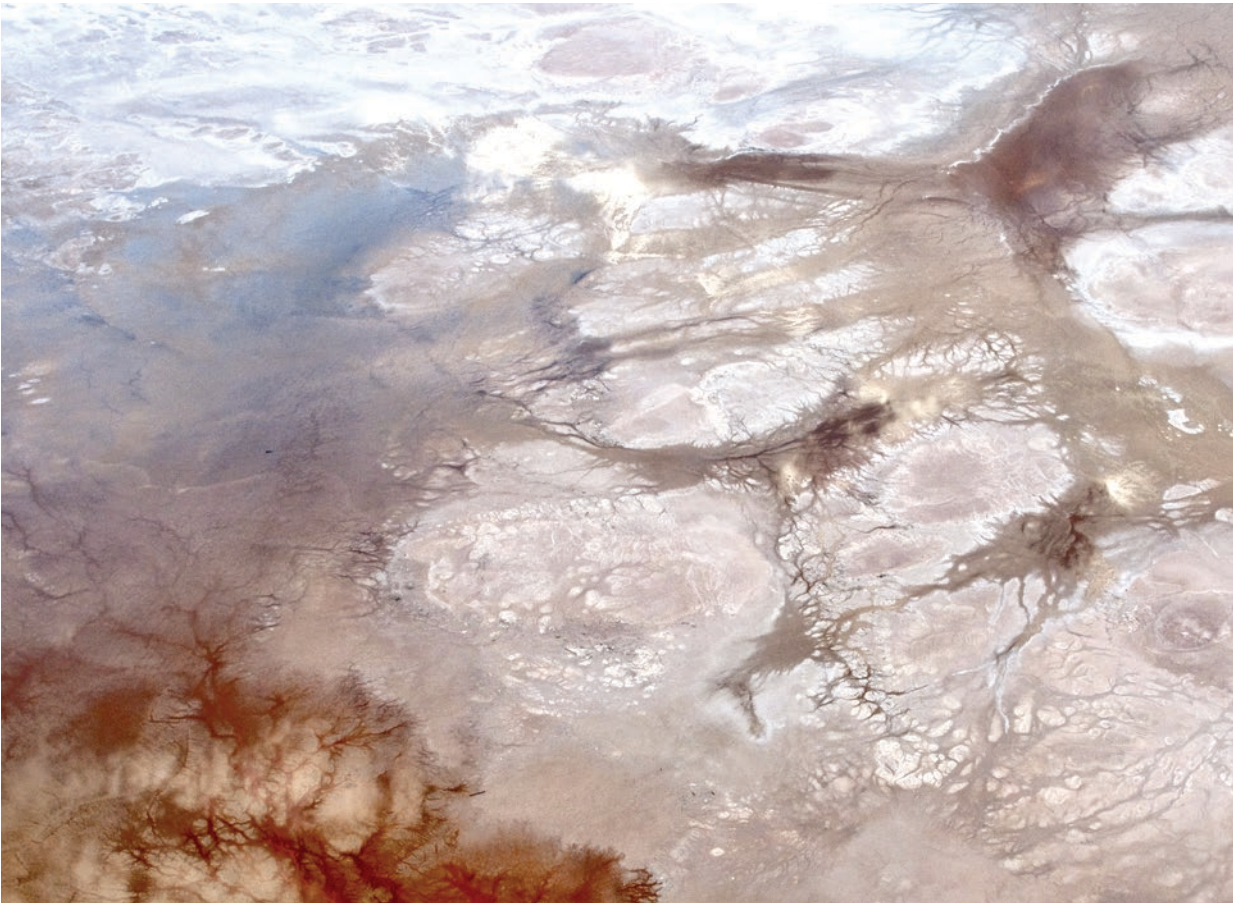


The conversation is now

Talking about the ‘E’ in ESG





Sustainable investing (SI) has evolved from a niche topic to become entrenched in our values, and our business and investing models. Investors often think of SI in terms of ESG – environmental, social and governance factors. Together these make up the fundamental framework for measuring sustainable investments. We take a look at the ‘E’ and why it matters.



