

ESG Investing

FOR ASSET OWNERS WHO SEEK TO INTEGRATE ESG

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How to implement ESG

ESG leaders have demonstrated increased sophistication across their organizations

ASSET OWNERS

PENSION FUNDS <ul style="list-style-type: none"> ESG Mandates Manager Selection & Monitoring Policy benchmark Engagement 	CONSULTANTS <ul style="list-style-type: none"> RFP Fund selection OCIO solutions
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INSURANCE <ul style="list-style-type: none"> Manager Selection Policy benchmark Low carbon Tobacco 	ENDOWMENTS & FOUNDATIONS <ul style="list-style-type: none"> Fund Selection Fossil divestment Impact investing
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WEALTH MANAGEMENT

CIO OFFICE <ul style="list-style-type: none"> Model portfolios ESG themes Fund Profile Philanthropy 	FUND SELECTION <ul style="list-style-type: none"> Due Diligence Fund Selection / Peer Analysis Screening
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FINANCIAL ADVISORS <ul style="list-style-type: none"> Portfolio Analysis & Reporting Stock and Fund Research 	RETAIL <ul style="list-style-type: none"> Robo Stock and Fund Research
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ASSET MANAGEMENT

FUNDAMENTAL EQUITY <ul style="list-style-type: none"> ESG Integration Engagement Low carbon Compliance 	FUNDAMENTAL FIXED INCOME <ul style="list-style-type: none"> Corp. Credit EMD credit Green bonds 	QUANT <ul style="list-style-type: none"> ESG Integration ESG solutions ESG + Factors Low carbon
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ESG SPECIALIST <ul style="list-style-type: none"> ESG Themes Engagement 	STEWARDSHIP & GOVERNANCE <ul style="list-style-type: none"> Active Ownership Engagement ESG Themes
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RISK MANAGEMENT

RISK MANAGEMENT <ul style="list-style-type: none"> Risk monitoring Risk Reporting TCFD stress test 	COMPLIANCE <ul style="list-style-type: none"> Mandates Global Sanctions
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OTHER / PRODUCT

EMERGING <ul style="list-style-type: none"> Custodian Hedge Fund 	ACTIVE FUND <ul style="list-style-type: none"> Core EQ / FI ESG + Factor Thematic 	PASSIVE FUND & ETP <ul style="list-style-type: none"> Core EQ / FI ESG + Factor Thematic
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Asset Managers are moving beyond fundamental equity and **integrating ESG into fixed income and quantitative** strategies with growing sophistication

Largest consultants are incorporating ESG dimensions into manager selection in reaction to Asset Owner requests

Engagement is becoming an important tool for improving company performance and returns

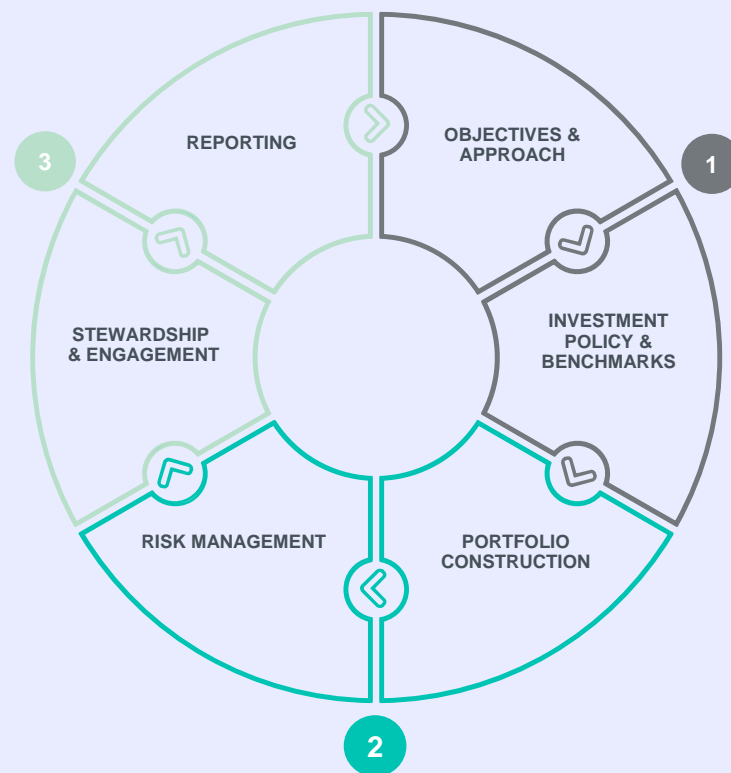
Risk teams are increasingly **systematically reporting** on ESG risk

