

Special Report

ESG Investing



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Introduction

Evolution of ESG in Investing

ESG has been around for over a decade now. However, only in the past 2–3 years, have many investors started shifting to sustainable investing

<2005

Though the idea of integrating ESG with capital markets was conceived in 2005, many institutional investors were initially reluctant to accept the concept of ESG investing and focused on maximizing shareholder value irrespective of the nature of and impact on the business.

2006–
12

Launch of Principles for Responsible Investment (PRI) at the New York Stock Exchange (NYSE) in 2006 and Sustainable Stock Exchange Initiative (SSEI) in 2007 ignited the interest of investors. Starting 2012, investors avoided investing in tobacco and gaming.

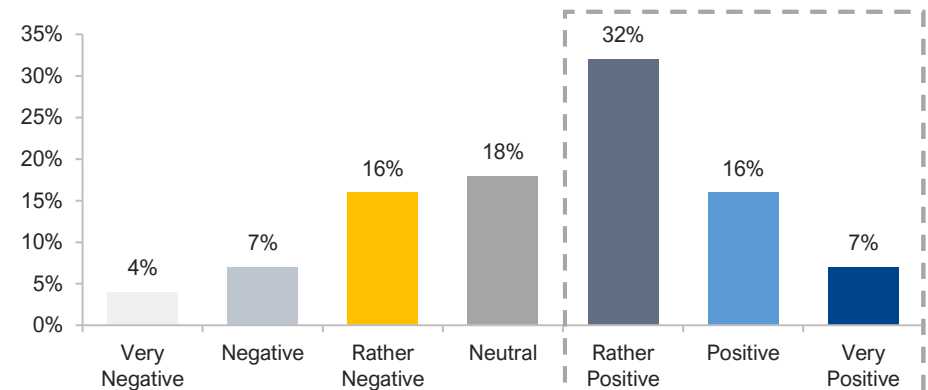
2012–
18

The Paris Agreement was adopted in 2015 to bring a positive impact to climate change, incorporate responsible investing practices, and promote sustainable businesses. By 2018, 80% of the world's largest corporations adopted GRI standards and over USD20 trillion of AUM was infused in ESG-related investments.

2018–
22

The Covid-19 crisis has changed the purview of investing. Investors in Europe and North America are foremost in following sustainable investing practices, accounting for more than 90% of the ESG market. Investors are now increasingly focusing on companies with a good track record in ESG aspects.

More than 57% of investors believe the COVID-19 crisis would boost the momentum of ESG investments in the next three years



Source: JP Morgan

Source: Forbes, Morningstar, Aranca Research

Key Sectors



Sectors of Interest



Alternative Energy



Major Disease Treatment



Nutrition



Green Building



Sanitation



Sustainable Impact Solutions



Sectors to Avoid



Alcohol



Conventional and Controversial Weapons



Civilian Firearms



Gambling



Tobacco



Nuclear Power and Weapons

Source: Aranca Research



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Private Equity in ESG

Drivers for PE's Focus on ESG

The changing investment landscape is forcing PE firms to adopt ESG policies.

Access to Capital

- According to the UN, an estimated USD3-5tn per year is needed to meet the United Nations Sustainable Development Goals (UN SDGs), and PE would play an important role in providing financial support to achieve these goals.

Improved Risk Management

- Investments in non-ESG funds are increasingly perceived as riskier. Considering the current scenario, ESG indices and ESG funds have somewhat outperformed most of the conventional peers.

Miss Out on Opportunities

- Firms face the risk of losing projects in case a competing firm has more mature ESG capabilities to leverage.
- ESG can attract better talent and lead to better engagement with them.

Investor-Driven Demand

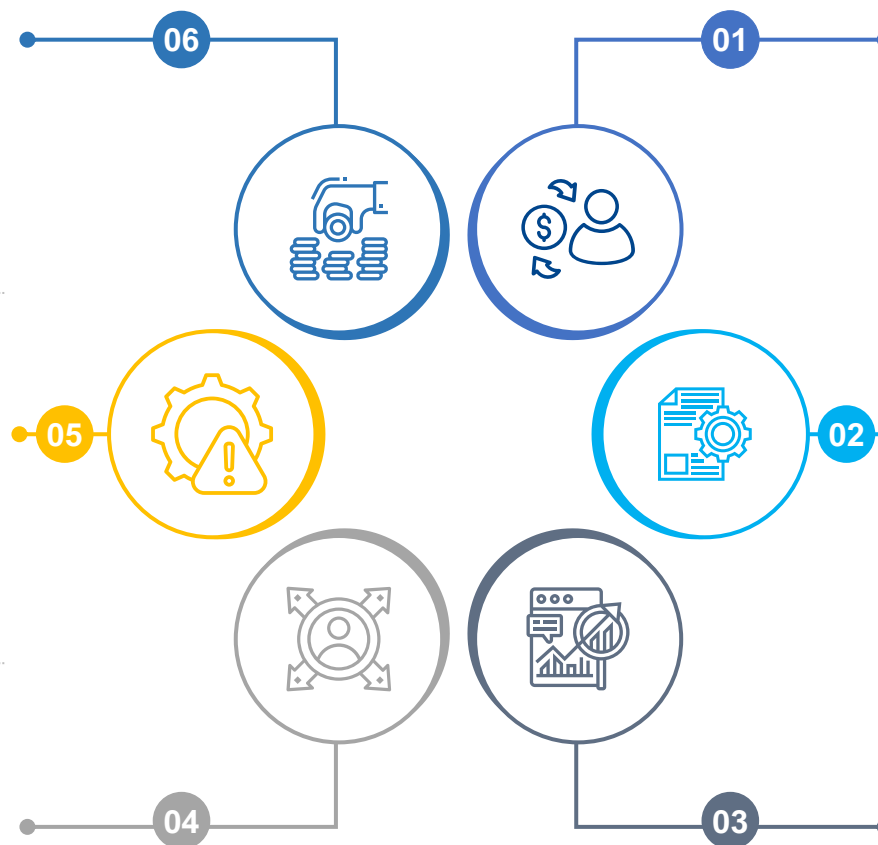
- PE investors are demanding better returns, along with the safety of investment.
- Certain investors are also facing disclosure issues from their regulators, the requirements of which they are passing on to asset managers.

Increasing Disclosure

- PE and VC funds are expected to face more stringent regulations in future.
- Alternative investment fund managers (AIFMs) are being required to make detailed disclosures to the public (and not merely to their own investors) at both the manager and product levels.

