could argue that some of the biggest investors in renewables today are those same companies that are extracting fossil fuels, so how do you reconcile those two objectives? But that's indicative of the industry as a whole trying to get to grips with this transition from simple divestment through to complex engagement, which is not an easy question to answer.

Van Hyfte: It's a good point you're making. We are managing a low carbon strategy for a pension fund and they were surprised to see that in terms of coal and fossil fuels it scored well, but for renewables it was 30% under the benchmark. That's the issue today, we have to realise that most of the companies that invest in fossil fuels do realise what the future is and they are trying to change. Is this purely the result of engagement? That's difficult to say, but at least they realise that society has changed and they have to change their business model.

The second point, what is probably changing my feeling in terms of asset management, is the collective engagement where you see that asset managers and asset owners sitting around the table and trying to

achieve the same kind of objective. Ten years ago you would not see big competitors sitting round the table to vote on the same thing. A powerful tool of the financial industry now is that we all sit around the table trying to achieve those objectives that are either imposed from regulation or from society, but at least we're trying to achieve that together.

PI: What is going to push ESG into the mainstream?

Shackleton: The ESG risk management process has definitely become mainstream. Eighteen months ago, fund managers were coming to client meetings with presentations and occasionally you would have a slide on ESG. Now, I can't remember when a fund manager didn't come through the door with at least one page on ESG. To me that means the processing of environmental, social and governance factors is now embedded to a greater extent by fund managers in their stock selection.

Hollond: I'm slightly more cynical than you on that. What I've seen from the investment trust world, where I sit on four different boards, is they all have dedicated ESG people. Those teams are growing and they have quite a slick presentation, but when you ask how fund managers take the information that you have given them and do they embed what you are saying, I have had varied responses.

Shackleton: It's a fair point. There's some variability in terms of what they're actually doing. Interestingly, some of the managers who embed it most effectively don't have separate teams.

Hollond: As you were talking earlier about the direction of travel, everybody understands that it's something that has to happen.

Olsen: You have people that do a lot of research; you have people that don't do any research, just do trading and other things. So you are going to have people that do good ESG work and some fund managers who don't, but at least they take it into account. So I would agree it is becoming a lot more mainstream in terms of thinking about ESG.

Taking it mainstream in terms of the broader public, sustainability funds are probably the best solution. It is a lot easier to understand and it's more thematic. So it's a good message.

Hollond: It is in the name, isn't it?

Olsen: It is. ESG is a bit more complex. It's more of a process and is dull and tedious. It's something that institutional investors ask about, but in most cases an investor would be interested in the overall proposition of the fund and sustainability is the proposition.

Shackleton: Sustainability is something that's quite easy to implement in the listed markets. The interesting question for me is when will the un-listed space become mainstream? I could quite easily see in the next three to five years most pension funds moving towards some sort of sustainability emphasis in their equity and bond portfolios, but the more challenging part comes when you look at the un-listed space and particularly if you're trying to achieve social impact. When it comes to environmental impact: you can invest in a renewable energy fund, but trying to address social problems is a little more challenging in terms of the business models that you're going to come up with.

Olsen: It is super illiquid, so it is difficult to trade. It's difficult to find the projects, so you wouldn't have scale. That is probably what is holding it back from becoming mainstream.

Shackleton: It is a shame. We ought to be able to solve that somehow.

Van Hyfte: We've not been used to investing with a social purpose. It's like "Social? What type of investment do you do?" It feels awkward for investors to integrate that into an investment strategy, although we see the added value of it from a more societal and financial perspective. Doing this kind of investment with your own money takes it a step further. There's still a lot of work to do around that social part. The E part may mean climate change and everybody knows that we will be impacted somehow, which means myself, my family, but with social you go outside of your own comfort zone and you're trying to achieve something with your money that contributes to others. You can't talk about social in this way. It is difficult to talk or to approach it that way.

Shackleton: You have to look at the underlying investment and check that it is robust. I'm involved with a small impact manager called Resonance and they have a homelessness property fund. As a standalone that can sit on its own merits, but then it's what do they do with that residential property investment. Are they working to house the homeless?

