ESG – its Growing Impact on the World of Wealth Management in Asia

It is estimated that the managers of one-third of all professionally-run assets globally, equivalent to over USD20 trillion, now use Environmental, Social and Governance (ESG) data to drive their investment decisions, and far more than that – an estimated 75% of them today – pay some attention to ESG criteria. As the world's leading global investors continue to embrace ESG, what progress is being achieved amongst investors in Asia, and specifically are Asia's private clients jumping increasingly on the 'ESG Express'? A fascinating Hubbis Digital Dialogue analysed the state of play globally and in the region on November 5, with some truly experienced proponents of ESG participating, including leading private bankers, asset managers and consulting firms. Together they painted a picture of an unstoppable force in the world of investing, but also one that needs to be better understood by the wealth industry and the private clients in order to boost its adoption in Asia.

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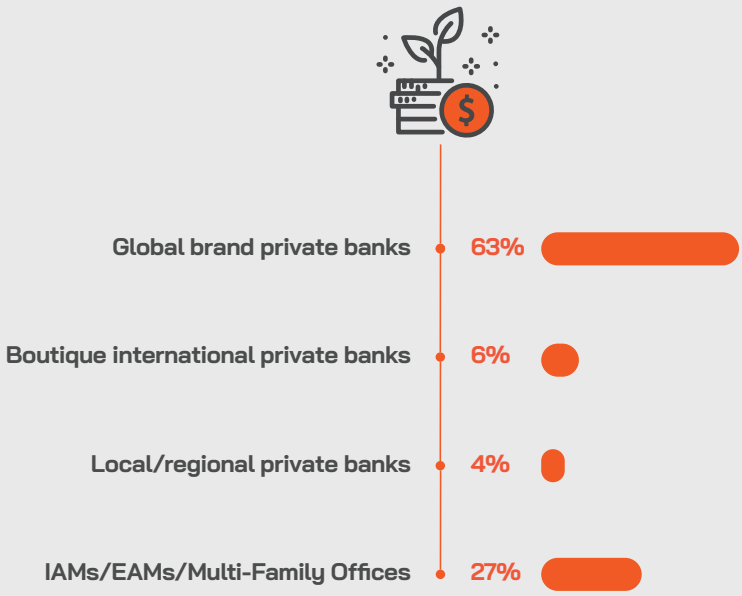
Environmental criteria aim to define how a company performs from an environmental impact perspective. Social criteria define how a company manages relationships with employees, suppliers, customers, and the communities in which it operates. And governance deals with a company's corporate culture, its leadership, executive and broader compensation, audits, internal controls, and shareholder rights. In short, these ESG criteria are used to help investors identify companies with corporate values that they feel comfortable with and therefore that meet their investment requirements.

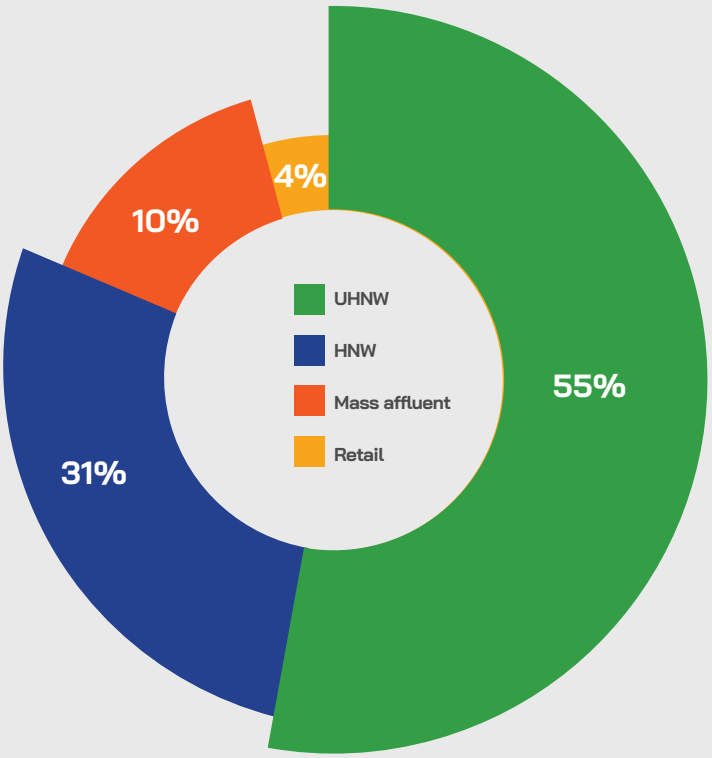
Most professional investors today rely on third-party sourced ESG ratings data and there is no doubt that the collective influence of the providers of such data is set to grow and increasingly influence the decisions of fund managers from sovereign wealth funds through the world's largest pension funds and all the way down to retail investors, especially these days the HNW and UHNW investors.

