INVESTING IN CHANGE

ENVIRONMENTAL, SOCIAL & GOVERNANCE INVESTING

Defining Environmental, Social and Governance (ESG) Investing and explaining why the sector is not only here to stay but is likely to flourish.

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ESG INVESTING

WHAT?

Environmental, Social and Governance (ESG) Investing takes a holistic approach to asset management and is designed to widen the focus of investors, integrating ESG considerations with a traditional focus on risk-adjusted return. It comes in many shapes and sizes and to avoid confusion, it is first sensible to lay out the three primary pillars of ESG and to determine what is and is not ESG Investing:

Environmental – climate change risks, innovation and clean technology, natural resource scarcity

Social – human rights, economic and gender inequality, bribery and corruption, cybersecurity

Governance – judicial and penal system, stability and peace, stakeholder rights, executive incentives

Largely interchangeable with terms like ‘sustainable’ and ‘responsible’, there are two common approaches to ESG Investing:

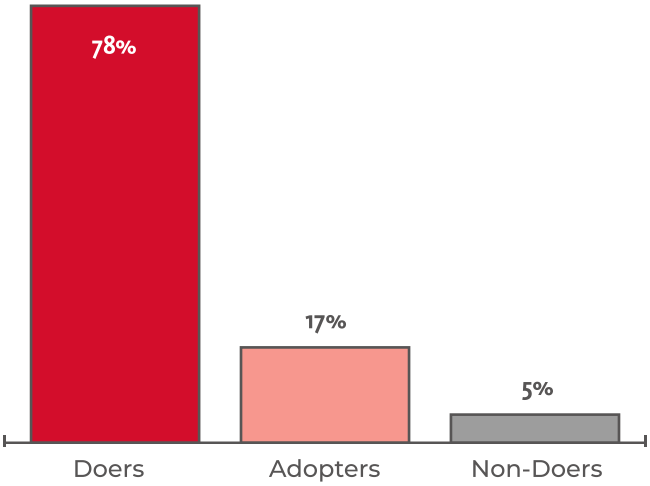
Advance: prioritising investments that exhibit strong quantifiably verifiable ESG characteristics – a superior MSCI ESG Rating, for example.[1]

Avoid: minimising exposure to investments exposed to significant ESG risks, and those poorly managing ESG risks – violators of the United Nations (UN) Global Compact, for example.[2]

Asset owners are warming to ESG Investing as the sector matures – a report recently published[3] by UBS and Responsible Investor found that a significant portion of funds felt positively towards ESG – and consequently BlackRock forecast[4] healthy growth of assets in sustainable investments throughout the decade ahead.

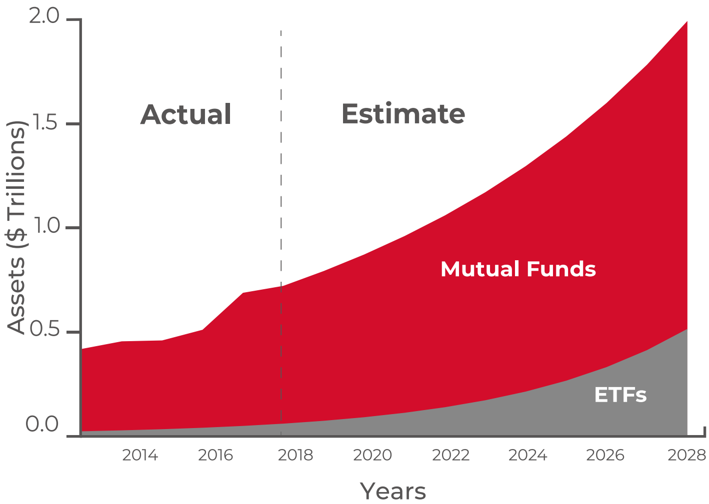
Positive Attitude[3]

Overview of respondents’ attitudes towards ESG



Doer: A fund which acknowledges ESG as material in its day-to-day investment activities
Adopter: A fund which does not currently integrate ESG into its investment process but would like to in the future
Non-doer: A fund which does not see ESG as material in its day-to-day investment activities

Sustainable Swell



Actual Data: 01/01/2013 to 01/01/2018. Estimated data: 01/01/2018 to 01/01/2028
Source: Refinitiv Datastream / BlackRock / Broadridge / Simfund / Tavistock Wealth

WHY?