Brooke Turner: We've had some tremendous returns from life science funds. One recently came up with a treatment which has now been licensed for people with a terrible congenital condition. That is exactly where we should be putting our money.

Hollond: From an Esmée Fairburn perspective, we started social investing for impact about 10 years ago. When we started it was very much trying to be a cornerstone investor in small funds that were just setting up where we felt we could help develop the market. Now, we've put our social impact investing into our mainstream grant-giving because we feel that it's become mainstream enough that we don't need to have it separated anymore.

Out there is a wide variety of views about if you impact invest are you doing it for return of your capital or return on your capital. There are different outcomes depending on whether or not you get lucky in life sciences or you are developing housing for homeless people. The market is still unsure of what the message should be.

Olsen: In terms of mainstream, we have to prove that we can make a return out of it, so it has to be competitive for it to become really mainstream.

Shackleton: I'm going to challenge that. A lot of un-listed investments have attractive characteristics when considered in the context of the whole portfolio.

It may be that they have a lower correlation than listed assets so at the total fund level they can actually improve risk-adjusted returns, even if they are not looking particularly sexy on their own merits. They may have a steady cash-flow, which is attractive to the pension fund for meeting pension payments.

Manuel: If the question is about bringing it into the mainstream then it's about dealing with investors that don't have a natural alignment around a set of values. The reality of it is dealing with the question of how it impacts risk and return.

There's that double due diligence that's still required, which is: "Does it satisfy my financial requirements and is it delivering on some of the impact outcomes that I'm looking for?" Mainstream requires that first question to be answered about risk and return.

Van Hyfte: I agree with that, but then again it's like the benchmarking issue and the short-term issue that jumps in. I agree that we need to show that it adds something from a financial perspective but then again the E bit is misguided because if you talk about financial reporting we are always talking about benchmarks or performance and that is the difficult part about that sustainability discussion. I'm not sure whether regulation can help here because benchmarking was created for a purpose but now it doesn't serve a purpose anymore.

Manuel: We shouldn't be scared or shy away from trying to answer this question because what we are discussing here is the belief that following these approaches, following responsible investment, leads to better outcomes in the longer term. We are all saying that these investments will have better risk and return characteristics so it's something that needs addressing.

Olsen: Most of the funds that are being launched are talking about five-year rolling periods of time where they at least want to match the market. The wording around just beating the benchmark has become different. You could allow yourself to do that when you talk about sustainability because you have a second proposition as well, so it's not just about beating the benchmark all the time.

Brooke Turner: Something else you could add to the list of problems is the requirement to diversify. The



Karen Shackleton

more you diversify, the weaker your engagement becomes. If you own one stock you are going to be really interested in that, if you own 200 then you are going to be much less interested.

Manuel: You can argue this from both ends of the market. For some passive managers, with the amount of assets they have and the weight of ownership in the companies that they are buying into, the opportunity for them to engage with those underlying companies has to be there just through the sheer force of ownership. But you are right, what they're not capable of doing is direct active intervention into how those companies are operating.

Brooke Turner: One of the key factors in this is the amount of governance time you have for it. These are complicated discussions and the amount of board time – it has to be a board decision, you have to go through what is good and what is not good – is limited. You can make it more but you have to decide what you are not going to do instead. What you are not going to be able to do is have more meetings, I suspect. That is the difficulty. It is about how much time you can spend on the nuances of this.

Van Hyfte: It's enormously resource-intensive.

Shackleton: So does that mean it's something that is more attractive for a fund of funds structure, for example, where you're appointing somebody to do that.

Brooke Turner: No, because then you lose the transparency. That's the trouble, you never know what you own.

Holland: Which is what happened with the Church of England and Wonga.

Manuel: One topic we never touched on was the connection to the underlying beneficiaries. You mentioned about millennials becoming more influential. They've overtaken baby-boomers in the workforce and we're starting to see them move into more influential decision-making positions. With the different pension funds we work with it's the defined contribution (DC) schemes that are leading the way in terms of thinking about what their members might want. That's more natural because in a DC scheme

the members are more directly impacted by investment outcomes.