Demand for active and passive **ESG Funds across asset classes** for total portfolio exposures

Integrating ESG across your entire investment process

MSCI can help you:

- 1 Define objectives & policy**
 - Define investment and ESG objectives
 - Set targets and strategies to enhance ESG profile
 - Develop investment policy
 - Select benchmarks
- 2 Integrate into investment process**
 - ESG in portfolio construction
 - Active and index-linked ESG products
 - Scalable risk management reporting
 - Stress testing
- 3 Engage stakeholders & report**
 - Engage companies and external stakeholders
 - Provide transparency through client reporting



Define: objectives & policy

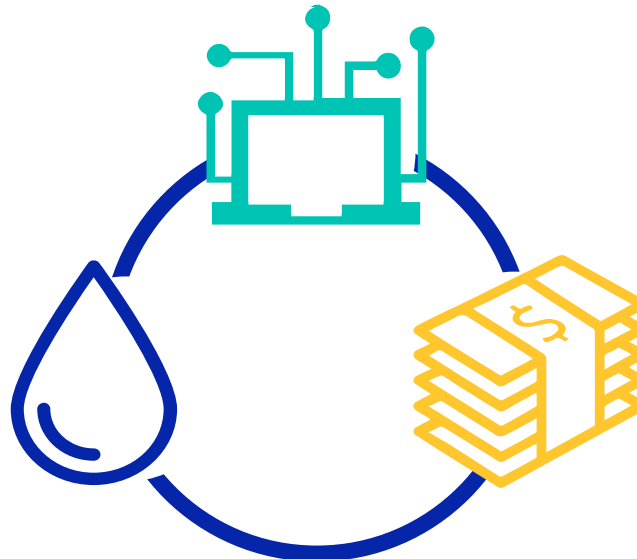
ESG integration can be used by asset owners as a mechanism to manage the long-term risk & return drivers of their portfolios and influence corporate behavior.

SYSTEM IMPROVEMENTS

- Incentive to protect stakeholders interest
- Stewardship of capital
- Overvalued assets

LONG-TERM RISKS

- Climate change
- Societal change
- Technological change



LONG-TERM OPPORTUNITIES

- Proactive capital allocation
- Long term economic growth

Define: assess your needs, define your objectives

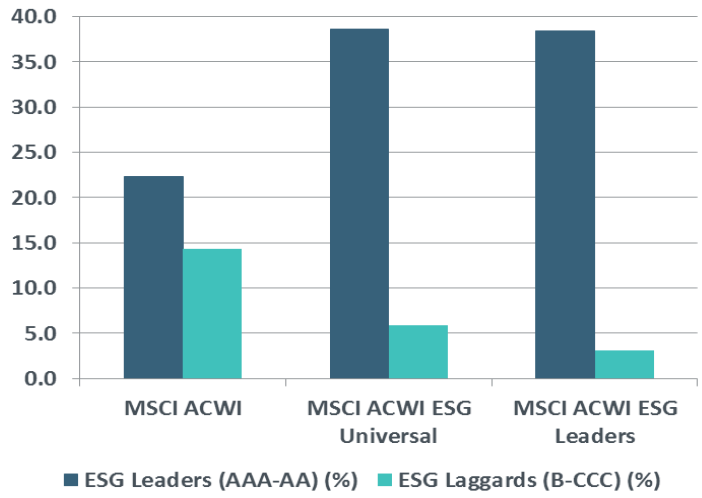
Articulating the objectives, policies and expected outcomes is a critical step in the process of ESG integration. MSCI's research, tools and analysis can assist in assessing your needs.

