INVESTMENT

Putting ESG on the bloc

With the European Union making plans to position itself at the centre of the sustainable finance revolution, Elizabeth Pfeuti **looks at which countries are the leaders and laggards of ESG investing across Europe, and beyond**

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In 2018, the European Union published an ambitious roadmap that aimed to position the trading bloc at the epicentre of the sustainable finance revolution.

Within it were plans to make both investors and fund managers disclose how they integrated environmental, societal and governance (ESG) issues into their processes, and the intention to design a taxonomy to ensure everyone was using the same set of measurements.

The move was widely welcomed by a fund management industry that is increasingly alert to both a shift in overall investor sentiment and a society more aware of the impact of capital investment.

But with 28 countries at all stages of development – and, crucially, interest – in sustainable finance, the task before the union is not straight-forward and will require significant input from all sides if any of the targets are to be met.

The leaders

Institutional investors in the Nordics, including pension funds and insurance companies, have been ahead of most for some time and are not looking to slow now, according to Hermes Investment Management head of global equities, Lewis Grant.

"For the largest investors in the Nordics, this mindset has evolved from being a sustainable investment 'thing' to this approach being just 'investing'," Grant says.

Their approach has evolved, too, from one that screened out industries that have earned global disapproval, under the principles of the United Nations Global Compact for example, to taking a closer look at the companies themselves and allocating to those that are having a positive impact.

The Netherlands has also traditionally led in the ESG field, with the largest pension funds using their might to influence global trends.

APG and PGGM, which together run close to €700 billion for domestic pension funds, have widely implemented ESG principles through their entire, gigantic portfolios, and their staff regularly appear as advocates for smaller investors to follow in their stead.

BNP Paribas Asset Management head of sustainability research and policy, Helena Viñes Fiestas, says these investors were buoyed in their approach through external factors.

"The society is in tune with how these larger investors operate, as is the government and regulator," Viñes Fiestas says. "All the stakeholders are involved, which is important."

Degroof Petercam Asset Management senior responsible investment specialist, Florent Griffon, says Belgium sits alongside its Dutch neighbours as being one of the most mature markets "with the most robustness in implementing ESG in their investment process".

Griffon says: "They have changed their investment portfolios to reflect their ESG thinking and have gone deeper into what it means." He says the influence of a handful of large investors should not be underestimated in the drive to change an entire industry's thought process – especially in a specific geography.

"They are sustainability-oriented and are prepared to narrow their investment universe for their beliefs," he adds. But pulling ahead of these 'usual suspects' of ESG, is a new leader.

A la mode Française

"France was not a leader in this sector until COP21," Viñes Fiestas notes, referring to the 2015 Climate Change Conference. "Now it is ahead."

Since the conference, thanks to Article 173 of the French Energy Transition law, asset managers and owners have had to explain how they take ESG into account when making investment decisions and disclose their carbon footprint. No other nation has such tight measures.

"There is a public awareness of these issues and the government is keener to implement these types of rules on private companies than elsewhere," Griffon explains. Despite large French investors taking ESG considerations seriously, the shove from the government has made a material difference.

"The French and increasingly the European regulator are playing a key role. Without them, the implementation would not have been so widespread," he says. "If they were only investing for performance, there would be less money in sustainable finance."

Viñes Fiestas says the French government since COP21 – alongside institutional investors – had leapt into the gap left by the US, leading to a real 'race to the top' in this space. Further afield, the nudge has been felt by some who had been largely absent from the sustainable finance conversation, according to Unigestion client portfolio manager in equities, Maria Musiela.

She says: "China notifying the World Trade Organisation that from 2018 it would stop accepting 24 kinds of solid waste, including prevalent forms of plastic waste, (which many western countries exported to them), made us stop and wonder 'what next?' on better waste management solutions."

With headlines such as these, ESG has moved from the fringes of specialist organisations to major boardrooms and even living rooms, pushing fund managers and investors to "ensure better outcomes for future generations", says Musiela.

However, there is one nation that is suspicious by its absence from experts' list of leaders in ESG.

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The UK, despite being the world's largest fund management hub and arguably the source for much ESG and sustainable investment research and initiatives, trails its European neighbours, according to experts.

"The UK – and London in particular – has been a leader for a long time, in terms of think tanks, pioneering stewardship and the level of discussion," Viñes Fiestas notes. "But many in the country are really behind."

There are some that are "on the front line" she says, but most investors show little inclination for change. Some are concerned that as the UK exits the EU, its investors may fall further behind their continental counterparts.

Similarly, Germany and Austria have lagged the leaders of ESG in Europe, but the fragmentation and a relatively small market is often cited as a reason for this. Spain and Italy, once disinterested in ESG, are forging a path to sustainable investment, says Viñes Fiestas, but she marked that there was still some way to go. While central and eastern Europe, with some still grappling with creating their own sustainable economies away from fossil fuel, have yet further to travel.

Lightbulb

The lightbulb moment for these laggards might come in the form of data, according to Grant.

He says the increase in the amount of plausible, reliable data being created by specialist research firms was already dispelling the long-held belief that 'nice guys finish last' and that ESG investing meant taking a hit to the bottom line.

APG and PGGM are already employing data science as a way of cutting through the noise on ESG and breaking down the elements into drivers of risk through a company, industry or whole supply chain.

While few pension funds have the resources to compete with this level of focus, they need to stay focused on what their partners are offering them, Griffon notes.

"Between 2010 and 2018 almost everyone launched ESG products, but this has created a two-level market. Some are more advanced with their products than others. Some integrate ESG across their entire process, others have a lighter touch," he says. "There is a risk of some greenwashing, so investors need to look at the product and see if it is serious enough about sustainability."

And this is where the EU's roadmap will be vitally important to bring all players in line – and offer more clarity to investors adopting this outlook for the first time. ■

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