Holland: And they are younger generally as well.

Manuel: In DC, why it's taking off is because schemes recognise that it's a way of dealing with engagement more generally. So we've got these problems that young people don't like pensions or don't like thinking about pensions but young people are really interested in sustainability issues. People in pension funds don't understand the connection with the contributions they pay and the fact that they're invested in these underlying companies who might have this impact on the environment and wider society. And you can put these things together to solve a whole load of issues which is capturing that theme of engagement of members with their underlying pensions and the need to save more in the future.

Van Hyfte: It's more a question of how do you align yourself with the fact that you have so many members, with so many different objectives and you need to get that into an investment philosophy which reflects sustainability? How do you deal with that? That's very complex.

Shackleton: Well it would have to be a dialogue with the pension fund committee. That would be the starting point. This is such a new area in the greater scheme of things that I'd say there is not a lot of expertise on how to take trustees through that thought process.



James Brooke Turner

Responsible investment: delivering for the long-term?

Tim Manuel, UK Head of Responsible Investment, Aon



Globally, investors are beginning to acknowledge that non-financial risks may have a meaningful impact on long-term financial performance. Companies and investment managers are reacting to increasing demands from investors to understand specific, non-financial aspects of their business by providing more appropriate disclosures.

Many governments around the world increasingly view responsible investment as imperative and are encouraging, guiding or legislating that investors and companies operating within their borders must be able to deliver on sustainability, climate and social development goals and promises.

Responsible investment, and more specifically environmental, social and governance (ESG) integration, builds on the premise that robust, long-term sustainable investment returns are dependent on stable, well-functioning and well-governed companies, industries and economies.

While consideration of ESG data has not traditionally been included as part of traditional fundamental financial analysis, assessing these non-financial risks can provide financial opportunities.

This area should be of interest to investors hoping to build investment portfolios that are resilient to change and deliver better long-term risk-adjusted returns.

The universe of investment approaches

Responsible investment can be viewed as an overarching theme for a number of investment approaches. At Aon, we consider the universe of responsible investment to have four main components: ESG integration, impact investing, mission-related investing (MRI) and socially responsible investing (SRI).

From our global survey on responsible investment, 47% of the investors we polled favoured the integration of ESG factors into investment decisions over other types of responsible investment. SRI came second at 24% (Source: Global Perspectives on Responsible Investing).

As the oldest of the four broad responsible investment categories, SRI tends to be the area most investors are familiar with. SRI tends to use a negative selection process; excluding certain sectors or investments from a portfolio based on an individual's or an organisation's value system. On the other hand, impact investing typically focuses more on positive investment inclusion criteria rather than negative screening.

Investment approach	Definition	Impact on selection process	Examples
ESG integration	Integrates environmental, social and governance non-financial data into fundamental investment analysis to the extent they are material to investment performance	Positive/negative/neutral	A fund manager who has a clear and systematic process on financially material ESG factors are identified and incorporated into the decision-making process
Impact Investing	Looking for investments that have a positive investment return as well as a desired social, economic or environmental outcome	Positive	Low-income housing, clean drinking water, clean technology projects, protecting biodiversity
MRI	Placing investments (or avoiding investments) into companies or funds that complement (or are counter to) an investor's mission	Positive or negative	Healthcare, child issues, religious beliefs
SRI	Attempting to screen out investment in stocks, companies or industries based on a set of ethical values	Negative	Private prisons, carbon, coal fossil fuel, cluster munitions

What can investors do?

A great place for investors to start is to understand the risks and exposures already embedded in their portfolio and to review their current policies. Scenario testing, for example, is a useful tool to understand how broader influences such as climate change may impact future results.

Investors should have a clear understanding of their investment managers' policies and actions. We have set out five questions below which investors can ask their investment managers to begin this process.

