

WHY SUSTAINABLE INVESTING AND WHY NOW?



Live more,
Bank less

Figure 1: United Nations (UN) Sustainable Development Goals
Source: UN



1 THE WORLD IS CHANGING RAPIDLY

We are living in times of environmental and sustainability changes, from climate change to inequality. The United Nations has identified 17 “Sustainable Development Goals” (SDGs), a blueprint that aims to address the current global challenges the world faces, by 2030.

Indeed, sustainability is no longer a checkbox exercise in companies’ annual reports, but fundamental to the fabric of modern business. And as investors, how and where we choose to park our money matters—not only to us, but to society at large.

2 COMPANIES THAT DO GOOD, DO WELL

Firms with a strong sense of purpose and that embed sustainability in their DNA tend to perform well. For example, index provider MSCI’s 2017 research found that companies with higher environmental, social and governance (ESG) ratings are associated with higher profitability and lower tail risk¹. Another study by the University of Cambridge in 2019 found that Chinese technology small and medium enterprises with gender-balanced management teams performed better during adverse conditions, posting a 19.5% and 24.8% rise in profitability and return on assets, respectively².

Figure 2: Examples of companies hurt by inattention to sustainability

Conversely, companies embroiled in controversies increasingly find themselves punished by shareholders, regulators, and the public.



The Deepwater Horizon oil spill in the Gulf of Mexico in 2010 cost BP more than US\$60 billion in lawsuits, economic and clean-up costs³



In the 1990s, accusations that Nike used sweatshops and child labour hurt its image and sales. It spent the next decade changing its practices



Singapore’s water treatment firm Hyflux faces criminal investigation for corporate governance breaches; its stock was suspended and it needed a white knight investor

In the age of social media, ESG violations can go viral quickly, hurting a company’s branding and customer trust for a long time. The loss of “social license to operate” can severely impact business and financial performance.

3 SUSTAINABLE INVESTING AND ALPHA GO HAND-IN-HAND

Investing sustainably need not mean sacrificing returns. On the contrary, research has shown that companies with strong sustainable practices tend to outperform the broader market or peers. For example, over the past five years, ESG leaders in the Emerging Markets (EM) Asia Index beat the broader index by 266 basis points (Figure 3).

Other studies concur:

Bank of America Merrill Lynch’s (BoAML) 2019 research on US equities found that stocks with strong ESG scores outperformed the broader S&P 500 Index by up to 3 percentage points every year between 2014 and 2019⁴.

A 2015 study on public companies across Asia, Europe and North America, by asset manager Robeco and the Hong Kong University of Science and Technology Business School, concluded that Asian equity investors can enjoy higher returns and lower portfolio risk when they consider ESG factors, particularly corporate governance⁵.

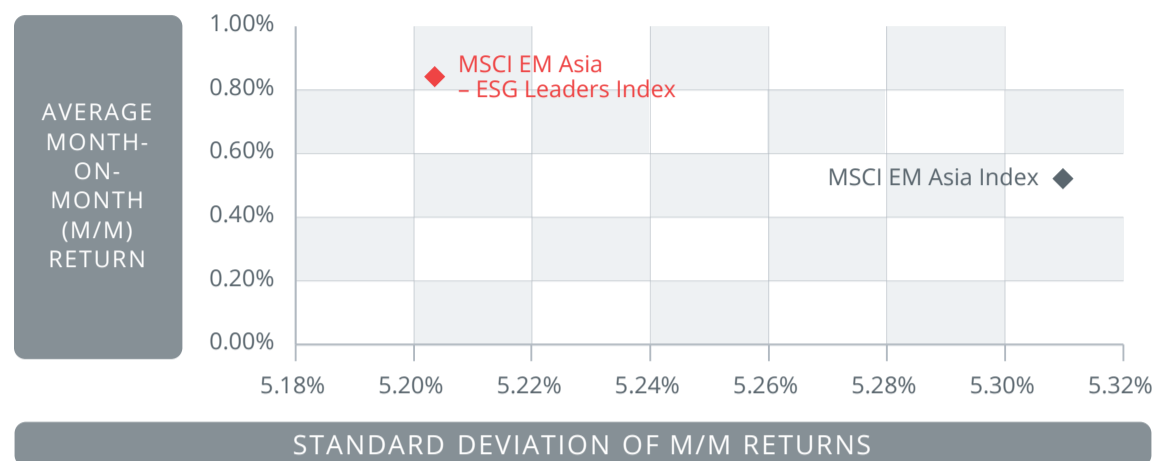


Figure 3: In emerging Asia, ESG Leaders have outperformed the broader index
Source: MSCI, DBS, as of 29 May 2020. Performance in USD and net of fees