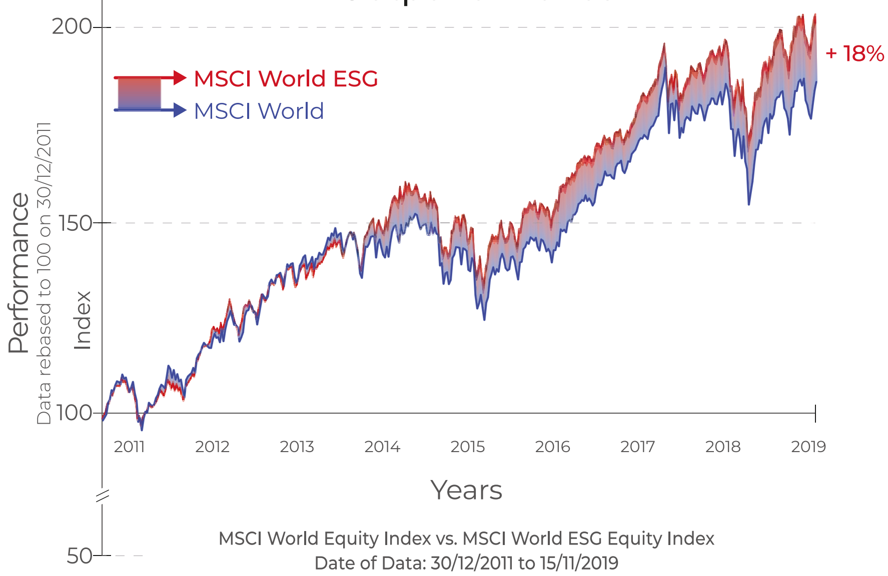
Reflecting on 2019, one would be hard-pressed to arrive at any conclusion other than that this was the year ESG Investing became mainstream around the world. The year in which:

- The Investment Association launched[5] a set of industry-wide definitions for ESG Investing, following a lengthy consultation process with more than 40 investment management companies.
- The UN-backed Principles for Responsible Investment announced[6] 476 new signatories, ballooning total AUM to $89 trillion.
- The European Union published[7] a pioneering 'taxonomy' to help guide companies reporting on climate-related information.
- The Business Roundtable, an influential group of American CEOs, redefined the purpose of a company to consider the stakeholder as well as the shareholder.
- Japan's Global Pension Investment Fund, the world's largest retirement scheme, announced[8] plans to increase its already significant ¥3.5 trillion (£25 billion) allocation to ESG investments.

The pace and breadth of change has been remarkable, and it is quite clear the conversation has shifted from a 'why' to a 'how' to get on board.

The growth of ESG Investing has been catalysed by a growing body of academic and industry research recognising that investments intelligently tilted towards ESG tend to outperform traditional investments over the long term. Non-monetary benefits accrue also, and with the help of big picture initiatives like the UN Sustainable Development Goals are increasingly possible to quantify.

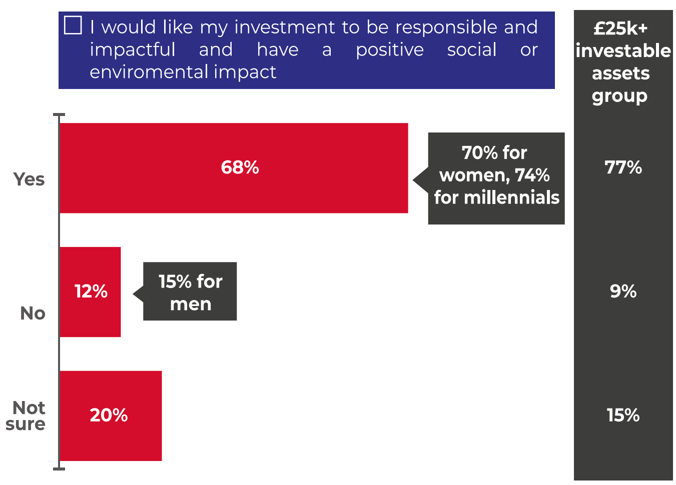
Outperformance



MSCI World Equity Index vs. MSCI World ESG Equity Index
Date of Data: 30/12/2011 to 15/11/2019
Source: Refinitiv Datastream / Tavistock Wealth

Appetite for ESG[9]

In the future, if you were going to save or invest and were given the following option, would you be likely to select this option?



