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ESG and Climate Guide for Financial Advisers

Investing with Purpose

The world is changing rapidly. Global challenges, such as climate risk, represent new or increased challenges.

Today, Environmental, Social and Governance (ESG) is impacting all facets of the financial industry. ESG assets are expected to exceed $50 trillion globally by 2025.[1] In the US alone, millennials are expected to direct between $15 and $20 trillion into ESG investments, doubling the size of the US equity market.[2]

More investors are looking for their money to work in alignment with their values – and they are increasingly specific and sophisticated about what that alignment should look like. Advisers with the knowledge and tools to address these unique needs and position client portfolios accordingly will deliver considerable value and strengthen relationships.

[1] Source: Bloomberg Intelligence

[2] Source: Bank of America Corporation (2016) 'Environmental, Social & Governance Report', pg.3

Agenda

1. Understanding ESG and Climate Investing

Defining key factors
An evolving global framework fuels progress
Climate change is impacting the environment and the world's economies
The path to Net-Zero
Investor demand for transparency and action is accelerating

2. Integrating ESG and Climate into Portfolios

Building a framework
MSCI's disciplined ratings methodology
Ratings in practice
Improved equity returns
Improved risk-return profile for bonds
The positive impact of climate investing

3. Talking to Clients About ESG and Climate

"What are your goals?"
"Let's build a portfolio to meet your goals"
Telling the the portfolio story to clients
Contact us

Resources Key

- Webpage
- Brochure
- Video
- Research
- Infographic
- Podcast

1 Understanding ESG & Climate Investing

Defining Key Factors

While the term ESG – Environmental-Social-Governance – was commonly used shorthand for seeking to screen out or add in companies and investments with certain characteristics, today there is far more sophistication and depth to the conversation.

Governance
Ethical standards, corporate transparency, conflicts of interest

Social
Eg. Diversity, treatment of employees, corporate donations etc.

Environmental
Eg. Climate change, habitat loss, fossil fuels

Climate

In one sense a subset of the E in ESG, climate issues have emerged as a specific and important focus for investors. Climate-focused investing can be viewed as its own category and has unique measurements and criteria.

Tools and Resources

- ESG 101: Explore the fundamentals
- Why ESG Investing?
- Principles of Sustainable Investing
- What is an ESG rating?
- Fact Check: The Truth Behind 5 ESG Myths
- ESG Investing: Finding Your Motivation
- War and ESG

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An Evolving Global Framework Fuels Progress: Key Terms

Net-Zero:

Setting a Net-Zero target means reducing carbon emissions to the greatest extent possible, and compensating for the remaining emissions via removal.

COP26:

The 26th United Nations Climate Change conference was held in Glasgow in late 2021. The conference was the 26th Conference of the Parties (COP) to the United Nations Framework Convention on Climate Change. (UNFCCC.)

The Paris Agreement:

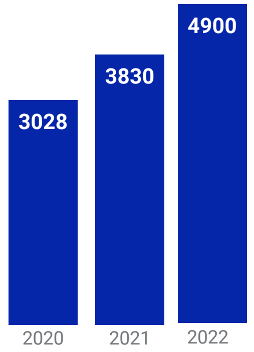
A legally binding treaty on climate change, at COP 21 and entered into on November 4th, 2016. The agreement seeks to limit global warming to below two degrees Celcius by reducing greenhouse gas emissions.

UN's Principles for Responsible Investment (PRI):

The Principles for Responsible Investment (PRI) call on investors to incorporate environmental, social and governance factors into their investment practices.

Greenwashing:

The term refers to companies falsely claiming to be doing more for the environment than they actually are - a misalignment of public statements, marketing or product labelling being with quantitative ESG data and ratings.



4900+ PRI Signatories
USD 121 trillion in assets*

Tools and resources

- [MSCI Net-Zero Knowledge Hub:] An interactive guide for professional investors
- [Net-Zero Tracker:] quarterly gauge of progress by the world's public companies toward curbing climate risk
- [SEC Climate Disclosure: Target Standardization]
- [Steps to Net-Zero:] Considerations for companies and investors (infographic)
- [ESG Now Podcast:] Hosts Mike Disabato and Bentley Kaplan discuss pressing ESG news

*Source https://www.unpri.org/signatories/signatory-resources/quarterly-signatory-update

An Evolving Global Framework: ESG, Climate and Impact

ESG INTEGRATION

"Incorporating ESG may improve our investment results."

Invest in companies **better positioned to manage their most financially relevant ESG risks** vs. industry peers.

CLIMATE INVESTING

"We want to invest in companies 1) aligning their products & services with their climate impact and 2) minimizing their contribution to global warming."

Invest in **alternative energy, energy efficiency, green building, pollution prevention, sustainable agriculture, & sustainable water** companies.

Invest in companies **better positioned to operationally withstand risks from global warming** by actively working to lower emissions, that have less enterprise value at risk from global warming.

IMPACT INVESTING

"We want investment opportunities that achieve a double bottom line – an attractive return and a positive impact."

Spanning all major asset classes, invest to simultaneously achieve positive social/environmental outcomes and financial gain.

Separate from ESG ratings, Impact is typically measured in accordance with the UN's 17 Sustainable Development Goals (SDGs.)

Tools and Resources

- Climate Matters: What an ESG Rating is and is Not
- Intro to Climate Solutions
- Impact Solutions
- UN Sustainable Development Goals: How do companies stack up?

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Climate Change is Impacting The Environment and The World's Economies

The warming of Earth's atmosphere caused by human-generated emissions of carbon dioxide and other greenhouse gases is causing sea levels to rise and endangering human health, biodiversity and property.

Averting a climate catastrophe will require the largest reconstruction of the global economy since the Industrial Revolution. Capital markets participants, including asset owners, companies, and asset managers will all be part of the solution.

The financial risks

$900 billion:

Or roughly one-third of the value of big oil and gas companies that estimates suggest would disappear if governments move to restrict the rise in global temperatures to 1.5° C above pre-industrial levels for the rest of this century[1].

Two to three:

The number of notches the sovereign credit rating of an oil-exporting nation could fall by 2050 absent steps to diversify its economy[2].

The financial opportunities

90%:

The share of global energy generation that is projected to come from renewable sources by 2050 according to a pathway to net-zero put forward by the International Energy Agency[3].

$1.5 trillion:

The value of new revenue opportunities from low-carbon goods and services, according to European companies in their 2019 disclosures to CDP[4].

