2016 ESG TRENDS TO WATCH

OPPORTUNITIES AND RISKS

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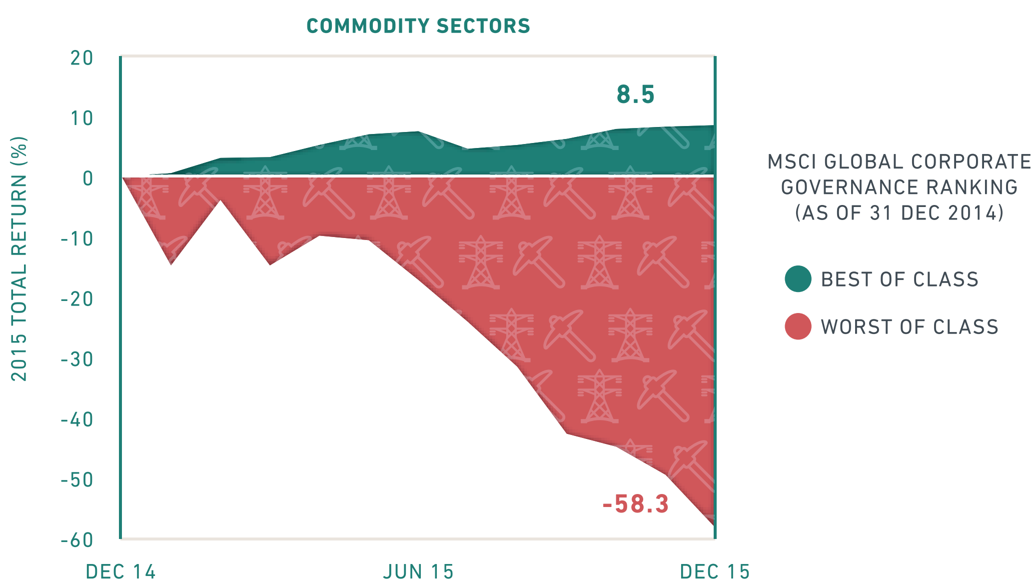
Environmental, social and governance concerns may play a growing role in investment matters in 2016. These trends reflect a softening economy, a long-term shift to a low carbon economy, a generational changeover and institutional forces. Below, we summarize these shifts; greater detail can be found in our report, "2016 ESG Trends to Watch."

TIDE TURNS ON CREDIT?

Academic research indicates that strong governance mechanisms may have led to reduced default risk and lower bond yields. A recent study by Barclays also found that investment-grade bonds with higher ESG scores outperformed those with low ESG scores between 2007 and 2015.

In 2016, we anticipate that if credit spreads widen, identifying ESG-related exposures and potential governance failures may play a bigger role as bond investors reprice underlying risks.



DIVIDE AND CONQUER

After the Paris climate agreement, how will institutional investors align their portfolio exposure to a low carbon economy? One issue is that companies with the largest renewable energy capacities also often have significant operations powered by fossil fuels such as coal, oil and gas.

In 2016, we may see utilities increasingly spin off renewable assets from legacy generation assets as investors seek exposure to the low carbon energy assets of the future.

2.2 MW

GENERATION
CAPACITY FROM

COAL

1 MW

GENERATION
CAPACITY FROM

WIND

SOLAR

OTHER
NON-HYDRO
RENEWABLE
SOURCES

WEALTH OF DATA

Wealth management, particularly in the U.S., is looking to serve a new generation of investors some of whom are focused on making a measurable social and environmental impact with their dollars.

In 2016, wealth managers may seek to differentiate themselves by offering new insight at the fund level, enabling advisors to more closely align products to their clients' individual values and philosophies. Such information might tilt toward ESG data, including values-based judgments, impact-based preferences or risk-based convictions for long-horizon investors.