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Figure 4: Risk-return Profile of MSCI EM Asia Indices

Source: Bloomberg, as of 8 May 2020



4 A SUSTAINABILITY FOCUS HELPS MITIGATE RISKS

Sustainability has proven an effective risk management tool for companies and investors alike. From an investment standpoint, sustainable assets or portfolios have demonstrated lower risks. MSCI's EM Asia ESG leaders, for instance, show lower standard deviation (a measure of risk) while delivering higher average returns compared to the broader index.

5 GO WITH THE MONEY FLOW

Sustainability increasingly plays an integral part in investors' decision-making, investment philosophy and process. The interest is clear: in the United States, sustainable funds' assets under management surged to a new high in 2019, fuelled by record net inflows of nearly four times compared to the year before⁶.

Sustainable funds' growth trajectory is expected to continue. Institutional investors, including large asset managers and asset owners, are leading the pack, as evidenced by the rising number of signatories to the United Nations Principles of Responsible Investing (UNPRI). The UNPRI are a voluntary set of six principles to incorporate ESG into investment practice. Some companies use the UNPRI as screening criteria to evaluate asset managers.

Figure 5: Sustainable Funds' Estimated Annual Flows

Source: Morningstar Direct, as of 31 December 2019

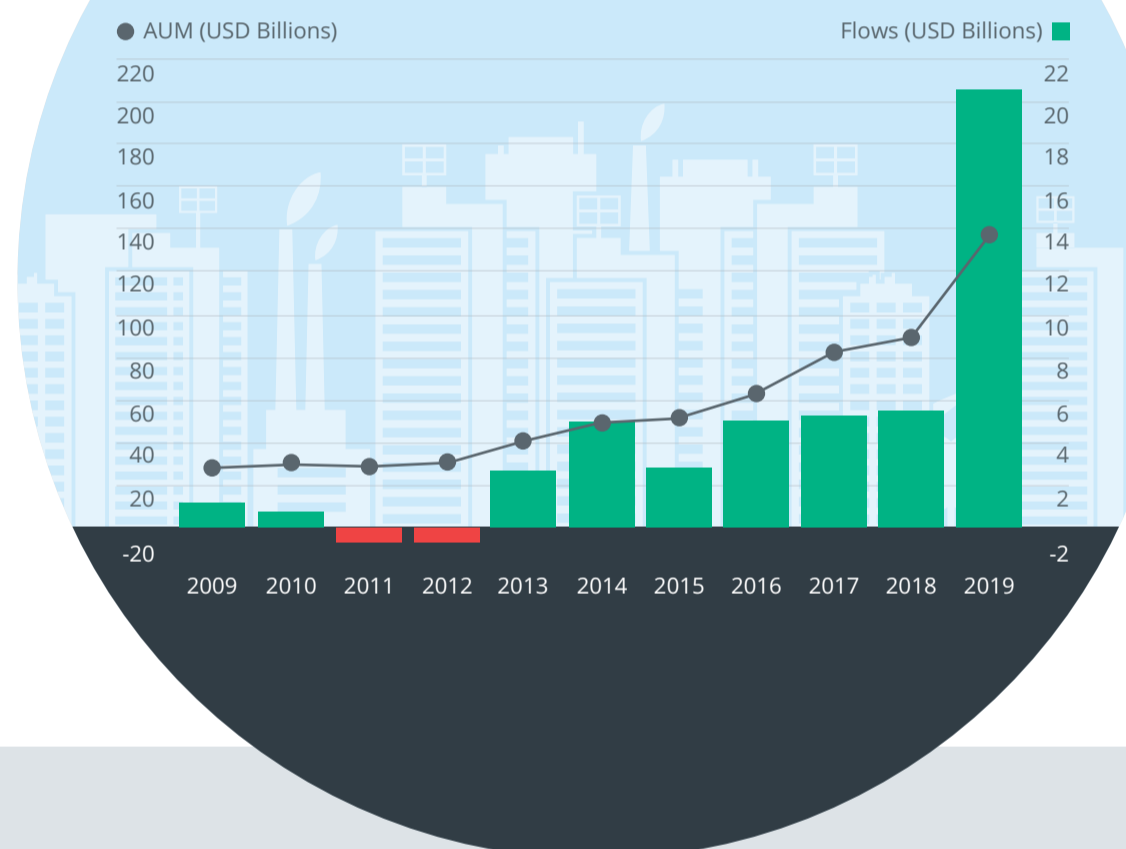
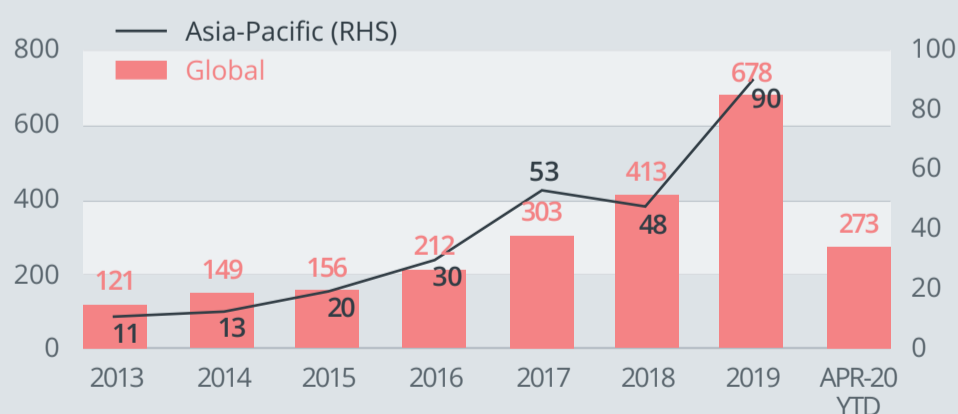