MSCI ESG Research Provide Guidance on Trends and Best Practices



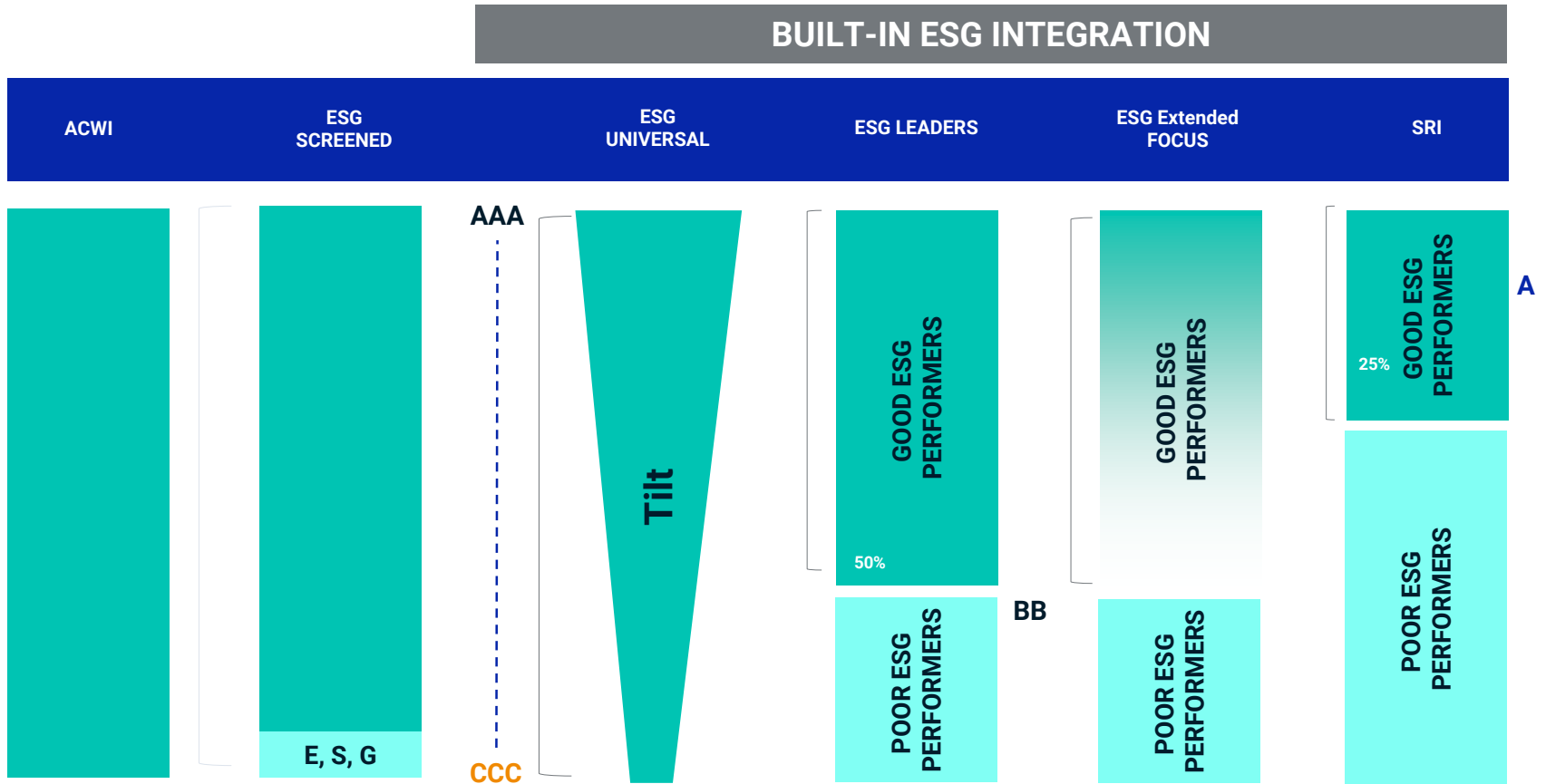
Portfolio & Index Metrics Reports Assess Potential Impact of ESG Approaches

Exposure to ESG leaders and laggards



Define: select a benchmark

Select a benchmark aligned with your ESG investment objectives, and to help you assess managers.



Integrate ESG into your investment strategy

1 2 3

There are numerous approaches for integrating ESG into portfolio construction—whether active or passive strategies—in equities or fixed income. Here are some common approaches.

1

Improve ESG Quality /
Reduce Risk

ESG



MSCI's ESG Ratings can be used for security selection or within systematic strategies to help improve ESG quality and reduce risk. *Foundations of ESG Investing* illustrate various investment approaches.¹

2

Reduce Carbon Footprint

CO₂



The MSCI Low Carbon Target Index targets an 80% reduction in carbon emissions while maintaining similar characteristics as the parent Index, including a 0.5% tracking error.²

3

Exclude Business
Activities

VALUES



Asset owners increasingly require screens on their funds. MSCI offers a full range of screens and thresholds to help managers meet client needs.

Integrate ESG indexes as building blocks

ESG Indexes can be used as building blocks for passive, factor and active mandates, across equity and fixed income.