Tools and Resources

- Climate 101: Aligning your portfolio with a net-zero economy
- MSCI Net-Zero Knowledge Hub: An interactive guide for professional investors
- The Role of Capital in the Net-Zero Revolution
- Foundations of Climate Investing
- The Paris Agreement and Your Portfolio
- Global Progress Towards the Paris Agreement

[1] Financial Times, *Lex in depth: the $900bn cost of 'stranded energy assets*
[2] Fitch Ratings, *Stranded Assets a Long-Term Risk for Major Fossil Fuel Exporters*
[3] Fitch Ratings, *Stranded Assets a Long-Term Risk for Major Fossil Fuel Exporters*
[4] iea, *Net Zero by 2050*

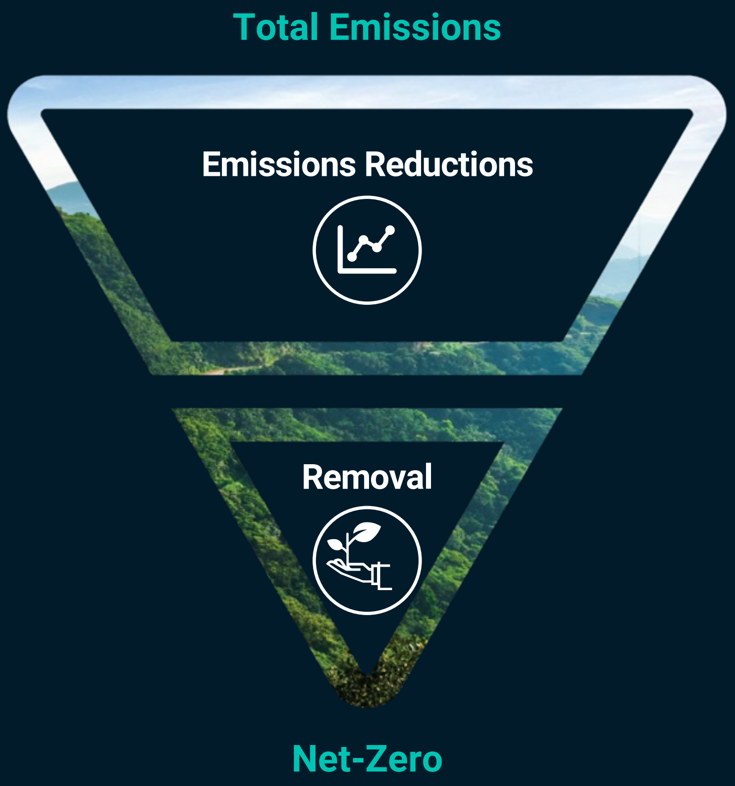
The Path to Net-Zero

To prevent the worst effects of climate change, we need to drive carbon emissions down to Net-Zero by 2050.

Net-Zero Investing

means aligning with the Paris Agreement goal of limiting global warming to well below 2°C, preferably no more than 1.5°C , above pre-industrial levels by 2100.

It means investing in companies with ambitious carbon reduction goals and compensating for remaining emissions that cannot be mitigated using carbon removal technologies.

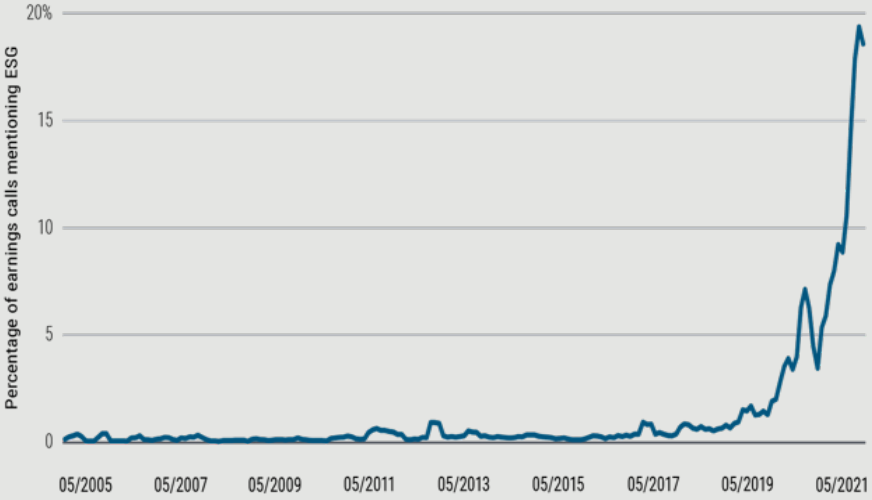


Investor Demand for Transparency and Action is Accelerating Rapidly

ESG is being integrated into all facets of the investment industry, and the rate of change is increasing.

- $30 trillion wealth transfer from baby boomers to 90 million millennials to take place over the next few decades[1]
- 67% of millennials believe investments "are a way to express social, political, and environmental value" versus 36% of baby boomers[2]
- 89% of millennials want to grow their allocation to responsible investments in the next five years[3]

Rapidly Increasing Mentions of ESG on earnings calls[4]



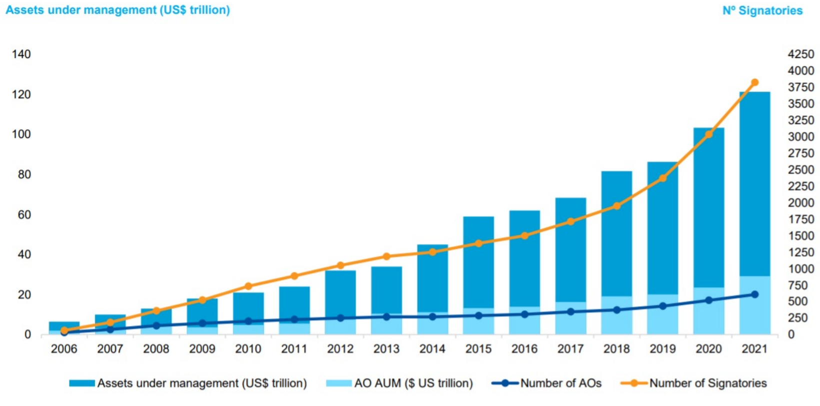
Tools and Resources

[The Sustainable ETF Universe]

[1]Source: Accenture. "The Greater Wealth Transfer – Capitalizing on the Intergenerational Shift in Wealth," 2012
[2]Source: US Trust's "Insights on Wealth and Worth," 2014
[3]Source FactSet's "HNW's Vision for the Wealth Management Industry in the Information Age"
[4]Source: PIMCO, July 2021

