

ESG Equity Barometer H2 2021

What do the ESG fund flows look like in H2 2021?

As responsible investment continues to rise, both in the media and on the financial markets, Euronext Corporate Services has decided to shed some light on this trend.

With this ESG Equity Barometer, we want to make responsible investment more concrete for European issuers. Responsible investment is becoming mainstream and it is getting increasingly important for listed companies to know their shareholders and investors in general who apply an investment methodology based on ESG criteria.

With the support of Morningstar, we have analysed which types of funds are performing well in the second half of 2021, which non-financial indicators are most scrutinised by investors, and which sectors are attracting ESG funds.

The non-financial risk assessment specialist Sustainalytics also produced an analysis of the industries that attracted the most ESG fund flows in the last six months. Finally, Euronext Corporate Services met with 2 thematic funds for a discovery interview.

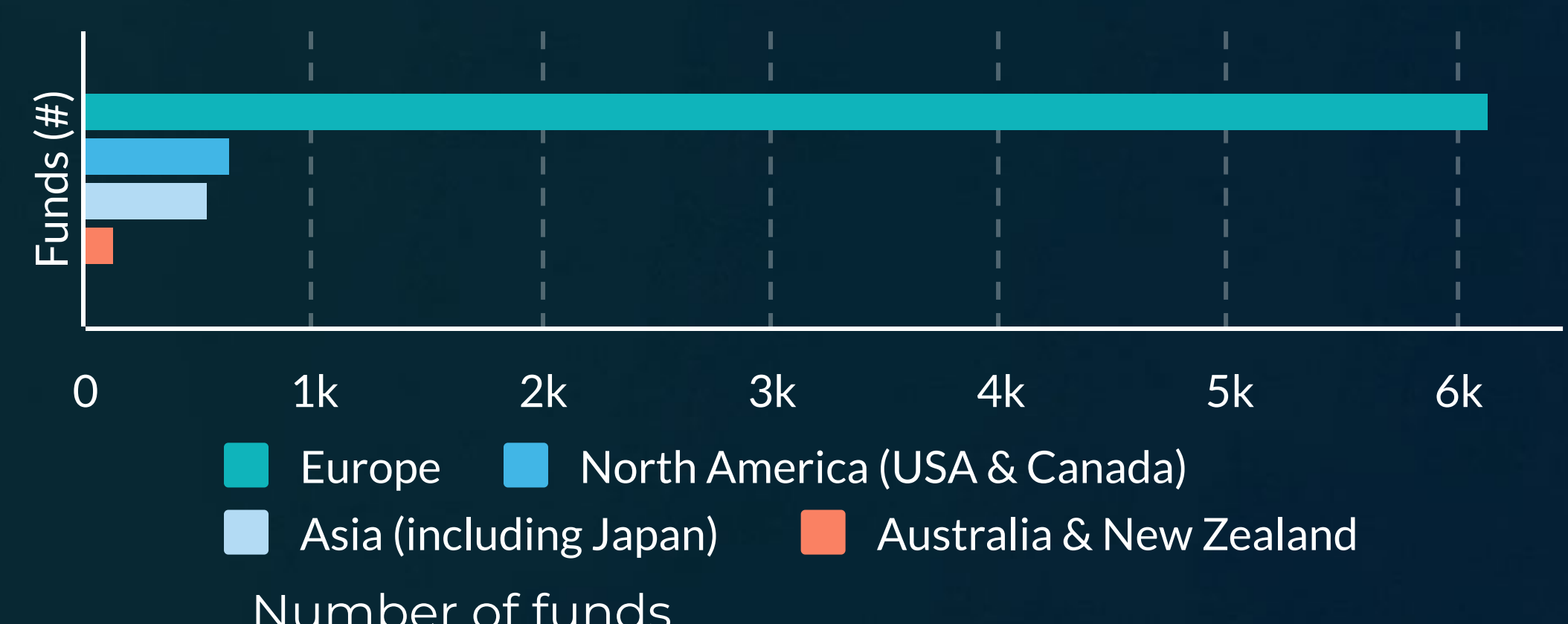
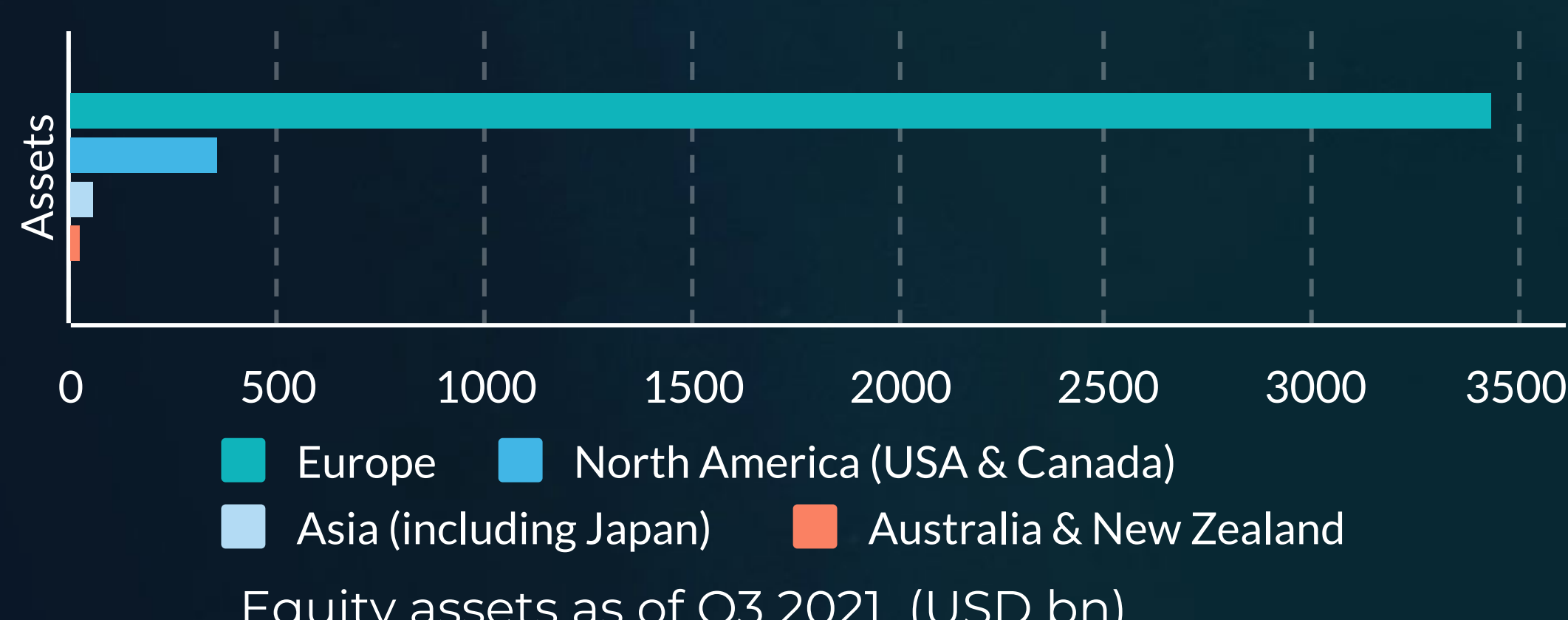
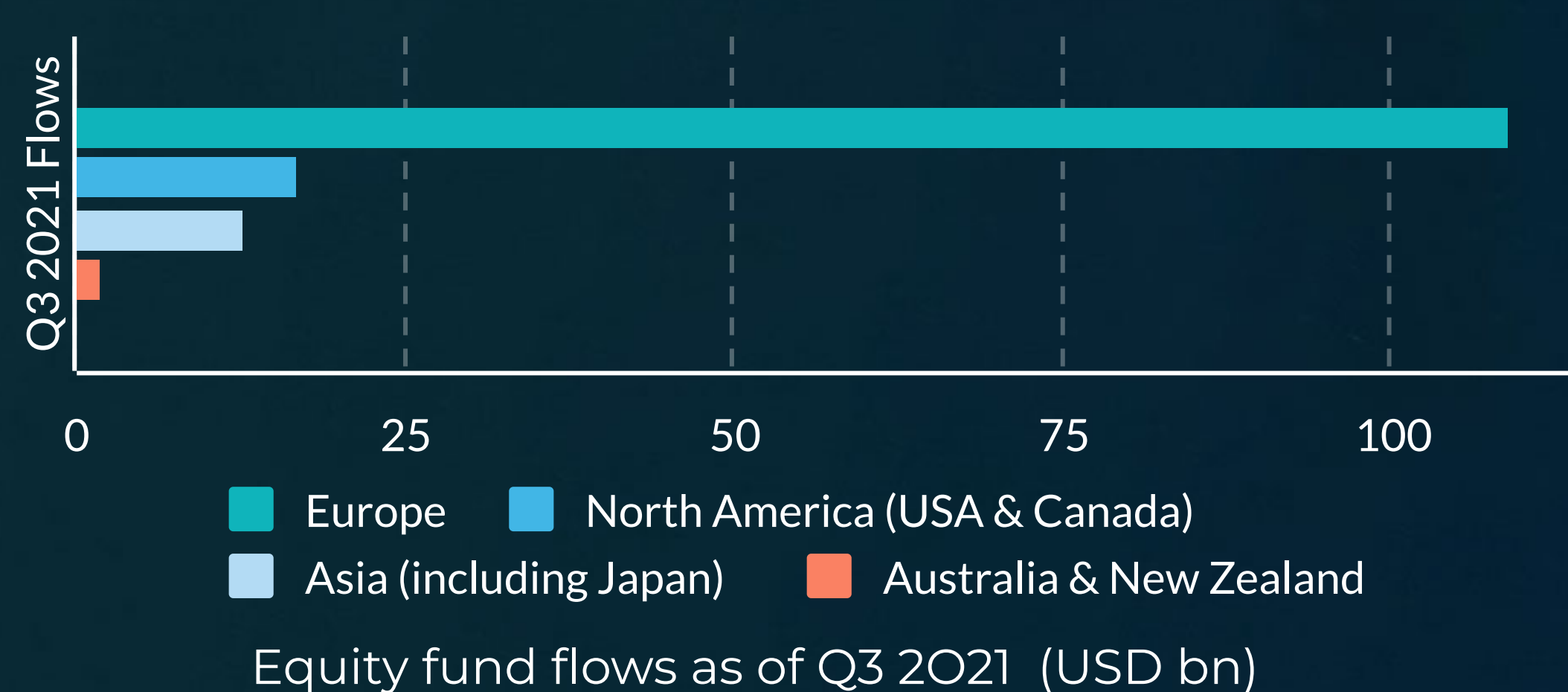
ESG Fund Flows Trend: Impact of the Sustainable Finance Disclosure Regulation

