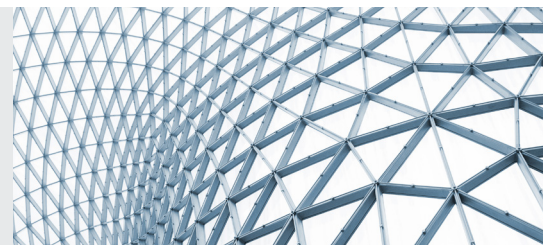


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Why ESG is not just a green bubble

ESG is no passing fad, as more investors are convinced that alpha can be found in ESG and regulators continue to introduce rules to lift ESG standards.

Key Takeaways:

- ESG investing logged a breakout year in 2020 amid the pandemic after more than a decade of development. More institutional investors are now making long-term plans on ESG.
- Institutional investors increasingly believe that ESG has alpha potential and is not just a public relations stunt.
- This favourable trend is set to grow further, as asset owners and asset managers are facing external pressures from regulators pushing the industry to enact more sustainability measures as well. Although Asia is lagging its Western peers, the region is catching up rapidly on the regulatory front.

Environmental, social and governance (ESG) discussion has fired up amid the pandemic, but this is no overnight sensation. More asset owners and asset managers, including those in Asia, will continue to incorporate ESG into their investment processes to lift returns.

ESG investing logged a breakout year in 2020 amid the pandemic after more than a decade of development. The last quarter of the year marked a watershed moment as ESG strategies brought in record flows of \$152 billion, reached record asset levels of \$1.6 trillion, and drove a record number of 196 product launches¹.

More institutional investors are now making long-term plans on ESG, and they will unlikely put the plans on the backburner even after the pandemic.

Responsible investment is increasingly viewed as a risk reducer while enhancing performance. It is a force for change. It will help protecting the environment, enhancing diversity and inclusion, promoting social equality and ensuring proper governance, said Fabrice Chemouny, Head of Asia Pacific (APAC) at Natixis Investment Managers (Natixis IM).

“APAC investors realised ESG was not only a feel-good investment strategy. [It] can really generate outperformance versus non-ESG indices. 2021 will certainly confirm this,” Chemouny said.

Indeed, institutional investors increasingly believe that ESG has alpha potential and is not just a public relations stunt. In Natixis IM’s Global Survey of Institutional



Fabrice Chemouny
Head of Asia Pacific
Natixis Investment Managers

Investors released in 2015, half of the institutions who responded said there was alpha to be found in ESG, and the number rose to 62% in 2020. More of them also believe ESG produces higher risk-adjusted returns (29% in 2020 versus 15% in 2015).

There is also much higher levels of adoption among professional investors. The proportion of institutional investors implementing ESG climbed from 61% to 72%, as shown in Natixis IM’s data in its 2019 and 2021 outlooks.

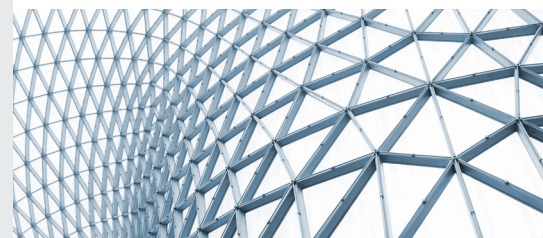
Regulatory push

This favourable trend is set to grow further, as asset owners and asset managers are facing external pressures from regulators pushing the industry to enact more sustainability measures as well. Regulators across the globe continue to press asset owners and asset managers to factor sustainability issues into their investments. The European Union has upped the ante with the corporate reporting guidelines requiring listed companies to publish a non-financial statement of environmentally sustainable economic activities.

Source: Natixis IM - 2021 ESG Investor Insights Report

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Although Asia is lagging its Western peers, the region is catching up rapidly on the regulatory front. Regulators in Singapore have set guidelines on environmental risk management, while Hong Kong is also mulling to oblige companies and investors to make mandatory environmental disclosures in 2025. Taiwan regulators are also drafting new ESG rules to prevent greenwashing.

“ESG investments started to become a key topic in Asia Pacific only recently. APAC investors were quite late compared to Europe. But now I would say the pandemic played as a catalyst”, Chemouny said.

The ESG adoption from local investors in Asia Pacific can go fast from now on. APAC has a young population who feels the importance of building a better world. In the region, there are more and more requests for proposals (RFPs) that are coming from large asset owners, sovereign wealth funds, corporate pensions, life insurance and even private banks that are stressing the need for robust ESG capabilities, he said.

ESG strategies

Not only has the number of professional investors implementing ESG strategies grown considerably, they are also deploying a wider range of ESG strategies.

“Diverse approaches to ESG are needed, because the issues are complex. They are deep-rooted, they have been long in the making, and they will be long in the resolving,” Chemouny said.

ESG integration, which considers ESG issues that can materially affect company performance in investment analysis, is most frequently deployed by institutions and fund selectors. However, given the wide range of factors that can be taken into account under ESG, it could be hard to know which data is significant to the analysis, according to Natixis IM’s 2021 ESG Investor Insights Report.

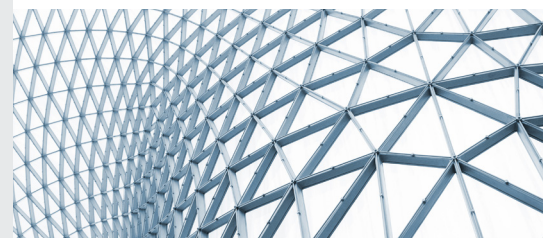
Professional investors also rely heavily on negative screening as part of their ESG strategies, which excludes companies or industries deemed unethical or harmful to society from their portfolio. But while it can contribute to investment performance, the industry has found little evidence that it can help to address societal problems or is effective in risk management.

In active ownership, investors leverage their rights of ownership to influence corporate behavior to ensure that corporations are better positioned to withstand systemic transitions. More professional investors also engage in impact investing, which aims to achieve financial outperformance while contributing to solving societal challenges, the report shows.

This article first appeared on the AsianInvestor website on June 7 2021.

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