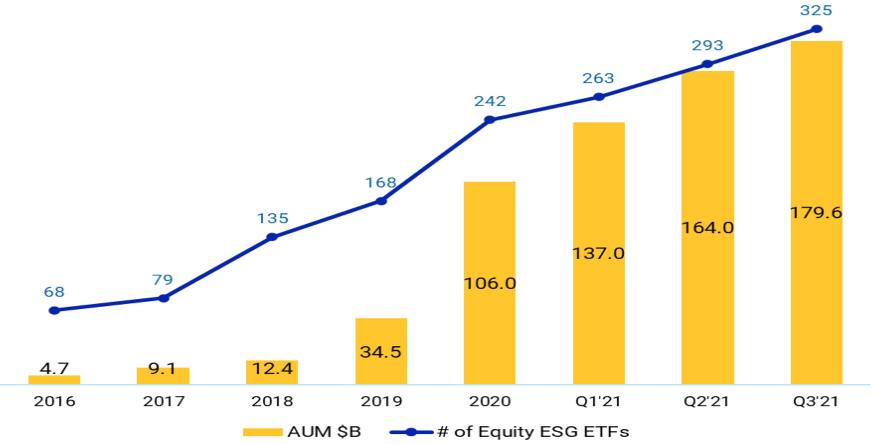
ESG and Climate Investing is Growing Dramatically

UN PRI* Has Grown to Over 4,902 signatories in managing over $121 trillion in AUM



*Total AUM include reported AUM and AUM of new signatories provided in sign-up sheet that signed up by end of March of that year.

#1 in no. of ETFs and ETF assets linked to ESG Equity Indexes**



In the next 10 years we think:

Every **company** will have a climate strategy with explicit objectives and targets for emission reduction, with **pathway to net-zero**

TCFD reporting will be mandatory in most European countries, and the norm globally

Company **climate disclosure** around **emissions and targets** will be required by regulation, audited and standardized

Engagement with companies will focus on climate strategy with emphasis on targets for **emission reduction**

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*Source https://www.unpri.org/signatories/signatory-resources/quarterly-signatory-update
**As of Q3'21, 152% growth YOY in ETF AUM tracking MSCI ESG indexes

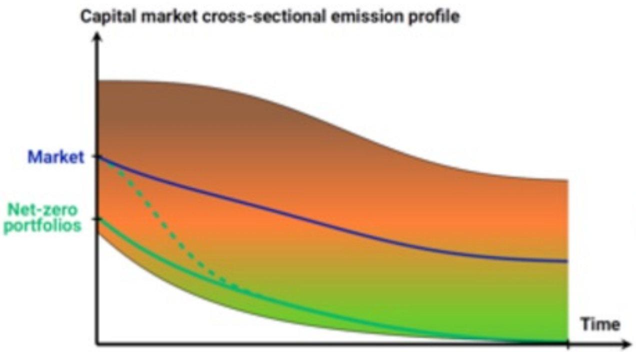
Climate Investing Delivers Real World Change

Climate investors face two scenarios.

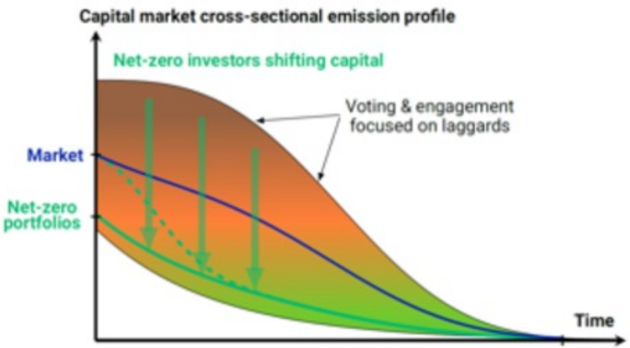
1 The divergence scenario - focus on net zero portfolios comprising of low greenhouse gas emitters, with periodic rebalancing. Net zero portfolios and the market portfolio diverge.

2 The convergence scenario – tilt investments towards “emissions improvers.” These companies may have high emissions now but also have ambitious and reachable targets to decarbonize. Their operations over time. This net zero portfolio converges with the market portfolio.

Divergence scenario scenario



Convergence



Tools and Resources

- [Using MSCI Climate Solutions]
- [Constructing Net-Zero Portfolios: Three Approaches]

The Climate and Net-zero Revolution is an Opportunity to Seize for Companies and Investors

POTENTIAL TO LOSE VALUE

Low carbon transition (LCT) CATEGORY	EXAMPLES
Asset Stranding	Coal mining & coal-based power generation; Oil sands exploration/production
Product Transition	Oil & gas exploration & production; Petrol/diesel-based automobile manufacturers, thermal power plant turbine manufacturers etc.
Operational Transition	Fossil fuel-based power generation cement, steel etc.
Low Impact	Consumer staples, healthcare, etc.
Solutions	Renewable electricity, electric vehicles, solar cell manufacturers etc.

POTENTIAL TO BENEFIT

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Source: MSCI, Foundations of Climate Investing, February 2021
GEMLT is the MSCI Global Total Market Equity Model for Long-Term Investors. Data from Oct. 31, 2013, to Jan. 31, 2021.
* e.g. controlling for possible biases due to sector, size, quality, country etc. to purely focus on the impact of LCT score