- Available across equity and fixed income
- Available for all regions, countries and sectors
- Universe, opportunity set
- For strategic asset allocation purposes
- Basis for regional, sectorial or style allocations
- Financial product creation
- Performance benchmarks

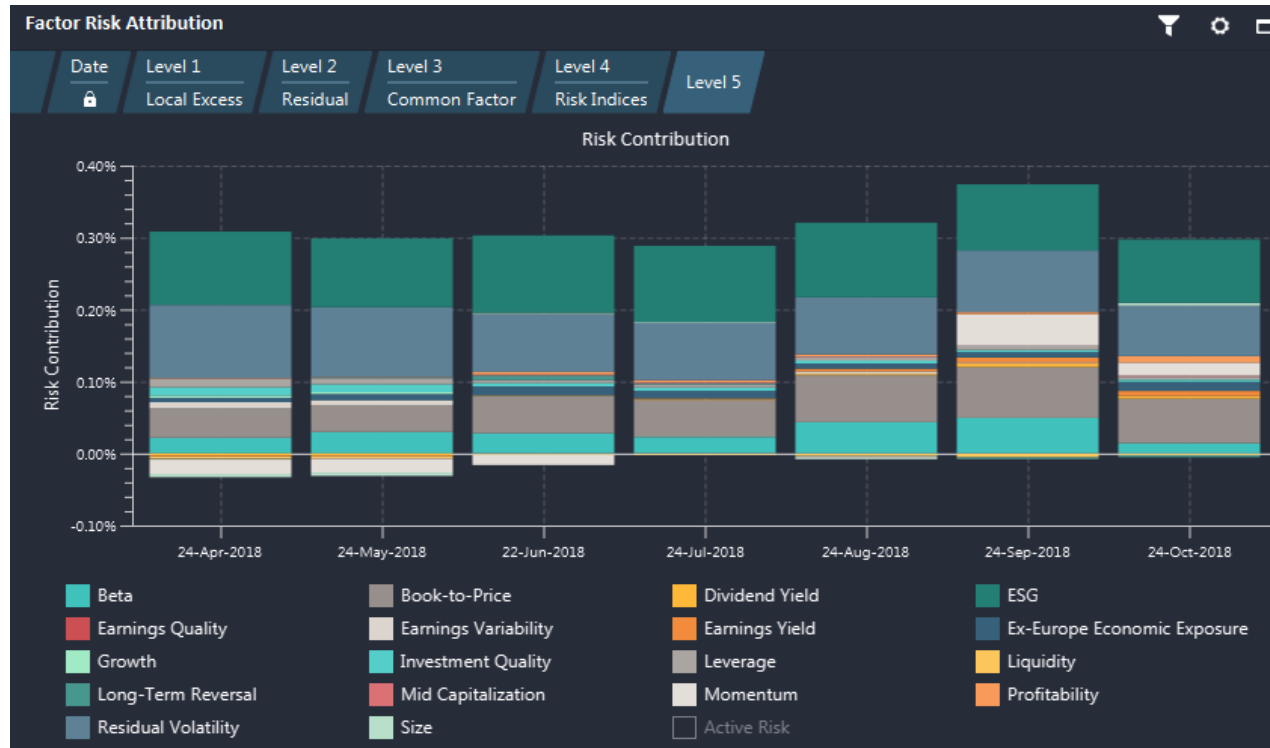
CLASSIC EQUITY ALLOCATION BEFORE ESG INTEGRATION

POLICY BENCHMARK: ACWI IMI				
PASSIVE MANDATES	FACTOR MANDATES		ACTIVE MANDATES	
ACWI IMI	VAL	VOL	AM1	AM2
	SZE	QTY	AM3	AM4
	MO	YLD	AM7	AM8
			AM9	AM10

POLICY BENCHMARK: ACWI IMI				
PASSIVE MANDATES	FACTOR MANDATES		ACTIVE MANDATES	
ACWI IMI ESG UNIVERSAL	VAL + ESG	VOL + ESG	AM1 + ESG	AM2 + ESG
	SZE + ESG	QTY + ESG	AM3 + ESG	AM4 + ESG
	MO + ESG	YLD + ESG	AM7 + ESG	AM8 + ESG
			AM9 + ESG	AM10 + ESG

