SUSTAINABILITY
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2021

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SUSTAINABILITY IN INVESTMENT PORTFOLIOS

The unstoppable rise of ESG Investing

In 2015 the United Nations issued its famous 17 Sustainable Development Goals as a "blueprint to achieve a better and more sustainable future for all", effectively calling for action to promote prosperity while protecting the planet.

WALTER KÜNG
Senior Portfolio Manager

MICHAEL BÖSCH
Senior Relationship Manager

The 17 UN goals cover a wide range of topics including: poverty, hunger, responsible consumption and production, clean water and sanitation, sustainable cities and communities, affordable and clean energy, climate action and life below water among others.

Most of these goals are reflected in what is known in the financial community as ESG (Environment, Social and Governance) Investing.

In the last few years, numerous rating agencies have started to systematically analyze and categorize companies and investment funds and assign them an "ESG rating", depending on criterias which are usually publicly available. Such ratings are very helpful for asset managers and investors alike, as they begin the process of establishing a standardization that was lacking in the industry. The most widely used agencies include MSCI ESG research, Sustainalytics, FTSE Russel or Bloomberg to name a few. The number of providers is increasing as is the appetite of investors for such information.

Ratings are not undisputed among professionals. A famous and striking example is Tesla. While for many Tesla admirers the company is the most sustainable stock in the world since it is the leading force of the global electric car trend, for others Tesla is not as ESG-friendly as one would assume: in particular the battery end-disposal is an unsolved issue. MSCI for example has initially given the company a friendly AAA rating, but has reduced it to a modest A in 2019, ranking Tesla only as average among the 40 companies in the automobiles industry!

The ESG thematic has recently become almost a fashion among asset managers. Unfortunately, many actors are claiming to be "ESG friendly" for marketing purposes – as particularly wealthy and millennial investors ask for such investments – and they simply pretend to have a green bias. Investors need to be careful and understand the detailed process which the manager is applying. Transparency and accountability are paramount as asset owners evaluate the managers to whom they entrusted their wealth.

Empirical studies show that investing in a sustainable manner is not only good for the world, but also delivers superior returns. Reasons for this include: the reduced risk of natural catastrophic liabilities, the exclusion mechanism or poorly governed entities, and higher valuations assigned by investors to technological companies compared to older industrial firms. This trend was confirmed by the ongoing Covid-19 crisis, which hit some ESG-unfriendly sectors like airlines, cruisers, oil companies much harder than the ESG-friendly FAANGs of this world. In any case, the times are bygone where investors accepted inferior returns to follow ESG guidelines for ethical reasons, as ESG and superior performance go now hand-in hand as documented academically.

At Hyposwiss Advisors, we had for years a positive attitude towards sustainable investments. In 2020 however, we decided to go a step further and move from a non-binding general behavior into a setup with firm and guiding principles, valid for all decision making and members of our firm.

We agreed upon our ambition to become more ESG-oriented in the portfolio management and the selection of investments. This footprint will over time include more ESG compatible investments; non-ESG compatible investments will slowly be reduced until vanishing completely from the portfolios. The gradual approach was preferred to a radical shift, in order to preserve stability in portfolios.

We set up a list of binding rules to make sure that our guidelines become valid and not remain a set of nice words. From the beginning, we held the opinion that our transition to grow more ESG friendly would not be an operation to be finalized within a few trading days but rather over a few years.

How did the ESG process work in practice? We have experienced ourselves that to invest in an ESG-beneficial way is not only healthy for the environment but also delivers superior investment results. This later fact alone will push this new trend and we have noticed that clients are extremely enthusiastic about this idea and encourage us to continue on our path to increase our ESG-footprint ■

Exclusion of certain sectors We believe that some industries and sectors should be excluded from investment, among others arms and weapons, tobacco and fossil energy companies with a large share of non-renewable energy production mix (such as nuclear energy, coal, etc.).

Positive selection for individual stocks and bonds When choosing a new investment, ESG criteria are an integral part of the decision making process. In general, if two securities appear similar, the one with the better ESG rating should be selected.

Exclusion for new investments We are excluding new investments in individual companies with low ESG-ratings.

“Luck shouldn’t be part of your portfolio.”

HYPOSWISS
ADVISORS

Expect the expected

Rue de Hesse 7, 1204 Geneva – Switzerland
Hufgasse 17, 8080 Zürich – Switzerland
Tel. +41 22 310 76 40, www.hyposwissadvisors.ch