ESG is therefore an increasingly popular investment strategy worldwide. A growing body of research shows that ESG can reduce portfolio risk, generate competitive investment returns. Moreover, ESG investors accept this and recognise also that by supporting sustainable companies they can make a positive difference whilst harvesting competitive financial returns. This recognition is spreading and the growth of ESG in both popularity and coverage is almost certain to continue.

IN THE WEALTH MANAGEMENT INDUSTRY IN ASIA, WHICH ORGANISATIONS ARE LEADING THE WAY IN TERMS OF PROMOTING ESG-DRIVEN INVESTING?



IN THE WEALTH MANAGEMENT INDUSTRY IN ASIA, WHICH TYPES OF INVESTORS ARE LEADING THE WAY IN TERMS OF ADOPTING ESG-DRIVEN INVESTING?



Doing the right thing

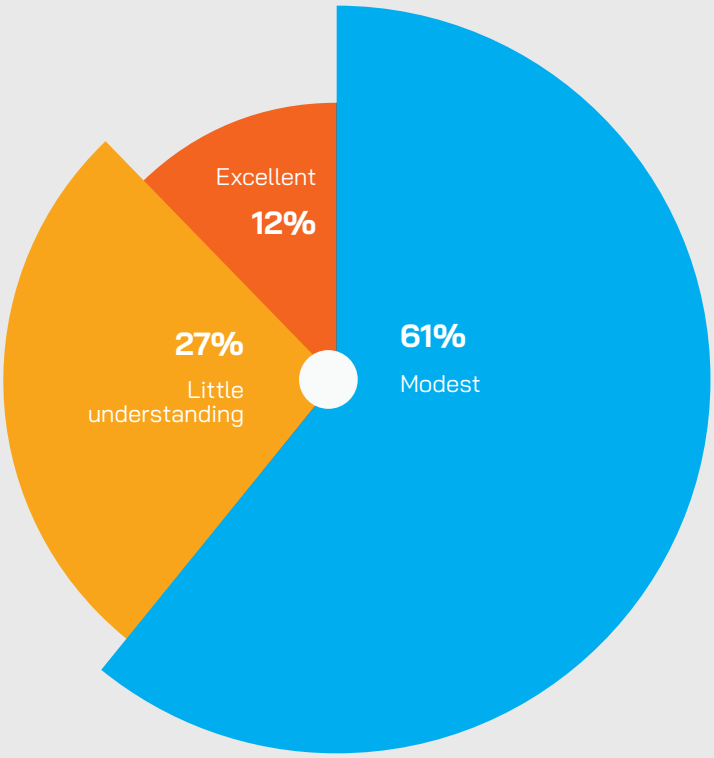
An expert opened the discussion by remarking that not only are ESG principles helpful for investors in 'doing the right thing' but there is now real empirical evidence in ESG's favour in terms of returns. "This is well beyond a marketing gimmick," he said, "as more and more investors understand that those companies' investment products with very high ESG credentials actually perform better and deliver better returns than those with lower credentials. Europe leads the game, then the US and Asia, although late, is now really waking up to this phenomenon."

He explained that his bank signed up to the UN's Principles for Responsible Investing (UNPRI) back in 2005 and had been a champion of ESG since. "We even report the E, S and G scores in the reports we send to clients or our client statements, thereby providing our clients an insight to what their portfolio looks like in terms of ESG. We also have what we call ESG scorecards, where our bankers and our investment advisors sit down with clients and look at their portfolio. Looking through an ESG lens, clients who have an interest can then see how they can improve the ESG performance of their portfolio."