Description of Data Scope and Main Trends

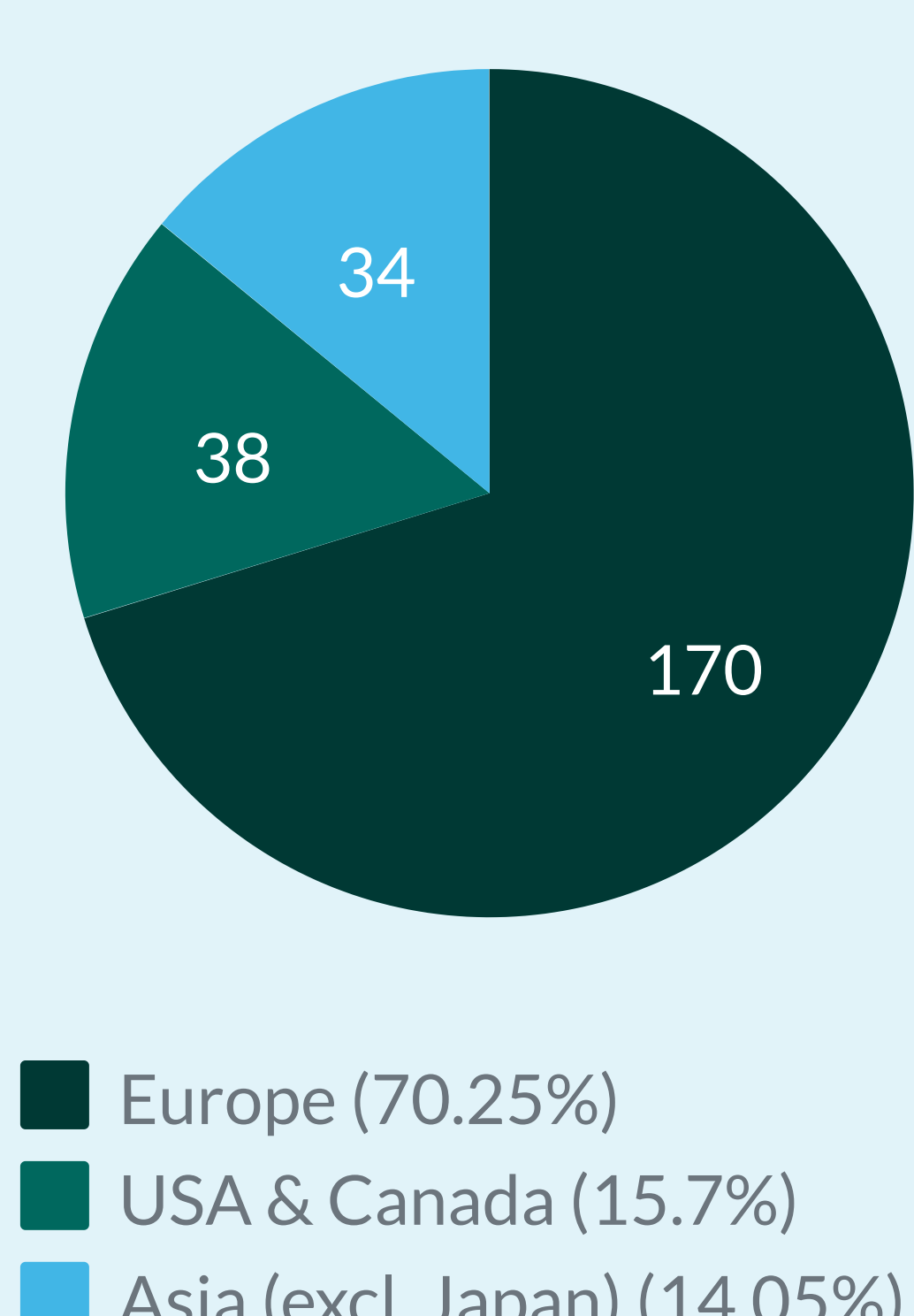
All data provided from Morningstar Global Sustainable Fund Flows Q3 2021.

Europe accounted for 77% of Q3 2021 world net inflows

The introduction of the **EU Sustainable Finance Disclosure Regulation** in March increased Europe's dominance in the sustainable fund space. In **Q3 2021, Europe accounted for 77% of the quarter's net inflows**, while **North America accounted for 12%**. As of the end of September 2021, the total assets under management flagged as ESG Equity amounted to 3,905 bn USD worldwide.



260 new ESG funds on average launched every quarter since the end of 2018



- Product innovation globally remained strong, with 270 new sustainable fund launches in the third quarter of 2021
- The introduction of the EU Sustainable Finance Disclosure Regulation in March has also led to an increase in the number of products included in Morningstar's universe of sustainable funds
- Since Q1 2021, the average of new ESG funds launched is around 260 per quarter