Integrate ESG into risk management

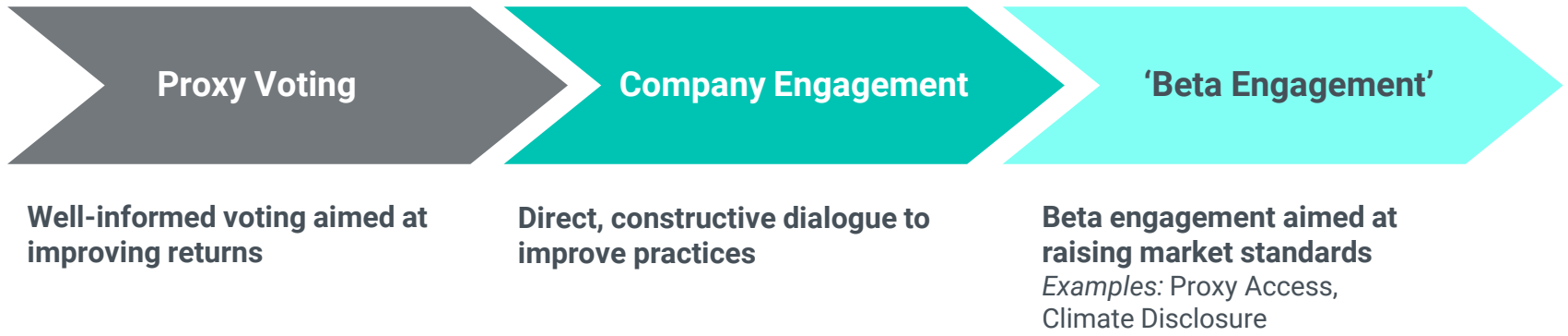
Asset owners increasingly incorporate ESG into their risk reporting, and conversations with portfolio managers. Incorporating ESG into systematic risk reporting can help identify unintended risk.



MSCI Analytics enable the attribution of portfolio risks to the portfolio's ESG exposure, as part of the Risk/Style Indexes

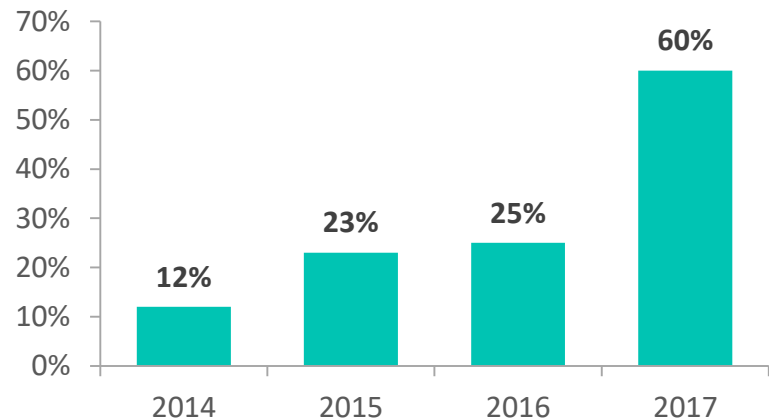
Engage with stakeholders and communicate 1 2 3

Many asset owners expect managers to be active stewards of capital and to exert oversight and influence on companies they own. Leaders in field use engagement to improve company performance.



Corporate Inquiries/Feedback from Japanese Companies

As part of Japan's Government Pension Fund (GPIF) allocation to MSCI ESG Leaders Index mandates, MSCI initiated engagements with Japanese corporates in 2017 to raise awareness of ESG best practices. As a result, we have seen a dramatic increase in interest, measured by an increase in response rates from Japanese companies.