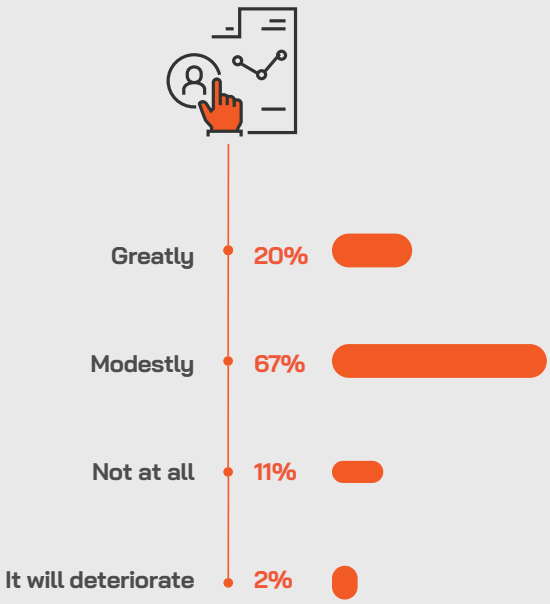
ESG rises from the SRI roots

Another expert explained that ESG evolved really some two decades ago out of the socially responsible investing (SRI) drive, whereby asset owners, it could be pension funds, endowments, family offices had their own religious or ethical preferences, and that they wanted to reflect in their portfolios. "Then we have seen within the last

HOW WOULD YOU CHARACTERISE THE GENERAL UNDERSTANDING OF ESG INVESTING PRINCIPLES AMONGST ASIA'S UHNW AND HNW WM CLIENTS?



TO WHAT EXTENT DO YOU THINK ADOPTING ESG INVESTMENT CRITERIA WILL ENHANCE YOUR CLIENTS' PORTFOLIO PERFORMANCE?



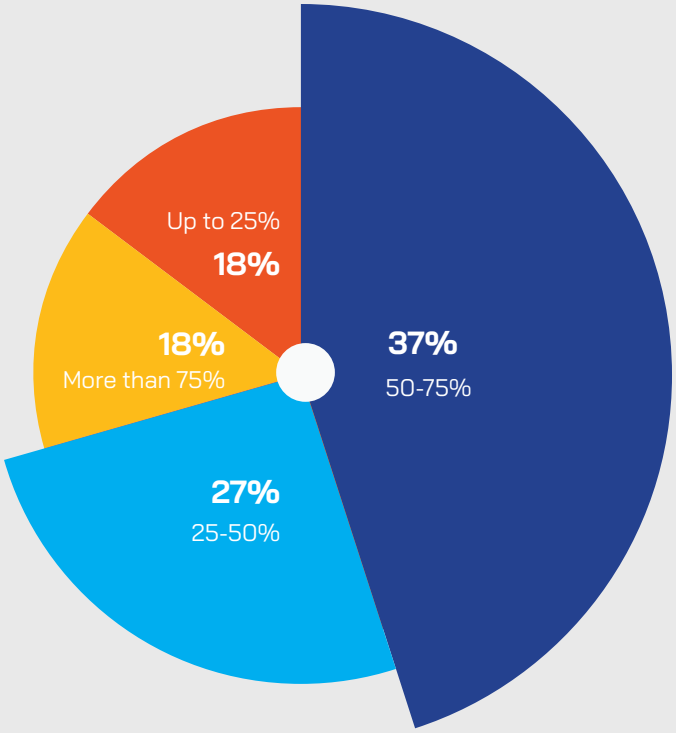
roughly eight years or so that ESG has gone mainstream with asset managers as well as asset owners who might not have any particular ethical or religious criteria. People see the impact, for example so many of the disasters around the world – such as fires across Australia or California - are events accelerated by climate change, which is one of the key environmental risks that people focus on."

He explained that the biggest roadblock amongst potential investor clients in Asia is the notion that embracing ESG means sacrificing performance. "But there is plenty of evidence today that it does as well, or better. So, in the last year and a half, I'm seeing a tremendous acceleration in terms of Asian asset owners, Asian family offices, and others on ESG."