Acting for Long Term

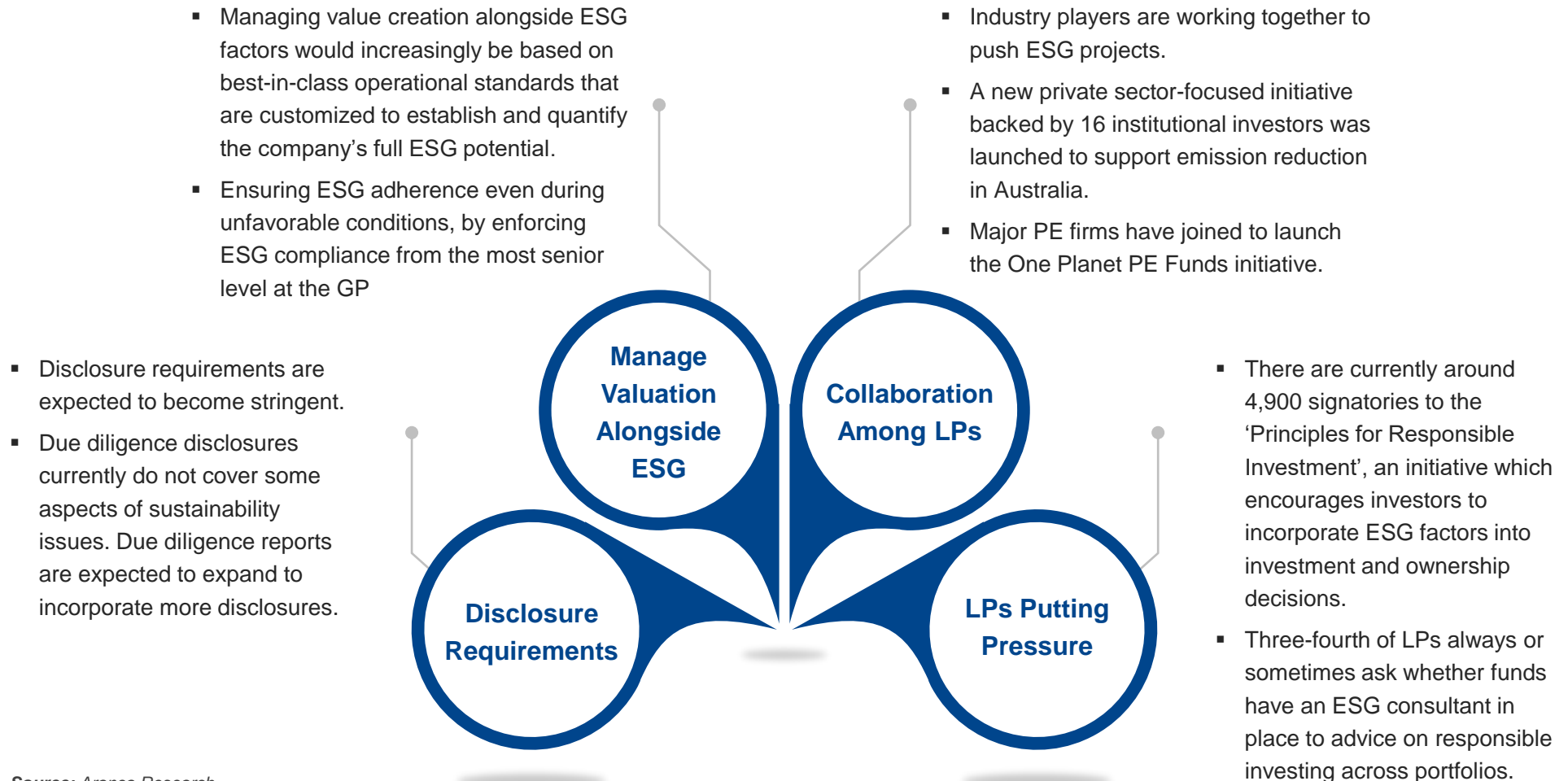
- ESG is being rapidly adopted by public companies and may eventually be adopted by private players as well.
- In the long term, adopting ESG would give PE access to capital at lower costs.