Engage: provide ESG transparency to stakeholders through systematic reporting

1 2 3

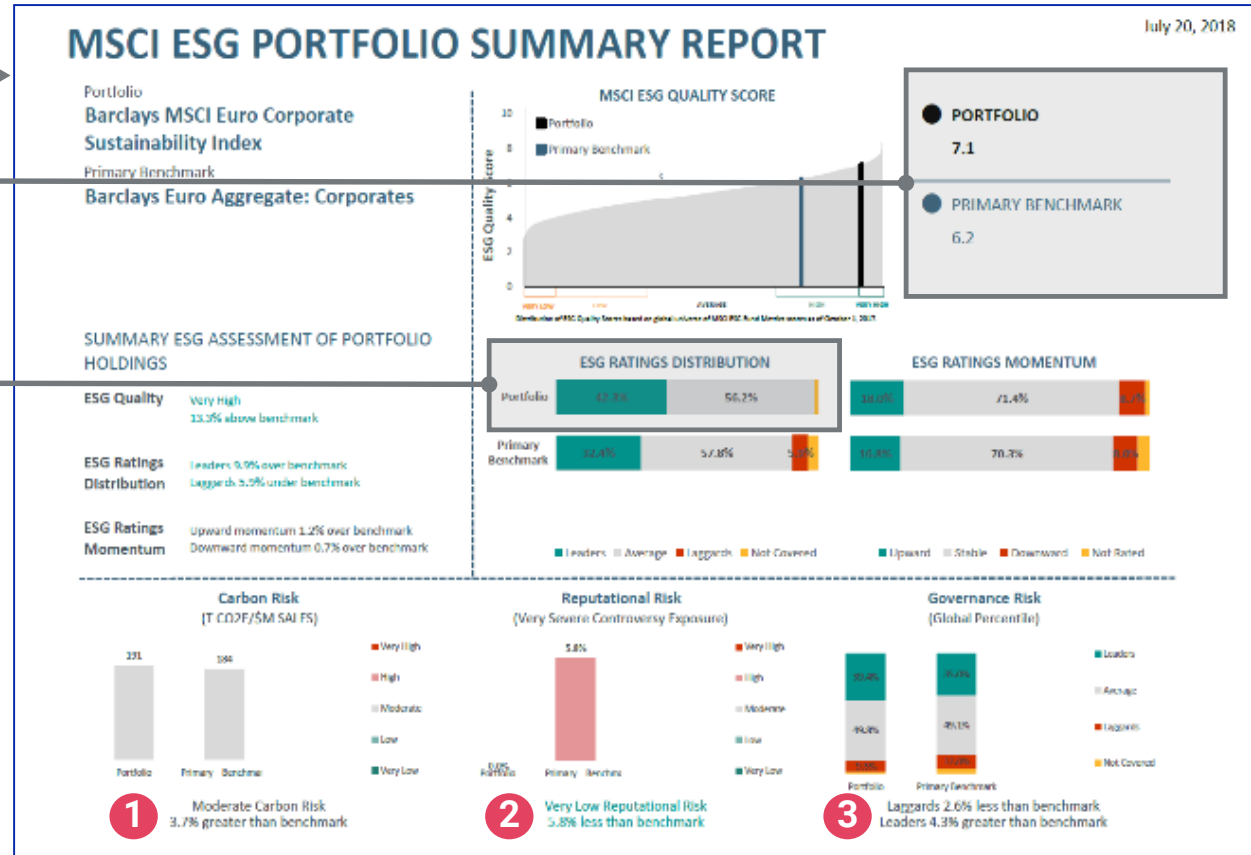
Investors are demanding transparency on ESG portfolio characteristics to understand how their capital is being deployed, and what the environment and societal impacts are. In particular we see asset owners reporting on climate risk exposure, and increasingly alignment with the United Nations Sustainable Development Goals.

Sample report used by large fund manager for quarterly risk reporting

Portfolio has a **higher ESG Quality score** than the benchmark

High ESG Quality score coming from **higher exposure to ESG leaders** and lower exposure to laggards

Portfolio has **moderate Carbon Risk (1)** and **Very low Reputational Risk (2)**, as well as **4.3% more exposure to Governance Leaders (3)** than the benchmark



Available in MSCI RiskManager, MSCI BarraOne and MSCI Barra Portfolio Manager

Powering better investment decisions

MSCI can help you integrate ESG into your investment process and communicate with your stakeholders using the common language of ESG Ratings:

1 Leading ESG Ratings & Research

Broad coverage with more than 13,000 entities, >90% of equity and FI MV



2 Innovative equity & fixed income indexes for various ESG approaches

More than 900 indexes covering integration, values and impact



MSCI Emerging Markets ESG Leaders Index

3 Market-leading risk analytics platform & ESG reporting

Sophisticated ESG Analytics and scalable reporting across 700,000 multi-asset class securities



4 ESG expertise & network

350+ ESG experts and over 600 individuals working with investors around the world



