Eurosif

SDGs for SRI investors

The Sustainable Development Goals (SDGs) comprise a global and inclusive agenda to end poverty by 2030. They represent a follow-up to the Millennium Development Goals (MDGs) while including new areas such as climate change, economic inequality, innovation, sustainable consumption, peace and justice, among other priorities. They tackle the root causes of poverty and unite us together to make a positive change for both people and planet. The main difference with the MDGs is that, this time, the focus is on the private sector and how it can contribute to achieving this ambitious set of goals. There are 17 Sustainable Development Goals, with a total of 169 targets and 230 indicators. Several private sector players have been deepening their understanding of investment impact and have already sharpened their strategies accordingly.

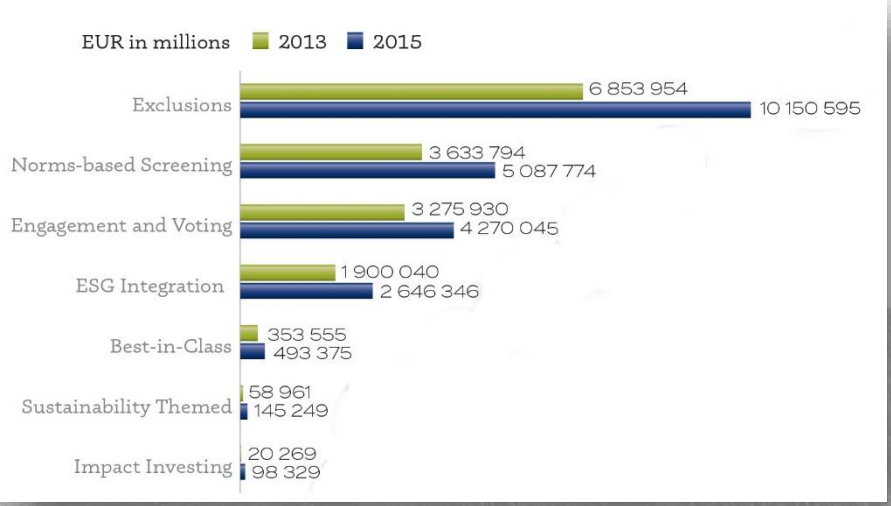
The adoption of environmental, social and governance (ESG) considerations in investments has evolved continuously in the past decades. This trend falls under the denomination of SRI - 'sustainable and responsible investment' - and it has evolved from a risk management focus (typically linked to investment exclusions of specific companies and sectors) to one that seeks opportunities for the creation of long-term value for business and society. Promoting ESG adoption throughout the investment value chain can encourage greater private investment in sustainable development, resulting in greater impact.

The various actors in the investment value chain, including asset owners, asset managers and companies, have been increasingly including ESG and sustainability information in their reporting processes. This has meant a strong boost for the SRI market which, to quote the latest Global Sustainable Investment Alliance (GSIA) report 2016, is now at $22.89 trillion of assets being professionally managed, registering an increase of 25 percent since 2014[1].

From ESG investing to SDG in practice

Today, several practitioners apply at least some form of extra-financial evaluation in their portfolio, though this is not sufficient to fall under an SRI denomination or to meet the requirements of one specific strategy. The different categories of SRI strategies can be applied individually or in an aggregated fashion. In Europe, the evolution of SRI strategies has represented a continually rising trend, growing from 14[2]% Compound Annual Growth Rate (CAGR) to up to 120%[3].

Table 1 Overview of SRI strategies in Europe



[1] 2016 Global Sustainable Investment Review page 3
[2] Registered for Engagement and Voting
[3] Registered for Impact Investing

ESG integration refers to the explicit inclusion of ESG factors by asset managers into traditional financial analysis. This investment process has been gaining momentum, not only in Europe but across the globe, becoming the most widely used strategy by SRI investors, whose large majority[4] reportedly has a formal integration policy document. The ESG efforts by the various private actors are consistent with the Sustainable Development Goals (SDGs), but need to be leveraged further to achieve stronger outcomes. Eurosif has recognised different degrees and approaches to ESG integration on the part of investors[5], as the fundamental methodology for the realisation of SDGs and their ambition. The spectrum of revenue models range from social return only with little or no profit through blended models to the socially motivated businesses with market-based financial returns. The different approaches as illustrated below, show how investments strategies have evolved towards the intention to generate social and environmental impact alongside a financial return, which should be financially sustainable in the long run. At the time of the development of this framework, Bridges Ventures considered Impact Investing to cover both thematic strategies and impact-first strategies. SDG investors can opt to take ESG criteria into consideration to have a positive societal impact, targeting financial returns which can range from below market to market rate returns, committing to both measure and report the social and environmental performance and progress of underlying investments.