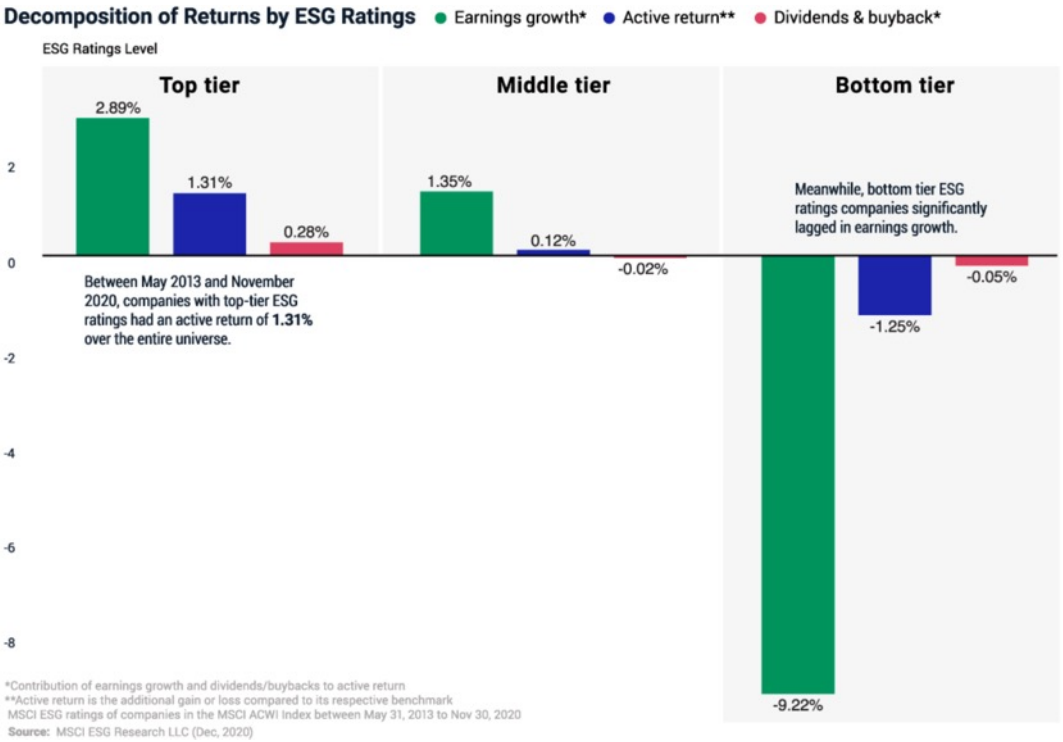
2 Integrating ESG and Climate into Portfolios

ESG Factors Have Improved Equity Returns…

While the perception that ESG principles hinder equity performance may linger in places, considerable data shows the opposite.

For example, ESG leaders showed resilience before and during the global pandemic. Worldwide, ESG-focused companies have not only seen higher returns, but stronger earnings growth and dividends.

Dispelling the myth that ESG comes at the expense of performance



Tools and Resources

- How Have Stocks Responded to Changes in Climate Policy?
- The Truth Behind 5 ESG Myths
- Foundations of climate Investing

… and Improved The Risk Return Profile of Bond Portfolios

Institutional investors made significant progress in incorporating ESG factors into their bond portfolios. Similar dynamics are now impacting retail portfolios and funds. ESG ratings had characteristics distinct from credit ratings and delivered financial value after accounting for credit ratings. The two types of rating systems complemented each other.

MSCI's analysis found that higher-ESG-rated bond portfolios realized higher risk-adjusted returns. They also exhibited significantly lower drawdowns, reflecting the defensive characteristics of an ESG bond strategy.

Tools and Resources

[Can Green Spreads Uncover ESG's Influence on Bond Prices?]

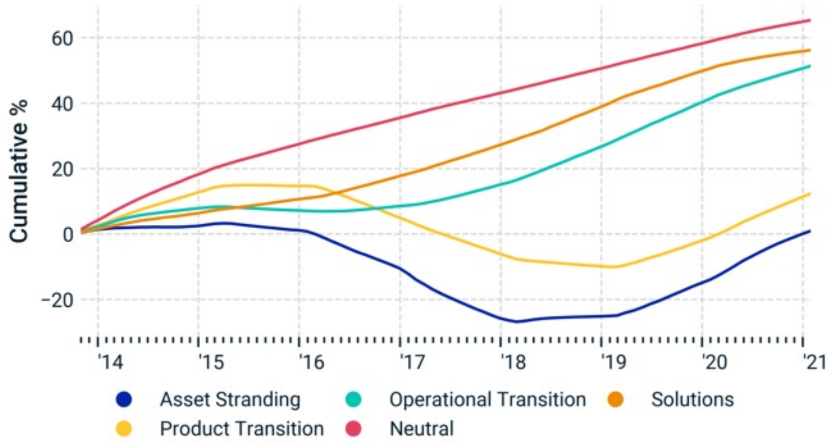
[What ESG Ratings Tell Us About Corporate Bonds]

Issuers from High-ESG-Score Tercile Had More Resilient Excess Returns

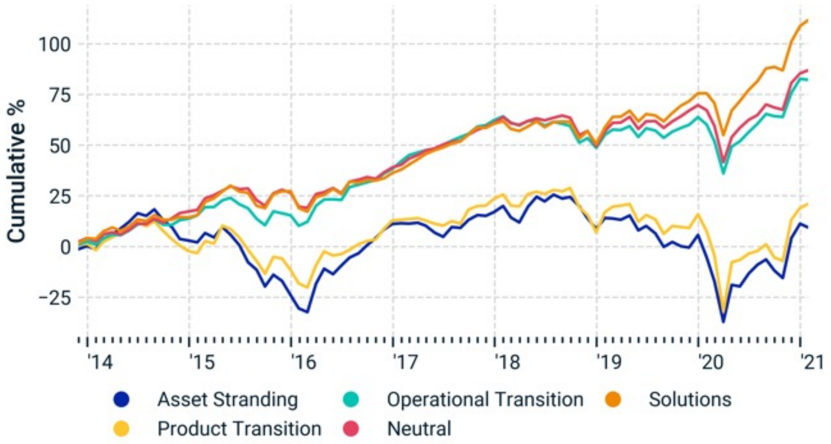
Financial Differences Between Greenhouse Gas Leaders and Laggards Can Be Significant

MSCI research has shown that higher carbon intensity leads to lower valuations, higher capital costs and a negative impact on stock price.
This impact is concentrated in the most carbon-intensive companies.

Earnings Growth



Stock Performance



Equal-weighted low carbon transition categories within MSCI ACWI IMI

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Source: Data from Oct. 31, 2013, to Jan. 31, 2021. EPS growth is taken from the GEMLT model and uses 5-year smoothing

