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How the World of ESG is Evolving to Help Filter & Select More Impactful Investment Opportunities

The Hubbis Digital Dialogue event on 17 March focused in on the 'whys' and the 'wherefores' of ESG-driven investment and issues of sustainability for Asia's private clients. This is a subject about which Swiss asset manager GAM Investments has both considerable passion and great experience. Stephanie Maier, the Global Head of Sustainability and Impact Investment at GAM Investments, was one of our five expert panellists. We have distilled some of her very insightful observations for private clients in this short article, which we have presented as a Q&A.

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STEPHANIE MAIER
GAM Investments

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How do you incorporate environmental, social and governance issues into your investment decision making at GAM Investments?

It varies across different strategies, and is forward-looking as the emphasis on some environmental, social and governance issues will differ in the future. Secondly, we are active stewards of our clients' capital, so as we analyse companies and engage with them to better understand the risks and opportunities. It is also increasingly about how we drive better outcomes and performance from those companies for our clients.

There is also the broader issue of the rising prominence and importance of the investment management community in the transition towards net –zero. The industry can really take a leadership role in helping our clients to decarbonise their portfolios and to reach some of the other key sustainability goals. In the wealth management market, there is greater focus and thinking around where private money is going, what that capital is achieving, as well as obviously the vital return element as well.

Transparency is vital, both for our clients and for us. Accordingly, we also provide our clients with external ESG scores for the strategies they hold, and we also look at a set of different climate scores on the portfolio and illustrations on the companies as well. This is an area where we're seeing a lot more focus.

And finally, the fourth element is the products and the solutions, and here there is great opportunity to deliver for clients. At GAM, we have been developing specific solutions, for example, around climate bonds or thematic equities, where we see clients increasingly interested in understanding and seeking to both drive and navigate some of those big trends. Reaching net zero is one of those big trends, but so too is sustainable consumption, the transition to a more circular economy, and some of the other challenges beyond climate change, such as biodiversity, and health, both areas that clients are really keen to access."

What about ESG data quality and consistency, or perhaps the lack of, and what about the roles of the regulators in helping drive these initiatives?

"Data has been and will continue to be a key issue given that increasingly, ESG-driven investment decisions are informed by this data. The data delivery and analysis is essentially all rules based. So, if the data is not right, then the outcomes are not right. We are seeing increasing scrutiny of that data, and we are also using a wealth of external research providers and data points.

At GAM we also conduct our own fundamental research, because that enables us to understand some of the limitations of the data that is out there, and also to plug some of those gaps and overlay some of that with a vital qualitative assessment as well.

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towards better disclosure on a range of sustainability indicators.

I think the other element around regulation that we really need to touch on is within Europe, where we now have the EU taxonomy, and we have other countries developing their own taxonomies. Accordingly, the definition of what is green, and what is green activity are coming into a sharper and very specific focus from a regulatory perspective.

And I think it is an important conversation and a key part of the evolution, because when we get down to client choice, not everyone has the same understanding or view around what is green. So, this is particularly where taxonomy and the consistency of data and clarity are really key."

"Data, as I have explained, and taxonomy are vital, but so too is the reporting of the findings and the communication around all this. Communication only works if both the information you provide and the receiver of that understand the same thing, in other words, it is essential that they are speaking the same language."

There are detractors who say ratings, scores and taxonomies are more hype than substance and somewhat dismiss them as the latest marketing tool to sell more products. What would you say to them?

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We talked about ESG scores, which really look at the quality of companies, policies, management systems, disclosures. They do have performance elements in there, but we need to ensure that clients understand what that all means. And that is why GAM is introducing more indicators, for example, around the absolute carbon emissions, which tells you something about what the company is actually doing in the real world.

The EU's Sustainable Finance Disclosure Regulation (SFDR) is very important as it imposes mandatory ESG disclosure obligations for asset managers and other financial markets participants. The first deadline was in 2021, and one of the elements that's going to be introduced early next year is principal adverse impact indicators, which is a set of indicators that start looking at the impact of the companies in the portfolio. And that, for example, includes things like the proportion of women on the board, or perhaps the impact in protected areas on the biodiversity side, as well as the carbon emissions score, and so forth.

All this adds up to a robust move towards not just risk metrics and scores but towards impact metrics. The big picture answer is that as an industry we must ensure that the client understands what we mean when we put numbers, letters and diagrams on our factsheets and reports. For this to all be effective, the investors must truly understand what these really mean."

What are some of the challenges and opportunities in relation to data and developing sustainable products for clients? ?

"We are active investors at GAM, and while there's definitely a place for rules-based products [such as indices and ESG ETFs], they are essentially limited by the criteria and the formula that you write in. That means they end up with a lot of big-name tech and financial sector companies as large holdings. But take for example, the banks. There is no assessment built into those indices or ETFs on the emissions the banks finance through their lending or other activities, and there is no direct link to those lower carbon companies that are out there.

But we are seeing an increasing interest in products that can look beyond all those front-line data points and scores to the future and the right opportunities in the years ahead. This is particularly evident in the thematic space, where there is more alignment of green revenues and other sustainable development goals, and these areas are not coming through with sufficient importance or quality in the passive products. And that is where the dynamic, actively managed curation of ideas and opportunities scores so well.

The other challenge around some of those more formula-based approaches is the data is largely backward-looking data. And we are now entering into a world where we think regulation is going to play a much larger role in shaping the market and the winners and losers. We have consumer preferences driving more sustainable practices, and to more sustainable products.

Now, we are seeing more clients thinking about what it is they really want to target. I think we are moving away from ESG as just a risk lens, which is definitely still important, and more towards how we integrate ESG factors alongside the impact, and then leading through to the opportunities that arise. That process and thinking is leading us to the curation of a much more varied set of companies and opportunities that are of greater interest to clients." ■