Source: Aranca Research

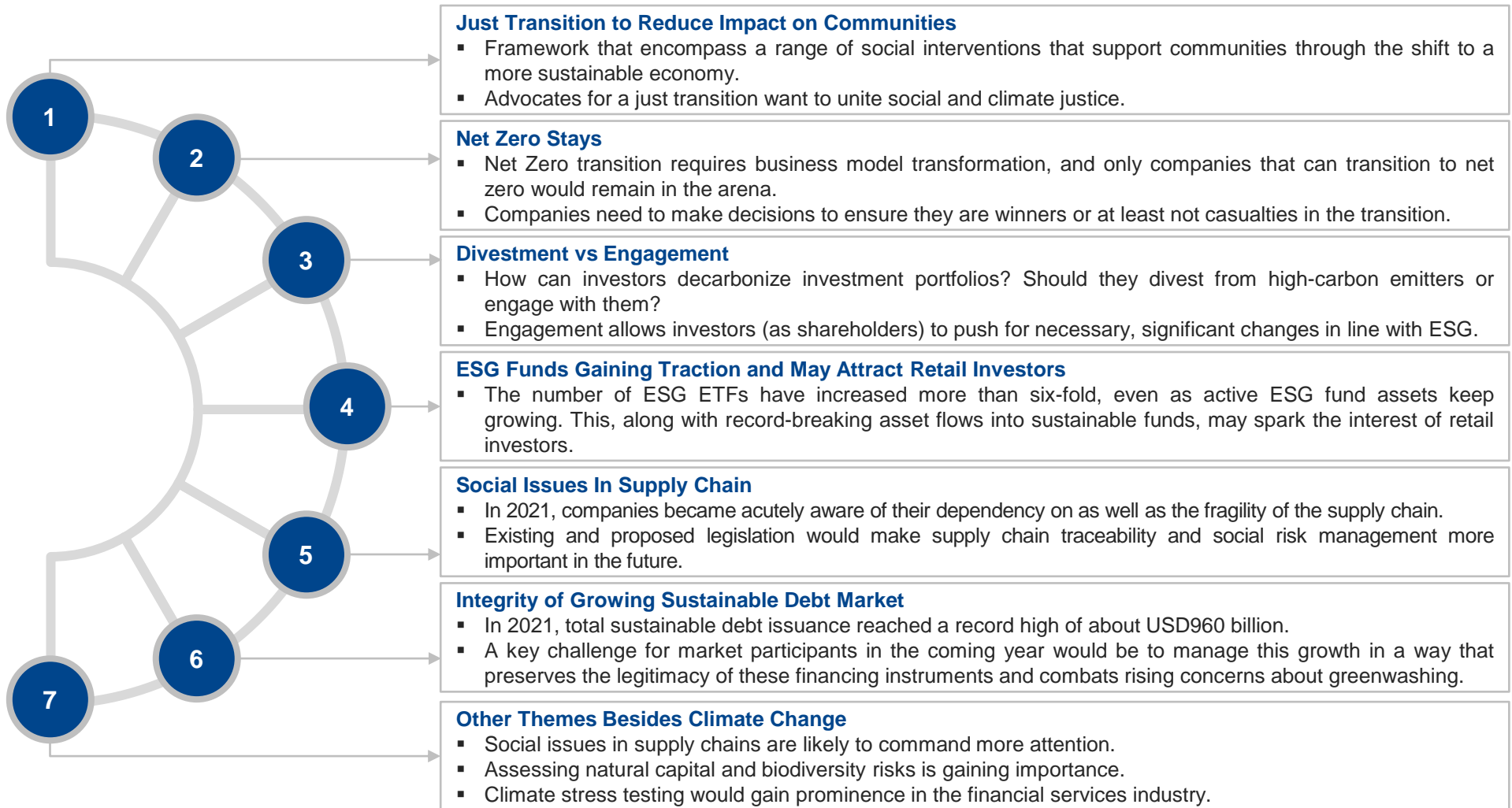
Key ESG Trends Affecting PE Players

PE firms are facing ESG-related demands from the regulatory agencies, investors and partner level



Source: Aranca Research

Key ESG Themes within PE Space

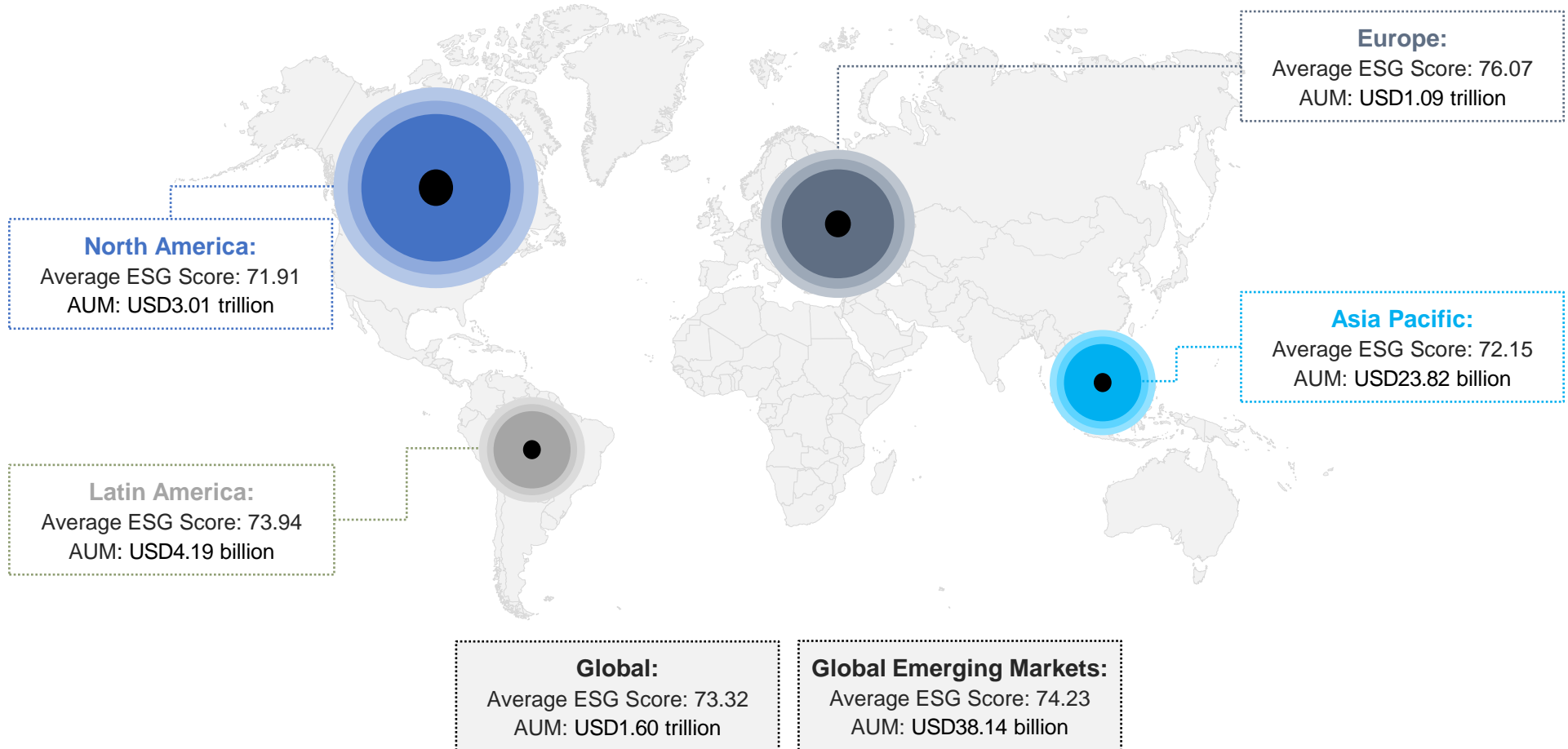


Source: Aranca Research

Public Fund Investments in ESG

Geographic Overview

North America and Europe are global leaders in ESG investments, while Asia Pacific, Latin America, and other emerging markets are witnessing increased awareness.



