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Swipe to invest: the story behind millennials and ESG investing

We take a look at recent studies examining whether ESG investing may help meet growing demand from millennials who want to do good with their investments and how wealth managers are responding to that trend.

ESG Research

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Millennials and ESG

In recent years, adoption of environmental, social and governance (ESG) investing has accelerated in part due to momentum from key industry organizations such as the Principles for Responsible Investment (PRI), availability of better ESG data and tools, and demand from the next generation of investors known as millennials. According to new analysis by the Pew Research Center[1], millennials are defined as those born between 1981 and 1996. With ages between 24 and 39 in 2020, members of this generation have entered their prime earning years.

A 2018 survey indicates that 87% of high net worth (HNW) millennials consider a company's ESG track record an important consideration in their decision about whether to invest in it or not. [2] 90% of millennials want to tailor their investments to their values.[3]

ESG Investing – a term that is often used synonymously with sustainable investing, socially responsible investing or mission-related investing – can be defined as the consideration of ESG factors alongside performance factors in the investment decision-making process.

A 2019 Morgan Stanley Institute for Sustainable Investing survey of high net worth investors says that 95% of millennials are interested in sustainable investing.[4]

The collection of studies below suggests that millennials, as well as women and, increasingly, individual investors of all ages and genders, are interested in directing their investments toward companies with good ESG records. They want their money not just to earn a return but to reflect their personal values and contribute to the social good. The research suggests they are asking more questions of their wealth managers and are scrutinizing their investments to understand what they own and how it impacts society and the planet at large.

Why millennials matter

Millennials are a large demographic representing 79.4 million people in the U.S. alone, and immigration could lead to an increase in this number to 81 million by 2036.[5] This group is also poised to inheret a significant amount of wealth.

“We’re in the middle of a $30 trillion intergenerational wealth transfer from baby boomers to their children,” says Dave Nadig of ETF.com. “And those kids—not really millennials only, but people from 25 to 40 years old – simply think about their investment decisions differently.”

"Demand for sustainable investments is being driven, in part, by millennials who prefer to invest in alignment with personal values," said a 2019 report by Julian Seelan, the sustainable investing lead for wealth and asset management clients at Ernst & Young. Firms typically lose 70% to 80% of assets when it is transferred from one generation to the next. "Consequently, the wealth and asset managers who supply millennials ESG investment options will be strongly positioned to attract new assets to the firm as well as retain beneficiary millennial clients." [6]

Interest in sustainable investing among the general population of investors jumped from 71% in 2015 to 85% in 2019, and in millennial investors from 84% in 2015 to 95% in 2019. In years past, women were more likely than their male counterparts to factor sustainability into investment decisions, and see the benefits of doing so. However, this difference in interest has dropped from 17 percentage points in 2017 to three in 2019.[7]

According to Pew Research Center analysis[8] new census data[9], households headed by a millennial now earn more than young adult households did at nearly any time in the past 50 years. This growth can be partially attributed to millennial women, who are working more and being paid more than similarly aged women in previous years.

Wealth managers are preparing for this new generation of investors. 43% of the affluent millennials who responded to a 2019 Investopedia Affluent Millennial Investing Survey said they use a financial advisor. Those surveyed said they trust financial advisors more than they trust TV shows, books, newspapers, podcasts, websites, magazines, or online video content.[10] More than any other generation of investors, millennials are also flocking to robo advisors (though only 20% of affluent millennials Investopedia surveyed currently use them and a Charles Schwab report found that even among millennials, 79% would want their robo advisor to augment their offerings with access to human advice[12]). Ellevest, Motif, Merrill Edge, and other robo advisors offer ESG portfolios to help attract and retain their clients.

A Harvard Kennedy School Mossavar-Rahmani Center for Business and Government study concluded that asset managers who are not fluent in ESG investing will end up being less successful than those who are.