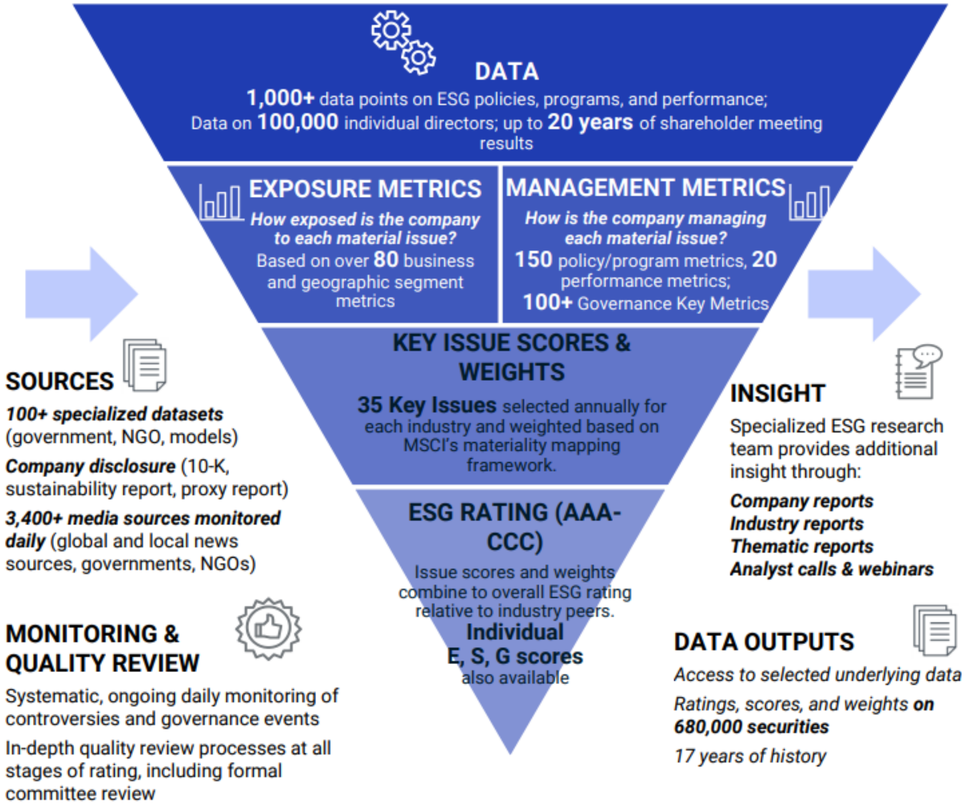
Building an ESG Framework

ESG ratings provide a consistent framework to facilitate comparative decisions. This consistency is the foundation of security analysis and subsequent ESG-driven portfolio construction.

It enables decisions based on factors that go deeper than corporate statements on ESG intent. Experience has shown that these statements have, on occasion, been misaligned from ESG reality (often referred to as "greenwashing.") Advanced technology, including artificial intelligence, will further reduce reliance on voluntary disclosures from companies.

Tools and Resources

- ESG Fund Ratings Search Tool for 8500+ companies
- ESG and Climate Funds in Focus
- ESG Indexes
- Understanding MSCI Climate Indexes



Source: https://www.msci.com/documents/1296102/21901542/ESG-Ratings-Methodology-Exec-Summary.pdf

MSCI's Ratings Methodology

ESG risks and opportunities can vary by industry and company. Our MSCI ESG Ratings model identifies the ESG risks, (what we call Key Issues), that are most material to a GICS® sub-industry or sector.

MSCI's ESG ratings measure a company's resilience to financially material environmental, societal and governance risks. While not a general measure of corporate "goodness" or a barometer on any single issue they provide a window into a critical facet of risk to financial performance.

With over 13 years of live track history we have been able to examine and refine our model to identify the E, S, and G Key Issues which are most material to an industry.

Tools and Resources

- Inside ESG Ratings: How Companies Are Scored
- What are ESG Fund Ratings?
- Climate Matters: What's in an ESG Rating. And What's Not.

CCC	B	BB	BBB	A	AA	AAA
LAGGARD A company lagging its industry based on its high exposure and failure to manage significant ESG risks		**AVERAGE** A company with a mixed or unexceptional track record of managing the most significant ESG risks and opportunities relative to industry peers			**LEADER** A company leading its industry in managing the most significant ESG risks and opportunities	

MSCI's Ratings Methodology

We assess thousands of data points across 35 ESG Key Issues for more than 8,500[1] companies globally. MSCI focuses on the intersection between a company's core business and the industry-specific issues that may create significant risks and opportunities.

The Key Issues are weighted according to impact and time horizon of the risk or opportunity. Corporate Governance and Corporate Behavior are typically broadly applied while environmental and social factors can vary significantly by industry.

Tools and Resources

MSCI's ESG Ratings

MSCI ESG Score									
Environment Pillar				Social Pillar				Governance Pillar	
Climate Change	Natural Capital	Pollution & Waste	Env. Opportunities	Human Capital	Product Liability	Stakeholder Opposition	Social Opportunities	Corporate Governance	Corporate Behavior
Carbon Emissions	Water Stress	Toxic Emissions & Waste	Clean Tech	Labor Management	Product Safety & Quality	Controversial Sourcing	Access to Communication	Board	Business Ethics
Product Carbon Footprint	Biodiversity & Land Use	Packaging Material & Waste	Green Building	Health & Safety	Chemical Safety	Community Relations	Access to Finance	Pay	Tax Transparency
Financing Environmental Impact	Raw Material Sourcing	Electronic Waste	Renewable Energy	Human Capital Development	Consumer Financial Protection		Access to Health Care	Ownership	
Climate Change Vulnerability				Supply Chain Labor Standards	Privacy & Data Security		Opportunities in Nutrition & Health	Accounting	
					Responsible Investment				
					Insuring Health & Demographic Risk				