Table 2: Spectrum of Capital

		SDG investing				
	Traditional	Responsible	Sustainable	Thematic	Impact-first	Philanthropy
	Competitive returns					
		ESG risk management				
			ESG opportunities			
				High-impact solutions		
Focus	**Finance Only** Limited or no focus on ESG factors of underlying investments	← The New Paradigm → Focus on ESG risks ranging from a wide consideration of ESG factors to negative screening of harmful products	Focus on ESG opportunities, through investment selection, portfolio management and shareholders	Focus on one or a cluster of issue areas where social or environmental need creates a commercial growth opportunity **for market-rate or market-beating returns**	Focus on one or a cluster of issue areas where social or environmental need requires **some financial trade-off**	**Impact only** Focus on one or a cluster of issue areas where social or environmental need requires **100% financial trade-off**
Examples		• Through **ESG integration** PE firm analyse ESG risks as part of their investment analysis	• **Best-in-class** SRI fund	• **Sustainability themed investment** choices: Clean energy mutual fund	• Fund providing debt or equity to social enterprises and/or trading charities also through **Engagement and Voting**	

[4] 80% of Eurosif SRI study respondents have indicated to have formally adopted ESG integration in the form of a policy.

[5] Eurosif SRI study 2016 page 50

The best SRI strategies for SDG investors

Impact Investing

Since the beginning of the articulation of the SDGs, investors have seemed rather keen to focus on Impact Investing as the SRI strategy which is best able to embody the attainment of the Goals. This strategy was the protagonist of Eurosif's last review, as it proved to be the fastest growing strategy and the one associated with landmark events such as the 21st UN Climate Change Conference of the Parties (COP21), which set the framework for further investment in low-carbon technologies and infrastructure. Impact Investing foresees specific characteristics which underpin the strategy, these being:

1) intentionality of ESG impact

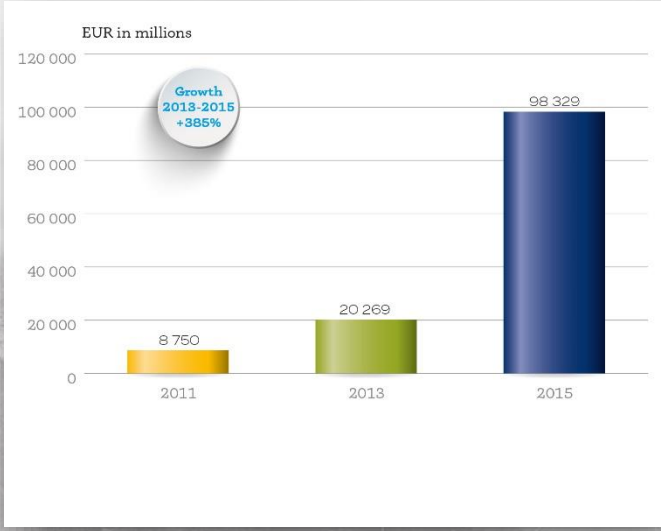
2) return expectations

3) impact measurement

4) a long-term horizon

All the mentioned criteria are linked to all SRI strategies, except for the focus on impact measurement, which is therefore considered the key criteria for this investment approach. Eurosif has analysed carefully the elements which constitute impediments to impact investing and in that respect, there is a strong link with the possibility to galvanise further potential for SDGs. The risks investors see are actually linked to the lack of set metrics which can hamper the comparability. This can have repercussions on the investor's due diligence process. SDGs have done much in terms of stimulating the development of metrics and international investors have responded by choosing the right strategies and objectives to pursue SDGs.

Table 1: Impact Investing in Europe



Best in Class

This strategy allows investors to pick those companies that have the best ESG score in a particular sector. It is therefore possible to take a specific performance indicator which is in line with one of the SDGs. For example, when evaluating its impact performance on decent work (SDG 8), investors can measure and track KPIs such as the number of training hours per employee and the turnover figures.