Michael Baldinger
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Environmental issues have long been a consideration for investors looking to invest sustainably and there is no shortage of initiatives designed to raise awareness of those concerns. A good example is the Earth Day Network, the organization behind Earth Day worldwide. This year it shone its spotlight on Plastic Pollution, raising global awareness of the risks surrounding the use and disposal of plastics, not just to human health, but also to oceans, marine food chains and wildlife. In particular, it called for the elimination of single-use plastics, together with global regulation for the disposal of plastics and sought to promote alternatives to fossil fuel-based materials.

The support for movements such as Earth Day, with their focus on key environmental issues, is reflected in the changing attitudes towards Sustainable Investing (SI). We believe that SI is at an inflection point.

It has moved from a niche investment strategy to a new standard for investment management, enabled by the increased availability of material, non-financial data commonly referred to under the umbrella of ESG, or environmental, social and governance criteria. Sustainable assets under management increased from USD 14 trillion in 2012 to USD 22 trillion in 2016, according to the Global Sustainable Investment Alliance.

We asked some of the key members of UBS Asset Management's Sustainable and Impact Investing team, what sustainability and ESG investing means to them and to the environment.

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Q: Why is the environment important to UBS Asset Management and its clients and how are you able to mitigate climate change issues through the investments you make on behalf of your clients?

A: Michael Baldinger, Head of Sustainable and Impact Investing: We believe the transition to a low carbon economy is vital and we are focused on supporting our clients in preparing for success in an increasingly carbon constrained world.

More specifically we do this by supporting our client's efforts to assess, manage and protect them from climate-related risks by offering innovative products and services in investment, financing and research, such as our Climate Aware indexing capability.

In the broader context, UBS Asset Management is striving to become a global leader in Sustainable and Impact investing, and that is why we have made the strategic decision to bring sustainable investing into the mainstream of our offerings. This commitment is reflected by the expansion and transformation of our sustainability research and stewardship capabilities; to support the objective of integrating ESG considerations into the investment processes throughout our firm.

Having a dedicated SI research & stewardship team to lead the integration across our offerings, allows us to create customized solutions for our clients, that meet both their financial and sustainability requirements, across active equities, active fixed income, infrastructure, real estate and passive strategies.

Q: We are hearing from clients that they want to invest in a way that could have a positive environmental and social impact, but we also know they want to realize their investment goals. Can they do both?

A: Bruno Bertocci, Head of Sustainable Equities Team: While we as a firm, as well as our clients, are deeply concerned about the environment, we also firmly believe that it has become increasingly important to incorporate ESG factors into stock-picking decisions. The availability and quality of non-financial data about companies is improving and it is clear that information not on a company's balance sheet may have a material effect on the future value and performance of that company.

UBS Asset Management has a long and rich history of more than 20 years investing in sustainable equities, employing our proprietary, multi-stage, forward-looking cash flow model to document our internal analysts' independent views of a stock's intrinsic value. Incorporating material sustainability factors—or factors that matter—is a natural extension of this process and improves our ability to capture more elusive information that may contribute to a company's intrinsic value and future performance.

Our Sustainable equity portfolios are constructed with a mix of investments that align with sustainability priorities, and include only companies that have both attractive valuations based on their financials and high sustainability scores based on their ESG profile.

We believe that sustainable investing not only does not compromise returns, it may actually improve them and reduce risk.

Q: More and more people are talking about “impact” investing, but it seems to be a hard target to pin down. What is UBS doing to make impact investing a reality, and why is it important to the environment?

A: Dr. Dinah A. Koehler, Sustainable Investment Research: Impact investing is real and it is up and running here at UBS. For example, we have teamed with Harvard, The City University of New York and a Dutch pension fund client to develop a framework to scientifically measure the positive impact on the environment and human well-being of the products and services of the companies we invest in.

The team is leveraging advances in fields such as earth observation and modeling, as well as epidemiology (the study of the distribution and determinants of health and disease conditions in defined populations), and linking these to corporate data to show whether products and services are contributing to more sustainable environmental and human conditions. We are specifically targeting four challenges—water, climate change mitigation, human health and food security—and we will be measuring the impact in these areas over time from the companies that we invest in on behalf of Dutch pensioners.

For two years our unique partnership has been testing the methodologies across a range of products and services. Earlier this year we began research on food security with the University of Wageningen, Netherlands.