Data scope

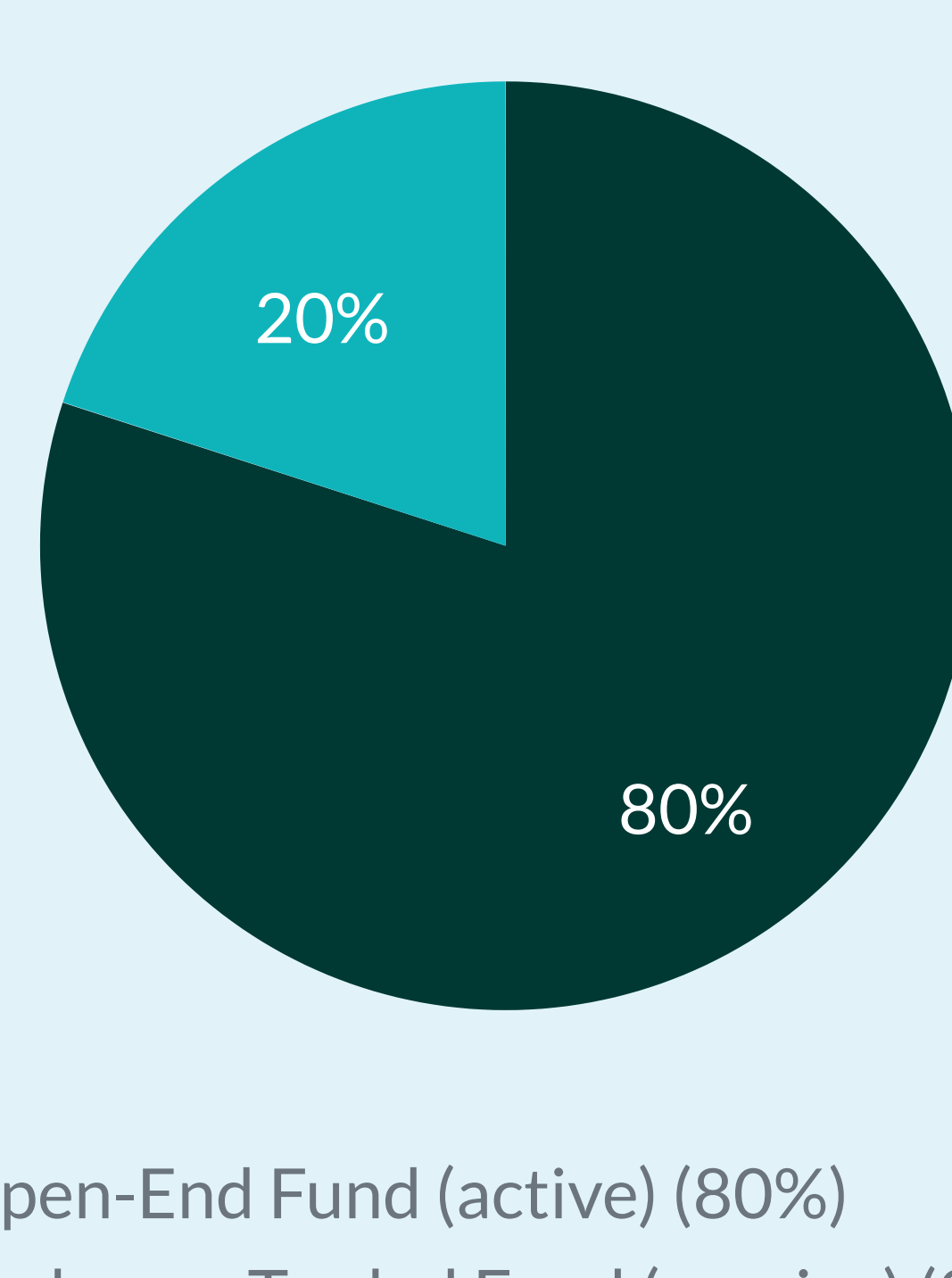
As previously identified by Morningstar, there are around 6,000 funds that meet ESG criteria in Europe. On this basis, we focused our analysis on funds that have an optimal rating by Morningstar (4 or 5 Globes = "High" or "Above Average") and that concentrates their investments in EU. In the end, we analysed a panel of around 500 funds (source: Morningstar Direct).

80% of ESG funds are actively managed

Out of this selection of 500 funds, 80% were labelled as Open-End Funds (i.e. actively managed investment funds) and 20% as Exchange-Traded Funds (i.e. passively managed investment funds).

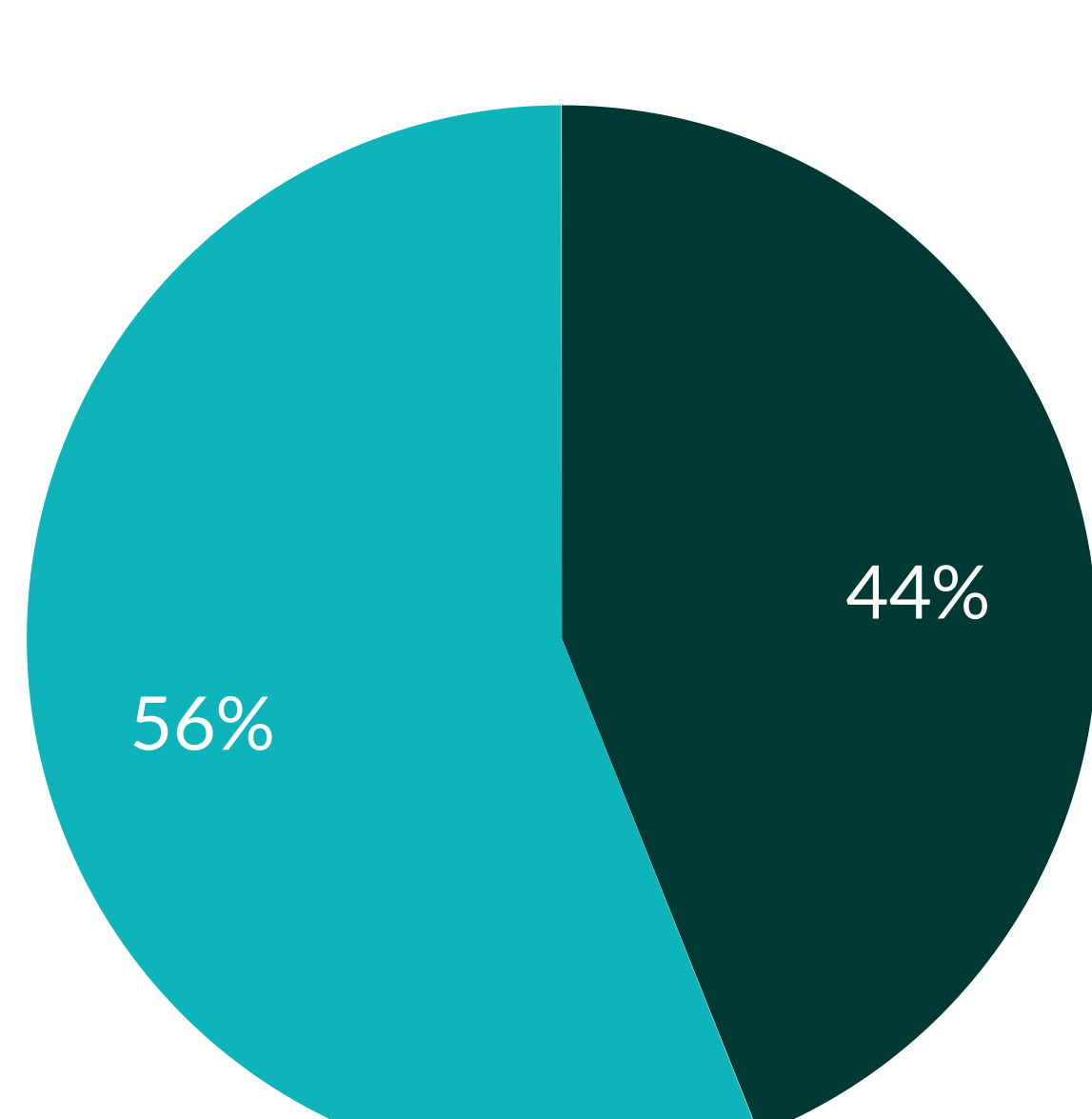
This data correlates with Morningstar's Quarterly Research Report (Global Sustainable Fund Flows) which states that on average 85% of the assets under management are designated as ESG and are actively managed.

ESG investment type



56% of funds focus on a sustainable thematic investment

How do ESG responsible investors tackle sustainability issues?



44% were labelled as having incorporated an ESG strategy (using any sort of environmental, social, and/or governance factors in their investment process). These strategies often use positive screens to make their investment choices, tacitly removing companies that do not meet standards in ESG areas. ESG incorporation typically includes best-in-class strategies selecting stocks based on stronger ESG performance relative to peers.

