Emerging trends towards impact investing as Asia's ESG revolution awaits

Basim El-Shoura, Investment Solutions Specialist for the UK, Benelux & Asia at Allfunds Bank is a keen proponent of impact investing, a trend that he believes is set to create a mini-revolution in Asia in coming years. He highlighted key trends in ESG and SRI investing at the Hubbis Investment Solutions Forum in Singapore.

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EL-SHOURA TOLD DELEGATES that his core topic for the presentation was sustainable investing. "This whole area is better known perhaps as Socially Responsible Investing, or SRI," he noted, "or as Environmental, Social and Governance, otherwise known as ESG. They are similar, but slightly different. SRI excludes some investor sectors, for example tobacco or armaments that might be considered environmentally, geo-politically or ethically unacceptable. ESG is more of a tool, with fund managers applying a scoring methodology to help them decide which companies are acceptable from environmental, social or governance standpoints."

BASIM EL-SHOURA
Allfunds Bank

Allfunds - in tune with the evolution of the global investment industry

Allfunds was created in response to the increasing complexity of the financial industry, enhanced by the demand for simplification, agility, flexibility and operational efficiency. "Allfunds facilitates the administration of our clients' third-party fund distribution," El-Shoura added. "We are an institutional platform offering a pure B2B full service approach. We have no proprietary asset management, insurance, pension nor end-client B2C businesses that could cause any conflict of interest."

El-Shoura explained that Allfunds is the leading European B2B platform, working with more than 1200 fund managers intermediating around EUR370 billion of assets, across more than 64,400 funds that are accessed by over 600 institutions through 44 different countries.

Allfunds Group is headquartered in Madrid and has a presence in London, Luxembourg, Milan, Santiago de Chile, Dubai, Zurich, Bogota and Singapore. El-Shoura reported that in 2017 Allfunds processed some 12.7 million trades, all automatically and with no manual intervention. Core clients are private banks, wealth managers, family officers, pension funds, insurance companies.

The key difference, he explained, is that ESG can be used to boost alpha as fund managers use it to help them beat the market, while the focus of SRI is very beta-focused and aims to match market cycles.

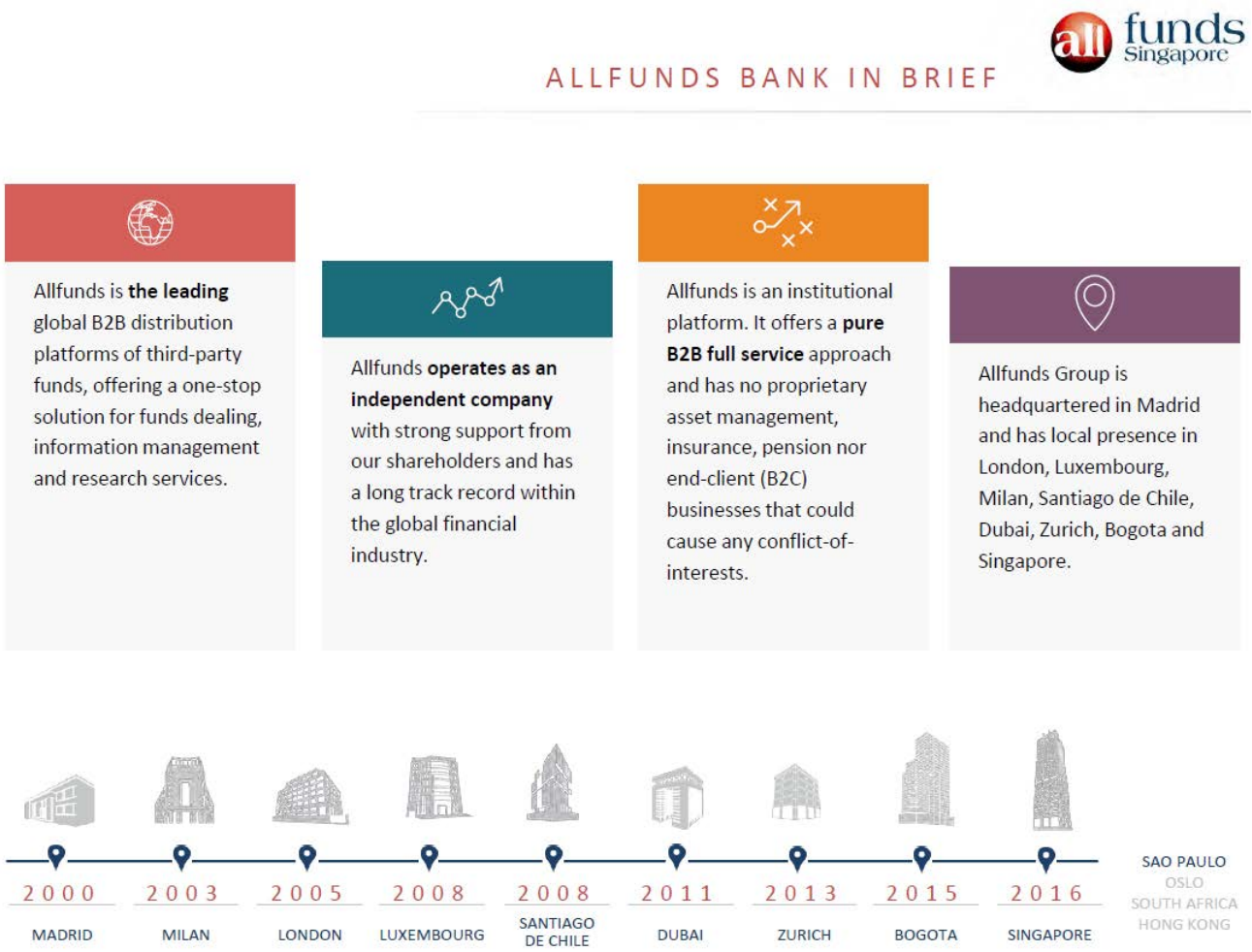
"We are seeing remarkably strong growth in both areas globally," he reported. "Over the last few years, we have seen a growing number of government pension funds, most visibly the Dutch, Japanese, Norwegian and South Korean state funds invest heavily into ESG-related products. Additionally, Australia, New Zealand and Europe have heavily integrated ESG into their processes."