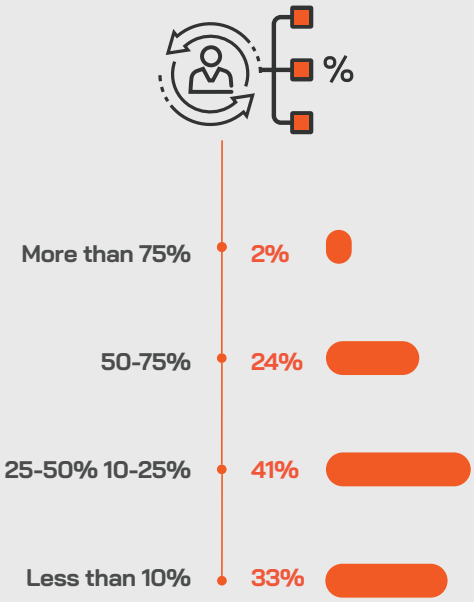
Insuring a better future

On the insurance front, a guest highlighted how ESG is now far more engaged in their investment decision process. "We really try to incorporate ESG parameters or considerations when it comes to the decision making of our business model, and one of my areas is the China/Asia green bond market. Having started slowly, the pace of learning and the pace of enhancement of ESG within the China and Asia market is actually tremendous. China green actually started off only in 2015, and just in the last couple of years the market has multiplied in size and also in terms of the diversity of issuers that you can find many interesting types of underlying projects to invest in. This whole area is also under researched and under allocated from a global investor perspective, be it institutional or private family offices or private banking clients,

WHAT PERCENTAGE OF ANY WELL-MANAGED EQUITIES INVESTMENT PORTFOLIO FOR ASIAN UHNW AND HNW CLIENTS SHOULD BE SELECTED BASED ON ESG CRITERIA?



WHAT PERCENTAGE OF EQUITIES INVESTMENT PORTFOLIOS FOR ASIAN UHNW AND HNW CLIENTS ARE TODAY DETERMINED BASED ON ESG CRITERIA?

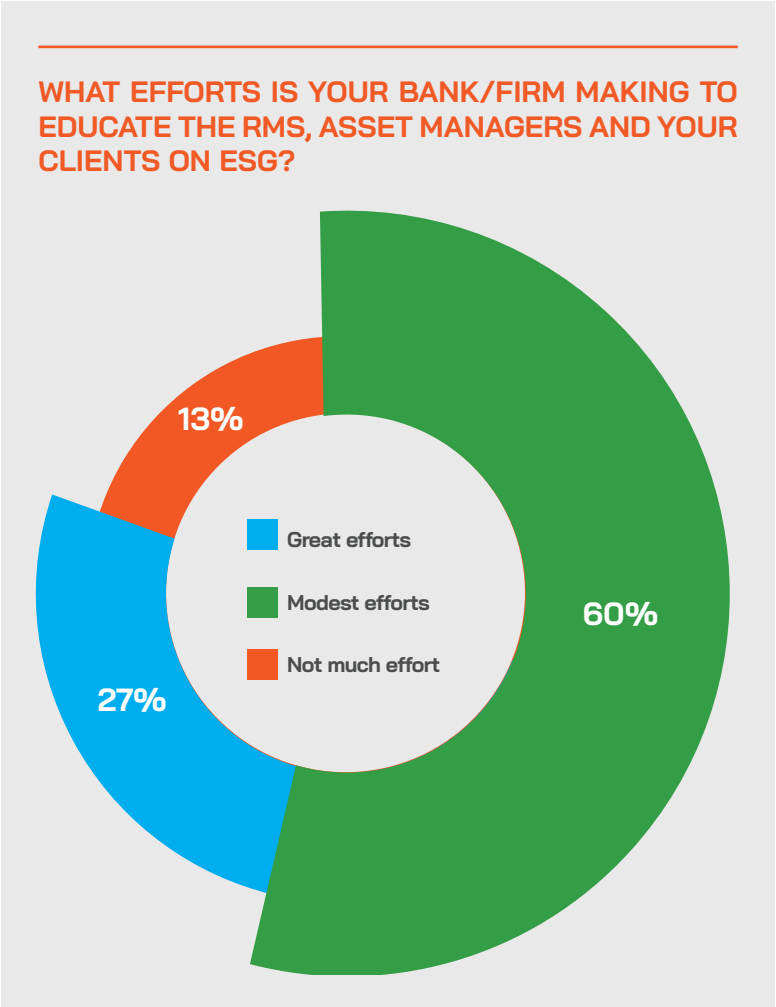


and represents a great opportunity, as the green bond space is actually providing equal if not better, long term risk adjusted returns for any multi-asset portfolio."

