

How to talk to your clients about Responsible Investing

Steven Glass – Pengana International Equities
Michael Blayney and Jeremy Dean – Pental Group
Dugald Higgins – Zenith Investment Partners

IMAP and COVID-19

- 2020 Events
 - Awards - August
 - InvestTech - September
 - Portfolio Management Conferences - November
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IMAP Webinar: How to talk to your clients about Responsible Investing

August 2020

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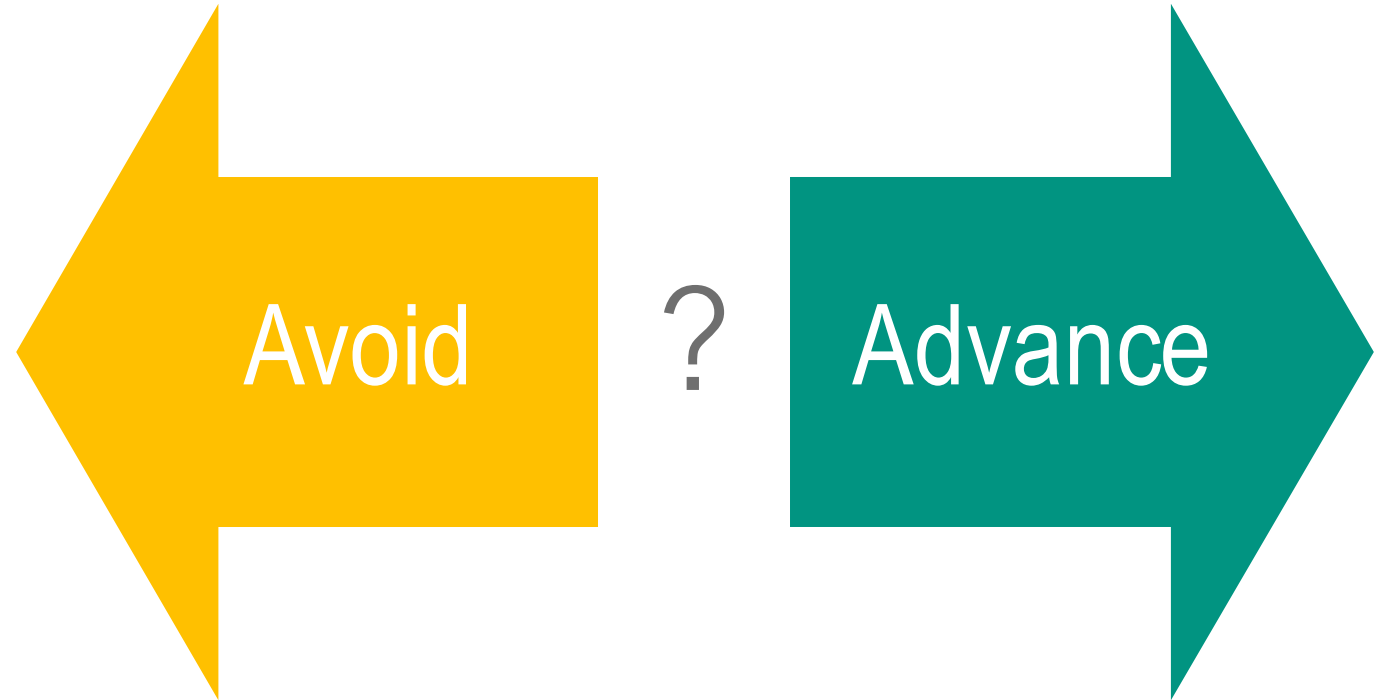
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Which way?

- Engagement?
- Negative screen?
- Positive tilt?
- Thematic?
- Impact?
- What are the implications?