Source: Eikon, Bloomberg

Major Fund Managers across the Regions



Source: Eikon, Bloomberg

Global ESG Funds

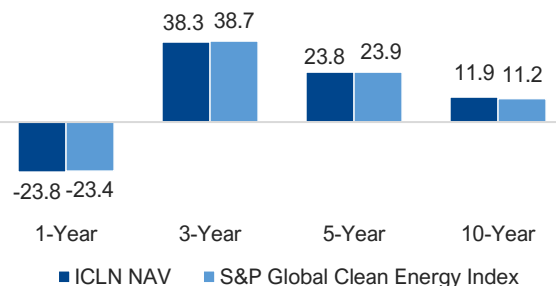
Global Clean Energy Fund

iShares Global Clean Energy ETF

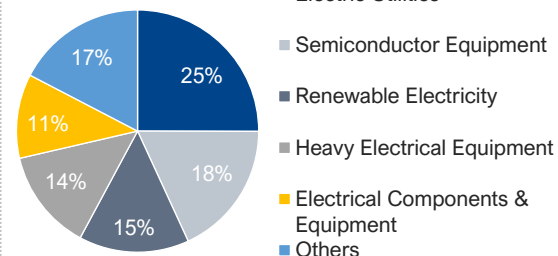
Investment Strategy: The iShares Global Clean Energy ETF seeks to track the investment results of an index composed of global equities in the clean energy sector.

Fund Size	USD5.61 billion
Fund Launch Date	06/24/2008
Ticker	ICLN
Number of Holdings	76
Expense Ratio	0.42%
Price to Earnings	25.14
Beta vs S&P 500	1.09

Annualized Performance (%)



Top Sectors



Top Holdings



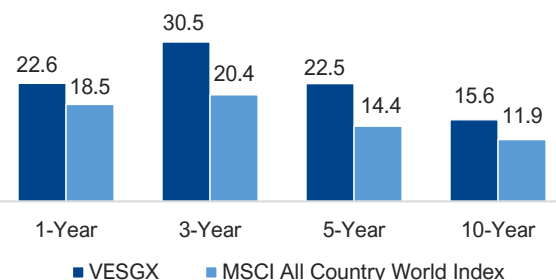
High Performing Thematic Fund

AllianceBernstein Sustainable Global Thematic Fund

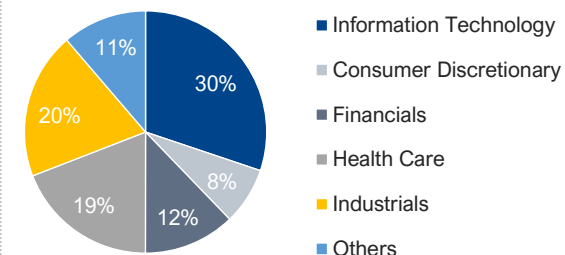
Investment Strategy: The fund employs a “top-down” and “bottom-up” investment process with the goal of identifying securities that fit into sustainable investment themes. The fund identifies sustainable investment themes that are broadly consistent with achieving UN SDGs such as health, climate, and empowerment.

Fund Size	USD2.65 billion
Fund Launch Date	10/01/1996
Weighted Avg. Capital	USD179.0 billion
Ticker	ATEYX
Number of Holdings	59
Turnover Rate	35%

Annualized Performance (%)



Top Sectors



Top Holdings



Source: Eikon, Bloomberg

Select ESG Funds in US

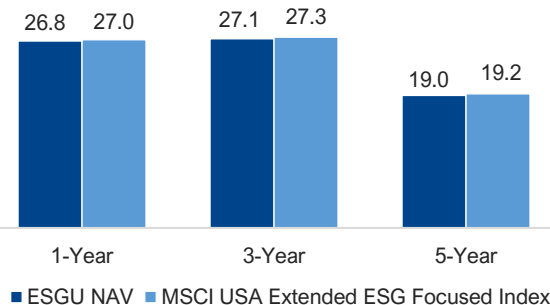
High Performing Fund

iShares ESG Aware MSCI USA ETF

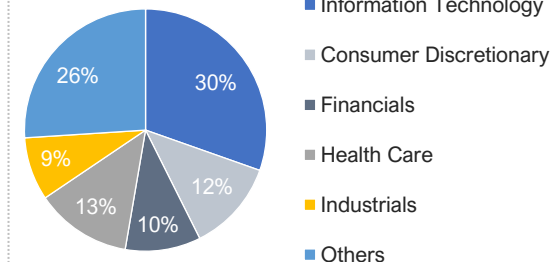
Investment Strategy: The iShares ESG Aware MSCI USA ETF seeks to track the investment results of an index composed of US companies that have positive ESG characteristics. The fund aims to obtain exposure to higher rated ESG companies while accessing large and mid-cap US stocks.

Fund Size	USD25.7 billion
Fund Launch Date	12/01/2016
Number of Holdings	321
Avg. Weighted Market Cap	USD569.27 billion
Expense Ratio	0.15%

Annualized Performance (%)



Top Sectors



Top Holdings



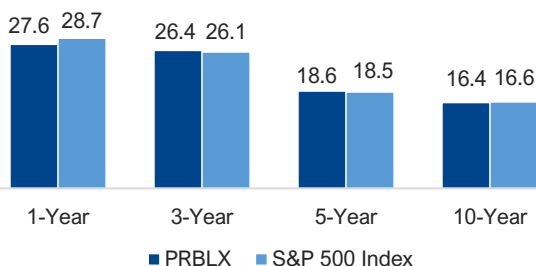
Large Blend Fund

Parnassus Core Equity Fund

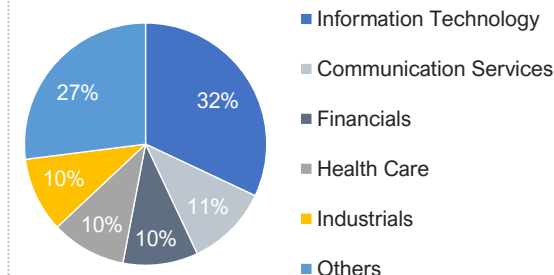
Investment Strategy: The Parnassus Core Equity Fund invests with low turnover and high conviction in approximately 40 holdings. The fund focuses on identifying high-quality companies and strives to outperform the S&P 500 Index on a risk-adjusted basis with a high active share. Every investment made must meet rigorous fundamental and ESG criteria.

