

MARKET

Mainland China



在投资者需求和监管要求的推动下，中国市场的ESG意识、数据监测和相关信息披露发展在不断加速。2013年，有54%的沪深300指数成分公司发布了正式的ESG披露报告。而截至2019年，披露率以提升到85%。

目前上交所和深交所都提供了对ESG报告的书面指导。而在2021年中国证监会进一步收紧了ESG披露规则，强制披露环境相关处罚，并鼓励自愿披露为减少碳排放、扶贫和乡村振兴而采取的措施。此外，习近平主席已表示在2060年前实现碳中和的目标，这将进一步推动中国市场向ESG的转型。

Hong Kong (HK)

Interest in Environmental Social Governance (ESG) has increased exponentially, due to investor demand, and regulatory drives. ESG is believed to be beneficial for driving long term sustainable growth as high ESG rating is associated with lower compliance and systemic risks. As a result, fund managers are increasingly leveraging on ESG to market products to investors. Moreover, ESG has also been a focal point for the public sector in HK, where regulators such as the HKEX, SFC, MPFA and HKMA are increasingly incorporating ESG standards into their policies with the intention to develop Hong Kong into a regional ESG hub.

WHO ARE THE MARKET MAKERS IN HONG KONG ?

In HK, ESG funds have performed 9.5% above equity funds on average in 2020



HK ESG Mutual Fund issuers include: Pictet AM, Allianz Global Investors, Blackrock

HK ESG ETF issuers include: Mirae Asset Global Investments, Haitong IAM, Harvest Global Investments

What drives ESG performance today?

An example of US ESG ETFs

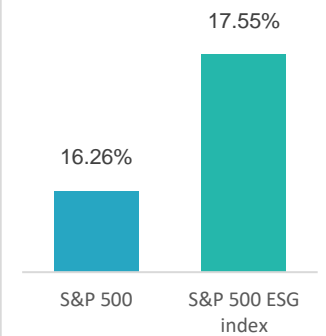
ESG funds, Invesco Solar ETF (TAN) and iShares Global Clean Energy ETF (ICLN) which were up **65.67%** and **141.31%** in 2020 respectively, are down **29%** and **26%** at Q2 2021.

Why?

In 2020, S&P500 ESG Index beat SPX by 1.29%, and the heavy bias of ESG funds towards growth and tech stocks allowed the funds to significantly outperform the market. However, a non-ESG portfolio with the same industry focus would have outperformed the market all the same.

'The outperformance of ESG funds cannot be said to be related to the purposely designed ESG strategies' but more to heavy asset allocation to tech companies which perform well in the environmental aspect of ESG ratings due to low emissions. In Q1 and Q2 2021 when energy rebounded strongly and tech underperformed, tech heavy ESG funds lagged behind the broader market.

Index Return 2020



Both ESG funds and ESG indexes outperformed the broader market in 2020.

WHICH ESG METHODOLOGY: PASSIVE OR ACTIVE ?

In Europe, some UCITS ETFs' allocation to sustainable increased to >50%. Will HK domiciled funds follow ?

POSITIVE SCREENING

Overweight in companies with high ESG rating (e.g., IT, financials). "Heavy technology, light energy".

NEGATIVE SCREENING

Exclusion Strategy: Avoid investments in industries such as fossil fuels, firearms, tobacco, alcohol, etc.

SUSTAINABILITY THEME

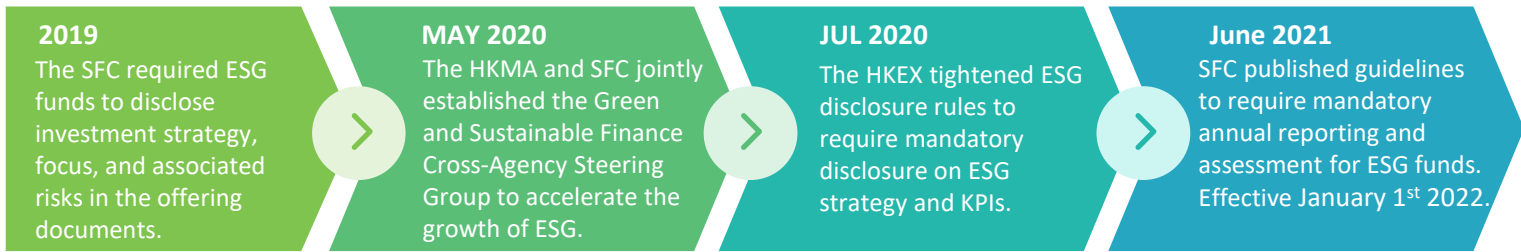
High percentage of NAV (SFC requirement: **70%**) invested in an ESG theme. E.g., Carbon Neutrality.

ASSET ACQUISITION

ESG metrics in the asset acquisition process to enhance corporate and financial performance.

WHAT ARE THE LATEST REGULATORY UPDATES ?