- What is your approach to responsible investment and how do you believe it will add value or reduce risk?
- Are you a signatory to the United Nations Principles for Responsible Investment (UNPRI)?
The UNPRI is a set of six principles – signatories should be able to provide their latest transparency or assessment reports. These outline a manager's approach and provide high level assessment from the UNPRI.
- Do you have resources dedicated to responsible investment?
- How do you incorporate responsible investment into your investment decision-making for our portfolio?
- Are you able to provide examples of how you have incorporated responsible investment views into your investment decision-making?

This type of exercise can help investors shape their own Responsible Investment policies and ESG beliefs.

Evolving landscape

The responsible investment landscape is evolving and the pace of change is rapidly accelerating. Regulators are applying pressure on investors globally and investment managers are reacting by launching products and implementing and updating ESG policies. We believe long-term investors should define their own Responsible Investment beliefs.

Speak to your Aon contact for more information or get in touch with our responsible investment team directly by emailing DG-AH-UK-INV-ESGWorkingGroup@aon.com.

You can read the results of our recent survey by visiting www.aon.com (search "Global Perspectives on Responsible Investing").



Electrifying investment portfolios (and its limitations)

Wim Van Hyfte, global head of responsible investments and research at Candriam Investors Group



The transport revolution is here. Electric cars are more powerful, more efficient and soon will be cheaper than petrol-burners. That does not mean responsible investors need to ignore the whole hydrocarbon chain: there are sustainable companies in every industrial sector.

Revolutions of any kind are typically volatile, and the advent of electric vehicles (EVs) is proving no exception. The share price of Tesla, the world's most well-known electric car producer, has yo-yoed 30% since late February. Heroism and hyperbole accompany most ventures guided by Tesla's CEO, Elon Musk. But analysts are now concerned lest the company crashes in debt before it fulfils its order book – approximately 450,000 Model 3 saloons alone. Whether Tesla survives its own rapid growing phase is debateable: there is absolutely no doubt that EVs will eventually dominate our roads.

The science is compelling from two aspects. First, battery engines are five times more energy efficient than combustion engines: up to 95% of battery power gets converted versus 17% to 21% for gasoline. Second, EVs mitigate climate change. Sure, much of the electricity powering them might come ultimately from hydrocarbons. How much depends on the speed of adoption of wind and solar. But if EVs force petrol and diesel cars off the road – or from even being built – not only does the transport sector become greener, oil extractors and sellers start losing their second-biggest customer base. In the case for stranded assets, a collapse in revenue hits oil producers hard.

The quantum of revenue collapse is a matter of estimation, reflected in the volatility around EV adoption and the share price of related businesses. Bloomberg New Energy Finance predicts 7.3 million barrels of oil a day will be displaced by EVs by 2040.

Bill Gates once said that we overestimate change over two years but underestimate it over 10. That adage seems pertinent to the situation right now for EVs. Globally, there are just over 1 million electric cars on the road right now. But remembering Gates' adage, this could all change very quickly. Bloomberg New Energy Finance reckons there will be 30 million electric cars by 2030.

One of the remarkable features of battery engines is their simplicity. They only have 20 parts, compared with about 2,000 moving parts for a contemporary combustion-engine car. This relative simplicity cuts maintenance costs but puts greater onus on those few parts, and none more so than the battery.

The battery is an EV's key component, reflected in the rising prominence of battery manufacturers and the eagerness of car-makers to create joint ventures with them.

One aspect of battery manufacturing that interests Candriam is the component metals. We see opportunities for client investors to benefit from the growth in usage of lithium, nickel, manganese and cobalt related to battery development.

Other metals Candriam likes include copper, platinum, aluminium and high-resistance steel. Copper will be an obvious beneficiary of more EV sales. We reckon EVs could command 6% of global copper usage by 2025.

The appeal of aluminium and high-resistance steel relates to the preponderance of the battery in EVs. They can weigh up to 500kg – more than one-quarter the entire vehicle's weight. So not only are they

the vital component, they also necessitate as light a frame as possible to reduce total car weight and boost fuel efficiency. Aluminium will find new markets in car manufacture. High-resistance steel will have its place not only because it is currently cheaper but also stronger than aluminium for crash protection.