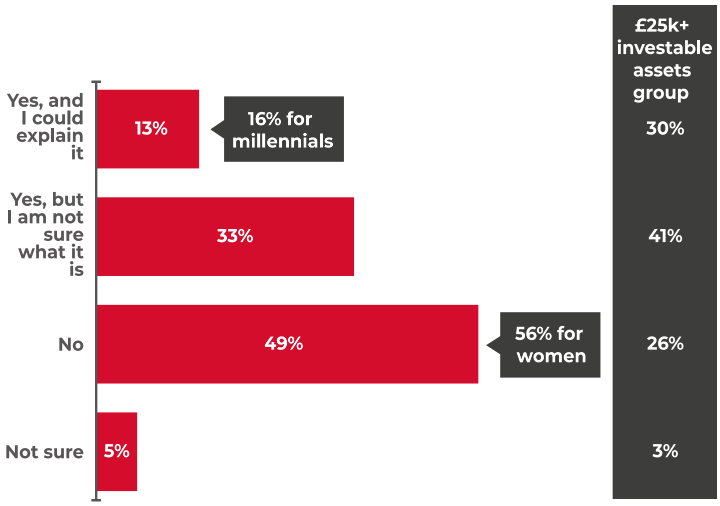
Taken together the rational for ESG Investing becomes clear. Indeed, demand for ESG solutions is strong – the Department for International Development (DFID) found[9] this year that 68% of the UK public (and 74% of millennials) would prefer for their investments to consider impact on people and planet alongside financial performance. Morgan Stanley posed a similar question to investors[10] in the US and found appetite there to be even greater.

OPPORTUNITY

One can become swept up in the positivity surrounding ESG Investing. It is worth remembering that several obstacles to progress remain. Oft-cited issues include 'greenwashing' (misleading investors by overstating the sustainability merits of a proposition) and a confusing lexicon – both of which relate to a wider problem of miscommunication between investment professionals and prospective clients[11] who would, if properly informed, be more enthusiastic about ESG Investing. Only 13% of those polled by the DFID[9] had heard of and could explain the concept.

Market Failure[9]

Have you heard of responsible or impactful investment (also referred to as ethical, sustainable, or socially responsible investment)?



Teething issues are an inevitability in a broad and highly regulated industry, especially when integrating novel and potentially subjective concepts. Yet, an asymmetry between awareness of and demand for ESG suggests there is a valuable opportunity for Independent Financial Advisers to illuminate for clients the increasingly diverse pool of active and passive ESG investments available – particularly in the UK where ESG accounts for just 3% of invested assets[11]. Improving the flow of accurate, jargon-free information is imperative to ensure the sustainability of ESG Investing which, by all accounts, has blossomed into a mainstream approach to asset management and is likely to flourish as we enter optimistically into the new decade ahead.

1 MSCI - https://www.msci.com/esg-ratings
2 UN Global Compact - https://www.unglobalcompact.org/what-is-gc/mission/principles
3 UBS - https://www.ubs.com/global/en/asset-management/insights/sustainable-and-impact-investing/2019/esg-do-you-or-dont-you.html
4 BlackRock - https://www.blackrock.com/ch/individual/en/themes/sustainable- investing
5 IA - https://www.ftadviser.com/investments/2019/11/18/ia-launches-esg-definitions/
6 PRI Signatories - https://www.unpri.org/signatories/quarterly-signatory-update
7 EU taxonomy - https://ec.europa.eu/info/publications/sustainable-finance-teg-taxonomy_en
8 GPIF - https://www.ft.com/content/8e5e0476-f046-3316-b01b-e5b4eac983f1
9 DFID Survey - https://www.gov.uk/government/publications/investing-in-a-better-world-results-of-uk-survey-on-financing-the-sdgs
10 Morgan Stanley https://www.morganstanley.com/ideas/sustainable-investing- growing-interest-and-adoption.html
11 IFAs - https://www.ftadviser.com/investments/2019/10/09/ advisers-still-blamed-for-slow-esg-take-up/