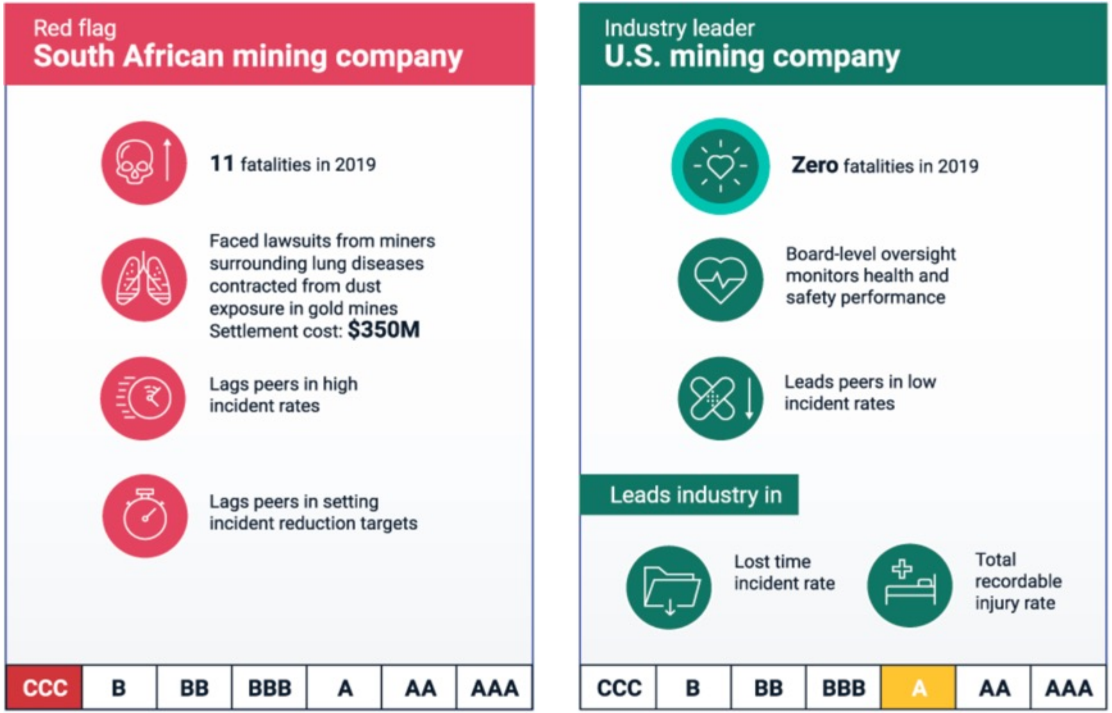
Key Issues selected for the Soft Drinks Sub Industry (e.g. Coca Cola)

Universal Key Issues applicable to all industries

[1]As of October 2020

Ratings in Practice: ESG and Working Conditions

Safety protocols are a key sustainability issue for the industrial sector. Here’s how two companies compare. Investors can choose to support companies that take greater lengths to protect their workers.



Source: MSCI ESG Research (Dec, 2020)

Tools and Resources

[The Power of a Sustainable Dollar]

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In Practice: Implied Temperature Rise (ITR)

What does it measure?

The Implied Temperature Rise (ITR) metric provides an indication of how well public companies align with global temperature goals

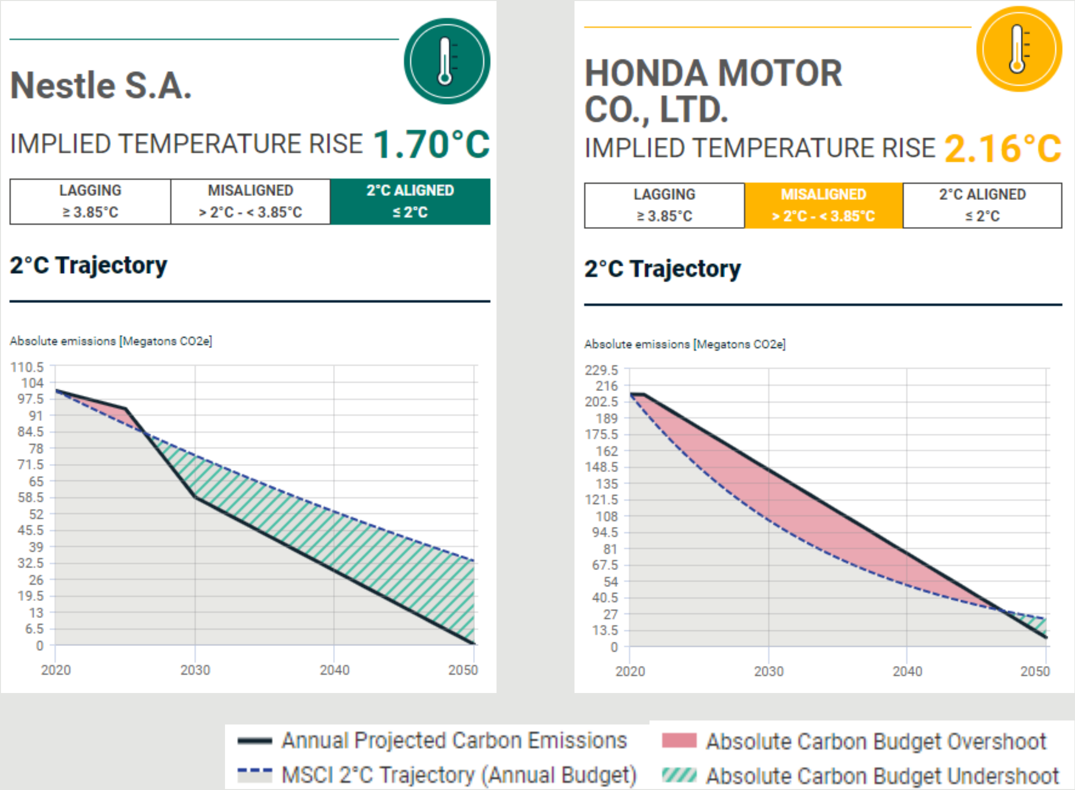
Expressed in degrees Celsius, it is an intuitive, forward-looking metric that shows how a company aligns with the ambitions of the Paris Agreement

It covers companies' Scope 1, 2 and 3 carbon emissions (may include estimates)

Based on data that can be easily examined and traced, together with analysis of companies' decarbonization targets

Tools and Resources

- What Implied Temperature Rise Means for Funds
- The Implied Temperature Rise of 'Paris-Aligned' Indexes
- ESG Ratings and ITR Search Tool