Platinoids – platinum, palladium and rhodium – are an exception to our grouping as their value lies in combustion engines. They make the process less dirty, ensuring nasty side-effects such as carbon monoxide and nitrogen oxide are mitigated, thereby satisfying rising requirements on exhaust emissions (not just cars but cargo ships are now subject to more onerous standards).

We include platinoids in our analysis because Candriam takes a holistic view of the investment world in our ESG analysis. Petrol-burning engines are not going to disappear overnight. The majority of new cars will use them until the late 2030s. So for two decades car manufacturing will occupy a hybrid position.

Candriam's policy is to identify those stocks which are best-in-class in a changing world. We do not invest exclusively in companies that seem deep green. This can lead to skews in portfolio composition that are not prudent because this opportunity-set is not representative of the economy. Sectors such as banking and insurance appear to be very green until one takes a closer look at the business of their clientele, which is what CO₂ Scope III emissions are supposed to do.

Candriam is a signatory to the 2015 Montreal Pledge on Carbon Disclosure so we firmly believe in transparency accounting of direct and indirect energy expenditure. Unfortunately, carbon emissions are still only reported by fewer than half the world's listed companies. Scope III emissions, defined as those caused upstream and downstream beyond the company itself, are the least accurately reported. Not only does this leave a huge amount of work for external analysts. They then have to put reported levels into context. Thus, Microsoft, Pfizer and Vestas all have similar footprints. Does that mean these three companies ought to be treated similarly, even though Vestas is building wind turbines? The carbon footprint tells us precious little about either a sector or specific company's direction and speed of travel, i.e. how willingly is it adapting to a changing world.

If we go back to car frames: there are arguments for investing in steel rather than aluminium manufacturers. The former can be less carbon-intensive but much depends on whether renewables are used in the extraction and smelting process. A tonne of aluminium in the US is extracted using almost a tonne less carbon dioxide than some factories in India or China. Then there is the remarkable recycling of aluminium to factor in: 95% of it gets reused at just 5% of the original energy cost. Responsible investors must do a lot of research to reach informed decisions. Simply screening out hydrocarbons by avoiding oil producers and energy utilities incentivises none of those enterprises to change their ways. Likewise, manufacturers of petrol-drinking machines. The preferred method of Candriam is to discover which businesses are making the most effective strides towards sustainability in a low-carbon world and engage with them as best-in-class enterprises. This is much more involved and complicated but it reflects the current energy transition we are all experiencing.



For any further information on Candriam's ESG solutions, please contact Fawzy Salarbux, Global Head of Consultant Relations (fawzy.salarbux@candriam.com, +44 203 868 7710)

A sustainable approach to investment

John William Olsen, fund manager, M&G Select fund range



The value of investments will fluctuate, which will cause prices to fall as well as rise and you may not get back the original amount you invested.

In recent years we have seen a rapid acceleration in demand for a more responsible approach to investment.

This means that, alongside traditional financial considerations, investors are increasingly expected to take into account a broad set of environmental, social and governance factors that can affect an investment. These ESG factors can represent risks and opportunities, and there is a growing body of evidence that they can have a material effect on how an investment performs, particularly over the long term.

For institutions such as UK pension schemes with long investment horizons, a more ESG-aware approach can offer the potential to mitigate a broad range of risks, from reputational damage to regulatory scrutiny, and support sustainable investment returns in their portfolios.

The principles underlying ESG investment are not new, but in recent years ESG-specific criteria has emerged as a dominant framework for assessing the long-term sustainability of a company or organisation.

As of February 2018, € 372 bn was invested in ESG investment strategies in cross-border and domestic Europe, according to finance company servicing specialist Broadridge, up from € 132 bn in 2010.

There has also been strong growth in asset managers becoming signatories to the United Nations PRI (Principles for Responsible Investment). Signing up to the PRI includes the confirmation that investors will incorporate ESG issues into their investment analysis and decision-making processes.