A wide array of global risks

Another expert pointed to work their firm had conducted in helping towards the UNPRI and to set the standards for the TCFD, a taskforce for climate reporting standards. "At the World Economic Forum, we talk annually about global risks, which might include things like climate change, extreme weather, social unrest, civil unrest, cybersecurity, and other key global risks that main corporate leaders are identifying around the world. We then also support the policy makers in thinking about the kind of regulations they want to develop, the impact on corporations, and also the support and framework for corporations to be able to comply."

From the asset owner's perspective, they reported what amounts to a sea change in the last couple of years in its ESG ratings, and how to integrate the consideration of ESG factors into the selection of asset managers. "Some seven years ago, this was not well received, but today we have seen that corporate pension schemes are widely involved, the sponsors now want to meet with their corporate sustainability teams. They are now very interested to learn more about different ratings and how they could actually start to develop ESG theme products. In a pension forum recently, around 78% of our audience of 200 plus were keen to see the government pension scheme in Singapore take up ESG themed funds. In short, the momentum is right ahead of us."



Resilience built into portfolios

A guest reported how his role now incorporates being head of sustainable investments. He reported that his firm had been focusing on the private side for some years a ready, investing into companies that were looking at sustainable solutions, but in general on the public markets side there is not great awareness, and somehow in Asia many investors think that they must sacrifice some returns in order to be more ESG-centric. "But this year's downturn has showed us that ESG portfolios were more resilient, and given the magnitude of what we have seen unfold in the pandemic, and as an advocate of sustainability, we really need to help the clients understand that there is absolutely no sacrifice of returns, if anything the risk adjusted returns are better. Advisors, either inside banks or outside need to up their understanding and their communication of these advantages. "Improving the education for the practitioners as well in terms of vocabulary and discussion points will help influence client behaviour."

Early to the table

A banker offered his insights, noting that many institutions and asset managers now have decided to apply a fully incorporated ESG investment process across

all their products or almost all their products. He said his bank decided on the same approach three years ago, incorporating ESG into all our products, and to even go one step further. He noted it was important to see the difference between sustainable investing and ESG. With ESG the investor might restrict themselves in scoring the companies, while remaining invested in almost all the sectors, all the industries, while with sustainable investing, they are going one step beyond simply scoring ESG, and more into an active, higher conviction approach.

"So, this is where we stand today at the bank," he explained. "ESG is across all portfolios, but then one step further to active analysis of what the business model is, the risk of disruption, is the company a long term solution provider in terms of green energy, in terms of being a leaner economic organisation, in terms of a more responsible consumption cycle. And all this requires a lot of qualitative analysis."

The world we all live in

To explain this to the clients, he said that it is really important to try to understand what world we will be living over the next five years to ten years. "There is no alternative than to see the regulation and the consumption and the demand from private agents to move towards something that will start to internalise all the externalities that the market has not priced in before," he remarked. "And if you believe in this vision, then the immediate conclusion is to say, companies that already are matching this business model will do better than those who are not."

And that, he said, is partly why 2020 has been an exceptional

Expert Opinion

ADELINE TAN, Head of Investment Advisory, Mercer

"At Mercer, we are embarking on the journey to help clients transform their current investment processes, where there is interest and a belief that integrating ESG considerations and even capturing thematic opportunities, can be an effective way to generate sustainable investment returns. Our clients are largely long-term minded asset owners but we believe that individuals are likely to follow suit, in the same way that institutional money allowed creation of index-tracking funds, that require large AUM to operate at low-cost, so will actions by institutional owners drive the development of new products."

Post-event Perspectives

In our Hubbis post-event survey, we polled delegates for their perspectives on the growth of ESG investing in Asia, and where they think it is making greater inroads, and why it might be slower progress in the region than in Europe and the US. We found that most of the respondents said 'yes', and that most of those who said 'no' reported that they were learning more about ESG in the meantime. We have selected the following comments:

IS YOUR BANK/FIRM ACTIVELY PROMOTING ESG-DRIVEN INVESTMENTS, AND IF SO WHY OR WHY NOT?

- We have selected some of the more pertinent comments.
- Yes definitely - sustainable investments are the key to our future.
- Yes, as ESG is proven to increase company valuations, and also ESG is benefitting society at large.
- Yes, we are consultants who advocate ESG integration and adoption.
- Yes, it is core to our offering now, and we may also launch an ESG fund.
- Yes, as ESG is increasingly becoming a popular investment strategy worldwide.
- As a multi-family office, it is a subject that is more and more important to our clients.

year globally in terms of raising AUM on sustainable product, on ESG products, globally speaking, and increasingly in Asia, which has started late. And I can say I'm very confident that Asia will catch up, as Asia has been quite sometimes late in many trends seen in asset management, but then can move very fast."