Fund Size	USD32.3 billion
Fund Launch Date	08/31/1992
Number of Holdings	38
Avg. Weighted Market Cap	USD510.4 billion
Net Expense Ratio	0.84%

Annualized Performance (%)



Top Sectors



Top Holdings



Source: Eikon, Bloomberg

Select ESG Funds in Europe

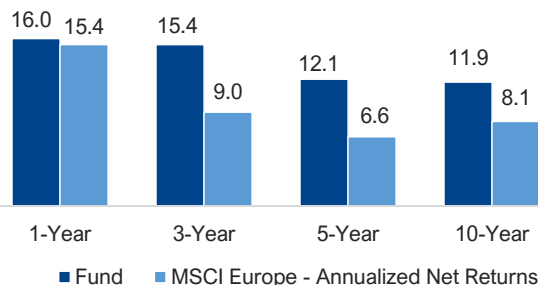
High Performing Value Fund

Comgest Growth Europe EUR Acc

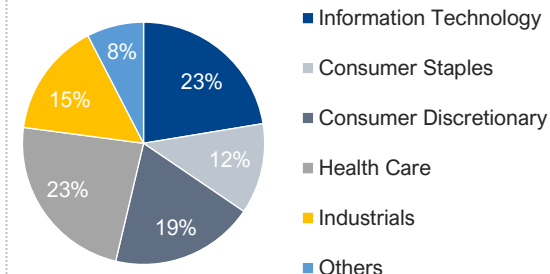
Investment Objective: In order to increase the value of the fund (capital appreciation) over the long term, it intends to invest in a portfolio of high-quality, long-term growth companies.

Fund Size	USD4.94 billion
Fund Launch Date	05/15/2000
Avg. Weighted Market Cap	USD110.43 billion
Number of Holdings	38
Current NAV	USD41.13

Annualized Performance (%)



Top Sectors



Top Holdings

ASML

novo nordisk

LVMH
MOËT HENNESSY · LOUIS VUITTON

Linde

ESSILORLUXOTTICA

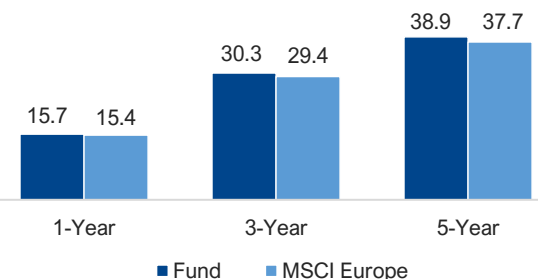
Top European ESG Fund

Amundi Index MSCI Europe UCITS ETF

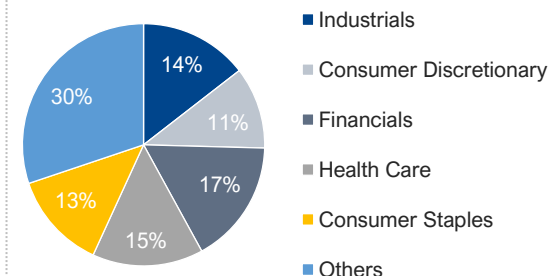
Investment Objective: The Amundi Index MSCI Europe UCITS ETF seeks to replicate as closely as possible the performance of the MSCI Europe Index, whether the trend is rising or falling.

Fund Size	USD3.93 billion
Fund Launch Date	06/29/2016
Average Market Cap	USD78.33 billion
NAV	USD75.71
Expense Ratio	0.18%

Annualized Performance (%)



Top Sectors



Top Holdings

Nestlé

ASML

Roche

LVMH
MOËT HENNESSY · LOUIS VUITTON

Shell

Source: Eikon, Bloomberg

Select ESG Funds in Emerging Markets

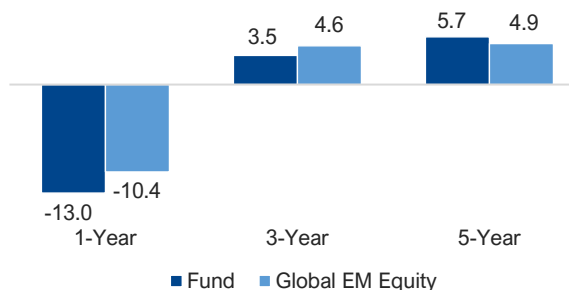
High Performing Fund

Vontobel Fund - mtx Sustainable Emerging Markets Leaders

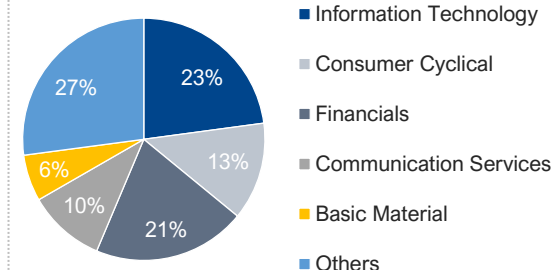
Investment Objective: The sub-fund aims to generate long-term capital growth and promote environmental or social characteristics by employing a number of safeguards and evaluating all investments against sustainability criteria with hard thresholds that must be met for inclusion. The starting investment universe is the Emerging Markets equity markets.

Fund Size	USD6.70 billion
Fund Launch Date	07/15/2011
NAV	USD157.78
Weighted Average M-Cap	USD148.67 billion
Net Expense Ratio	2.03%

Annualized Performance (%)



Top Sectors



Top Holdings



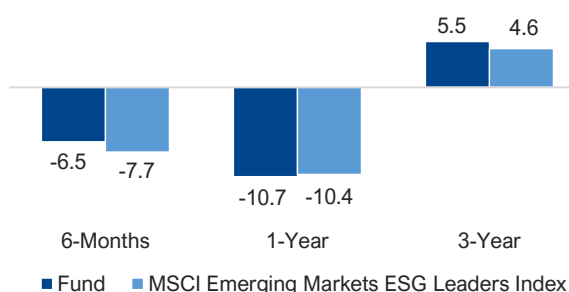
Top Emerging Market Fund

Credit Suisse Index Fund Equity Emerging Markets ESG

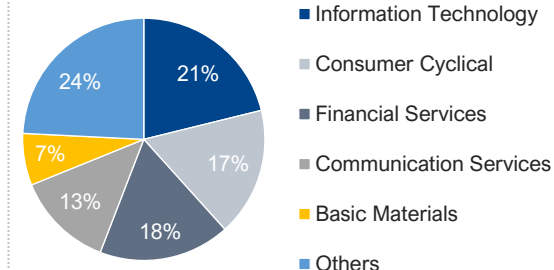
Investment Objective: The sub-fund tracks the MSCI Emerging Markets ESG Leaders Index as its benchmark index. The sub-fund aims to provide shareholders a return in line with the performance of the MSCI Emerging Markets ESG Leaders Index.

