NORTH AMERICA CATCHING UP TO EMEA ON SUSTAINABLE INVESTMENT

By Tony Campos

In the midst of the COVID-19 pandemic and increased focus on social justice, sustainable investment funds have attracted record inflows this year, pushing global AUM over $ 1 trillion, according to the Financial Times. This trend includes a sub-strategy of what we've classified as 'smart sustainabliity', or rather: the integration of ESG considerations into a smart beta index strategy.

To examine the uptick in sustainable investments and better understand the growing interest in smart sustainability, we surveyed 139 global asset owners earlier this year to gauge their evaluation and adoption of these strategies. The results are a striking reminder that sustainable investment has become an established consideration for institutional investors globally, with 72% implementing or evaluating ESG (rising 14% from last year). Yet interestingly, the survey reveals that while regional differences among usage persist, once drastically pronounced gaps have narrowed.

Europe has long been a leader in sustainable investing as the EU has steadily encouraged and even more recently mandated the integration of ESG data into fund reporting, whereas in North America investor demand rather than regulatory guidelines has predominantly driven the rise of sustainable investing, albeit at a slower pace.

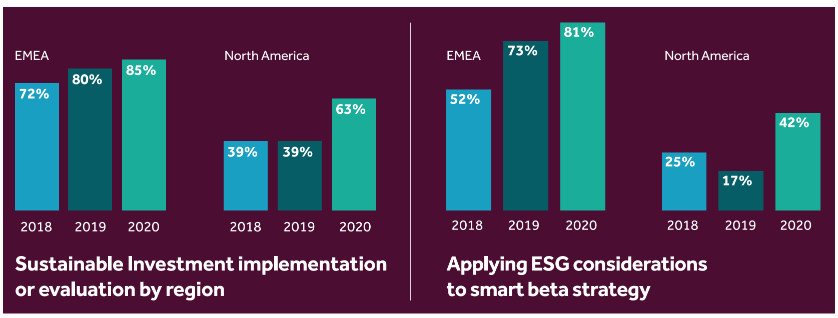
However, our 2020 survey finds North America is quickly catching up to EMEA when it comes to sustainable investment. In North America, 63% of asset owners surveyed said that they were either implementing or considering ESG, increasing from 39% in the last two years. That is still behind EMEA, where the figure is 85%, but regional differences are leveling off. This is especially true in the sub-strategy of smart sustainability. The survey highlights that while 81% of EMEA asset owners expect to apply ESG criteria to smart beta (up from 73%), North America has jumped to 42% anticipating the same, which is up significantly from only 17% in 2019.

These figures are a strong indication that interest in sustainable investing and smart sustainability has not only weathered the market uncertainty of 2020, but maintained a mainstream position despite disruptions like the global pandemic and heightened volatility.

We're also seeing a shift in how institutional investors choose to implement ESG within smart beta as technology advancements further drive innovation in ESG indexes and sustainable investment strategies continue to broaden. Findings show a growing emphasis on ESG integration over traditional screening in index-based portfolios. Notably this year, global asset owners are embracing more sophisticated approaches like re-weighting based on ESG/sustainability criteria (55%, up 19%), rather than the previously favored negative screening (48%, down 16%). This approach enables asset owners to tilt portfolios toward ESG characteristics by changing the weighting across various stocks, rather than having to exclude certain stocks.

In terms of sustainability issues drawing institutional investors' attention, climate risk has emerged at the top with 64% for global asset owners interested in smart sustainability. Environmental considera-tions trail close behind at 59%, while governance and social themes are also widely considered. However, it's important to note this survey was fielded at the beginning of the year, before the breakout of COVID-19, which we expect could have potentially swayed concerns. «

Figure 1: Regional differences between North America and EMEA relating to sustainable investing



Source: FTSE Russell's Smart Sustainability: 2020 global survey findings from asset owners

This article was written by Tony Campos, Director of ESG Americas, FTSE Russell.