VALUES-BASED INVESTORS

Preference to avoid business involved in tobacco, weapons manufacturing, or human rights violations;

IMPACT-BASED INVESTORS

Preference to capture measureable social returns per dollar invested including clean technology exposure, community building, or access to heatlhcare

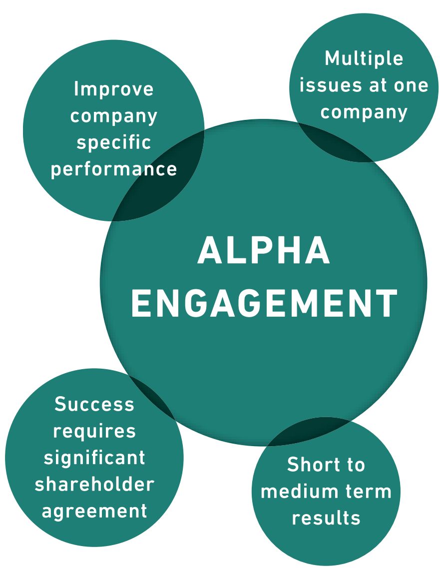
LONG-HORIZON INVESTORS

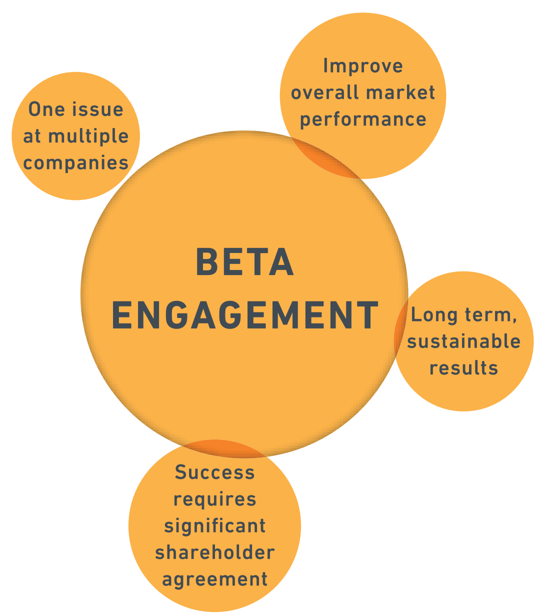
Goal of limiting potential financial costs connected with issues like water scarcity, energy costs, or carbon regulations

POWER IN NUMBERS

For years, asset owners have targeted governance problems at individual companies. More recently, some large pension funds have banded together to push for fundamental changes in boardrooms across the market.

In 2016, we expect that the power of “beta engagement” could expand beyond areas such as board declassification and proxy access to include board diversity and refreshment of long-tenured boards.

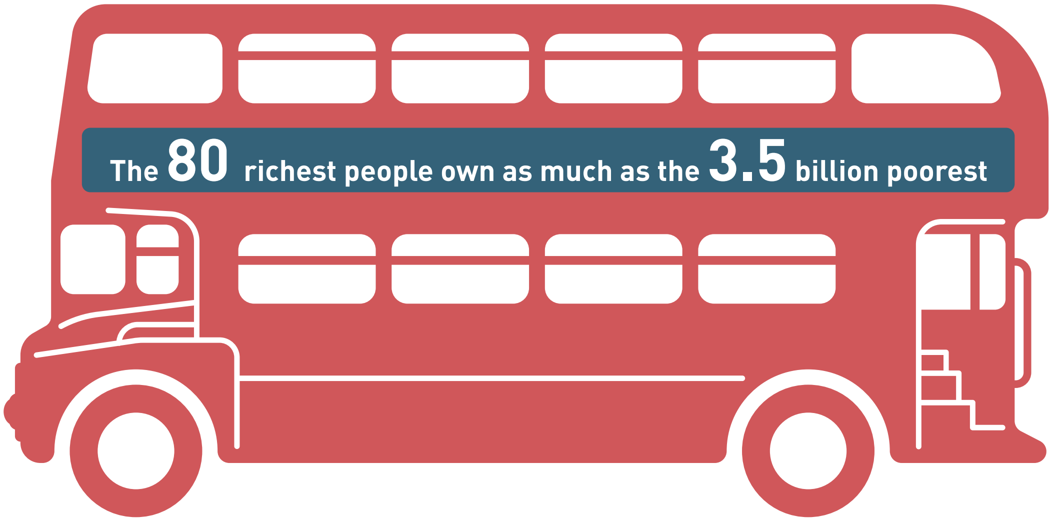




MIND THE PAY GAP

The growing disparity in pay between CEOs and median workers may be coming home to roost. The ratio has climbed to over 300:1 from 30:1 over the past four decades according to some measures.

In 2016, we may be nearing a tipping point as companies start to release pay ratio data and wage shocks occur. As a result, we expect that investor and academic focus could shift to how intra-company pay structures are linked to economic growth from sector- and country-level impacts of income inequality.



Source: Oxfam

READ THE PAPER, "2016 TRENDS TO WATCH"

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