PENGANA
CAPITAL

PENGANA
INTERNATIONAL ETHICAL FUND

Webinar

Presented by



Steven Glass
Deputy Portfolio Manager and Analyst

ESG INVESTING WITHOUT COMPROMISING RETURNS

ESG COMPLIANCE



SOLID RETURNS

APPLYING AN ETHICAL AND ESG LENS TO INVESTING

ESG investing can mean
different things to
different people



ESG INVESTORS' EXPECTATIONS

RIAA'S RESPONSIBLE AND ETHICAL INVESTMENT SPECTRUM

	TRADITIONAL INVESTMENT	RESPONSIBLE & ETHICAL INVESTMENT					PHILANTHROPY	
		ESG INTEGRATION (including shareholder engagement & voting)	NEGATIVE SCREENING (& norms based)	POSITIVE OR BEST-IN-CLASS SCREENING (& norms based)	THEMATIC/ SUSTAINABILITY THEMED INVESTMENTS	IMPACT INVESTING		
						MARKET RATE	CONCESSIONARY RATE	
FOCUS	Limited or no regard for environmental, social and governance factors	Consideration & analysis of environmental, social and governance (ESG) factors as part of investment decision making	Industry sectors or companies excluded/ divested from to avoid risk or better align with values	Investments that target companies or industries with better ESG performance	Investments that specifically target sustainability themes eg clean energy, green property	Investments that target social and environmental impact and deliver market rate financial returns	Investments that target social and environmental impact and deliver below market rate returns	Grants that target positive social and environmental impact with no financial return
IMPACT INTENTION	Agnostic	Avoids harm		Benefits stakeholders				
		Contributes to solutions						
FEATURES		Delivers competitive financial returns						
		Manages ESG risks						
			Pursues ESG opportunities					
			Intentionality: delivery of impact is central to underlying asset/investment					
			Impact of investment is measured & reported					

POSITIVE IMPACT AND FINANCIAL RETURNS

Vestas

- **World's largest wind turbine company**
- Large service business – c40% VWS' EBIT
- **Competitive advantages** - installed based, biggest R&D budget, reputation
- **Market share** (ex-China) grown from 17% (CY14) to 35% (CY19)
- **Fortress balance sheet**
- Green energy has positive outlook but regulation is a concern, particularly PTC (USA)
- Potential to benefit from fiscal stimulus
- 5% FY21 FCF yield



