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Getting Started

The Top 5 Sustainable Investing Questions

For Advisers

In a world flooded with information, it can be difficult to know where to start with environmental, social and governance-focused (ESG) investing.

However, when advisers ask the right questions, they can make more effective decisions for their clients.

What are the most important questions advisers need answered?

The Top 5 Questions for Advisers

First, let's start with the basics.

1 Which type of sustainable investing strategy is right for my client?

Understanding the terms used to describe investing is the first step.

Sustainable investing is an umbrella term that typically refers to all types of sustainable, impact and ESG integration approaches.

Impact investing

Generates measurable social or environmental benefits

Socially responsible investing (SRI)

Aligns with an investor's ethical, religious or personal values, while actively reducing negative environmental or social consequences.

ESG integration

Considers material environmental, social and governance factors to enhance long-term risk-adjusted returns.

Climate investing

Looks to reduce exposure to climate risk, identify low-carbon investment opportunities or align portfolios with "net zero" climate targets.

2 How can I start a conversation with clients about sustainable investing?

Begin by asking what motivates your clients. Priorities could include values, impact, financial returns or a combination.

Client motivations typically fall into one of these three core objectives.

Can ESG factors improve my risk-adjusted returns?
Will my portfolio benefit from the transition to a low-carbon economy?

Are my investments consistent with my ethical, political or religious beliefs?
Can I screen out certain industries such as tobacco or fossil fuels?

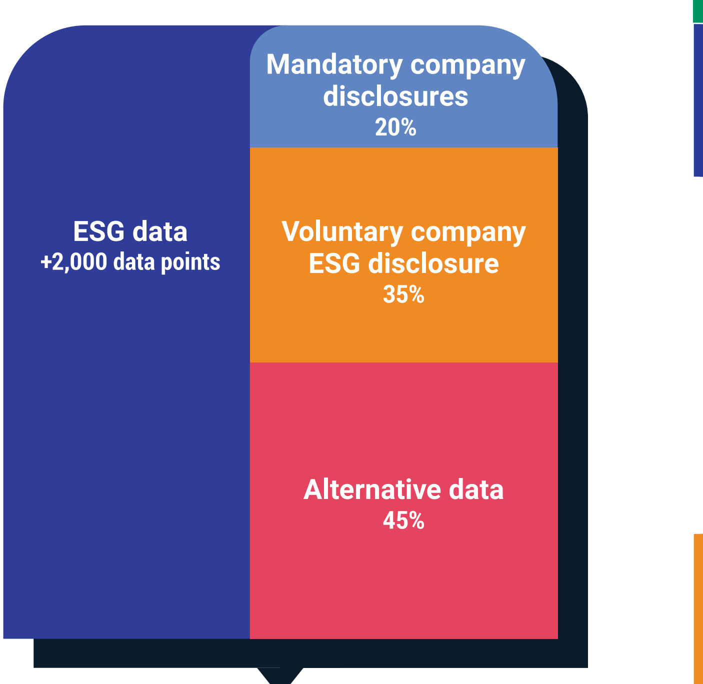
Can I have a positive impact on society through my investments?
Does my portfolio include companies that provide solutions to environmental and social challenges?

After identifying objectives, the next step is to determine the approach.

3 What is ESG data, and why is it important?

At the heart of ESG-focused strategies is data.

In fact, at MSCI, ESG analysis of companies is based on 2,000+ data points from a wide variety of sources.



Alternative data, such as flood risk analysis or geo mapping, often makes up **45% of the total ESG dataset**—far beyond what a company publicly discloses.

Source: MSCI ESG Research 2,434 constituents of the MSCI ACWI Index as of November 30, 2017 (MSCI, 2020)

Often, when people think of ESG data, it seems vague or elusive.

In reality, this isn't the case. Instead, ESG data can be broken down and obtained from the following sources:

After ESG analysts identify the risks and opportunities most relevant to a company, multiple data points coalesce to inform a company's ESG profile.

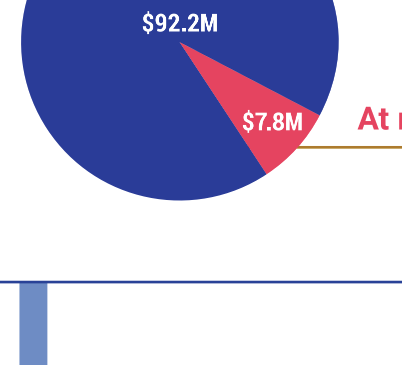
4 Why are environmental risks becoming increasingly important for investing?

Rising global temperatures and ecological disruptions pose imminent risks to humanity.

National, corporate and investor commitments to achieving net-zero emissions in alignment with the Paris Agreement have proliferated.

How does this affect the risk-return profile of investments?

According to research, climate change could erase $7.75 million in value over five years from a hypothetical $100 million portfolio.