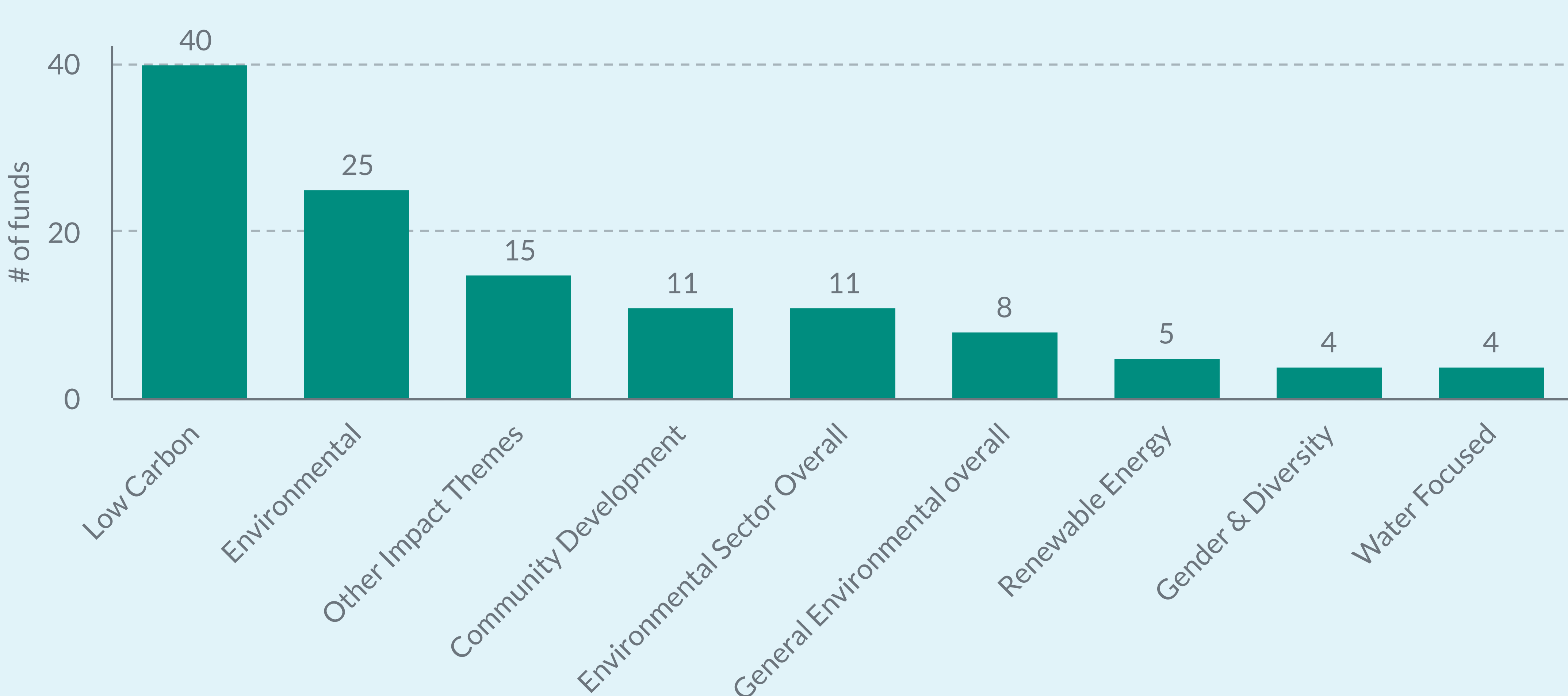
In contrast, we see thematic ESG investment ("no overall sustainable investment approach") becoming the norm, enabling asset managers to cover a range of sustainability issues while meeting commercial demand.

Main thematic scrutinised by ESG funds

It is not surprising that indicators related to climate and environment are the most frequently asked for ("Low carbon/Fossil-fuel free" and "Environmental"). However we observe that the Social dimension ("Community Development") and the search of a certain positive impact ("Other Impact Themes") are well ranked. One might have thought that the companies of Utilities, Clean Tech or Renewable Energy Producers ("Environmental sector overall", "Renewable Energy" and "Water Focused") be subject to the same level of exposure by ESG funds as climate and environmental topics due to the increased institutional investors' interest in this field. The uptake in the "Gender and Diversity" label demonstrates an increased interest from funds on Social and Governance issues for ESG investment.

Thematic definitions

- **Low Carbon/Fossil-fuel free:** investing in companies with small carbon footprint or low carbon risk
- **Environmental:** investing in companies with a positive environmental record, or specifically involved in industries that positively impact the environment
- **Other Impact Themes:** investing in companies with general impact themes that do not fall within the other impact categories
- **Community Development:** investing in companies with a positive record in community development and engagement
- **Water Focused:** intending to invest in companies with clean water practices
- **Environmental Sector Overall:** non-diversified funds that invest in environmentally oriented industries such as renewable energy or water
- **General Environmental Overall:** investing in other environmental industries that are not renewable energy or water
- **Renewable Energy:** intending to invest in companies involved in the renewable energy sector
- **Gender and Diversity:** investing in companies with a record of measurement and improvement in gender and diversity or related initiatives



Top 10 Sustainable Investment Labels Used by Active Thematic Funds

ESG Fund Investment by Industry

(Powered by Sustainalytics)



About Sustainalytics

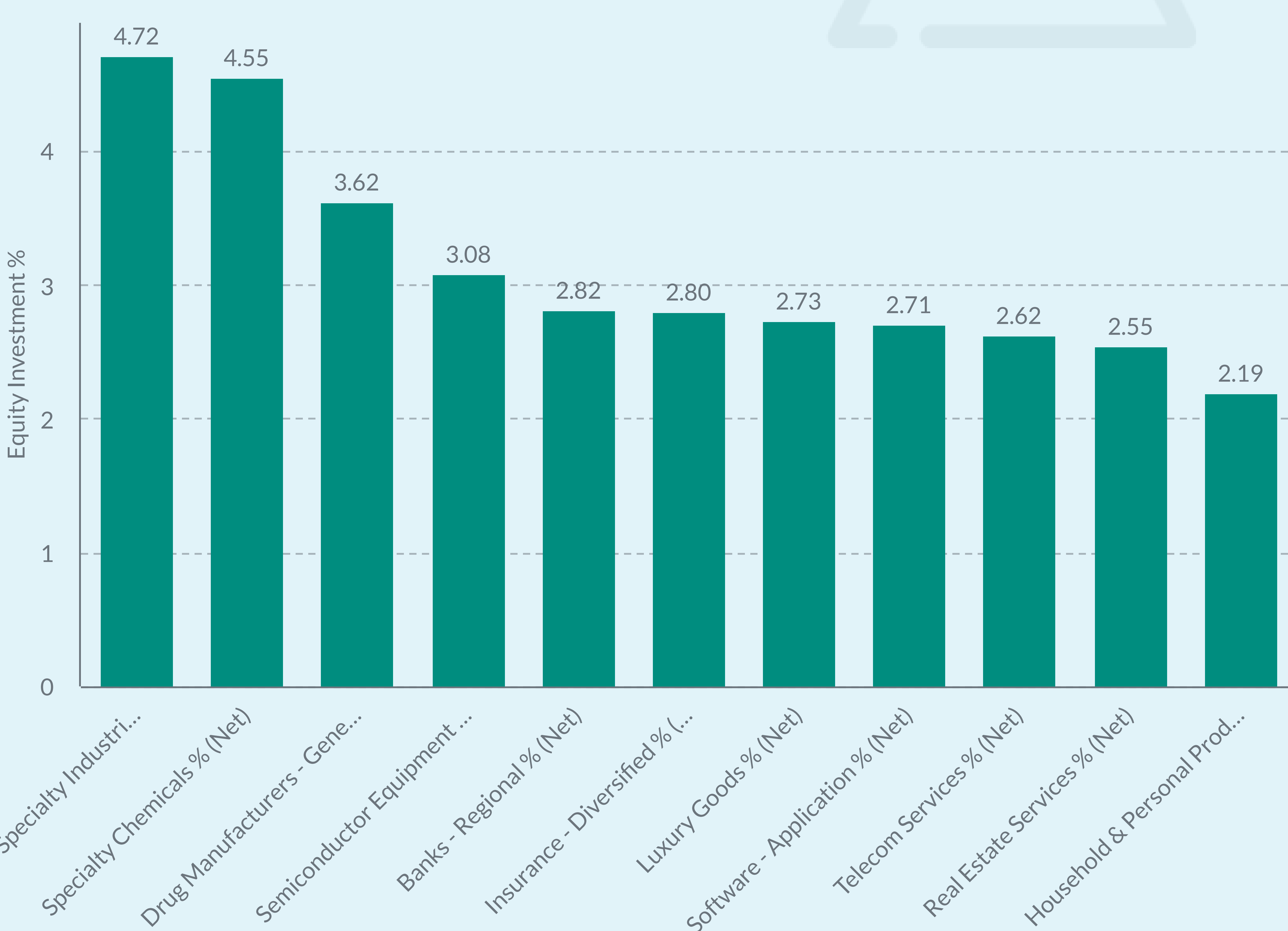
Sustainalytics, a Morningstar Company, provides high-quality, analytical environmental, social and governance (ESG) research, ratings and data to institutional investors and companies.