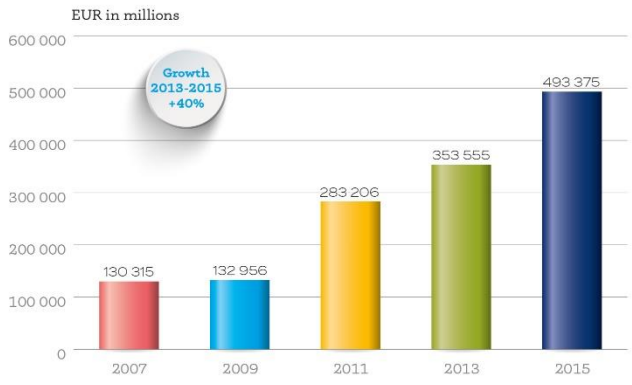


Table 2: Best in Class growth in Europe

Stewardship and engagement

SDG Investing has a long-term perspective, which entails the principle of continuous improvement as much for investors as for investees. For this reason, it is imperative for an SDG investor to be an engaged one, as well as one that is prepared to interface with any issuers present in the management portfolio who are not on track with the SDG targets as part of their business strategies.

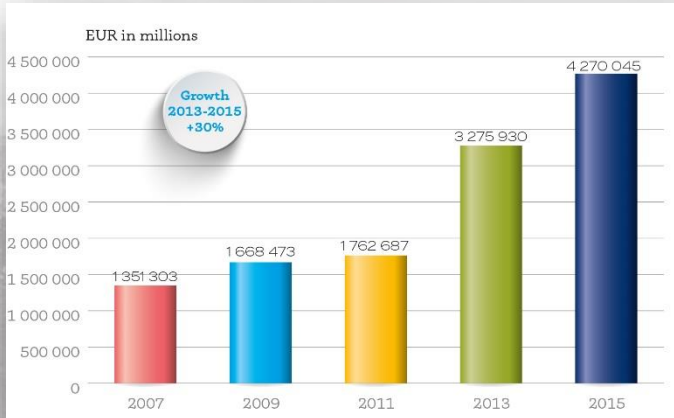


Table 3: Stewardship and voting growth in Europe

Sustainability Themed

This strategy includes a variety of themes, which allows investors to choose specific areas of investments, typically with a close link to sustainable development. The emergence of new product and focus on certain themes has sharply increased, as demonstrated by the exponential growth in this strategy over the last five years. European sustainability-themed assets have grown to reach €145 billion at the end of 2015.

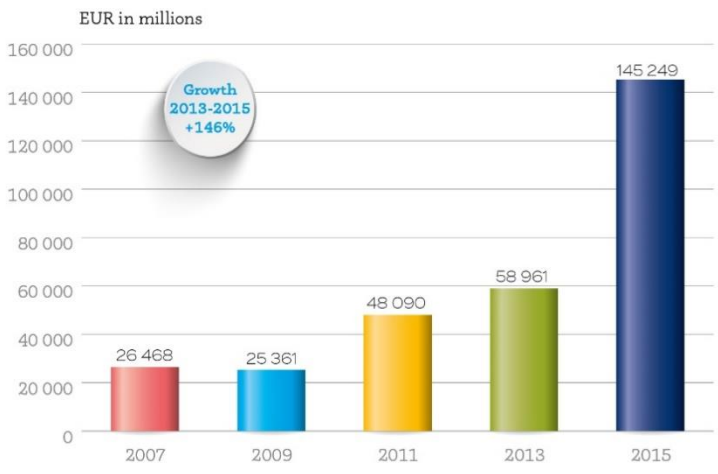
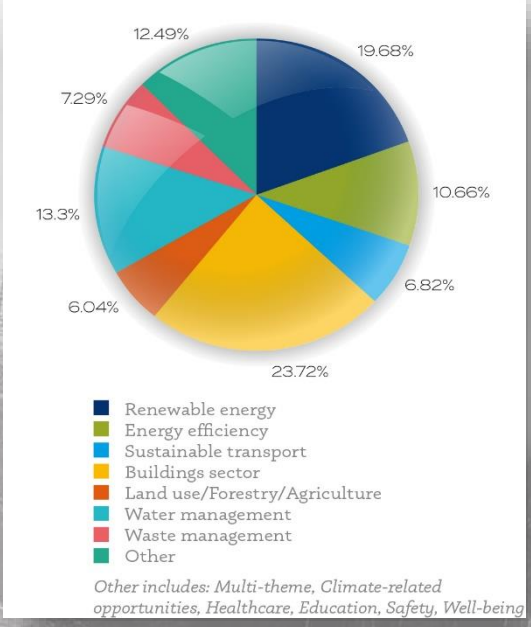