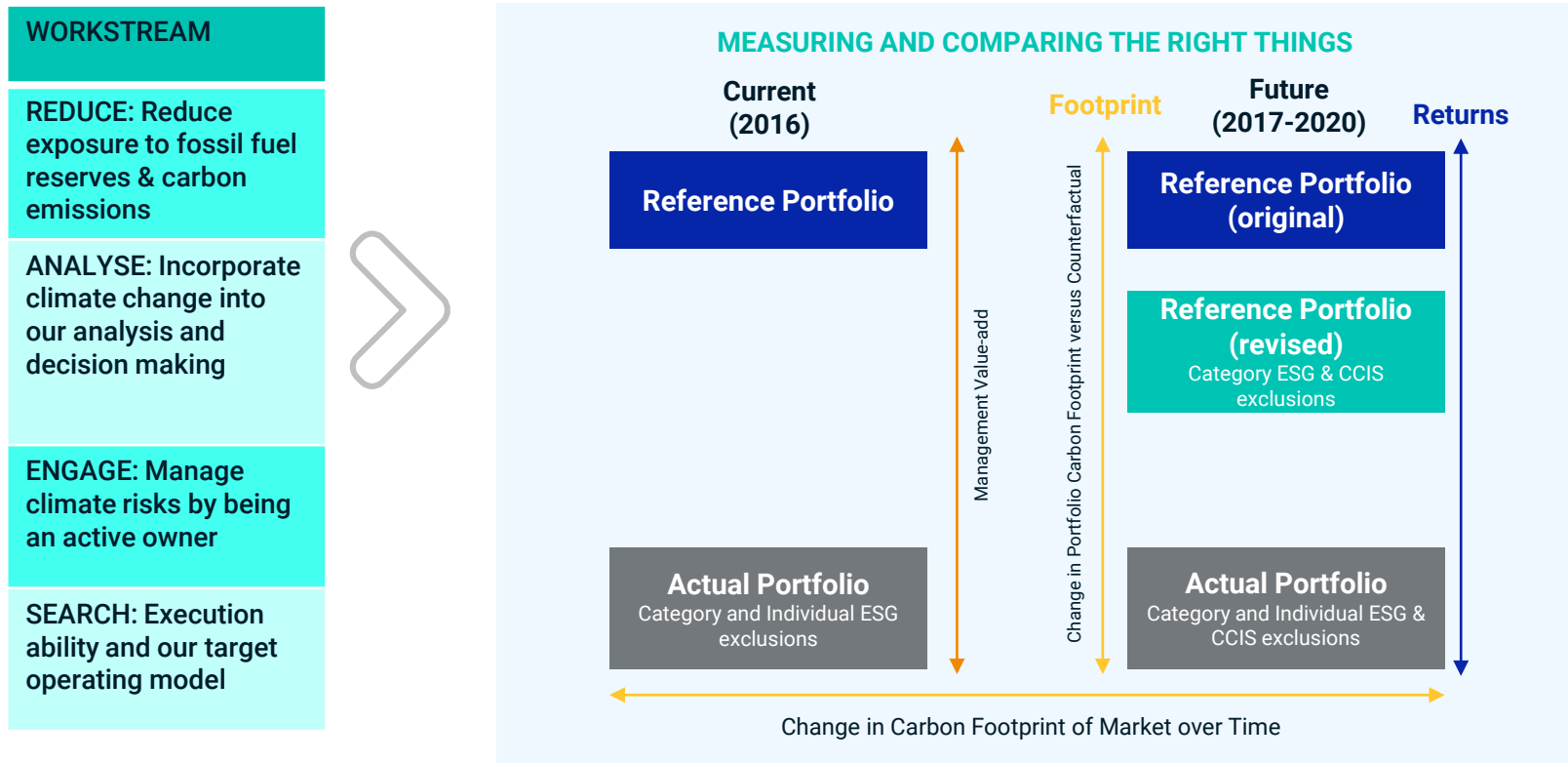
Use cases

- **ESG Integration across Equity and Credit Switzerland**
- **Low Carbon New Zealand**
- **Passive Allocation to ESG & Engagement Japan**
- **Integrated Factor and ESG Netherlands**

Asset owners have implemented low carbon

Example: NZ Super

NZ Super developed a 4 step climate change investment strategy, switching their equity reference portfolio and \$10bn passive equity portfolio to a custom Low Carbon Index (exclusions)



Aligning policy benchmark with exclusion policy

Examples: Ontario Teachers, UN Pension Fund

1 ONTARIO TEACHERS

MSCI ACWI	MSCI ACWI ex Canada ex Tobacco
Tobacco	⊗

“Ontario Teachers' Pension Plan adopted MSCI ACWI ex Canada ex Tobacco as policy benchmark for its global equity portfolio reflecting its decision to divest from Tobacco companies ”

2 UN PENSION FUND

MSCI ACWI	MSCI ACWI ex Tobacco ex Controversial Weapons
Tobacco	⊗
Controversial Weapons	⊗

“The United Nations Joint Staff Pension Fund (UNJSPF) adopted a custom MSCI ACWI ex Tobacco ex Controversial Weapons index. The UNJSPF has historically not invested in Tobacco and Controversial Weapons companies. The Index will therefore better reflect the available investment universe for UNJSPF’s active and passive global equity investments. It will provide a more accurate measure of performance from, and risk in, UNJSPF’s global equities portfolio”