Fund Size	USD4.16 billion
Fund Launch Date	05/26/2017
NAV	USD1324.77
Weighted Average M-Cap	USD229.55 billion
Expense Ratio	0.13%

Annualized Performance (%)



Top Sectors



Top Holdings

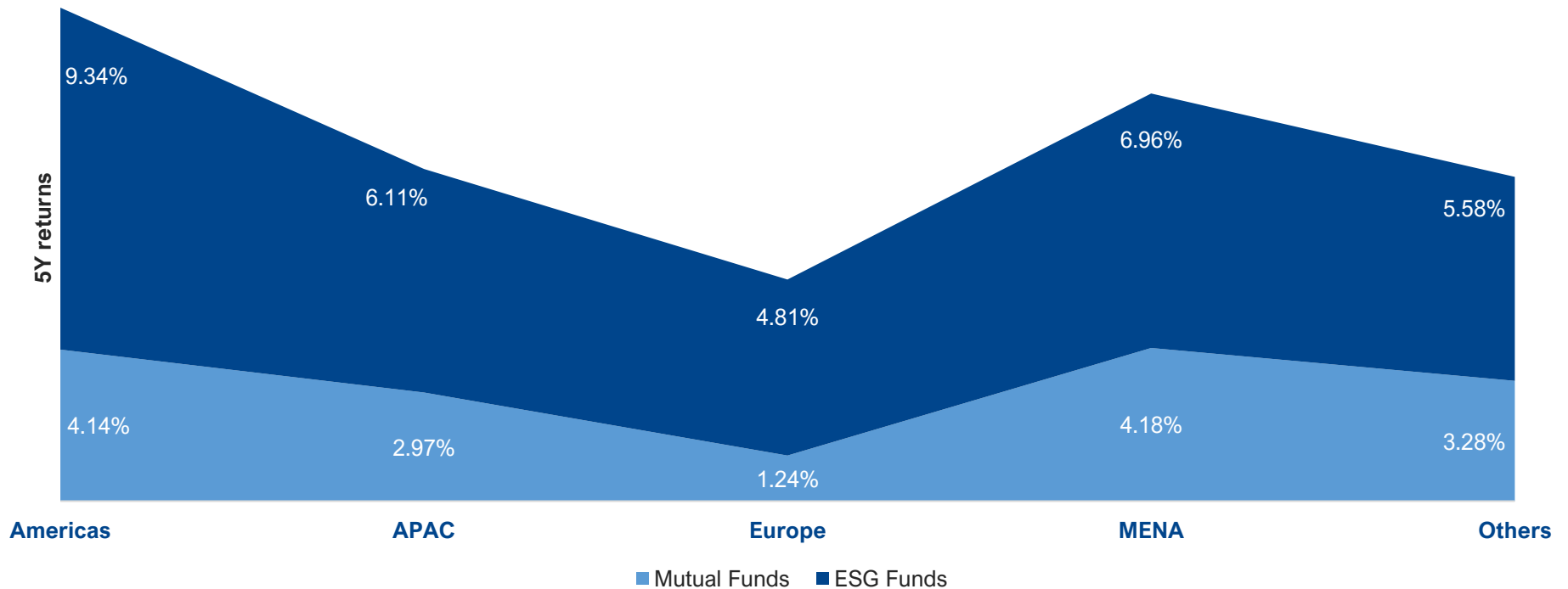


Source: Eikon, Bloomberg

ESG Fund Performance Analysis

Returns Generated by ESG vs Traditional funds

Better ESG scores result in 10% lower Cost of Capital as risks to operate business are reduced, improving returns in the long term



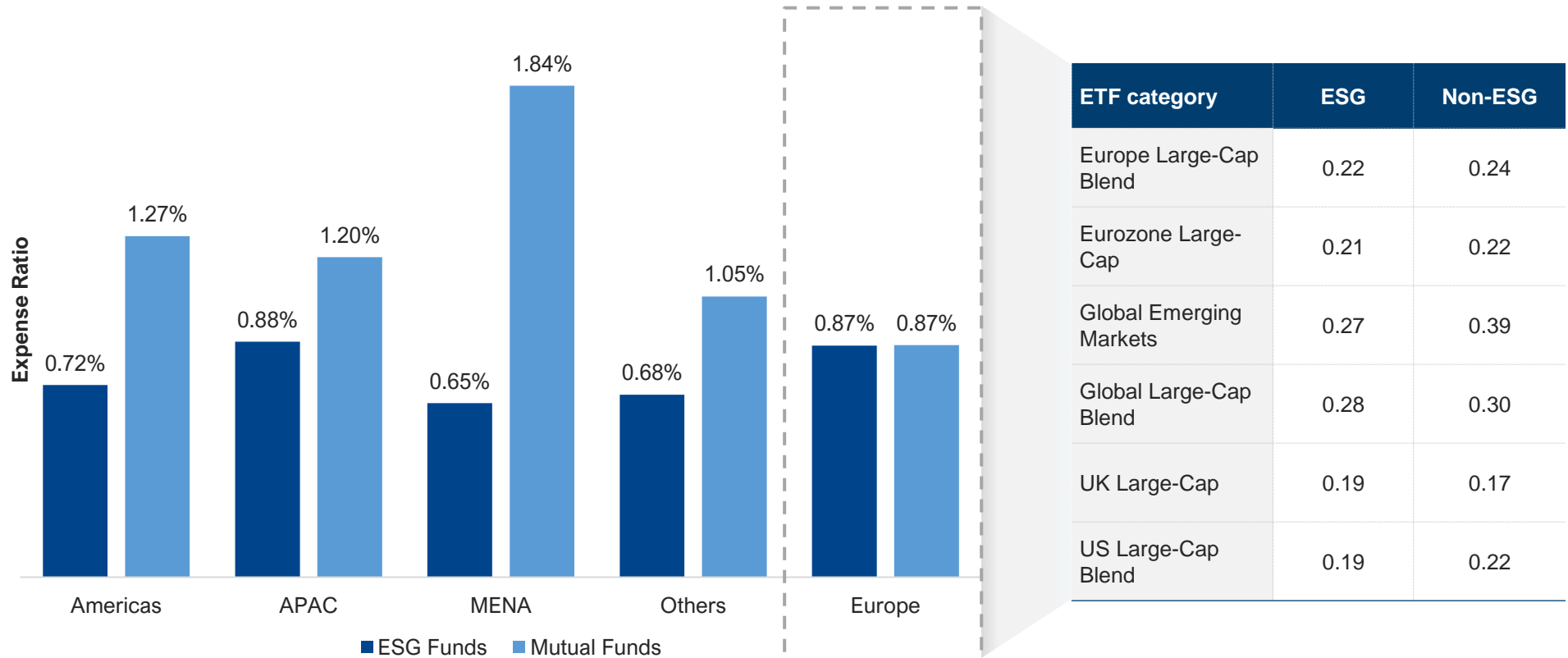
ESG funds outperformed conventional mutual funds by an average of 3.4% over a 5-year period