M&G's Select equities team integrates in-depth ESG analysis throughout its investment process, and actively engages with companies to encourage best practice or to help bring about positive change. Our approach focuses on long-term, sustainable investments. 'Sustainability' refers to the long-term durability of a business, and factors affecting that durability include the competitive landscape, industry structure and how a company is run as well as how it treats its customers, the communities in which it operates, its employees and the environment.

We believe that these considerations are a matter of stewardship, and a sensible part of any investment strategy aimed at maximising long-term economic returns. In our view, social consciousness and responsible management are important elements in many companies' ability to generate economic value in the future, and that disregarding ESG factors could affect a company's performance – as well as its share price.

We focus on three fundamental investment pillars – quality, deltas and valuation – which we view as integral to the overall investment return profile of the companies in which our strategies invest.

We think that ESG factors must be integrated within financial analysis, and these factors, as appropriate, are modelled within the three-pillar framework.

Quality: Moats (or the level of protection from competition) and sustainable business models – can include business culture, brand preservation and ability to retain talent.

Deltas: Long-term drivers and risks – may include energy efficiency measures for an industrial company, or supply chain monitoring for a consumer business.

Valuation: Probability-based scenario modelling – discount rate upward adjustment to factor in higher regulatory risks in utilities, for example, or potentially stranded assets in ‘asset heavy’ companies.

We believe that the importance of ESG factors should not be over-emphasised or under-emphasised. Those factors form part of the mix that needs to be considered alongside more traditional financial analysis, looking at all the relevant elements to make a more informed decision.

It is important to note that ESG research is not outsourced to a third party, but is undertaken by the Select team’s embedded analysts, with judgements on ESG factors not dissimilar to forming views on financial metrics. While some companies may score well or poorly on a third-party ESG rating system, we prefer to analyse those factors ourselves.

A medical waste disposal company, for example, may appear on the surface to fall down on systematic ESG criteria – but our research can uncover the positive impacts this company brings to society and the systems it has in place to minimise negative impacts, as well as its cash-flow profile and the evolution of its margins. We can also engage with that company to gain comfort in the sustainability of its business model or to encourage positive change – this is fundamental to our investment philosophy.

We engage with companies, not only to assess non-financial aspects, but also to advise on ESG matters and, again, to help foster change. This is important for a number of reasons, not least of which is an increasing body of evidence that shows engagement can have a positive impact on company performance. We believe that active asset managers can have significant influence on corporate behaviour and that, alongside like-minded investors, we will be able to strengthen corporate responsibility, culture and long-term performance of the companies in which we invest.

For more information please visit www.mandg.com/equities



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Just reward

With research claiming that companies with high ESG standards make better investments, are sustainable strategies on the verge of a mainstream breakthrough?

Mark Dunne reports.



It sounds too good to be true. Companies who avoid the “do anything to make money” mantra in favour of adopting better corporate behaviour could be more profitable and ultimately boost shareholder value.

This is the conclusion of *Foundations of ESG Investing*, a paper published by index

and analytics specialist MSCI that looks at how a healthy environmental, social and governance (ESG) policy affects valuation, risk and performance.

It has widely been accepted that companies scoring high on ESG benchmarks carry lower risks. Now, however, it seems there is

evidence that those adopting practices, such as providing greater transparency to shareholders, employing a more diverse workforce and removing climate change risks from their operations could generate higher longer-term profits too.

“Companies with good ESG ratings are



significantly more profitable and pay higher dividends,” concludes Guido Giese, executive director, applied equity research at MSCI.

He adds that this could appeal to long-term investors. “Knowing that companies with good ESG characteristics in the long run

are good dividend payers is definitely a motivation for pension funds to look into ESG,” Giese says.

Newton Investment Management’s investment director, Jon Bell, is not surprised by MSCI’s findings.

“We have long believed that a good ESG

policy is part of being a successful company,” he says.

Invesco Perpetual’s head of ESG, Cathrine De Coninck-Lopez, says stocks with an improving ESG performance, also often have improving valuations. “Furthermore, the opportunity related to sustainability of

future earnings is potentially better for companies that produce in an innovative, less resource intensive manner; or provide solutions for the world's problems," she adds.