RAFT OF AREAS WE ARE LOOKING AT

But they
must fit our
financial
requirements



REQUISITE CHARACTERISTICS



**POSITIVE
TAILWINDS**



**GOOD
MANAGEMENT**



**UNLIKELY
TO BLOW UP**



**CASH
GENERATION**

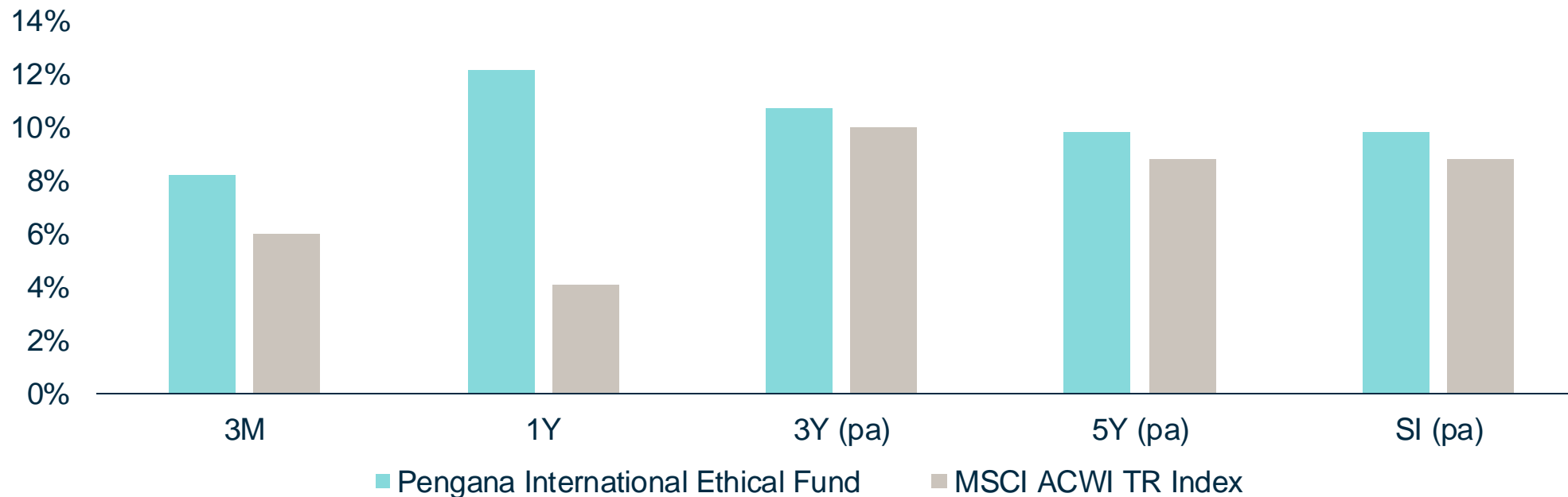


**REASONABLE
VALUATION**



GROWING

ESG INVESTING WITHOUT COMPROMISING RETURNS



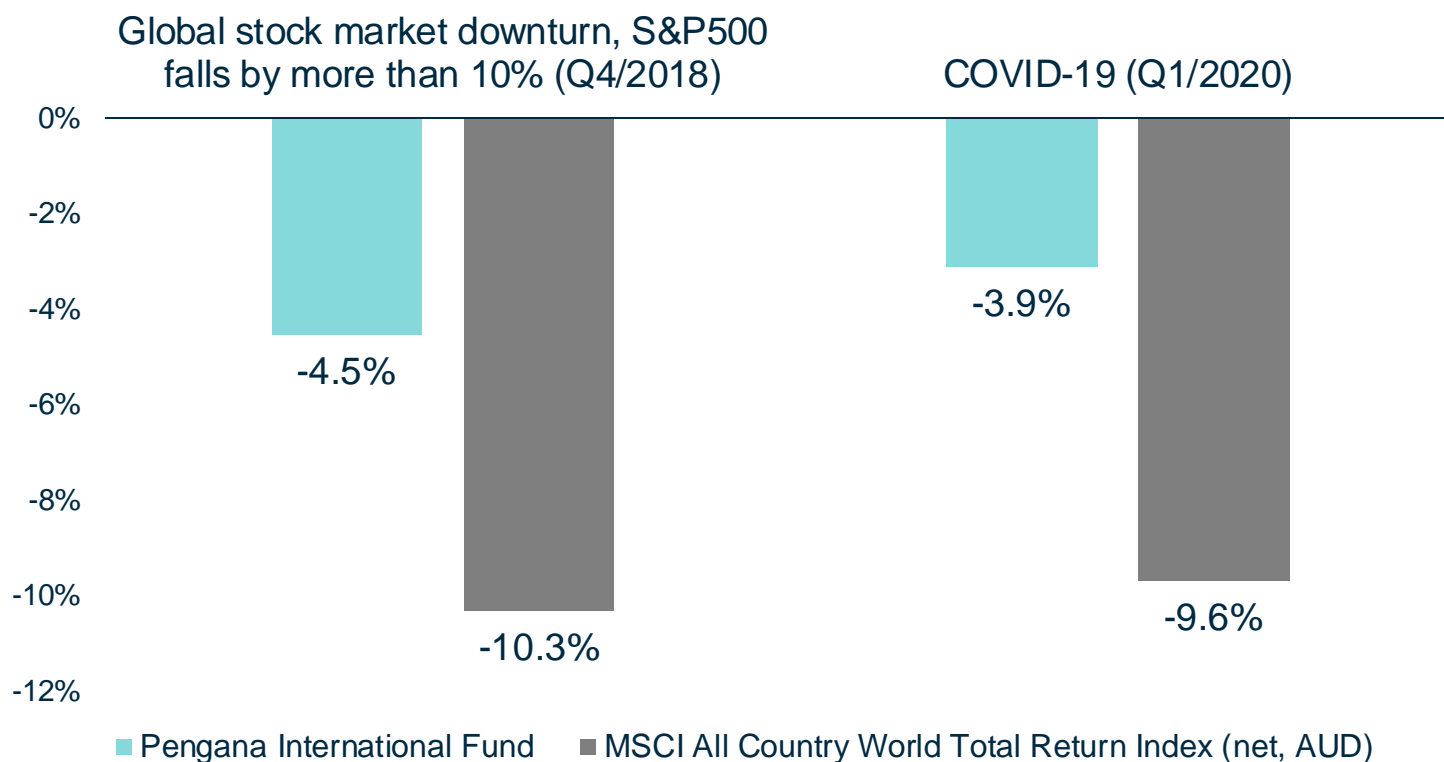
	3 months	1 year	3 years	5 years	Since inception
Relative Return	2%	8%	1%	1%	1%

Source: Bloomberg and Pengana Capital

The performance calculations for the Fund in this report have been calculated net of fees and expenses, on a pre-tax basis and assume that all distributions are reinvested. Past performance is not a reliable indicator of future performance. The value of investments can rise and fall. From July 2017, performance figures are those of the Pengana International Fund - Ethical class A units (net of fees). Between July 2015 and June 2017 performance figures have been recalculated by adjusting the Pengana International Fund's (ARSN 610 351 641) net returns to reflect the management fee of the Pengana International Fund - Ethical. From July 2017 the Pengana International Fund - Ethical has been managed by the same team and with the same strategy as the Pengana International Equities Fund. The Pengana International Fund's net track record data is historical.