The interest from millennial investors and HNW millennials in particular has already helped drive the rapid growth in ESG investment. Bank of America Merrill Lynch says that they can "conservatively estimate" USD $20 trillion of assets growth in U.S.-domiciled ESG funds over the next two decades, equivalent to the value of the S&P 500 today.[13] Overall, sustainable investing experiences a compound annual growth rate of 17.44 percent, and increased assets under management from $8.7 trillion to $12.0 trillion in 2018.[14]

Nearly $4 billion flowed into ESG funds in the first three quarters of 2019. The year end total in 2018 was $5.5 billion, which at the time was a calendar-year record, but sustainable funds were on track to triple that during the waning months of 2019.[15]

How wealth managers are responding

"The No. 1 question I get from advisors is how to handle the coming generational wealth transfer," said ETF.com's Dave Nadig, "ESG has emerged as one of the dominant answers to that question."[11]

Wealth managers subscribe to MSCI ESG Research for various reasons. Through these relationships we have observed that wealth managers are building out ESG capabilities in five key areas in response to the growing demand for ESG investing options:

Screening on managed accounts

Wealth managers may offer negative screening through managed accounts. Negative screening refers to the exclusion of stocks from a portfolio, like the removal of tobacco stocks. We observe a range of criteria being used to screen SMAs, including traditional SRI screens like alcohol, tobacco, and weapons to Faith-Based screens like Catholic or Islamic Values. Business ethics screens including involvement in issues like child labor and animal testing are also popular. In recent years, we have also seen screening on emerging issues like fossil fuel involvement, nuclear power, and for-profit-prisons.

With increased ESG data on mutual funds and ETFs, we have also observed the emerging use case for screening funds on ESG criteria.

Due diligence and manager research

We observe that due diligence and manager research teams are leveraging ESG data to better understand the ESG characteristics of managed products and funds. We see due diligence integrating ESG into fund research and selection to complement their efforts to understand manager capabilities and processes. ESG reporting and data may help align what managers say they are doing with ESG outcomes. For example, where a manager says they are building a portfolio designed to minimize exposure to climate change risk, due diligence and research teams may leverage

ESG reporting to measure the Carbon Footprint and performance on climate change risk management of a portfolio and compare it to a benchmark.

Portfolio construction and management

We observe that wealth managers are integrating ESG factors into portfolio construction and management. While some wealth managers convert a portion of their client's portfolio allocation to an ESG or impact strategy, increasingly we've seen wealth managers seek to build portfolios based on a strategy that is entirely ESG. We have observed a number of model ESG portfolios launched by wealth managers over the past year that integrate ESG across the total portfolio, often in the form of a multi-manager model.

Reporting and transparency

We observe that investors are increasingly asking for more transparency on the ESG characteristics of their investments, they want to "know what they own". Not only are investors asking their wealth managers to consider ESG in their portfolio, they also want to understand the benefits of doing so. Reporting may provide wealth managers with the ESG data to respond to client queries and to also help point out things that may not be obvious or that are unknown to investors, e.g. "You have limited exposure to companies with significant environmental controversies compared to a benchmark". MSCI is increasingly supporting wealth managers who are providing transparency into the ESG characteristics of client portfolios, individual companies and funds.

Marketing and education

We observe wealth managers increasingly place emphasis on education and marketing to both internal and external stakeholders. Internal education on ESG may be fundamental to helping their advisors engage with the next generation of millennial investors. External education and marketing on ESG can be an opportunity to deepen client relationships, to increase client retention and to attract new assets.

At MSCI ESG Research we provide wealth managers with content and tools designed to support their education and marketing efforts, including introductory content to help investors learn about what ESG is and reporting capabilites that allow managers to market the ESG characteristics of their portoflios.

Highlights from the studies

$30 trillion

wealth transfer from baby boomers to 75 million millennials to take place over the next few decades.[16]

77%

of millennials cite owning ESG or including impact investments in their portfolios.[17]

89%

of millennials expect their financial professional to do a deep dive into a company's history, compliance, and values before recommending an investment opportunity.[18]

2X

57%

of millennials have intentionally stopped investing or declined to invest in a company because of the impact that company's products or services have on people's health and well being.[19]

95%

In the study by Morgan Stanley, 95% of millennial investors they surveyed said they are interested in sustainable investing, up 9 percentage points from 2017.[20]

85%

of individual investors are interested in sustainable investing, up 10 percentage points from 2017.[21]

The studies

Below are 13 studies published about the growing demand for ESG investing options.

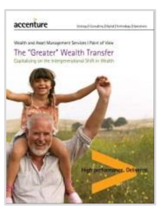
From time to time we may publish updates to this article to reflect new information.