For more than 25 years, the firm has focused on delivering innovative solutions that have enabled the world's leading institutional investors to identify, understand, and manage ESG-driven risks and opportunities.

With Sustainalytics now a part of Morningstar, the firm is accelerating its efforts to deliver meaningful ESG insights to investors of all types across different asset classes at the company and fund level.

Sustainalytics' Corporate Solutions unit works with hundreds of companies and their financial intermediaries to help them consider sustainability in policies, practices and capital projects.

Top 10 industries of equity investment by ESG funds



Focus on the top 3 industries

The top 3 industries for equity investments by ESG funds are 1) **Specialty Industrial Machinery**, 2) **Specialty Chemicals** and 3) **Drug Manufacturers**.

Below, Sustainalytics assesses these industries based on the ESG Risk Rating score and aims to explain why they are overweighted.

ESG Risk Rating scorecard:

>40

is considered as severe ESG risk for the company

30-40

is considered high ESG risk for the company

20-30

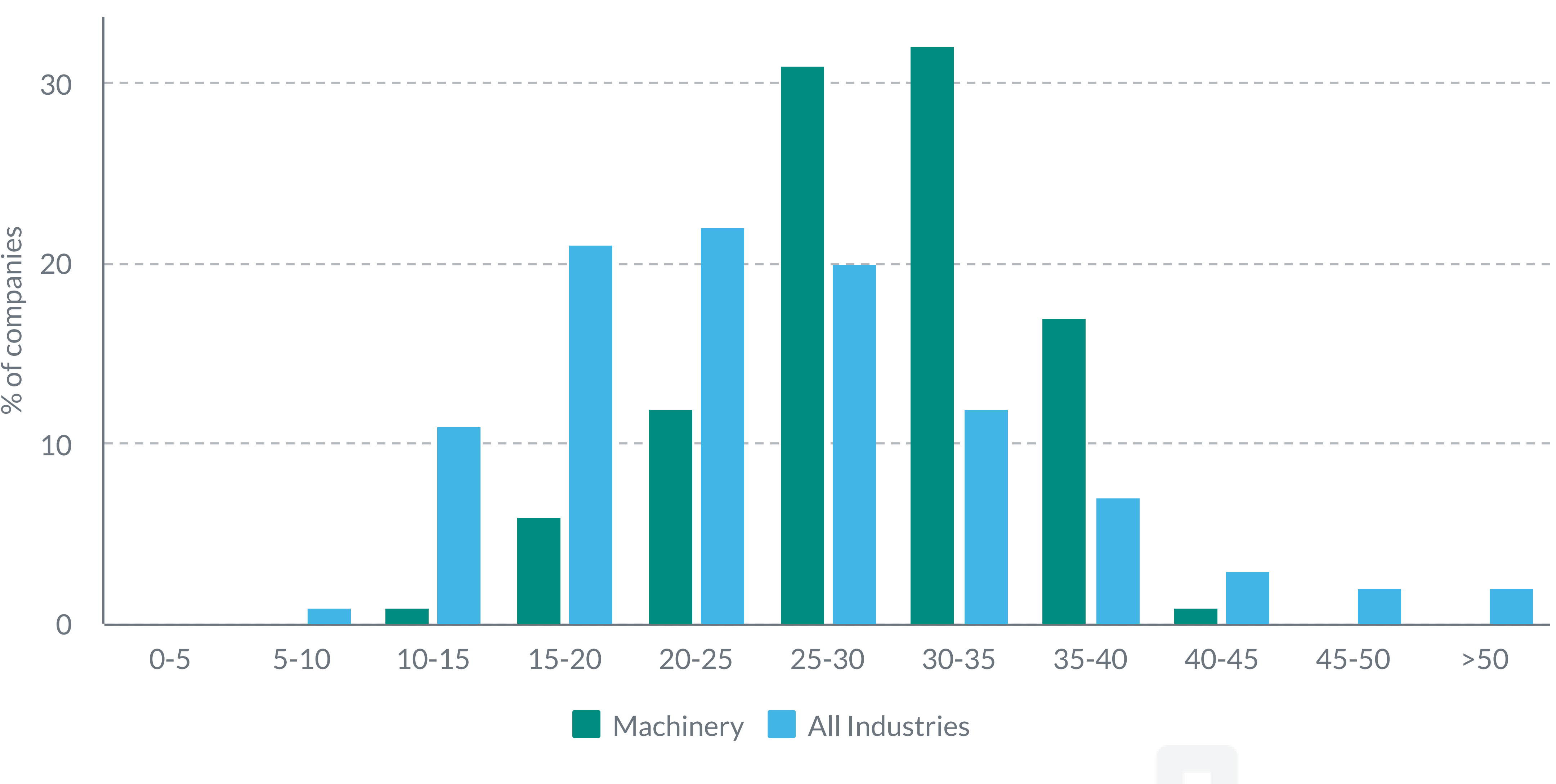
is considered as medium ESG risk for the company

1 Industrial Machinery

Companies in the industrial machinery industry are involved in manufacturing equipment and specialised machinery for several industries ranging from energy and urban mobility to pulp & paper and construction.

Trends shaping the industry include demand for more energy efficient products and stricter non-GHG (greenhouse gas) emission standards. Investments in carbon reduction measures are likely to increase due to both changing regulatory frameworks (EU Climate Law) and continued competitive pressure.

The Industrial Machinery industry has a medium-level exposure risk (total exposure scores of 47), the majority of which are based in Europe.



54% of companies are considered high risk (scores of 30-40) and 20% as severe risk (scores >40).

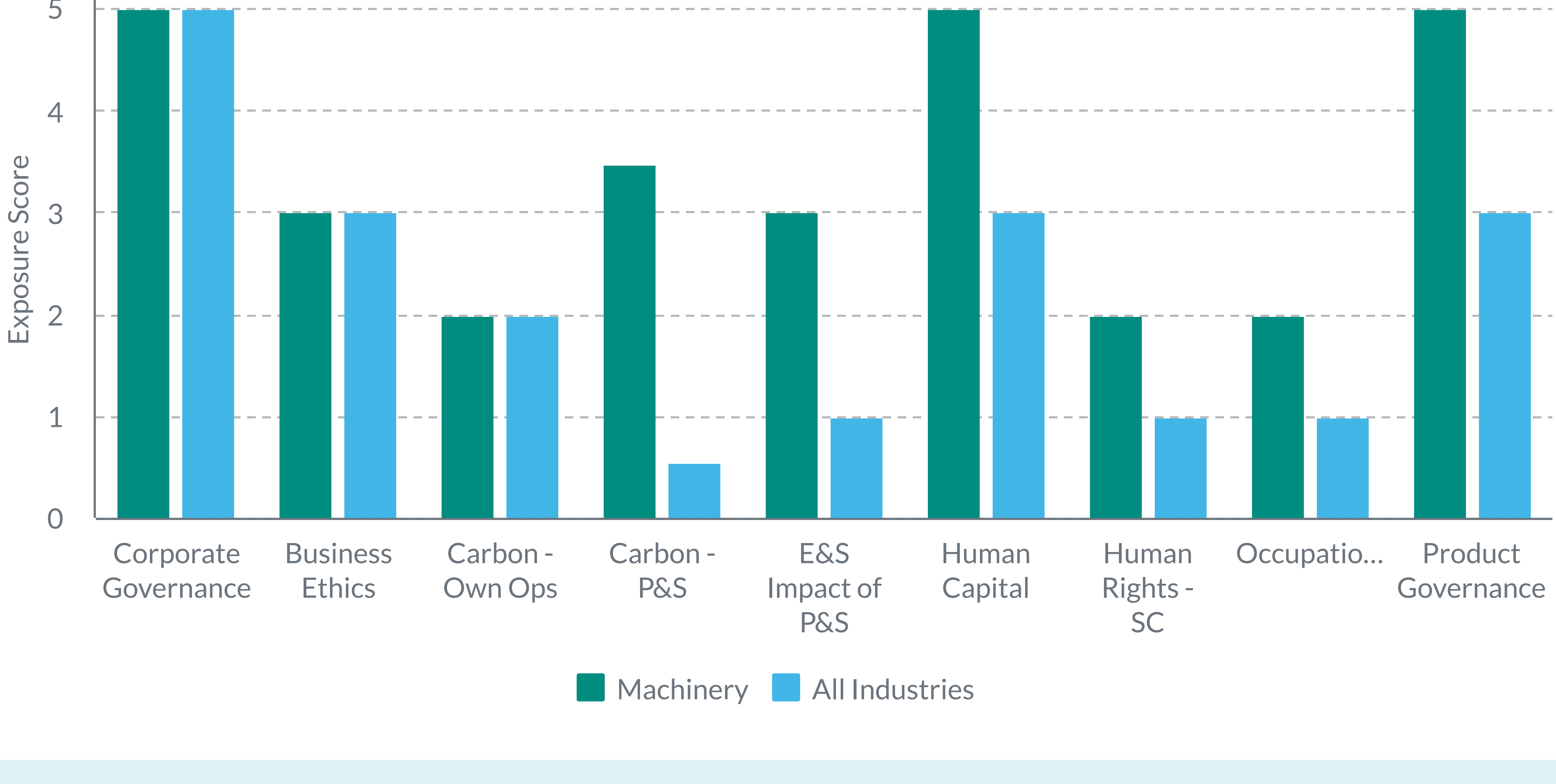
These scores are primarily due to weak management of material ESG issues.