PROTECTING CAPITAL AND MANAGING VOLATILITY

MANAGING VOLATILITY AND PROTECTING CAPITAL



Annualised Volatility Since Inception	
Pengana International Ethical Fund	9.7%
MSCI All Country World Total Return Index (net, AUD)	11.0%

Source: Bloomberg and Pengana Capital

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SUMMARY

Comprehensive Solution

- ESG compliant
- Deliver solid point to point returns
- Minimize drawdowns
- Minimize volatility

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How to speak to clients about ESG

Jeremy Dean | Head of Responsible Investment Distribution

Michael Blayney | Head of Multi-Asset

August 2020



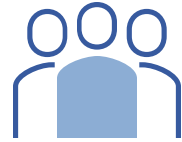
What is responsible investing?



ESG integration

Considering Environmental, Social and corporate Governance (ESG) factors - both risks and opportunities - in the investment process.

An essential element of RI. BAU.



Ethical or socially responsible investing

Investments which incorporate ethical and/or other values-based considerations.

Example: Exclusions/ negative screening



Sustainability investing

Investments that target companies with sustainable business practices & products.

Example: Best of Sector', Thematic, positive tilting



Impact investing

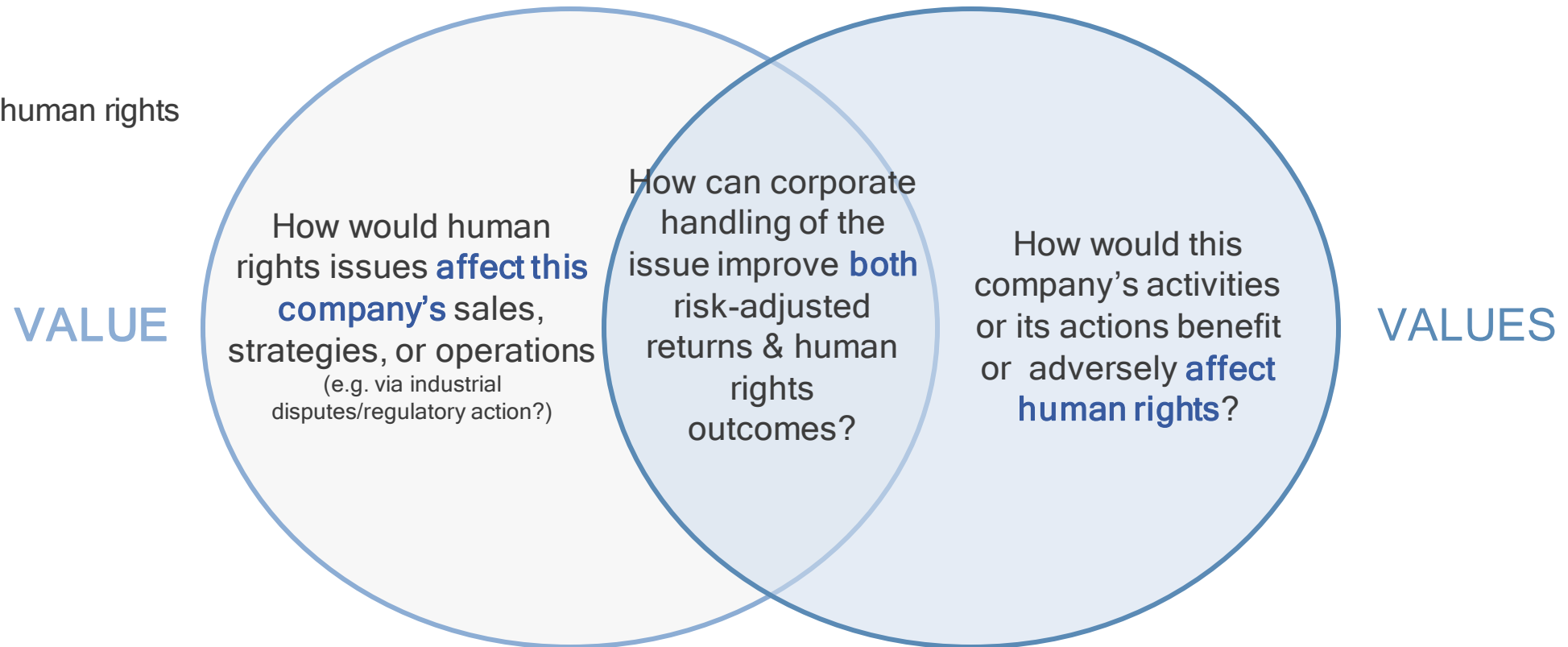
Investments that seek to achieve targeted environmental and social outcomes in addition to financial returns.