Source: Bloomberg, Morningstar



Cost of Funds – Traditional vs ESG

ETFs categorized as sustainable in 5 out of 6 large fund categories, charge lower average annual fees than non-ESG funds in Europe, as quoted by Morningstar

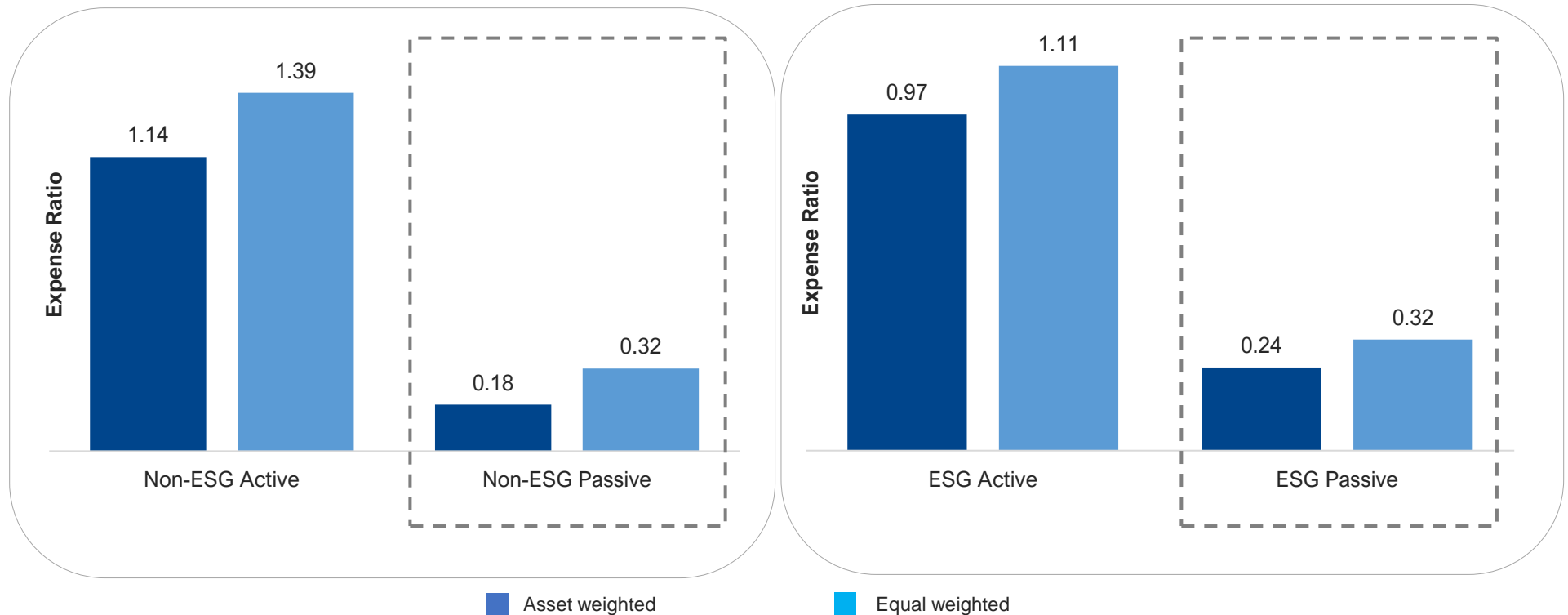


ESG funds have showed lower volatility during black-swan events in the past when compared to traditional funds according to the study conducted by Morgan Stanley

Source: Bloomberg, Morningstar

Cost of Funds in ESG – Active vs Passive

ESG funds are often perceived as the greenium funds because of expensive fees paid for actively managed funds



However, many passive funds (through index funds and ETFs) came into existence which brought the average expense ratio of ESG funds down when compared to conventional mutual funds

Source: Aranca Research



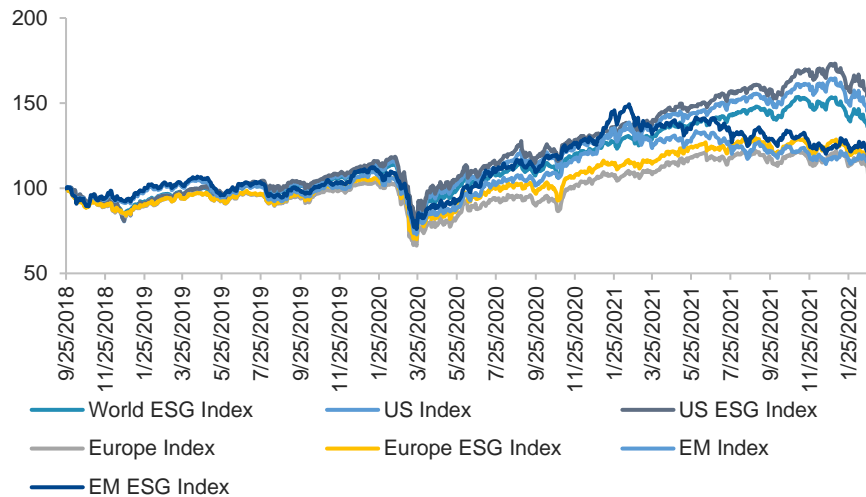
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Performance Analysis (1/2)