Impact investing is one of the fastest growing sectors in SI: it may lead to specific, measurable environmental and human health results by supporting companies that manufacture high positive impact products while effectively managing ESG issues.

Q: When we hear about environmentally conscious investment we often hear about the “carbon footprint” of a company. How are you able to assess the CO₂ emissions of a company as you make investment decisions?

A: Francis Condon, Sustainable Investment Research: The carbon footprint of a company, and more broadly the greenhouse gas, or GHG, footprint of a company is extremely important from an ESG perspective and is also increasingly measurable as companies are pressured, and in many cases required, to issue disclosure about their carbon emissions.

For instance, in 2010, while it did not issue a new rule on carbon emission disclosure, the Securities and Exchange Commission in the United States issued interpretive guidance that in fact required companies to disclose information about their carbon use or production.

The guidance came in the form of a request that companies disclose to their shareholders, along with other risks to their business, the extent of its exposure to legislation and regulation related to climate change, international treaties on climate change, and other effects that climate change could have on the operations of the business.

In addition to this, in recent years a group of large institutional investors, including CalPERS (the California Public Employees Retirement System), as well as state and federally elected officials, have called on the SEC to specifically require greater disclosure on climate change, from energy companies in particular, citing its material nature to their businesses and to shareholder value.

This increased pressure has led to better disclosure, even when it is on a voluntary basis, and many shareholders are, in fact, going directly to the company with proposals for greater disclosure.

The UBS Asset Management Policy and Procedures on Corporate Governance and Proxy Voting states: “We will support proposals that require an issuer to report to shareholders, at a reasonable cost and excluding proprietary information, information concerning their potential liability from operations that contribute to global warming, their goals in reducing these emissions, [and] their policy on climate risks with specific reduction targets where such targets are not overly restrictive.”

Greater disclosure leads to more and better data which can allow investors to make more informed ESG investment decisions.

Q: In your work at the Principles for Responsible Investing initiative at the United Nations you collaborated with investment companies to engage companies on ESG issues. How can corporate engagement help protect the environment?

A: Valeria Piani, Director, Sustainable Investing: Engagement with companies at the management, board and through proxy voting on behalf of our investors can be an effective way to support issues that encourage management to make changes or adopt more constructive policies with respect to social, environmental, political and other special interest issues if we believe they have economic relevance to the investment.

For instance, we expect companies to have a strategy for reducing greenhouse gas emissions, to be clear about goals, and to report on progress. ESG risks may create significant impacts on the reputation and financial stability of a company. It is therefore essential that the Board has a robust policy and control process in place to manage these risks.

Increasingly, our clients are concerned about environmental issues. As stewards for our shareholders, we can proactively communicate our clients’ concerns about these issues from both a sustainability and economic standpoint to the board and management by voting on proposals before the shareholders and by engaging with the key stakeholders in person, and this can have both direct and indirect impact on the environment.

Q: Sustainability has become a key component of successful real asset management. How do you approach the question of sustainable investing when it comes to the properties and infrastructure projects you invest in?

A: David Hirst, Head of Operations Real Estate UK: Undoubtedly, climate change, energy needs and water scarcity rank among the biggest challenges of our century. UBS Asset Management's Real Estate & Private Markets (REPM) business, acknowledges that real assets such as properties and infrastructure contribute significantly to CO₂ emissions and the consumption of natural resources.

While the financial objectives of our clients remain the primary focus of our investments, our responsible investment strategy also considers long-term resilience, climate change, environmental, social and governance aspects.

In order to maximize our results with regards to the implementation of our responsible investment strategy, an integrated approach is required. This helps us to harmonize financial goals with environmental and social challenges.

One consequence of climate change and population growth has been an increased focus on preserving natural resources. This has led to new laws, regulations, price changes, incentives and technologies which must be analyzed and incorporated into our investment strategies.

We are committed to reducing the environmental impact of our real assets by conserving resources, which, in turn, reduces the operating costs of our properties, assets and funds.

Responsible investment aims to add value to an investment by increasing resilience and limiting the risk of regulatory non-compliance or the erosion of its competitive position in the market, increasing the appeal of a property to tenants and purchasers and, in many cases, reducing expenses and improving returns.

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