A timeline of ESG regulatory development in HK



What is new in the SFC's ESG fund reporting guidelines that come into effect on 1st January 2022?

Disclosure in Offering Documents

- **Focus:** Description of ESG focus and list of criteria used to measure attainment of fund's focus.
- **Investment Strategy:** Description and summary of investment strategies and process of consideration of ESG criteria.
- **Asset Allocation:** Expected proportion of fund's NAV that is commensurate with the fund's ESG focus.
- **Reference Benchmark:** Description of how fund tracks/measures ESG focus against a designated ESG benchmark.
- **Additional Information Reference:** Additional information such as description of how ESG focus is measured, or description of due diligence carried out as part of the ESG asset acquisition process.
- **Risks:** Description of risks and limitations of the fund's ESG focus and investment strategies.



Periodic Assessment and Reporting

Conduct a periodic assessment, at least annually, to assess how the fund has attained its ESG focus.

Other Global ESG regulatory updates

Singapore



2021: Singapore is shifting away from an incentive-based approach to a stricter approach on ESG regulation. There is an upcoming review of the Singapore Stewardship Principles which is expected to provide specific direction to corporates for their stewardship of environmental considerations. In May 2021, the Green Finance Industry Taskforce released guidelines on climate-related disclosures and a white paper on green finance solutions.

USA



2021: The U.S. Securities Exchange Commission (SEC) is expected to announce a mandatory ESG disclosure framework to follow their April 2021 risk alert for examinations of ESG investing. This may require issuers to provide uniform and standardized line-item ESG disclosures.

EU



2021: The EU's Sustainable Finance Disclosure Regulation (SFDR) began implementation in March 2021 and imposes a detailed set of mandatory ESG disclosure obligations on asset managers and other financial markets participants. This new regime requires sustainability-related disclosures. Financial market participants are required to disclose on how they integrate sustainability into their investment strategy and decision making. SFDR compliance failure can result in sanctions by regulators in the EU.

UK



2021: As of June 2021, the Financial Conduct Authority is consulting on requiring climate related disclosures for asset managers, pension funds and insurers in line with the Taskforce on Climate-related Financial Disclosures published in 2017. This is a framework for corporates to disclose how climate-related risks and opportunities can impact their business.

Australia



2021: In April 2021, the Australian Prudential Regulation Authority (APRA) released for consultation its draft guidance to banks, insurers and superannuation trustees on managing the financial risks of climate change. This framework is a response to industry demand for greater clarity of ESG regulatory expectations.



CHALLENGES

Local asset managers face several challenges when addressing ESG in their product strategy:

DATA	Limited data and lack of standardized KPIs are a limit to a transparent ESG operating model. Moreover, there is often discrepancy between what data providers can offer and what fund managers are trying to monitor.
REPORTING	Lack of harmonized approach/expertise to ensure proper disclosure and reporting. Lack of resources to comply with reporting rules.
ASSET ACQUISITION	Difficulty in identifying ESG factors in asset acquisition due to GREENWASHING . Fund Managers lack resources or incentives to engage with companies represented in their funds.
TALENTS	There is a notable shortage of ESG specialist talent in the financial services market. Currently the combined understanding of finance and ESG issues such as sustainability is still incomplete.

ESG CHECKLIST

From high level
analysis



To operational
implementation

- Gap analysis : regulatory requirements vs existing
- Filling the gaps: Regulatory and business process upgrades
- ESG experts/teams within your organization to collect & share the data
- Impacts analysis on the affected business lines
- Anticipation of coming regulations / requirements
- Coordination with regulators/rule makers (e.g., HKEX for listed companies)
- Set up of tangible KPI for internal ESG monitoring
- Bretteville to draft reporting templates adapted to your organization
- Coordination with IT for automated reporting (on applicable KPIs)

BRETTEVILLE CONSULTING

HOW BRETTEVILLE SUPPORTS YOUR ESG STRATEGY

- **Market insight:** Implement end-to-end ESG strategy through market analysis (Hong Kong, APAC, other regions)
- **Risk management:** review ESG policies and procedures
- **Design:** Ensure data and reporting set up and monitoring
Project: KPIs design and implementation
- **Strategy:** Review and implement ESG product offering strategy



EXAMPLE OF ESG RELATED PROJECT: IMPACTS ON A CIB KYC PROCESS

As ESG importance is increasing and the trend is planned to continue, financial institutions will have to include ESG performance as a new risk factor

- **at onboarding stage**
- **continuously in periodic reviews.**

A new screening process must be setup internally to assess client's ESG performance.

A service provider for the data and an external rating company will be needed.



CONCRETE IMPLEMENTATION

- ☑ RFP and selection of service providers
- ☑ Build an internal ESG rating system
- ☑ Include the ESG rating in the overall risk management system
- ☑ Anti greenwashing solution
- ☑ Coordination of IT Improvements to include all above
- ☑ Change Management

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