Environmental, Social and Governance: What is ESG investing?

What are ESG investments and why should they be included in portfolios?

Mark Carney, the United Nations envoy for climate change and finance, recently reported that $3.5 trillion needs to be invested every year for the next three decades in order to mitigate global warming risks to the worldwide population. As much as it is socially responsible, Mr Carney also declared that it is "an enormous investment opportunity"i.

Taking this standpoint, an Environmental, Social, Governance (ESG) focus looks beyond the financial factors when evaluating a business or investment process and incorporates analysis of the impact it has on the planet and the community. The term ESG covers a wide range of issues from climate change and natural resources (Environmental), to human rights, and privacy and data security (Social), to diversity and inclusion, and transparency (Governance). Additionally, all of these criteria factor in to whether a business can be considered to be sustainable. As governments and policy makers increase regulations that push us towards a greener economy, sustainable investing must not merely be seen as a fleeting fashionable trend or niche. In fact, it's one of the strongest ways to help ensure long-term returns.

Using ESG analysis, alongside financial analysis, provides a more holistic way of assessing risk and opportunities. As we move forward in this new decade the world faces a multitude of severe challenges, including increased plastic pollution stemmed from the COVID-19 pandemic, around 75% of which will end up in landfills or the ocean[ii], decreasing availability of safe drinking water and rising malnutrition for many in developing countries, and the tackling of racial injustice to highlight just a few. These are not new issues, but the way the global standpoint has shifted is. More and more people are becoming conscious of the impact they have on the world and are welcoming sustainability as an essential cornerstone of good business and economic growth. This is made apparent in the US SIF (The Forum for Sustainable and Responsible Investment) Trends Report for 2020, which disclosed that the amount of professionally managed investor assets which consider ESG criteria grew to $17 trillion. That's is a 42% increase since 2018[iii]. Therefore, at LGT Vestra we believe that all companies wishing to achieve long-term success should consider their impact on the environment and society.

When it comes to putting these principles into action, investors can take a three pronged approach called Responsible, Sustainable, Impact (RSI) investing. Responsible investing excludes specific industries or sectors, based on a set of values or belief systems; common ones are tobacco companies, and the fossil fuel industry. Once you have screened those out you can then look at sustainable investing, which as previously covered, incorporates ESG analysis to understand both the operational sustainability of a company, and assess the positive contribution the business makes through the goods and services it produces. Lastly, an impact investment is an investment with the primary intention to deliver a measurable positive or environmental benefit, alongside a financial return. This differs from a sustainable investment as it is more targeted. It would only include companies that are directly involved with tackling the issues – such as those developing renewable energy technology, or businesses looking to enhance recycling capabilities etcetera. Rather than those which may be considered sustainable because they operate with ESG principles, but their product doesn't actively address the problems.

In recent months, we have seen some really positive climate-related commitments from several of the world's superpowers. Russia will cut 30% of their greenhouse gas emissions by 2030, China has announced their ambitions to become net-zero by 2060, and Joe Biden has brought the US back into the Paris Agreement. The new US President has also claimed that he wants the US to become carbon neutral by 2050 and is targeting $2 trillion of spending on infrastructure across a host of sectors in order to meet this goal. Additionally, throughout this tumultuous last year and the coronavirus crisis, we have seen businesses with strong ESG credentials fare the storm much better than those without. With this in mind and the jolting reminder of the threats our planet and global communities face, we are seeing a real pressure from the public, and opportunity, for economies to 'build back greener'.
Therefore, we are seeing that the integration of ESG conscious investments not only allows clients to uphold their ethical views but also aids in mitigating risk and yielding strong returns for portfolios. In the tail end of the last year, as momentum behind the green transition continued to gather pace, LGT Vestra's Head of Sustainable Investments, Phoebe Stone, stated "we believe this is part of a sustained long-term trend that will continue to attract attention from policy makers and increasing numbers of investors."[iv]

For more information on Sustainable Investing at LGT Vestra, please contact us at advisersolutions@lgtvestra.com.

[i] https://www.bbc.com/news/business-55944570

[ii] https://www.lgtvestra.com/en/news/plastic-pollution-a-second-wave/

[iii] https://www.ussif.org/files/Trends%20Report%202020%20Executive%20Summary.pdf

[iv] https://www.lgtvestra.com/en/news/what-does-a-biden-presidency-mean-for-the-green-revolution/