

SUSTAINABLE INVESTING: FACT VS FICTION

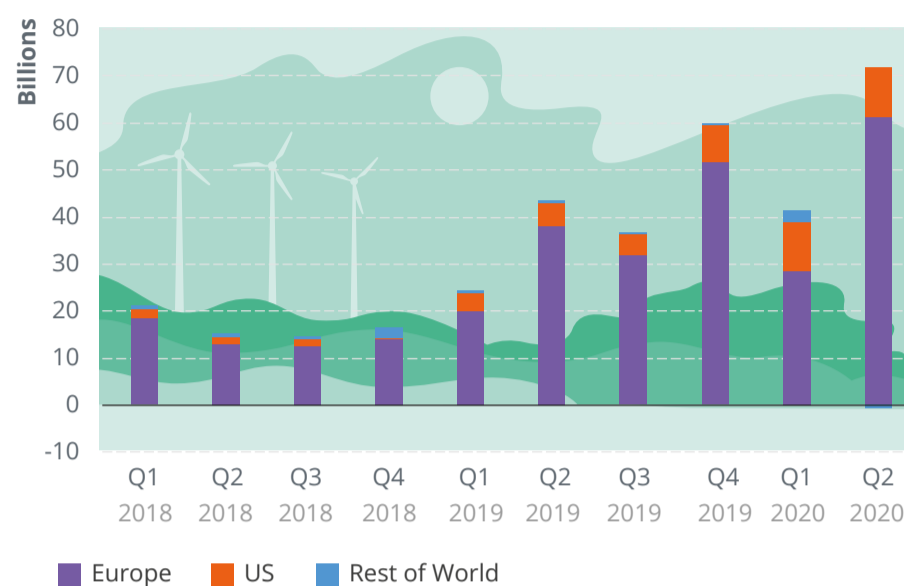
1 FICTION: Sustainable investing is a passing fad.

FACT The first form of sustainable investing took roots back in the 18th century, when religious groups set out guidelines on the types of companies their followers should invest in¹.

By the 1960s, the socially responsible investment movement led investors to exclude stocks and industries involved in unfavourable practices, such as tobacco production².

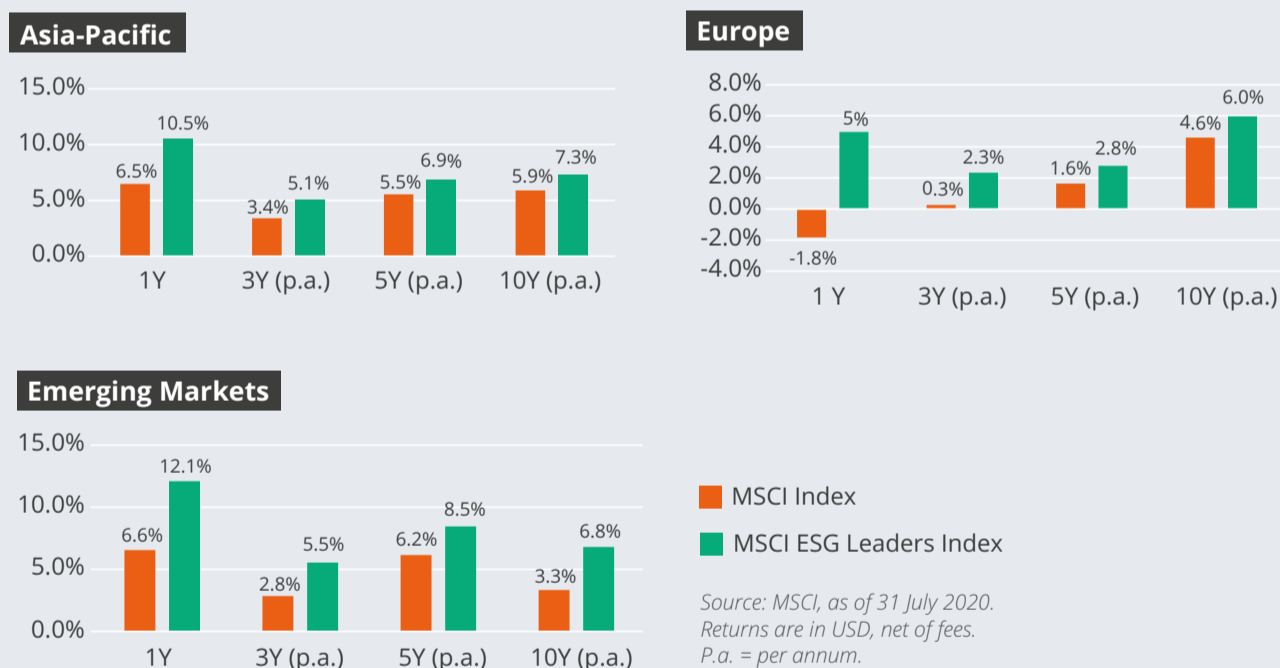
More importantly, sustainable investing is here to stay. Institutional and, increasingly, retail investors are ploughing money where their values are. Global sustainable funds drew US\$71.1 billion in net inflows in the second quarter of 2020 (Q2 2020), propelling their assets under management to a new high of US\$1 trillion, supported by the stock market recovery and growing investor interest in environmental, social, and governance (ESG) issues³.