Example: Green bonds, solar farms,

Motivations behind responsible investing

	Value	Values
Focus:	Investment risk/returns	Responsibility
Rationale:	Financial	Ethical (values-based, reputational)

Example:
A company's human rights



Changing consumer expectations

Consumers are expecting RI, and advisers should consider their clients' interests

A 2020 RIAA consumer survey of a representative sample of Australians showed:

86% expect their superannuation or other investments to be invested responsibly and ethically

74% would consider switching their investments to another provider if their fund engaged in activities inconsistent with their values

67% will consider making ethical or responsible investments in the next 1 to 5 years

88% believe it's important that their financial adviser provides responsible or ethical options

The Code of Ethics issued by **FASEA**, effective 1 January 2020, requires advisers to:

“...actively consider the client’s broader, long term interests...”

Which strengthens the case for advisers to consider other interests and expectations such as responsible and sustainable investments.

What Investors Want vs What Managers Deliver

FIGURE 17: Negative screening: consumer vs investment manager exclusions

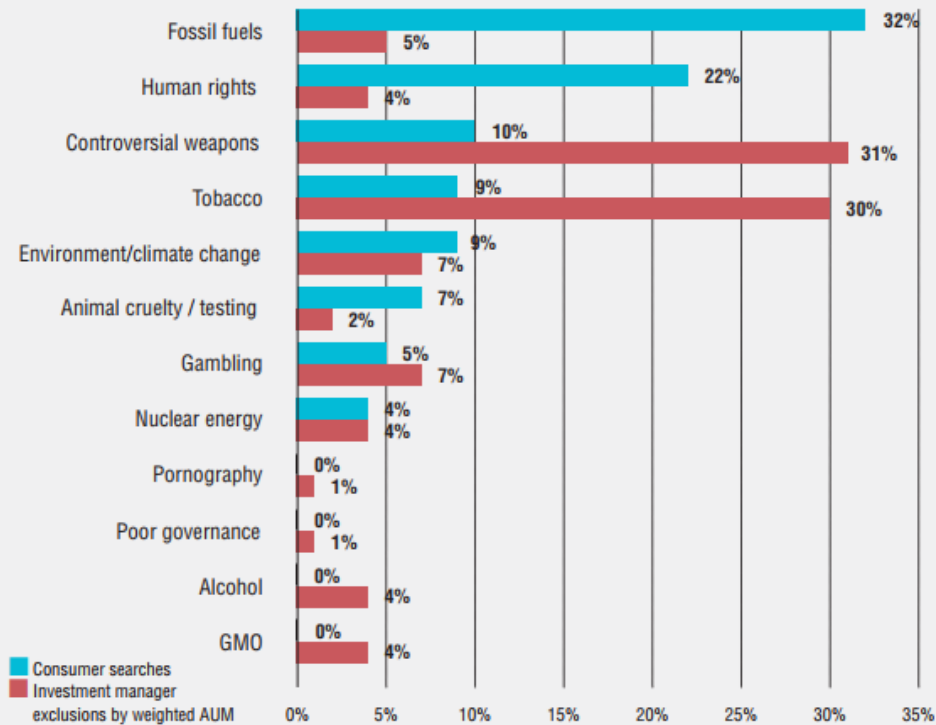
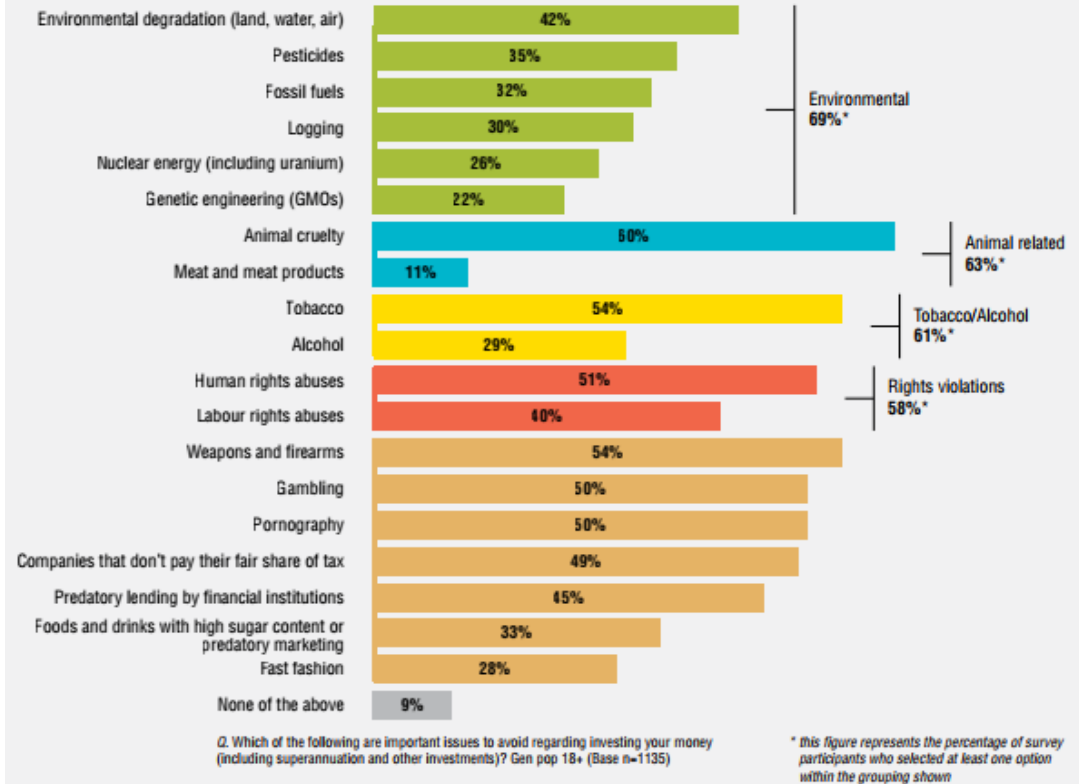