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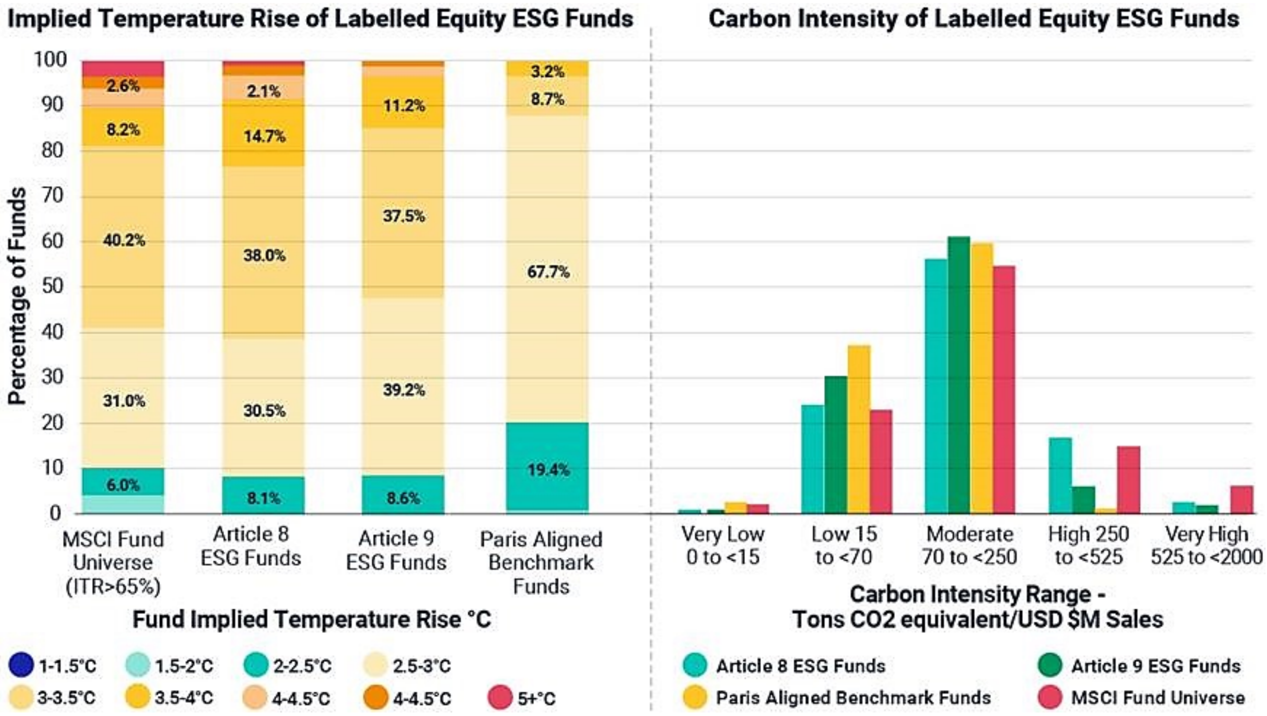
For illustrative purposes only. Past performance is not a guarantee of future results. There can be no assurance of any investment objective or outcome. Please see disclaimers at the end of this presentation.
As of April 08, 2022

In Practice: Sustainable Fund Selection

Wealth managers are increasingly integrating climate considerations into fund selection and portfolio construction. Data points such as Fund Implied temperature rise can be used to filter the universe in this regard.

Tools and Resources

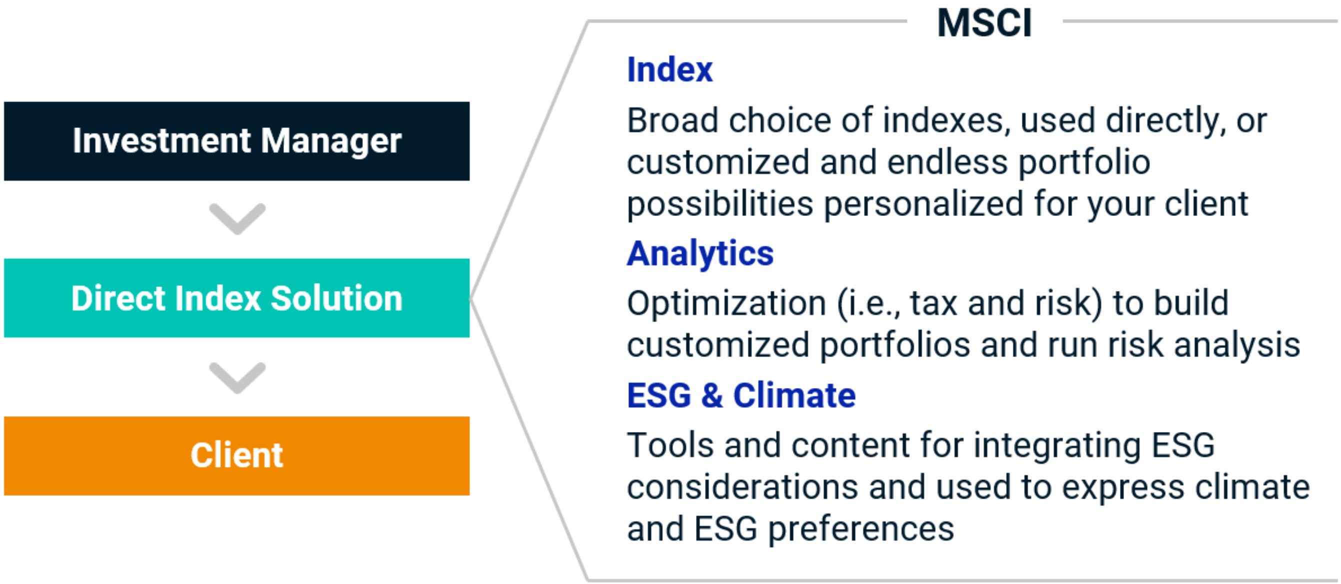
- ESG and Climate Funds in Focus
- ESG Funds – A Global shift in investments



Climate funds defined as mutual funds and ETFs that have "climate" in the product name and include climate specific considerations in the investment strategy. Uncategorized Climate Funds = 106, Article 8 Climate Funds = 45, Article 9 Climate Funds = 72. Data as of Nov. 11, 2021. MSCI ESG Research LLC

In Practice: Direct Indexing

Investors can customize any one of the MSCI Indexes suite to better align a client's portfolio with their climate preferences, lower risk and reduced tax burden.



Information Classification: GENERAL

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3 Talking to Clients About ESG and Climate

Different Roads to Travel

Constructing a portfolio that meets a client's ESG goals begins with understanding and defining their preferences. Some may be concerned with excluding firms or sectors viewed as having negative impact. Others may want to accentuate positive inclusion. The growing importance of climate investing adds another dimension to the conversation.

Tools and Resources

- MSCI ESG and Climate Indexes: An Index for Every Objective
- Top 5 Sustainable Investing Questions
- Climate Exposure and it's impact on the client portfolio

“What Are Your Goals?”

Incorporating ESG into investment strategy or creating products typically starts with understanding client objectives, which may combine elements of managing long-term risk, reflecting values and positive impact.