Figure 6: Number of UNPRI Signatories, 2013 - April 2020 Year-to-date (YTD)

Source: UNPRI, as of April 2020



Examples of institutions serious about investing sustainably include Japan's Government Pension Investment Fund (GPIF), the world's largest pension fund, the California Public Employees' Retirement System (CalPERS)⁷ and Norway's Norges Bank Investment Management⁸.

Rising demand for sustainable investments is poised to boost valuations, which will, in turn, benefit investors. As an investor, you can ride this wave by considering sustainable funds and companies or integrating ESG holistically into your portfolio.

FOOTNOTES:

1 MSCI, "Has ESG affected stock performance?" Published 29 November 2017. Retrieved 3 June 2020, from <https://www.msci.com/www/blog-posts/has-esg-affected-stock/0794561659>

2 IHS Markit, "Exploring ESG trends in the APAC markets." Published 24 April 2019. Retrieved 3 June 2020, from https://ihsmarkit.com/research-analysis/exploring-esg-trends-in-the-apac-markets.html?fireglass_rsn=true

3 The Conversation, "BP paid a steep price for the Gulf oil spill but for the US a decade later, it's business as usual". Published 23 April 2020. Retrieved 16 June 2020, from <https://theconversation.com/bp-paid-a-steep-price-for-the-gulf-oil-spill-but-for-the-us-a-decade-later-its-business-as-usual-136905>

4 Bank of America Merrill Lynch, "ESG Matters - US. 10 reasons you should care about ESG". Published 23 September 2019. Retrieved 1 July 2020, from https://www.bofam.com/content/dam/boamimages/documents/articles/ID19_1119/esg_matters.pdf

5 Robeco, "Corporate governance in Asia generates higher returns" press release. Published 3 July 2015. Retrieved 1 June, 2020, from <https://www.robeco.com/hk/en/insights/2015/07/corporate-governance-in-asia-generates-higher-returns.html>

6 Morningstar Direct, as of 31 December 2019. Flow data encompass 300 mutual funds that thoroughly integrate environmental, social, and governance factors into their investment processes, and/or pursue sustainability-related investment themes, and/or seek measurable sustainable impact alongside financial returns. Retrieved 2 June, 2020, from <https://www.morningstar.com/articles/961765/sustainable-fund-flows-in-2019-smash-previous-records>

7 AI-CIO, "CalPERS Puts 'Laser-Like Focus' on ESG, Board Diversity, and Executive Pay". Published 22 April 2019. Retrieved 3 June 2020, from <https://www.ai-cio.com/news/calpers-puts-laser-like-focus-esg-board-diversity-executive-pay/>

8 Bloomberg News, "World's Biggest Wealth Fund Tells Firms to Give It More ESG Data". Published 3 March 2020. Retrieved 3 June 2020, from <https://www.bloomberg.com/news/articles/2020-03-03/world-s-biggest-wealth-fund-tells-firms-to-give-it-more-esg-data>

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