Overall, regarding management for the machinery industry, about 61% of manageable risk is not yet fully managed and this indicates ample room for improvement.

In detail, we can see that the machinery industry is more exposed than others to risks stemming from issues related to Product Governance, Human Capital, Carbon – Products & Services and Business Ethics

54% of companies are considered as high ESG risk

20% of companies are considered as severe ESG risk

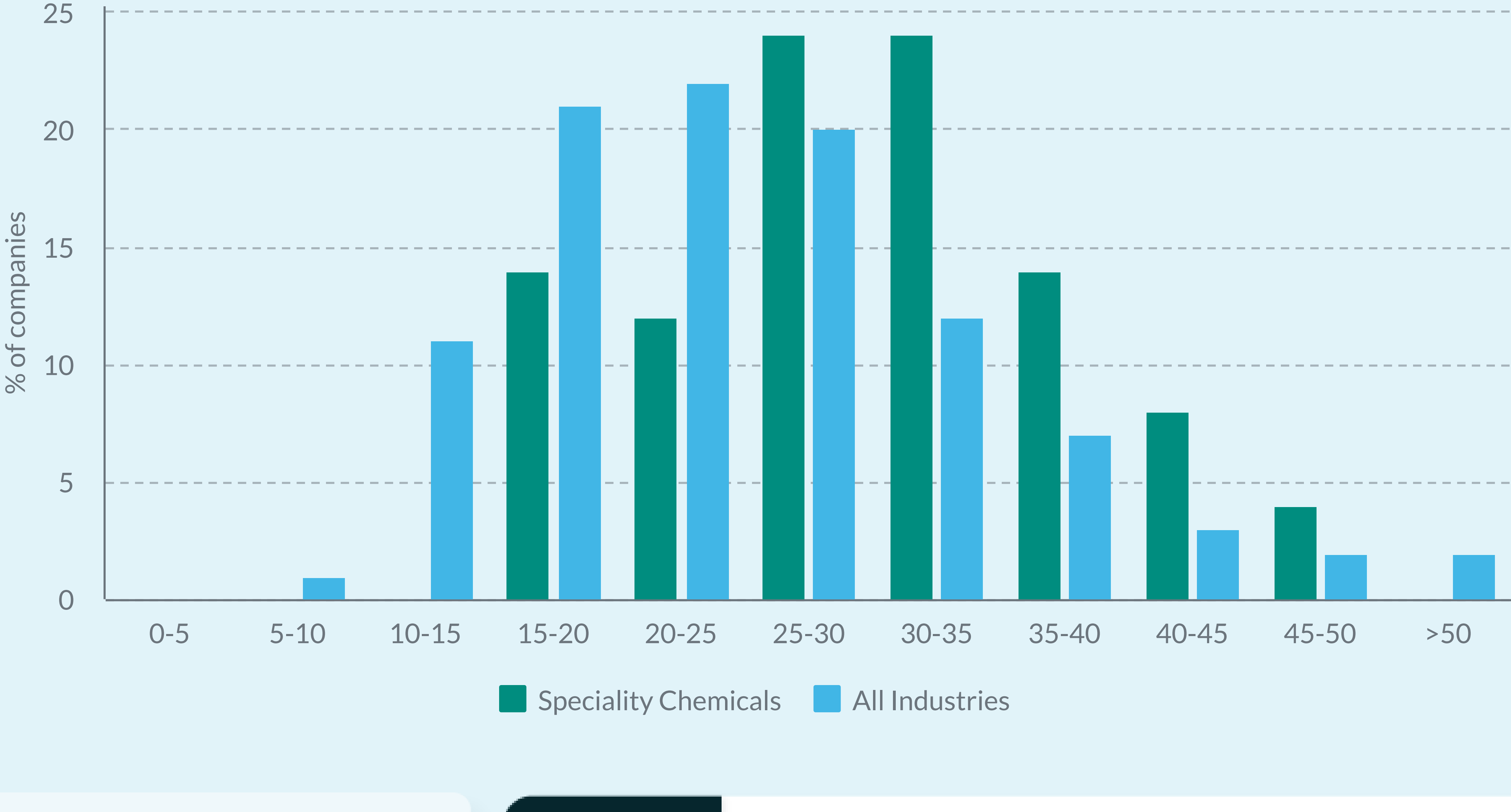


2 Specialty Chemicals

This industry caters to a variety of industries such as automotive, aerospace, food, cosmetics, manufacturing, coatings, and textile.

Overall, the Specialty Chemicals sector is responsible for more than 6% of global GHG emissions. Following increased global awareness and regulations, especially in the EU, regarding climate change, in recent years there has been a distinct shift in focus from chemical companies looking to decarbonise their business by setting targets and initiatives to reach net zero. Furthermore, Specialty Chemicals are well positioned to cater to the growing customer demand for more sustainable products.

The Specialty Chemicals Industry is skewed towards the higher-risk end of the scale.



More than 36% of companies are considered to be medium risk (scores between 20 and 30), while 38% are high risk (scores between 30 and 40) and 12% face the most severe risk (scores >40).