Investment Objectives

“Incorporating ESG may improve our investment results”

Integration

Financial returns

ESG criteria

Incorporate ESG criteria to enhance long-term return, manage ESG financial risk

Individual Objectives

Values

Values & Preferences

Financial Returns

Align portfolio with investor’s ethical or political values

“Our investments should reflect our clients’ values”

Impact

Values & Preferences

Financial Returns

Generate measurable social or environmental benefits as well as financial returns

“We want our investments to make a difference in the world”

“Let’s Set a Strategy to Reflect Those Goals”

Taking a multi-dimensional approach to integrating ESG And climate change enables you to:

- Construct model portfolios that meet your clients’ long-term financial objectives and ESG & Climate Change preferences
- Providing flexibility to make tactical calls

1. Improve ESG and Climate Change criteria

Allowing you to meet your headline financial objectives, while improving your ESG profile and /or reducing the carbon footprint

CORE

2. Personal ESG Preferences and Solutions

Enable your clients to strongly express their views on personal preferences ranging from social (e.g. diversity), or environmental (e.g. pollution) or thematic

IMPACT

3. Tactical Allocation

Allows you to retain your critical skills (tactical calls) within regions, country, sectors, factors or currencies, while still integrating ESG or Climate considerations

TACTICAL

“Let’s Build a Portfolio to Reflect Those Goals”

An ESG-first approach can comprise three components:

1. A core allocation to a mix of equities and bonds that broadly integrates ESG and climate considerations
2. An impact allocation to a mix of assets that reflects the investor’s specific ESG preferences
3. A tactical allocation that includes decisions around other considerations, including regions, sectors, style factors, durations, credit ratings or currencies

Tools and Resources

- Personalizing Climate-Focused Wealth Management Portfolios
- An ‘ESG-FIRST’ Approach to Portfolio Construction

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Information Classification: GENERAL

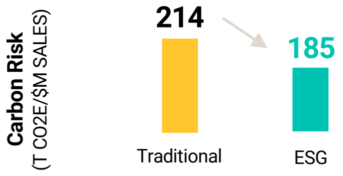
Telling The Portfolio Story to Clients: “Let’s Look at The Result of Putting Climate and ESG Goals First”

Similar risk profile to traditional model portfolio*

	Risk	Return (2 Yr)
Traditional	6.73%	16.86%
ESG	6.70%	14.80%

21% Improvement in ESG Quality Score

14% reduction in Carbon Risk



Traditional Model Portfolio	
US Equity	**Weight**
MSCI USA Index	33%
Non-US Developed Market Equity	
MSCI EAFE Index	20%
Emerging Markets Equity	
MSCI EM Index	7%
Fixed Income	
Bloomberg Barclays Global Aggregate Index	40%

ESG Model Portfolio	
US Equity	**Weight**
MSCI USA ESG Leaders Index	27.5%
Non-US Developed Market Equity	
MSCI EAFE ESG Leaders Index	16.7%
Emerging Markets Equity	
MSCI EM ESG Leaders	5.8%
Global Equity – Impact	
MSCI ACWI Sustainable Impact Index	10%
Fixed Income	
Bloomberg Barclays MSCI Global Aggregate Sustainability Index	35%
Fixed Income – Impact	
Bloomberg Barclays MSCI Global Green Bond Index	5%

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Simulated using MSCI Multi-Asset Class Model (MAC)

Telling The Portfolio Story to Clients: Measuring and Communicating Impact

What emissions do my investments currently generate?	How ambitious are portfolio company climate commitments?	How will my investments contribute to global warming in the future?	How will global warming impact the value of my investments?	How are my investments poised to capture climate opportunities?
Carbon Footprint Calculator	**Climate Target Commitments Dataset**	**Implied Temperature Rise (1.5°)**	**Climate Value at Risk (Climate VaR)**	**Low Carbon Transition Score, Patent Data, Green Revenues**

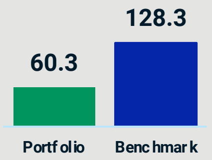
Using Climate Insights to Elevate Investment Proposals

Carbon intensity

(tCO2E/$M invested)

Measures the carbon efficiency of a portfolio, defined as the ratio of carbon emissions for which an investor is responsible to the sales for which an investor has a claim by their equity ownership.

53% lower carbon intensity than benchmark



Based on 81% company-reported emissions data, 19% estimated data

Implied Temperature Rise

Implied Temperature Rise (ITR) provides a portfolio level number in degrees of Celsius demonstrating how aligned the companies in the portfolio are to global temperature targets. Learn more

Portfolio	Benchmark
2.0 °C	2.9 °C

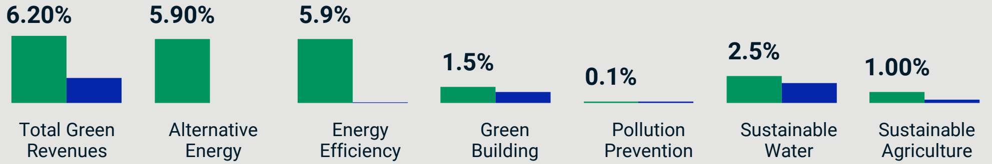
STRONGLY MISALIGNED	MISALIGNED	2°C ALIGNED	1.5 °C ALIGNED
above 3.3°C	between 2°C and 3.3°C	between 1.5°C and 2.0°C	below 1.5°C

Sample Portfolio AA

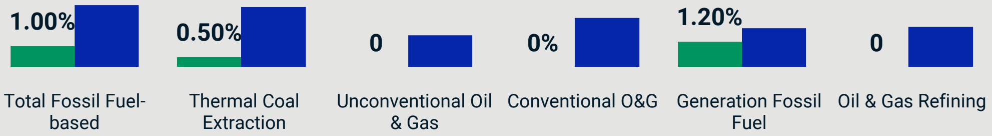
Sample Benchmark BBB

Climate Value at Risk	Portfolio	Benchmark	Active
Policy Climate VaR	-2.58%	-5.87%	3.29%
Technology Opportunities Climate VaR	+2.67%	+2.24%	0.43%
Physical Climate VaR (Aggressive)	-3.22%	-7.57	4.35%
Aggregated Climate VaR (Aggressive physical risk)	**-3.13%**	**-11.21%**	**8.08%**

Green activity revenue exposure %

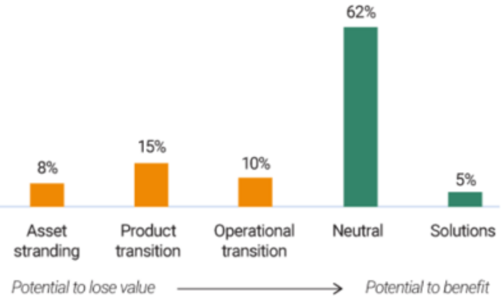


Fossil fuel-based activity revenue exposure %



Low-carbon transition categories

% of portfolio



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Better Outcomes for Clients, Advisers and The Planet

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