Asset owners demand ESG integration across equity, fixed income, and beyond

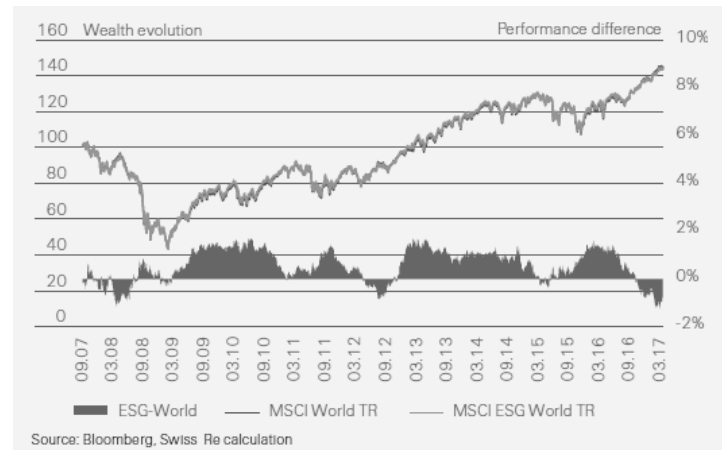
Example: Swiss Re

6th July, 2017 – Swiss Re switched all global equity and credit portfolio benchmarks to MSCI ESG Leaders and Bloomberg Barclays MSCI ESG Corporate Sustainability

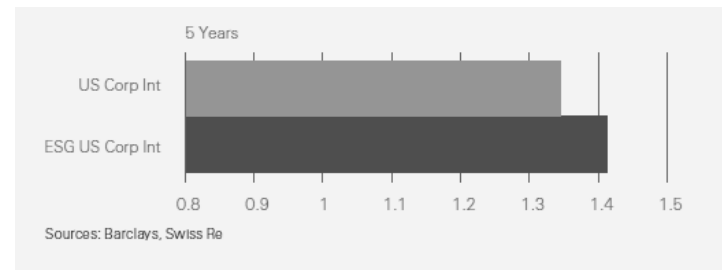
“Enhancing our investment portfolio by adopting broad-based ESG benchmarks has been the most meaningful and strategic step in our journey to integrate ESG considerations into the investment process.”

Guido Fürer, Group Chief Investment Officer at Swiss Re.

EQUITY



FIXED INCOME

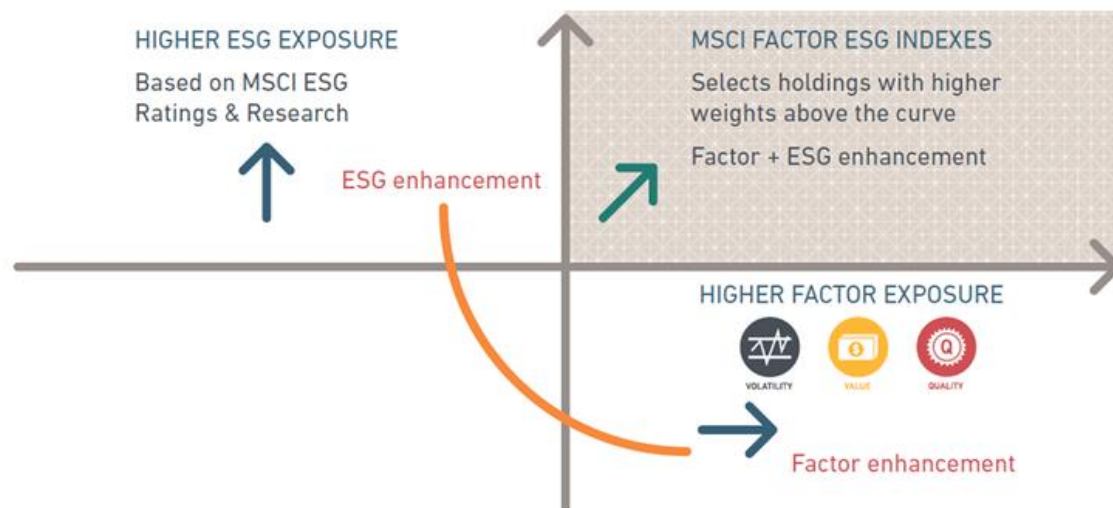


Factor investors are considering ESG

Example: Pension fund in Netherlands

The client wished to overlay their ESG policy onto their factor strategy, selected MSCI for its ability to combine a multiple factor strategy with ESG objectives in a seamless way, and for the quality of its ESG data and research

- \$4bn passive allocation
- Custom MSCI Multiple Factor ESG Target Index
- Value, Quality, Low Volatility
- **Target 20% improvement in ESG Score**



ESG index and engagement

Example: GPIF, Japan

GPIF have allocate to ESG Indexes in an effort to improve the overall market:

“GPIF believes companies want to be part of that [ESG] index, and so will improve their ESG ratings, and thus improve the market overall. I call it the incentive index.”

Professor Kato, GPIF Board Member

GPIF, as a universal owner (large-scale investor holding well-diversified portfolio), is responsible for yielding benefits for its pension beneficiaries by optimizing the investment value chain

GPIF – Universal Owner, Long Term Investor

Investment and Engagement

External Asset Manager

ESG Integration using an ESG Index

Company

Promoting ESG information disclosure

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