Figure 1: Global Sustainable Fund Flows (US\$ billion), Q1 2018 – Q2 2020



Source: Morningstar Direct, Manager Research. Data as of June 2020.

Figure 2: Performance of MSCI Indices



2 FICTION: I have to sacrifice returns if I choose sustainable investments.

FACT On the contrary, sustainable investments have outperformed the broader market.

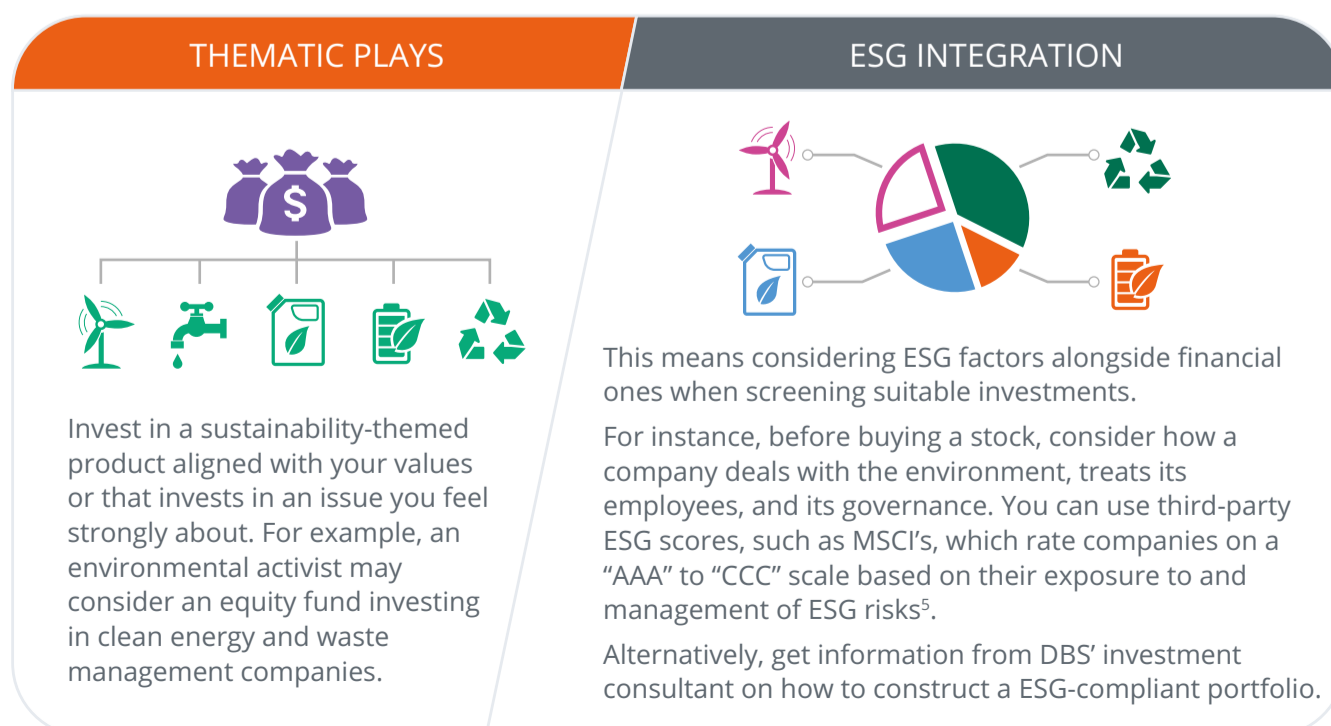
Index provider MSCI's ESG Leaders benchmarks have posted stronger returns than broader indices, across different regions and time periods (Figure 2). In addition, integrating ESG factors has been shown to improve portfolio risk-reward⁴.

3 FICTION: There is no space in my portfolio for sustainable investments.

FACT Sustainability-focused investments range across securities, asset classes, investment styles, and products.

Hence, there is bound to be something that fits your investment needs.