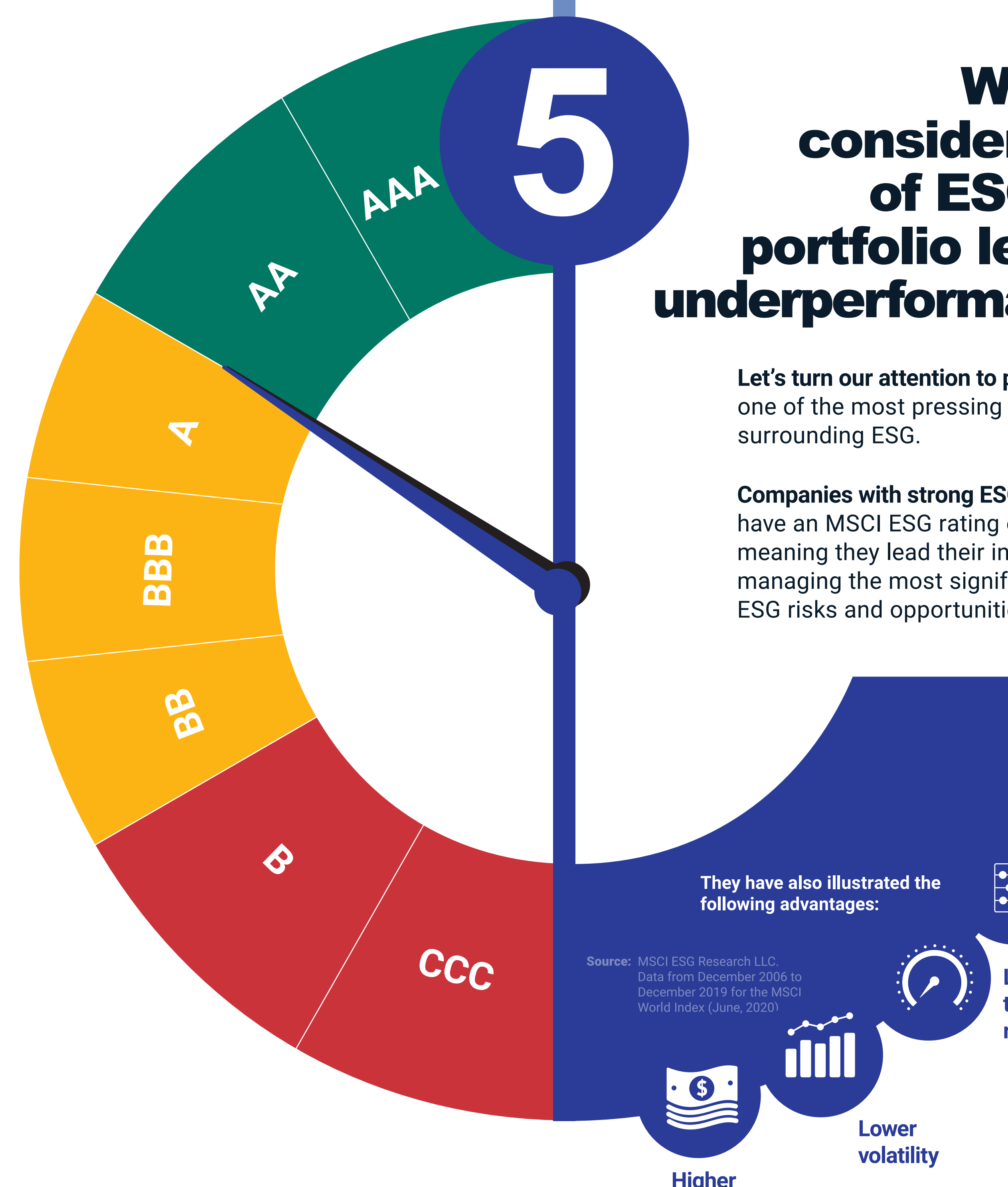
Source: MSCI ESG Research LLC. (June 26, 2020)
For illustrative purposes only.

Along with this, other future risks could include:

- Eroding shareholder value
- Blocked project proposals
- Regulation compliance costs
- Higher borrowing costs

Source: MSCI ESG Research LLC (June, 2020)

5 Will the consideration of ESG in a portfolio lead to underperformance?



Let's turn our attention to performance, one of the most pressing questions surrounding ESG.

Companies with strong ESG profiles have an MSCI ESG rating of AAA or AA, meaning they lead their industry in managing the most significant ESG risks and opportunities.

They have also illustrated the following advantages:

- Lower cost of capital
- Less exposure to systemic risk
- Lower volatility
- Higher profitability

Source: MSCI ESG Research LLC. Data from December 2006 to December 2019 for the MSCI World Index (June, 2020)

Shaping the Dialogue

As client demand is shifting toward ESG, the conversation is changing.

These questions can serve as a launching point for advisers to help clients seize new opportunities and mitigate investment risks.

This is part one in this series.

In part two, we focus on integrating ESG into portfolio construction.

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