If proof were needed to support investor bullishness, the negative impact on share prices of poor ESG standards have been laid bare by scandals involving energy giant BP, car-maker Volkswagen and social media darling Facebook.

DON'T LOSE YOUR HEAD

This report has, unsurprisingly, been welcomed by those pushing the ESG agenda. Yet it is easy for cynics to dismiss the noise about ESG helping to make the world a better place if the financial returns and improving shareholder value are not there. So if MSCI's conclusions prove correct, then could ESG be on its way to being considered a mainstream strategy?

But the man behind the report makes it clear that he is not saying that backing companies with high ESG ratings always means higher profits. "No investment approach guarantees outperformance," Giese says. He points out that traditional factors outperform on average for long periods as does the ESG signal on average in MSCI's benchmark universe. Giese does, however, fire a warning to investors and trustees: "It doesn't mean it outperforms every year and it doesn't mean it outperforms for every single stock, of course.

"The key message that we have seen is that ESG is a tool to achieve better risk-adjusted returns," he adds.

Indeed, in the US \$8.7trn (£6.5trn) of funds managed by professionals considered sustainable, responsible or impact investing factors when being put to work back in 2016, according to the US Forum for Sustainable and Responsible Investment. This bettered the \$6.5trn (£4.9trn) reported in 2014.

With so much already invested in companies with high ESG ratings, could this research be the catalyst that moves ESG into the mainstream from being just a niche for religiously-minded or ethically-focused investors.

While it is unlikely that on the basis of one report pension schemes, insurers and other institutions will start moving all of their portfolios over to an ESG mandate, this could be the start of a long journey to being an established investment style.

One investor believes that MSCI's findings will not be a game changer for ESG investing; but regulation could. "Research tends to evolve over time and change behaviours gradually," says Tim Manuel, Aon's UK head of responsible investment.

"What we haven't seen is that one piece of ESG research that really changes perceptions," he adds. "It is more about an accumulation of research over time that gradually brings people round to the idea that this is a material concern and can make a difference to their portfolios.

"It will help contribute to the debate, but it will take a lot more than one piece of research to shift perceptions," Manuel adds.

ESG is core to Newton's approach and a lot of people are already following that, Bell says. "Sustainable strategies will become much more common, but it will not happen overnight.

Legal & General Investment Management (LGIM), believes that momentum in this space is growing. "It is something that we have been looking at for many years," she says. "We are committed to it under the stewardship code, under our obligations under the Principles of Responsible Investment (PRI). It is something that our clients ask us about. They expect us to be doing it. "We are getting the data points now, we are seeing the research coming through demonstrating the materiality of it, so we are well on the road to it becoming a mainstream discussion," she adds.

Another investor seeing ESG on its way to becoming a major investment class is Candriam Investors. "People are looking in that direction more and more because it is making more sense to do things this way," global head of consultant relations Fawzy Salarbux says.

The people running the country have stepped in to help improve standards. The Environmental Audit Committee has asked the UK's top 25 pension funds about how they are dealing with climate change and how they manage those risks. "It has shone a spotlight on the issue and it has really

“ It is called ESG now, but maybe in 20 years it won't be called ESG it will just be called investing, because that will be the right way to do it anyway. ”

Fawzy Salarbux, Candriam Investors

"There are still a number of asset owners who don't want to restrict their investment universe, and they believe that the best chance of success comes from having the widest possible opportunity set," Bell adds. "There are strong arguments to suggest that investing along ESG lines can help the environment, help the world but also help your returns."

For some the arrival of ESG as a mainstream market feels a lot closer. Jeannette Andrews, corporate governance manager at

made those at pension funds take it seriously because their responses will be made public," Manuel says.

The Department for Work and Pensions (DWP) is planning to launch a consultation to roll that out to all pension schemes in the country.

"That is the right end of the investment chain to start," Manuel says. "If the asset owners take it seriously then their intermediaries will take it seriously, which then flows down to the companies themselves."

APPLES WITH APPLES

MSCI is not alone in claiming to have found a positive connection between ESG standards and corporate performance.