Figure 3: Examples of How to Incorporate Sustainability in Your Portfolio

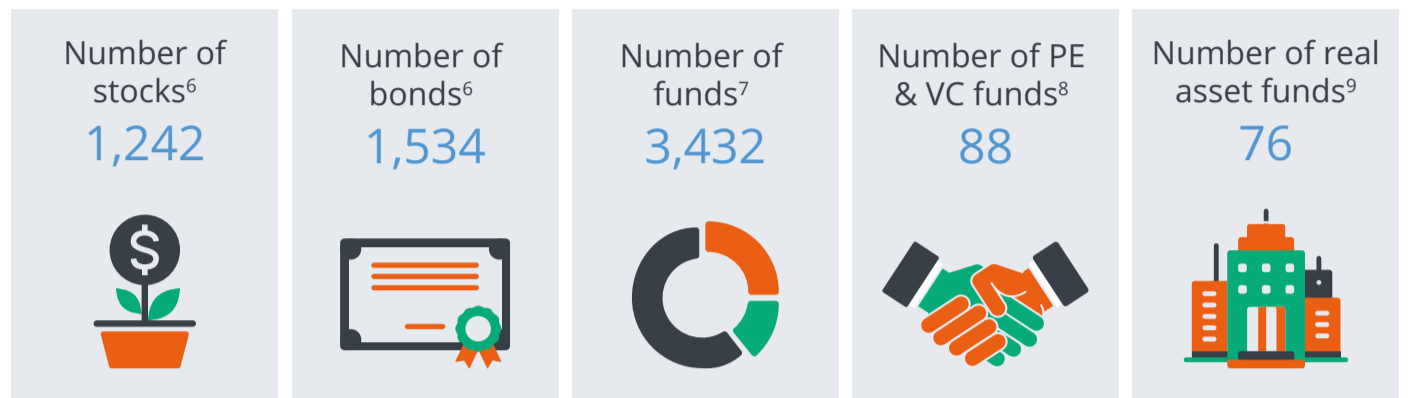


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4 FICTION: There is a limited pool of sustainable assets for me to choose from.

FACT The universe of investable assets and products is large, diversified, and growing. This is true across different asset classes, from stocks and bonds to impact investing-focused alternatives such as private equity (PE), venture capital (VC), and real asset funds.

Figure 4: Investable Universe of Sustainable Assets



5 FICTION: Sustainable investing is all about the environment.

FACT Sustainable investing goes beyond going green. While investors might be most familiar with the “E” in “ESG”—thanks in part to awareness of climate change and its tangible effects—investing sustainably means paying attention to “social” and “governance” factors too.

Figure 5: The “S” and “G” Factors Also Play an Important Role in Risk Management and Performance



“SOCIAL” FACTOR

A 2011 study by a University of Pennsylvania professor found that employee satisfaction is positively correlated with long-term stock returns¹⁰.

► Value-weighted portfolio of “100 Best Companies to Work For in America”:

- 3.5% annual alpha¹¹ from 1984-2009, 2.1% above industry benchmarks

“GOVERNANCE” FACTOR

Poor corporate governance has led to accounting scandals, share price plunges, and even bankruptcies.

- China’s Luckin Coffee (2020): Faked sales numbers, share price plunged
- US’ Enron Corporation (1990s): Went bankrupt following a saga involving hidden debt and toxic assets



¹ Schroders, “A short history of responsible investing”, published November 28, 2016. Retrieved from <https://www.schroders.com/en/insights/global-investor-study/a-short-history-of-responsible-investing-300-0001/>

² MSCI, “ESG 101: What is ESG.” Retrieved from <https://www.msci.com/what-is-esg>

³ Morningstar Manager Research, Global Sustainable Fund Flows report, 2Q20. Retrieved from <https://www.morningstar.com/lp/global-esg-flows>

⁴ CFA Institute’s interview with Jeroen Bos, Head of Global Equity Research, ING Investment Management, “How to Integrate ESG Considerations into Investments”. Retrieved from <https://blogs.cfainstitute.org/investor/2014/01/20/how-to-integrate-esg-considerations-in-investments/>

⁵ MSCI, “ESG Ratings”. Retrieved from <https://www.msci.com/esg-ratings>

⁶ Number of constituent equities and bonds in MSCI ACWI ESG Leaders Index and MSCI USD Investment Grade ESG Leaders Corporate Bonds Index, respectively, as of June 2020. Retrieved from <https://www.msci.com/msci-esg-leaders-indexes>

⁷ Morningstar Direct, Morningstar Research. Data as of June 2020. Number of open-end funds and exchange-traded funds globally that use ESG criteria as a key part of their security-selection process and/or indicate that they pursue a sustainability related theme and/or seek a measurable positive impact alongside financial return.

⁸ Cambridge Associates, Private Equity and Venture Capital Impact Investing – Index and Benchmark Statistics. Data as of March 31, 2020. Includes private equity (growth and subordinated capital) and venture capital funds that intend to generate social impact and target risk-adjusted market-rate returns. Retrieved from <https://www.cambridgeassociates.com/wp-content/uploads/2020/08/PEVC-Impact-Investing-Benchmark-Statistics-2020-Q1.pdf>

⁹ Cambridge Associates, Real Assets Impact Investing – Index and Benchmark Statistics. Data as of March 31, 2020. Includes timber, real estate, and infrastructure funds that intend to generate social impact and target risk-adjusted market-rate returns. Retrieved from <https://www.cambridgeassociates.com/wp-content/uploads/2020/08/Real-Assets-Impact-Investing-Benchmark-Statistics-2020-Q1.pdf>

¹⁰ Edmans, A. (2011). Does the stock market fully value intangibles? Employee satisfaction and equity prices. *Journal of Financial Economics*, 621-640. Retrieved from <http://faculty.london.edu/aedmans/Rowe.pdf>

¹¹ In investment management, alpha refers to an investment’s excess return relative to a benchmark index. The study used the Carhart four-factor model to measure alpha (market, value, size, momentum).

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