Mining down to specifics

Another guest remarked that ESG tends to be sector specific, and that there is no one size fits all ESG list of issues. He offered the example of a coal mining company facing environmental issues and climate risk, or perhaps biodiversity would be most important issues, whereas for Facebook and Google, it is areas such as data privacy. "The first step is to identify which are the material issues, or what are the most relevant topics for the companies that you're evaluating," he observed, "then the next step is to figure out how are they performing on with regards to managing that risk, and also comparing them to peers."

He explained that many leading asset managers are now taking the approach of defining their own view of materiality, which is what his firm is currently doing. "We do subscribe to some third-party data vendors like MSCI and Sustainalytics, but we don't rely on their ratings simply because the challenge with their third-party ratings is they are trying to address a wide variety of client interests with one particular product. Some of the leading asset managers are taking that as a starting point and then defining relevance to different industries, and then focus on those, as we do, while conducting our investment

- Yes, our initiative in this area is about a year old now. We are promoting ESG driven investments in order to remain relevant to our clients, as well as to remain relevant true to our values.
- Yes in a limited form through an ESG ETF, as ESG-driven investing is very 'green', in the sense that not many clients incorporate ESG values yet.
- Yes, it is in the mainstream now.
- Yes, it is part of our investment consulting philosophy and fund due diligence processes."
- Yes, ESG cannot be ignored, it is a trend that impacts every stakeholder in society, regardless of age, gender, occupation, and so forth.
- Not really. We do not specifically promote ESG focused investments, however the company that provides us with the recommendations does have ESG as one of the criteria. As most of our end clients are individuals, we do not have the same drivers as maybe a pension company or other larger institution.
- We are not currently explicitly incorporating ESG as a factor. We still focus on the fundamental of the investments, but I think ESG is part of the fundamental analysis, such as if a company's business may cause damage to the environment, then we may consider it face regulatory risks, for example if governments roll out new policies to tighten the industry regulation and thereby negatively affect the company's business.
- Yes, we are now taking into consideration ESG criteria when recommending investments and in general conversations with clients.
- Yes. We are rated A+ in the UNPRI for 2019. ESG is a core element in terms of our fund manager selection and we aim for all of them to be signatories of UNRPI.

ARE YOUR PRIVATE CLIENTS IN ASIA ADOPTING MORE ESG-DRIVEN INVESTMENTS, AND IN YOUR VIEW, WHY OR WHY NOT?

- Slowly, as they seem unsure of the actual benefits.
- Yes, especially the younger generations.
- We see rising interest, but not significant yet.
- No, as there is no solid, concrete evidence that ESG-driven investment achieves outperformance.

analysis and portfolio construction. So, I think that is probably the best way to approach this because there ESG ratings or ESG scores in general have a few flaws, they're still developing. However, I do think we are at a much better stage than we were five years back as well, but we need to sort the noise out and to differentiate yourself as an asset manager you have to do your own thinking, create your own value-added and then apply smartly."

Accepting the standard

He added that there are more widely accepted standards coming through, for example the Sustainability Accounting Standards Board or the SASB in the past several years, or historically, for sustainability reporting, the Global Reporting Initiative or the GRI, he reported had been followed for over a decade by corporates.

"I think combination of these two plus I would say adding your own perceptions and ideas is probably the right way to do it," he said. "The way I see this is there is in some ways like market inefficiency with regards to how market is perceiving and factoring in ESG risks, so you have to do your own thinking, there is some qualitative input required."

China and Green Bonds

Another expert agreed, noting that the Chinese regulators in trying to support the green bond market development are trying their best to adopt the international standard in terms of defining 'green'. "The first step is to get your bond certified as a green instrument, and for this China and Asia are adopting pretty much 99% the same standards that ICMA or the Green Bond Principles are advocating, so Asia is in line really, it is a good starting point for