Calvert Investments, in collaboration with George Serafeim, a Harvard Business School professor, found that a higher ESG performance correlates with greater management or business model quality. One of *The Role of the Corporation in Society: Implications for Investors'* conclusions was that the valuations of firms with a better ESG performance reflect higher expected growth and a lower cost of capital.

Calvert-Serafeim's research also found that firms with superior ESG qualities trade at higher valuation multiples in equity markets, while firms with better ESG performance also had the added benefit of lower credit default swap spreads.

Serafeim is not the only academic to contribute to the debate. A study by anthropologist Alex Edmonds, who is professor of finance at London Business School, found a positive link between how happy a company's employees are and stock price movements.

There is also a paper from Elroy Dimson called *Active Ownership*, which shows that successful ESG engagement has a materially positive impact on companies.

Other academic studies on the subject include the University of Hamburg, which studied 2,000 research papers in 2015. It examined the E, S and G individually and found a stronger correlation between them than when they are aggregated together. It makes sense because investors run the risk of averaging out when you aggregate something together.

Research from Harvard concluded that ESG factors lead to a lower cost of capital and better operational performance.

"They all look at the same issue but come back with slightly different conclusions," Andrews says.

Giese didn't find his research too taxing. He looked at companies in the MSCI World Index, where every company has an ESG

rating. "It is amazing how straight forward it is within MSCI to link the ESG ratings to financial analysis because we have integrated our ESG ratings into our portfolio risk analysis tool," he says.

"So every stock in the universe not only has standard measures like book value, market cap and volatility, but the ESG signal is also

“Sustainable strategies will become much more common, but it will not happen overnight.”

Jon Bell, Newton Investment Management

in the risk model. Therefore we can relatively easily run all sorts of risk analysis also using the ESG signal."

For others looking at ESG ratings is not so straightforward. Salarbux says that comparing apples with apples in an ESG basket is challenging. "Yes, some might use some common sets of data, but at the end of the day everyone comes at ESG from their own perspective," he adds.

In the same basket, he adds, you will have an ESG strategy that is merely excluding tobacco and alcohol, and you will have an investor doing it from a much more engaged perspective. "In the same ESG basket there is a lot of dispersion, so to draw an overall conclusion and say "yes, ESG works" is difficult."

GET THE MESSAGE

The main benefit of this research is the message it sends out to management and investors that ESG matters and, if done properly, could lead to improved risk-adjusted returns.

Salarbux adds that the research means that when an investor assesses a company they have to look beyond the traditional financial metrics.

The challenge is to have reliable and available data of non-financial risk to see which companies are exposed to long-term sus-

tainable trends and the long-term macro perspective.

Whatever the conclusion that asset owners and senior managers read into this research, for Newton this is an investment trend that is unlikely to fall out of fashion. "Studies suggest that the next generation of investors are more interested in engagement in the environment and the impact that companies have on the world than the older generation," Bell says. "As that comes through, you will see increasing pressure on asset owners and investment managers to take more account of these factors."

Whatever conclusion institutions glean from MSCI's findings, Giese believes that his

report is a game changer. "A decade ago ESG was a difficult field, even five years ago it was considered niche. It has changed in the past few years. We have seen enormous in-flows going into ESG. For example, the assets tied to our ESG indexes, in terms of people tracking the ESG index or launching an ETF, have quadrupled in the past two years, so it is exponential growth.

"The reason for that is that there is now a lot of evidence that ESG can help performance. The evidence is not only there in terms of research papers but also our ESG Leaders Index has an eight-year track record," Giese says. "With an eight-year track record people are comfortable to say that this works, ESG helps to make portfolio returns more resilient and now we see that flows are coming in."

Whatever happens following the publication of MSCI's report it is clear that change is in the air for ESG and the early adopters could be among the biggest beneficiaries of picking stocks on the financials alongside non-financial data. "It is called ESG now, but maybe in 20 years it won't be called ESG it will just be called investing, because that will be the right way to do it anyway," Salarbux says. "Mangers who have a framework today, we've had one for about 22 years now, will have a significant advantage in that respect."

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