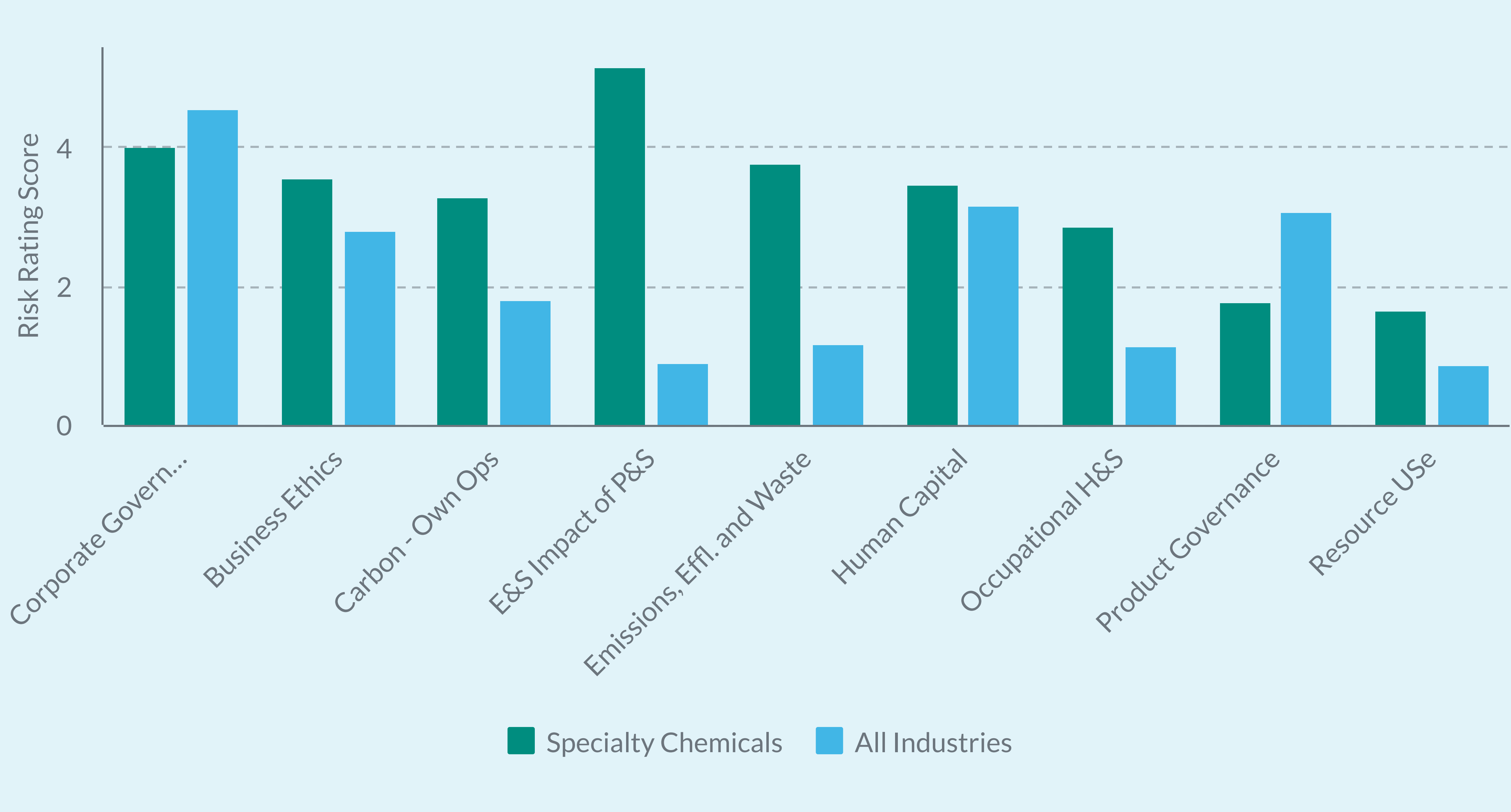
>36% of companies are considered as medium ESG risk

38% of companies are considered as high ESG risk

12% of companies are considered as severe ESG risk

The industry exhibits an overall average management score of 42, with 42% of companies exhibiting strong management (scores >50). The overall management gap shows that 52% of the risk has the potential to be managed, but is not at present.

In detail, we can see that the Specialty Chemicals subindustry faces higher risks than the rest to Carbon Own-Operations, Environmental and Social Impact of Products, Emissions, Effluents and Waste, Business Ethics, Occupational Health and Safety, and Resource Use.

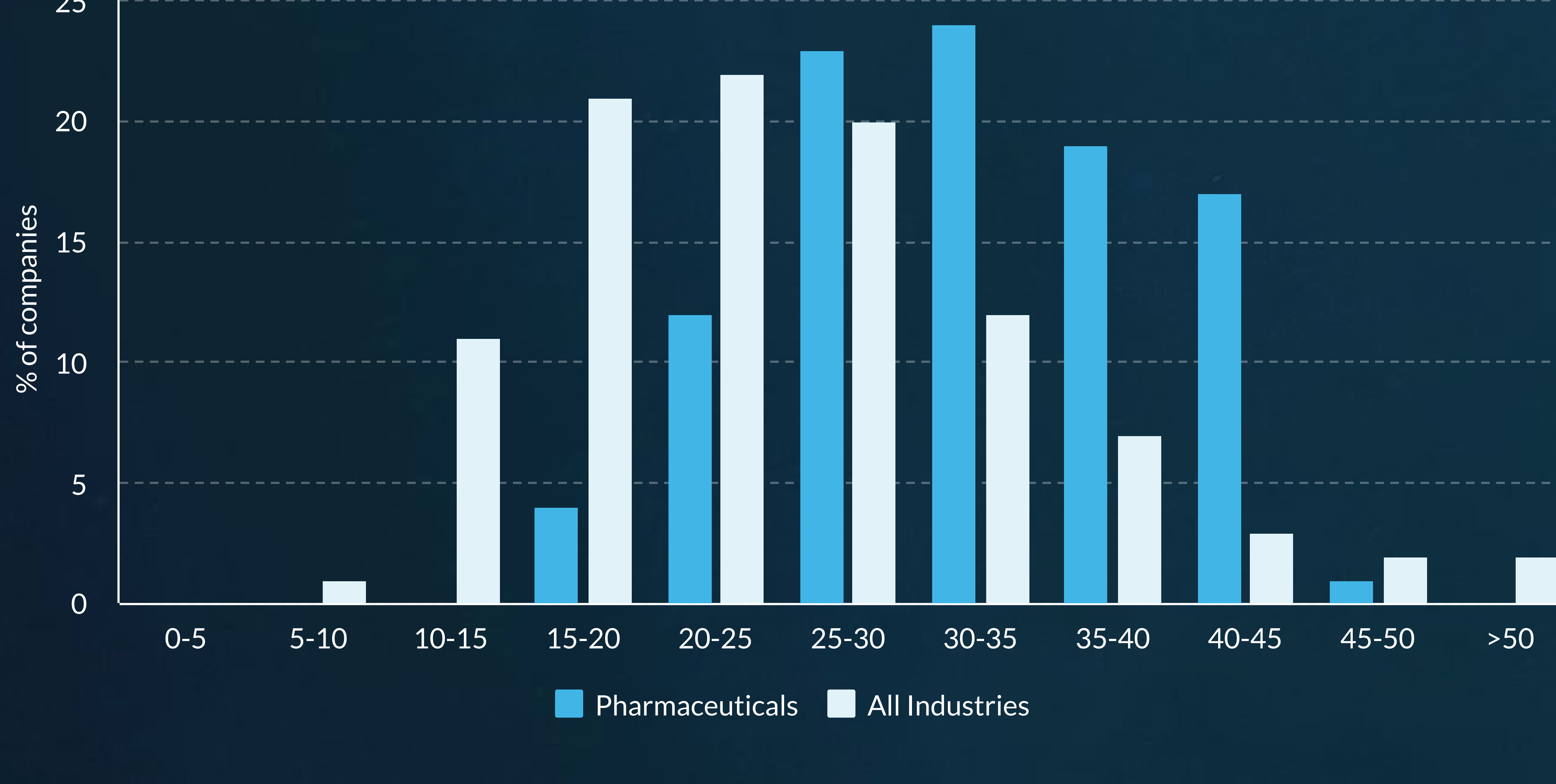


3 Drug Manufacturers: Pharmaceuticals

Companies operating in this industry discover, develop, manufacture and market drugs for use as medications.

These companies are facing intense scrutiny in recent years regarding their ability to provide affordable access to their vaccines globally, notably as public payers shift towards value-based models to control the cost of healthcare.

43% of these companies are considered high risk (scores of 30-40) and 18% as severe risk (scores >40), 80% of which are from Asia and a majority from China.