FIGURE 9: Issues consumers want to avoid when investing money

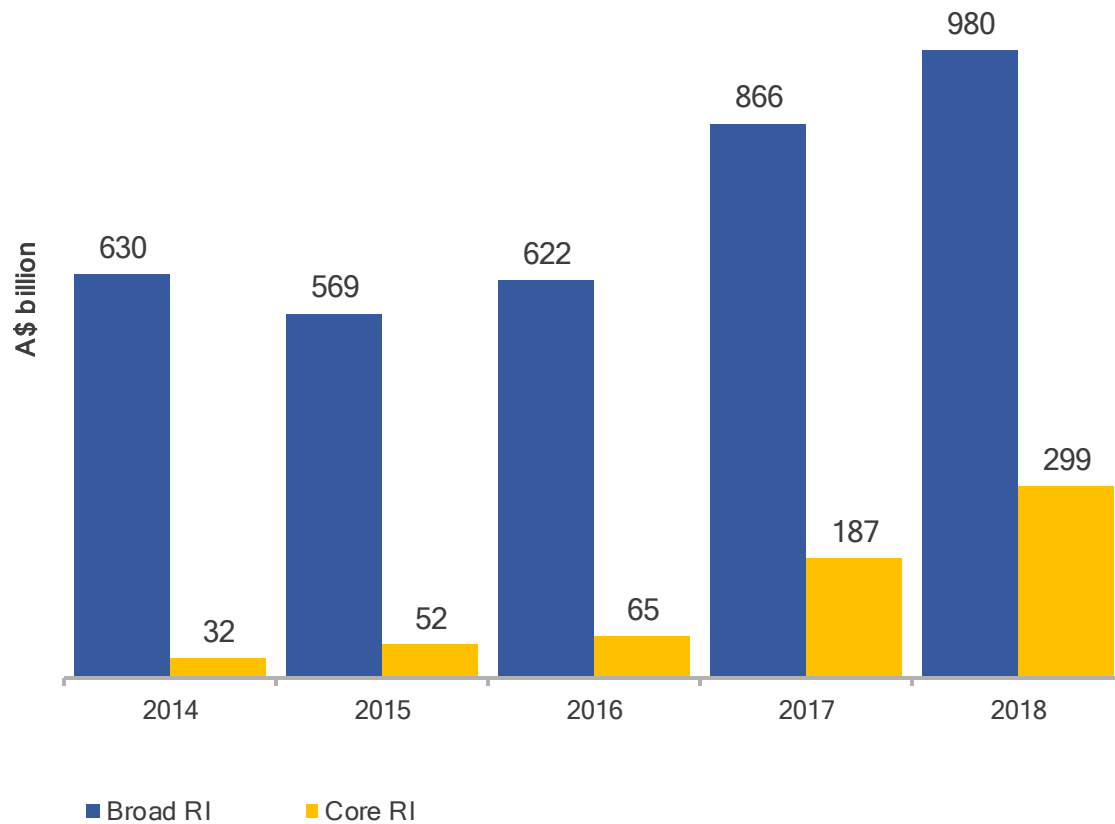


RIAA Benchmark Report 2019 - Figure 17,
RIAA From Value to Riches 2020 Figure 9

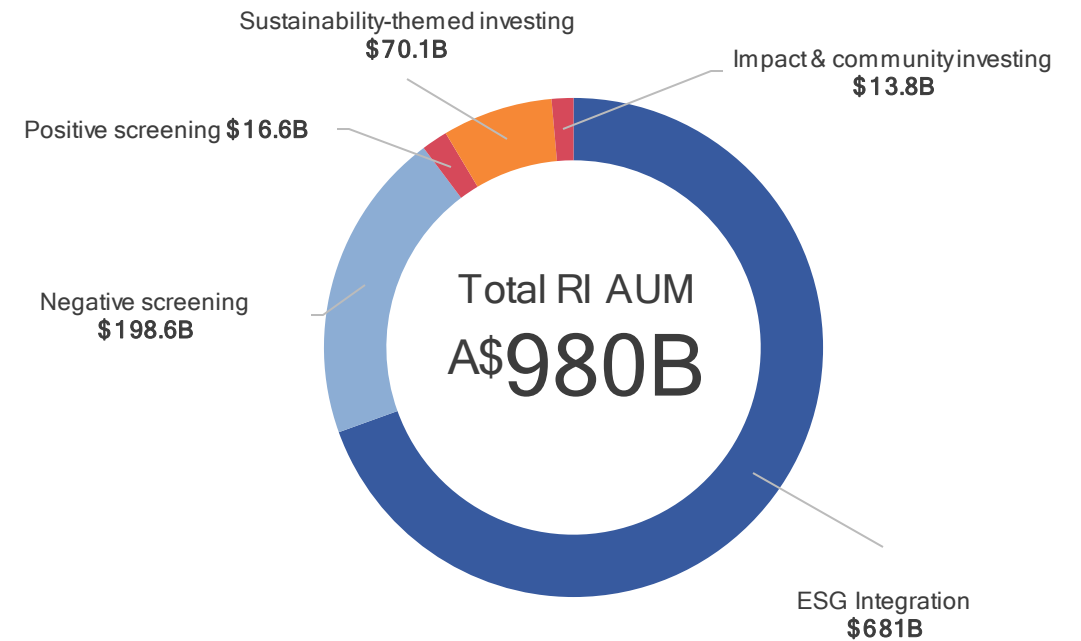
RI is no longer a niche market

Consumer demand is growing (and fund managers are responding)

RI strategies



Responsible Investments in Australia, A\$B



Framework

- 1. *Identify the objective***. What is the client looking to achieve? Feel good/ greater connection between the values of the client and the investments , opportunity for advocacy, avoid all harm , participate in conversation, etc
- 2. *Gather relevant information***. ...Investment managers/ research, need to help provide insightful , succinct information. How we will consider events in the future? It is not easy, there is a huge amount of information out there- collectively we need to make it easier.
- 3. *Look at the Options***. ... Can I actually implement what I want- Fund, SMA, direct holdings. It will not be perfect . What course of action can I take to achieve the objective ? How do I implement it? What strategy solution is available ?
- 4. *What if Questions***- Red flag events (Seen in financial services/ work place accidents , through to changes in strategy, acquisition of poor ethical companies) What would we do?
- 5. *Made a decision***- Take action. ...
- 6. *Review and engage***- as part of the ongoing advice.

Constructing the portfolio

Issues to overcome

Asset allocation

- Do I have to “lose” some diversification between asset classes?