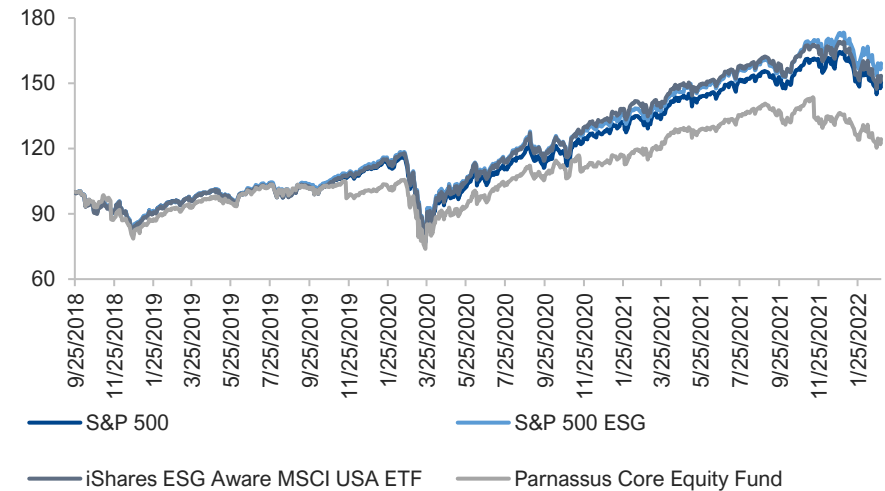
ESG funds outperformed their respective country indices by a narrow margin. In the US, ESG was the best performing fund

ESG vs World vs Region Index



- The World ESG Index outperformed the World Index by a small margin of 3%.
- With a 59% increase, the US ESG Index outperformed all the other indices by a significant percentage during the tracked time period.
- The Emerging Markets ESG Index showed 18% returns, which is higher than the European ESG returns of 13%.
- The outperformance of ESG funds compared to the market index was in range of 3–9%.

US ESG vs Index vs Select Public Funds



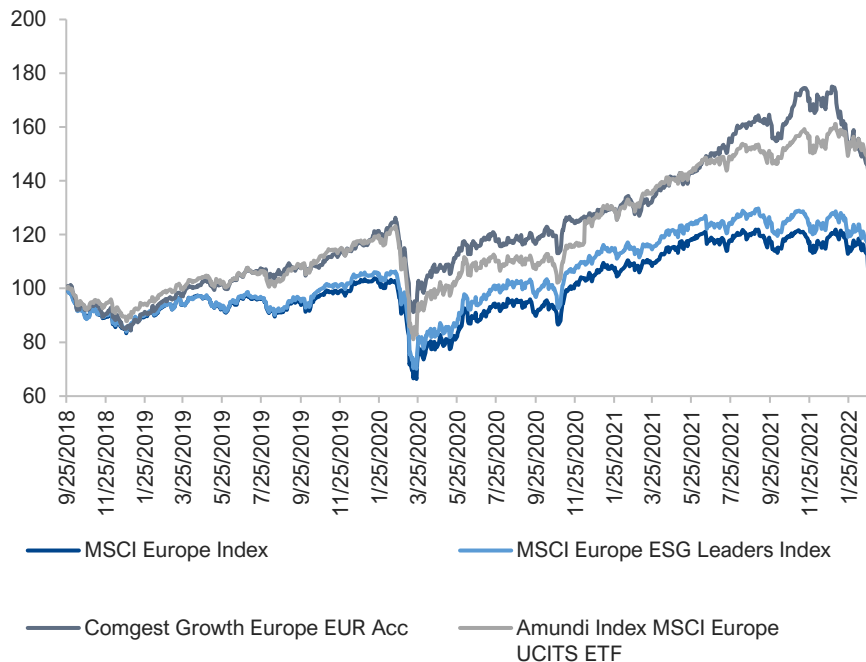
- The ESG Index outperformed both the market index as well as the leading public fund indices.
- iShares ESG Aware underperformed the ESG Index by only 6% and outperformed the S&P 500 by 3%.
- The top 10 constituents of both the S&P 500 ESG and iShares ESG Aware consist of the top technology companies, which can explain their outperformance and similar returns.

Source: Capital IQ, Bloomberg

Performance Analysis (2/2)

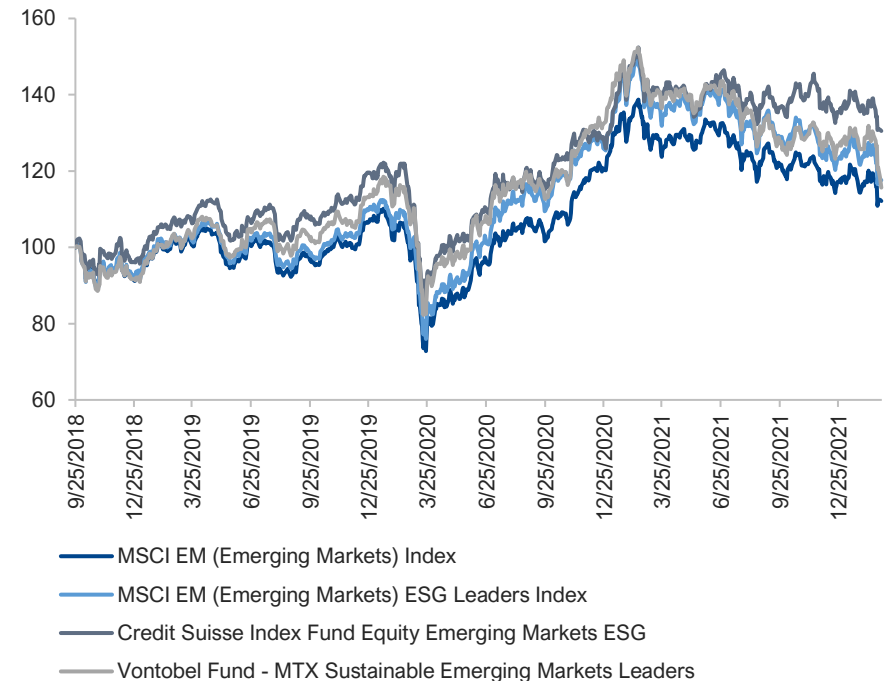
In Europe and EM, ESG funds outperformed the region index, but underperformed the public funds chosen

Europe ESG vs Index vs Select Public Funds



- The ESG index outperformed the overall Europe Index.
- Public funds managed to significantly outperform the ESG and Europe indices during the tracked time period
- ASML and Roche are in the top holdings of ESG and public funds.

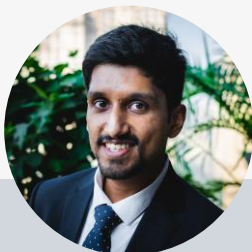
Emerging Markets vs Index vs Select Public Funds



- The ESG Index outperformed the overall EM Index.
- Credit Suisse Index managed to outperform the ESG and market indices by 18% and 13%, respectively.
- TSMC and Tencent are the top holdings of ESG and public funds.
- IT and Financials are the top allocated sectors in all three funds.

Source: Capital IQ, Bloomberg

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