1 U.S. Trust: **Insights on Wealth and Worth**
2018

Source:
https://newsroom.bankofamerica.com/system/files/2018_US_Trust_Insights_on_Wealth_and_Worth_Overview.pdf

2 Morgan Stanley: **Sustainable Signals – Individual Investor Interest Driven by Impact, Conviction and Choice**
2019

Source:
https://www.morganstanley.com/pub/content/dam/msdotcom/infographics/sustainable-investing/Sustainable_Signals_Individual_Investor_White_Paper_Final.pdf



3 Accenture: **The “Greater” Wealth Transfer -- Capitalizing on the Intergenerational Shift in Wealth**
2012

Source:
https://www.accenture.com/us-en/insight-capitalizing-intergenerational-shift-wealth-capital-markets-summary

4 Bank of America Merrill Lynch: **ESG Matters – US 10 reasons you should care about ESG**
2019

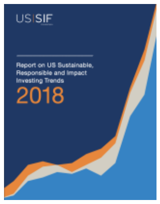
Source:
https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID19_1119/esg_matters.pdf

5 Ernst & Young: **The Millennial Economy**
2018

Source:
https://www.ey.com/en_us/tax/the-millennial-economy-2018

6 Investments & Wealth Institute: **Sustainable Investing – The Millennial Investor**
2019

Source:
https://investmentsandwealth.org/getattachment/bbdef004-2fe8-4e71-a445-918a270b5ff7/IWM19MarApr-TheMillennialInvestor.pdf



7 US SIF Foundation: **Report on US Sustainable, Responsible and Impact Investing Trends**
2018

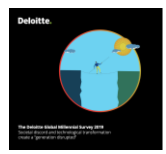
Source:
https://www.ussif.org/files/Trends/Trends%202018%20executive%20summary%20FINAL.pdf

8 Investopedia: **The Affluent Millennial Investing Survey**
2019

Source:
https://www.investopedia.com/the-investopedia-affluent-millennials-study-4769751

9 Morningstar: **Sustainable Investing Interest Translating Into Actual investments**
2019

Source:
https://www.morningstar.com/articles/952254/sustainable-investing-interest-translating-into-actual-investments



10 Deloitte: **The Deloitte Global Millennial Survey 2019**
2019

Source:
https://www2.deloitte.com/content/dam/Deloitte/global/Documents/About-Deloitte/deloitte-2019-millennial-survey.pdf

11 Allianz: **ESG Investor Sentiment Study**
2019

Source:
https://www.allianzlife.com/-/media/files/allianz/pdfs/esg-white-paper.pdf

12 Bank of America Merrill Lynch: **ESG: Impact on Companies Doing Business in America and Why They Must Care**
2019

Source:
https://www.bofaml.com/content/dam/boamlimages/documents/articles/ID18_0725/esg_impact_on_businesses.pdf

13 Investments & Wealth Institute: **U.S. Sustainable, Responsible, and Impact Investing Trends**
2019

Source: https://www.ussif.org/files/Article/IWM19JanFeb_US_SRITrends2018.pdf

Appendix: Defining ESG

No longer restricted to ethical screening, the term "ESG investing" now encompasses a wide range of investment objectives and beliefs, and different institutional investors sometimes pursue very different objectives when addressing ESG issues.

ESG Investing – a term that is often used synonymously with sustainable investing, socially responsible investing or mission-related investing - can be defined as the consideration of environmental, social and governance (ESG) factors alongside financial factors in the investment decision-making process. ESG factors include corporate governance risks, privacy and data security, supply chain management, labor standards or climate change and resource depletion risk.

Common investor approaches to ESG investing:

1. **Integration:** Some research suggests that ESG factors have historically contributed to long-term financial performance. ESG factors can be used to identify better-managed companies or to flag companies with business models that are likely to face headwinds or tailwinds driven by rapidly evolving regulatory, environmental, demographic or technological trends. Institutional investors may look to ESG factors as a way to manage these risks and to achieve long-term sustainable financial performance.[22]

2. **Values**: Some investors consider ESG issues a means for aligning investments with their ethical, religious or political beliefs. They have typically used ESG research to screen for controversial activities such as tobacco, weapons, alcohol, gambling or fossil fuels, and to help exclude such activities from their investment universe. Unlike the ESG integration goals described above, where ESG factors are considered on the basis of their potential economic impact, values-based goals are intentionally aligned to match an investor's beliefs.

3. **Impact**: A third group of investors focuses on the impact of their investments on the world around them. These investors direct their capital toward companies that provide solutions to environmental or social challenges and, through formal frameworks such as the UN Sustainable Development Goals (SDGs), monitor the extent to which their investments are generating positive social or environmental impacts alongside their financial returns.

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