- Yes, because ESG can reduce portfolio risk, and generate competitive investment returns.
- Not yet in Asia. Private clients in this region are not yet sensitive to these issues.
- Yes, they are. A good percentage of the clients are being driven by the next generations. And the next generation demands a change in the status quo. They are concerned about the environment. And they want to invest with good conscience.
- Yes, as there is now more awareness of ESG through education and media.
- Not really from our viewpoint. Malaysian investors are just aiming for a quick win with no concern for ESG yet.
- This is a 'work-in-progress' for Asian clients, partly because the decision-making power still rests with the first and founder generations who are less ESG-aware compared to the second/next generations.
- Not so much. The younger generation is more interested in ESG. The older generation who are still mainly controlling the assets are more concerned with returns.
- It is a topic of interest, but still they are looking for where is money to be made. It is more of a nice thing to have built in rather than a must-have at this time. I guess that the focus will increase over time.
- Yes, I think our clients generally focus on the G (which is governance), but not so much on E and S, mainly because corporate governance is easier to track and monitor, whereas for E and S, the standards are a bit controversial, so it is hard to determine whether the company is doing well in these areas.
- Yes, they have the idea to take on more ESG-driven investment, but they don't know how exactly to implement that concept."
- Yes, awareness on environmental and climate changes have enlightened clients, encouraging them to look into ESG-driven investments. Some would like to do their part for society, and also the returns of investments are appealing."
- Our clients are definitely doing more with due consideration to ESG. This is a slower process because it is not necessarily straightforward. People have different views. There is also a feeling that many people are saying they act this way, but then do things that are not ESG-driven at all. The banks are definitely covering themselves with as many ESG credentials as they can, but some of this is definitely not justified when you look deeper."

the future development. And as we move on to more sophisticated incorporation of ESG criteria in our investment decision or post investment, how are we going to measure the environmental impact of this portfolio of bonds? I think that part a lot of industry best practice and also education needs to be done in order to bring both the issuer, the third-party verifier, the asset managers as well as the investor to bring everyone on the same page.

Education required

A banker then commented on the need to educate teams internally before disseminating the ideas to the clients. Institutions are engaging more and more in Asia, but private clients less so, meaning that there is much hand holding required.

"It starts with very thoroughly educating your own staff before you can even start offering products," he cautioned, "and it is a very significant effort, because your frontline staff, first of all, probably doesn't understand it, secondly might not buy into it. And the bank, the distributor, must ensure that what is later offered is truly credible. We are lucky enough that a sister company has a whole team of sustainable investment analysts, some 36 across the globe, and on top of that help the bank with the ratings within our products. They in turn work with eight different companies like Sustainalytics, MSCI, ESG Research, and others to make sure that the ratings they come up with are very solid. We have not yet integrated that mainstream that in 100% of our products and services, but we are working towards that. For example, our discretionary mandates, we want to integrate ESG 100% in those by 2022."

Post-event Perspectives

In our Hubbis post-event survey, we polled delegates for their perspectives on why much more education is required in order to help propel ESG-driven investing in the region, both amongst wealth management professionals and the private clients, and what else needs to happen to advance the cause. We have also selected the following comments to offer further insights from the market.

ARE YOUR RMS AND ASSET MANAGERS KNOWLEDGEABLE ON ESG PRINCIPLES AND ESG RATINGS METRICS, OR WHAT NEEDS TO HAPPEN, E.G. MORE TRAINING/EDUCATION, GLOBAL CONSENSUS STANDARDS, AND SO FORTH?

IN YOUR VIEW, WHAT NEEDS TO HAPPEN IN THE ASIAN WM INDUSTRY FOR ESG INVESTING TO REALLY BLOSSOM?

- We are learning about ESG and developing more framework and principles within the Investment Team. It would be good to have global consensus standards. At the moment, we just rely on those metrics disclosed on Bloomberg, which is not really adequate.
- We really need to educate ourselves internally before we can educate our clients.
- ESG is a new topic in Asia and everyone is picking it up, but we definitely need more training.
- We are starting to be more and more knowledgeable on ESG and encouraging our staff to follow training and certification in that space. This is still relatively early stage and thus far mostly to meet demand from Europe.
- Not really, it is a process, we are still coming to terms with it. It would be fair to say that we need a fair bit of education and training before we are all on the same page. We do have ESG champions within the firm, and we hope they will drive the process of educating more broadly.
- While ESG is rapidly evolving, the principles and ratings methodology and so forth are still not fully grasped by RMs and asset managers. This gap can be filled via internal and external training, and perhaps finding ways to induce them to be self-motivated to explore ESG, for example comparing the performance of ESG vs non-ESG investments.
- Only to the point of the information we receive from our sources. We follow their metrics rather than anything in house. Our client

Looking to the longer term

Another panel member agreed with these views and plans, and added that "for us, our standpoint is still that if you're a long-term investor and you think about long-term sustainable returns, you really need to think about what your money is actually creating in terms of the world that we live in." Hence ESG-centric portfolios should be the norm, not the exception.