Manager selection

- Potentially narrower universe of managers / products to pick from

Within asset classes

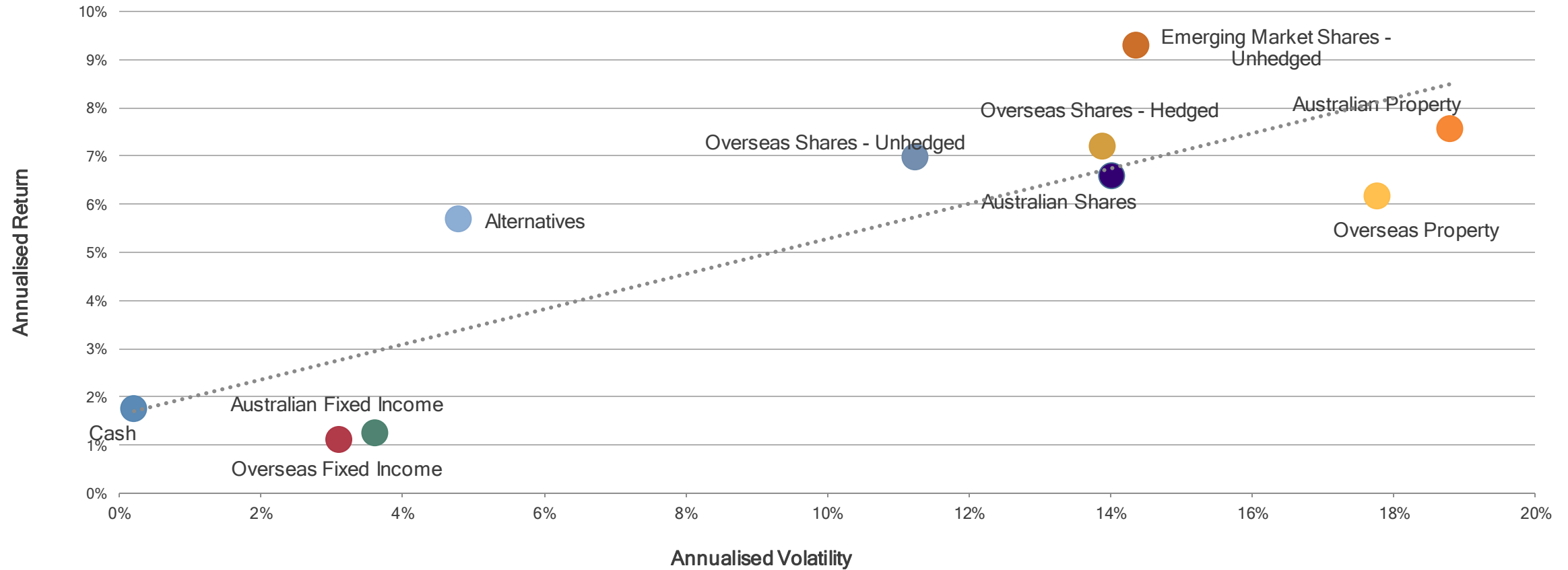
- Do negative screens result in lower performance or more risk?

Constructing the portfolio

Asset class	Sustainable Product availability	Issues
Australian equities	Plenty of choices	Holdings have greatest client visibility, small universe to start with - impact of screening
International equities	Less choices, but enough	Currency hedging, emerging markets harder
Property (REITs)	Fairly green asset class	
Infrastructure (listed)	Minimal in Aus	Sustainability of some asset types, e.g. airports
Liquid alternatives	Becoming available	Liquid alternatives have struggled of late
Fixed interest	Plenty of choices - incl exposures to green bonds, impact bonds	Comfort with some sovereigns (esp. emerging markets); bank exposure
Cash	Minimal	How does your client feel about the banks?

Asset class forecasts (10+ years)

Low interest rates make diversification challenging in a balanced portfolio



Source/: Pental Group

Implementation options expanding

- Active: managed funds, ESG SMAs
- Alternatives: starting to see products emerge
- Further growth of ESG indices facilitates growth in:
 - ETFs - bond and equity
 - ESG index derivatives - futures, and now even credit default swap indices

No need to sacrifice returns or increase risk

Indeed there is evidence of *better* financial outcomes

A vast body of academic

STUDY AUTHORS	TIME PERIOD	ESG ISSUE	ESG FACTOR	IMPACT (*)
Hamilton (1995)	1989	Volume of toxic releases	E	Positive (13)
Jacobs, Singhal, and Subramanian (2010)	2004-2006	Environmental performance	E	Mixed findings
Johnson, Moorman, and Sorescu (2009)	1990-1999	Governance quality/shareholder rights	G	No effect/no relation
Karpoff, Lott, and Wehrly (2005)	1980-2000	Environmental regulation violations	ESG	Positive (14)
Karpoff, Lee, and Martin (2008)	1978-2002	Financial misrepresentation	G	Positive (15)
Kasperleit and Lopatta (2013)	2001-2011	Corporate sustainability and GRI	ESG	Positive
Klassen and McLaughlin (1996)	1985-1991	Environmental management awards	E	Positive
Krüger (2014)	2001-2007	CSR news events	ESG	Positive (16)
Lee and Faff (2009)	1998-2002	Corporate sustainability quality	ESG	Negative
Smithy Fulmer, Gerhart, and Scott (2003)	1998	Employee wellbeing	S	Positive (17)
Statman and Glushkov (2009)	1992-2007	Composite CSR index	ES	Positive
Yermack (1996)	1984-1991	Reductions in board size	G	Positive

Does not have to involve any implementation “give up”

- Typical “institutional” screens reduce universes by only ~10%
- Growing implementation choices across shares, fixed income and now alternatives
- *Positive tilt to sustainability to support long term returns*

Source/ : Image extracted from “From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance” by Oxford University and Arabesque Partners from 2015,

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