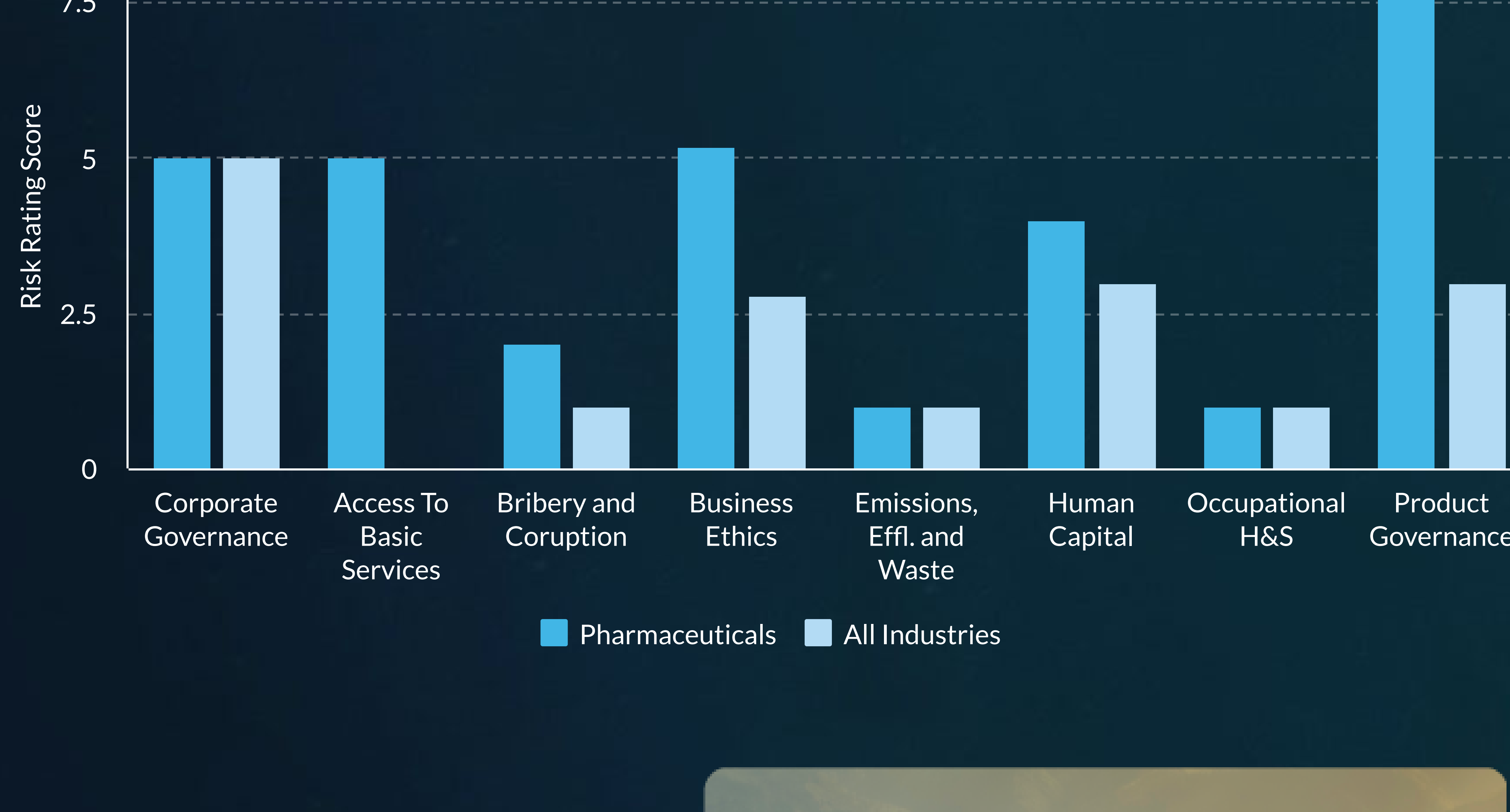


33% of companies in the industry fall into the medium risk category (scores of 20-30), the majority of which are based in Europe.

These ratings are primarily due to high exposure and weak management. Only 9% of companies have strong management (scores >50), most of which are large-cap European firms.

Overall, the industry's large management gap (67% of exposure) indicates ample room for improvement.

In detail, we can see that the pharmaceutical industry is more exposed than the others to risks stemming from issues related to Product Governance, Business Ethics, Access to Basic Services and Bribery and Corruption.



ESG Fund Focus

With this ESG Equity Barometer, Euronext Corporate Barometer also intends to highlight innovative responsible investment initiatives. For each edition, we will showcase 2 international ESG funds and describe which sustainable and responsible theme they have chosen, how they manage their investment process and which non-financial indicators they take into account.



1 Interview

**Fund:**

Sycomore Eco Solutions

Asset Manager:

Sycomore Asset Management

Fund Manager:Anne-Claire Abadie,
Alban Préaubert,
Jean-Guillaume Péladan**ISIN:**

LU1183791281

Can you introduce your fund, Sycomore Eco Solutions?

The fund was launched in 2015 and aims to actively contribute to the environmental transition. The portfolio holds an average of 70 lines and has approximately €650 million of assets under management. Since its creation, it has delivered a net positive performance of +86.9 % (I Share – data as of 24.11.2021 – Index [MSCI Europe NR]: 52.7%). The investment universe is international, all market capitalisations, with a current bias towards European stocks.

Why can Sycomore Eco Solutions be considered a responsible fund?

The fund focuses on companies whose business models contribute to the environmental transition in five fields: energy, mobility, renovation and construction, circular economy and ecosystem-related businesses.

Companies active in partial or significant environmental destruction are excluded, as well as companies whose ESG rating is insufficient to prevent significant negative externalities on other stakeholders.

Sycomore Eco Solutions has received the Greenfin label from the French Ministry for Ecology and Inclusive Transition, as well as the French SRI label.

Can you briefly describe your investment methodology? How do you assess ESG achievements and trajectories of the issuers you are targeting?

Our environmental selection is built around the NEC, Net Environmental Contribution, that we have been developing since 2015. This metric measures the degree of contribution of any economic activity to the environmental transition, based on products and services' physical impacts over their full life cycle on climate, biodiversity, water, resources & waste and air quality. We only select companies that demonstrate a strictly positive Net Environmental Contribution, on a scale from -100% for the most damaging activities to the environment to +100% for restoration activities and those with the smallest environmental footprint. The full methodology is publicly accessible on www.nec-initiative.org

We complete this assessment with work on trajectories and alignment, that serves also as a basis for our dialogue and engagement with companies. The fund does not invest in fossil nor nuclear activities.

2 Interview

Can you introduce your fund, RobecoSAM Sustainable Water Equities?

Addressing one of the world's most serious sustainability challenges – water scarcity & quality – the fund has been running for 20 years. The strategy and management have never changed, while delivering a consistent positive performance. This consistency and longevity is embodied by Dieter Küffer, who has been the fund's manager since its inception in 2001. This is the first sustainable thematic fund launched by Robeco, which currently manages over €12,300 m in this investment category. RobecoSAM Sustainable Water Equities has around € 3,500 m under management with an average of 70 lines in the portfolio.

Why can RobecoSAM Sustainable Water Equities be considered a responsible fund?

This actively managed fund focuses on companies that provide sustainable solutions along the water value chain. The manager focuses on the issue of reducing water scarcity and enabling clean and safe access to water resources. On this basis, he works on factors such as distribution, management, efficient use, treatment and analysis, as well as irrigation systems. The approach gives priority to the impact from products and services of the companies over pure ESG risk management.

Can you briefly describe your investment methodology? How do you assess ESG achievements and trajectories of the issuers you are targeting?

We make very little use of external data providers with the exception of controversy monitoring. The research is therefore entirely in-house. We focus on engagement with issuers, always with a constructive attitude. We monitor around 170 companies in this universe (issuers must have a minimum of 20% of revenues related to the thematic to be eligible).

We conduct fundamental analysis incorporating ESG criteria throughout the investment process, focusing on the contribution of companies' activities to sustainability. We also apply ethical, sector and thematic filters (e.g. hydro power generation, bottled water). In the current market context, we are increasingly looking at smaller caps, which is also a way to differentiate ourselves from the strong competition in this investment universe.

ROBECO

The Investment Engineers

Fund:

RobecoSAM Sustainable Water Equities

Asset Manager:

Robeco Institutional Asset Management BV

Fund Manager:

Dieter Küffer

ISIN:

LU2146190835



Key Take Aways

- ESG funds that are actively managed remain the leader of the responsible investment landscape
- Europeans are leading the race (up to 80% of the ESG AuM in Equity)
- ESG thematic investments are becoming mainstream
- It is also a unique opportunity for SMEs with sustainable business models to diversify their shareholder base
- Environmental labels are dominant but some social and governance indicators are strongly emerging
- Through active engagement, ESG funds support the environmental transition and encourage issuers to act more responsibly
- The next big thing for ESG funds would be impact investment
- It is necessary for issuers to publish granular sustainability reports and disclose concrete ESG objectives for funds to use

**Get in touch:**

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