Table 4: Sustainability themed Investments growth in Europe

Table 5: EU Sustainability themed investments by type



Sustainability-themed investments that focus on long-term investment themes associated to SDGs, such as water scarcity, energy efficiency, carbon reduction, agricultural yield and access to education, to name a few, can be easily integrated into portfolios. Furthermore, thematic investment proposals can be used to guide other approaches, namely best-in-class, stewardship and engagement, and impact investing. Eurosif's research classified the most popular themes for investors which clearly reflects a tendency to support the fight against climate change and renewable energy.

For investors to be sure they are truly using the right metrics, they can devise methodologies through which they can track the effectiveness of their sustainability choice, by measuring parameters (i.e. carbon intensity) they can track throughout the entire value chain.

Outlook and final remarks

As achieving the UN's SDGs will require 'pouring $1.4tn into low-and lower middle-income countries'[6], the private sector and investors will have a big role to play in this investment. For the private sector to act, policy-makers must step up and empower investors to help them mobilise private capital through regulations, incentive structures, and public-private partnerships.

The need to capitalise on the private sector's resources represents an opportunity for investors who are already keen on SRI. As outlined, there are a number of SRI strategies can be helpful in attaining goals in line with the SDGs. Although impact investing has been elected by some as the preferred strategy, we have seen how relevant other approaches are in pursuing specific sustainable themes and already deliver on these targets. The systemic integration of ESG criteria represents a solid starting point for investors who intend to structure an SDG investment policy. Not only the companies that are proving to be the best performers across classes and industries should, be their sole focus. The SDG investor has a responsibility to ensure that a positive change is made, and is therefore instrumental in making that change. In this respect, engaging with issuers is essential to guaranteeing that sustainability is embraced by many and in a consistent fashion.

The motivators to invest sustainably have only radically increased in the past years. What the future holds is an even stronger push and business case for investors to take the lead and reshape the economies and development agenda.

Impact Investing	Best-in-Class	Stewardship and Engagement	ESG Integration	Sustainability Themed Investment
Impact investments are investments made into companies, organizations and funds with the intention to generate social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets, and target a range of returns from below market-to-market rate, depending upon the circumstances.	Approach where leading or best-performing investments within a universe, category, or class are selected or weighted based on ESG criteria.	Engagement activities and active ownership through voting of shares and engagement with companies on ESG matters. This is a long-term process, seeking to influence behaviour or increase disclosure.	The explicit inclusion by asset managers of ESG risks and opportunities into traditional financial analysis and investment decisions based on a systematic process and appropriate research sources	Investment in themes or assets linked to the development of sustainability. Thematic funds focus on specific or multiple issues related to ESG
Investments are often project-specific, and distinct from philanthropy, as the investor retains ownership of the asset and expects a positive financial return. Impact investment includes microfinance, community investing, social business/ entrepreneurship funds and French fonds solidaires.	This approach involves the selection or weighting of the best performing or most improved companies or assets as identified by ESG analysis, within a defined investment universe. This approach includes Best-in-Class, best-in-universe, and best-effort.	Engagement and voting on corporate governance only is necessary, but not sufficient to be counted in this strategy.	This type covers explicit consideration of ESG factors alongside financial factors in the mainstream analysis of investments. The integration process focuses on the potential impact of ESG issues on company financials (positive and negative), which in turn may affect the investment decision.	Sustainability themed investments inherently contribute to addressing social and/or environmental challenges such as climate change, eco-efficiency and health. Since 2008, funds are required to have an ESG analysis or screen of investments in order to be counted in this approach.

[6] Investment Needs to Achieve the SDGs: understanding the billions and trillions, Sustainable Development Solutions Network (SDSN Working Paper) 12/11/2015