A guest commented that ESG, sustainable or impact investing can be value-based investing, it is not one or the other. He said the question for fund managers is whether their public markets strategy can also reflect their value system or ethos around investing, and the same for private clients. "What does wealth mean to you as an individual or family, that is a conversation which I think needs almost reworking on how people have looked at their wealth and what it needs to do. For us, we have started this journey in all earnestness in this year, and I am championing it, aiming to understand where we are in the context of what we are trying to do in the portfolios, and also take that step back to almost get the client to understand that there has to be a bigger anchor around how they invest. Accordingly, I would say impact investing is actually about both types of returns - financial and societal - and that needs to be explained. For me, this is a great journey."

Screening processes

A banker reported that his bank takes the first stage as a screening process, based on 115 data guidance is always founded on third-party providers rather than our own in house criteria.

- Yes, to some extent, but I think more education and much clearer standards are necessary. Most importantly, when markets realise that a company with better ESG tends to perform well financially, it will encourage more and more people to study it.
- We feel that there are no standard requirements to meet ESG and the market lacks a well-known authority to judge ESG ratings for companies or their investment products.
- Yes, I believe fund managers understand in depth, whereas us as RMs, we have an idea of ESG standards and how they are applied to a fund or selection of stocks, we understand the principles, but the application and rating process are relatively new.
- The basic principles are easily understood. There are still considerable differences and views on how 'ESG' a certain company or activity is. It will take time for these things to get ironed out. Is LNG bad for the planet? It is not the worst hydrocarbon out there. ESG wants to paint them all as bad. What about the different directions taken by Shell and Exxon. Exxon is still hardcore oil. Shell tries to build a future towards sustainability. Which is right? Closer to home, was the tax discount on buying Tesla cares in Hong Kong ethical? The power they use to recharge batteries is using high percentages of brown coal, but it was the campaigning by other luxury motor companies that changed the rules.
- We now need to see ESG delivering better alpha and lower risk versus traditional offerings.
- We need to show alpha for an ESG fund versus the non-ESG fund; at the end of the day, investors look at returns/yields.
- We need to learn and hear more about dealing with the greenwashing issue, and come up with a consistent taxonomy across markets, as well as come up with a robust framework/matrix on how to evaluate and price green opportunities.
- Education is required and I think it would be good if the world really creates a lot more transparency around all the anomalies, for example looking to the very end of the carbon chain to see what process is really more ESG compliant. This is slowly evolving now and people short cutting this process are gradually being called out. I think it is now almost irresponsible to give investment advice without knowing the ESG impact - not only for the planet, but also a true view of how an investment will perform.

touchpoints and different factors – the very traditional ESG axis, as well as action and results. He explained it is vital to see the intentions, the actions and the outcomes, as there had been so much 'greenwashing' n recent years, as corporations try to climb on the ESG bandwagon, even if they are really playing smoke and mirrors. He added that the bank also assesses its 115 data points based on the Sustainable Development Goals, centring on goals, such as fighting against inequalities, better education in emerging countries, water accessibility and so forth. And the bank also makes assessments based on any company's exposure to controversies, based on a 1-5 scale.

But he said when it comes to communicating this effectively to RMs and then to private clients, some arbitrary score such as 55 is not comprehensible, in fact, it is somewhat meaningless. "With the clients," he explained, "you need concrete metrics, very concrete result in terms of carbon intensity, water intensity, temperature alignment tools, it makes the discussion much easier, much more concrete, and much easier."

Dedicated to the cause

An expert closed the discussion explaining that they as a fund managers spend a lot of time dedicated to the pursuit of knowledge in these areas amongst the wealth management community, aiming to truly communicate and educate as well and as regularly as possible.

"There is no straightforward way to do this," he said, "but we try to share our learnings with the broad market so as to make sure that there is more wider adoption and there are fewer barriers to entry for even smaller players, or clients who are maybe sceptical about this. We are dedicated to being a part of furthering responsible investment." ■