While Europe is leading the way, with more than 52% of total investments currently driven by SRI or ESG principles, Asia is far behind this curve at just 0.8%. "But," El-Shoura reported, "we anticipate a dramatic acceleration in the coming several years and estimate this will leap to 20% or more within less than five years."

He delineated three main reasons for the widespread growth. ESG, he explained, has been shown in many research studies to offer higher returns in portfolios as many qualifying companies have achieved high profitability, higher dividend yield, and also lower volatility.

Secondly, he noted that many companies and many portfolio managers like to invest in ESG due to the way that they invest or the way that they look at risk management. "Reputational risk is very important, whether it is pollution or emission scandals or other safety issues, or even dreadful or wasteful misallocation of funds."

He referred to a South Korean company that instead of distributing dividends to shareholders, or investing in other profitable enterprises, spent it on a trophy office building in the very expensive Gangnam district of Seoul. The share price crashed over the next 12



months. "You can see how pivotal ESG can be to company valuations," commented El-Shoura.

The third element is the alignment of the company with all its constituents such as employees, shareholders and so forth. "HNW millennials in particular are keen to align and express social, political, or environmental values through their investment practices. The baby boomer generation who came before them were far less focused on these areas."

El-Shoura said that with an estimated USD30 trillion to be inherited by the millennial generation over the next few years, this will have another massive impetus on SRI and ESG activity.

He also then highlighted three central challenges for ESG investing. Firstly, the reporting of ESG, as there is no fixed template for reporting the way in which ESG is managed within an organization. "That," he said, "actually makes it very difficult for many investors to compare apples with apples."

Secondly, due to the nature of passive investing, the only type of ESG that can actually be included is a very basic methodology which simply excludes sectors. "If we wanted to incorporate ESG into passive investments, we would need definitions that are more sophisticated."

Finally, he noted, many investors actually outsource an element of their ESG scoring to third parties such as MSCI, or Sustainalytics. "Their methodologies are actually vastly different, so again we find that comparing one to the other is also quite difficult."

To conclude, El-Shoura observed that the impact of SRI, ESG, the millennial generation and ever-more women as investors will all significantly impact the formation of portfolios and how they are managed. "It is a very exciting time we see ahead," he ended. ■