ESG Investing

What you need to know

ESG explained

Environmental, social and governance (ESG) considerations have gained more recognition in recent years and ESG integration is increasingly viewed as an important differentiator in the investment processes of discretionary fund managers (DFMs).

It is now widely recognised that the ESG aspects of a company's activities can have a material influence on its ability to deliver long-term returns to its investors.

ESG factors are useful indicators of a company's overall strength, how it is likely to perform in the future, as well as material risks that could impact its prospects. Integrating ESG engagement and analysis into the investment process can help DFMs more fully assess the risk/reward opportunities for individual investments.

ESG factors are constantly evolving but can include how a company:

Environmental (E)

- manages waste and pollution, including greenhouse gases
- contributes to or controls its impact on climate change
- manages natural resources including water

Social (S)

- treats its employees and their working conditions
- values human rights and its stance on child labour and slavery
- considers impact on wider stakeholders and society, including local communities and animal welfare

Governance (G)

- approaches diversity and how it structures its board
- rewards and pays executives
- limits its exposure to corrupt practices and deals with bribery
- makes, declares or avoids political donations.

The benefits of an ESG approach

Better long-term returns

There was once a widely held perception that investors might need to sacrifice the potential for decent investment performance in order to invest ethically.

This debate has moved on considerably in recent years and there is now a weight of research showing companies that take their ESG responsibilities seriously are more likely to outperform their less well-managed peers.

Selecting companies that focus on the social and economic impact of their activities does not have to mean compromising on performance; in fact quite the opposite can be true.

An indicator of quality

By scoring companies on ESG factors, investment managers can gauge if a company may be exposing itself to risks that could impact its earnings. They can also be excellent indicators of any 'red flag' warnings that could affect future investment performance of a company, such as deterioration in operations or possibility of bankruptcy – ultimately helping reduce long-term investment risk. Considering ESG issues helps to significantly improve the assessment of a company's quality.

Transparency

An ESG investment approach by its very nature encourages transparency, with investors increasingly demanding clarity on where and how their money is being invested. Those companies that take their corporate responsibilities seriously tend to operate more openly, have measurable outcomes and are able to publically communicate their ESG practices.

ESG as standard

At Aberdeen Standard Capital, we have long understood the intrinsic connection between financial performance and how the companies in which we invest our clients' money approach these issues. We firmly believe that companies demonstrating a commitment to responsible business practices will likely enjoy a competitive advantage in the long run – ultimately rewarding shareholders.

Consideration of ESG factors is embedded in our investment process and investing responsibly on behalf of our clients goes to the very heart of our drive to provide superior investment returns and maintain client trust.

Analytical rigour

As the discretionary investment management arm of global asset manager Aberdeen Standard Investments*, we have access to company management on a global basis, which provides us with significant insight.

All our research incorporates consideration of ESG factors specific to a company or sector and information is corroborated by our engagement with competitors, supply-chain firms and customers. We combine this with market-leading independent analysis to form a complete picture of a company, taking into account fundamentals, such as its balance sheet, cashflow and overall management, alongside its ESG credentials. This adds depth to our investment process and makes for better-informed and more robust investment decisions.

*Aberdeen Standard Investments is a brand of the investment businesses of Aberdeen Asset Management and Standard Life Investments.

Scale and experience

The dedicated ESG Investment team at Aberdeen Standard Investments has been active in the governance and responsible investing field for many years. This provides us with extensive experience and research-intensive resources on which we can draw.

The ESG Investment team actively engages with companies and conducts in-depth analysis on the material issues affecting clients' investments. At Aberdeen Standard Capital, we can then apply that research to stocks we hold for our own clients invested in our Conventional and Enhanced Diversification range portfolios. Not all discretionary managers can offer private clients and charity clients this institutional-level of ESG expertise.

Investing for a better future

Memories of the global financial crisis, emissions scandals, the use of so-called 'sweat shop' labour by high-street brands and the collapse of staff pension schemes have all served to highlight the importance of good corporate governance and the human cost of poor business practices. These events have also reinforced the business case for investing in companies that take their ESG responsibilities seriously.

At the same time, people are increasingly looking for ways to reflect their beliefs and values in the investments they hold, or use their money to help promote positive change. Not that long ago, the only real opportunity to do this was through a limited number of ethical funds. These types of investments allow people to exclude from their portfolios companies such as those involved in gambling, alcohol and tobacco production, weapons manufacturing, or other sectors to which they are strongly opposed.

Now though, ethical portfolios are just one part of a rapidly growing 'good money' sector, which is much wider in remit and includes impact investing and socially responsible investing. These investment approaches are based on people's desire to make positive investment choices that 'do good', while still seeking to provide a financial return.

Impact investing in particular has grown in popularity over the past few years. Once a niche corner of the market, it has entered the mainstream, driven by increased awareness among investors of the role they can play in helping address the world's many environmental and social challenges. Impact investing allows them to meet this desire, by investing in mission-led businesses that aim to generate measurable, beneficial impact (environmental or social) while still seeking a financial return.

Enhancing our clients' investments

There are more options than ever for people to take control of where they invest their money and use it to promote positive change. The first step is choosing a discretionary fund manager that takes its research responsibilities seriously when it comes to ESG factors.

As well as embedding ESG into our investment process, we have the ability to provide further bespoke enhancements where required. We can apply values-based screening for clients invested in our range of Conventional and Enhanced Diversified segregated portfolios, who wish to reflect their own specific investment requirements.

We offer clients the ability to construct an ethical policy that reflects their specific views and values. We utilise an independent scoring resource and clients can choose from a broad range of factors to create a policy that is granular in nature. For example, a client may wish to exclude investment in companies that score poorly on labour rights in the supply chain or on child labour. Ethical policies such as this are tailored to the client's requirements and can be applied to any type of directly invested mandate, i.e. a growth or income portfolio.

We have also evolved our investment proposition to include a global impact investing strategy. This approach uses the UN's Sustainable Development Goals (SDGs) as an investment framework – an all-encompassing agenda to tackle the most significant problems the world faces. We are delighted to be able to offer our clients the opportunity to not only support this ambitious programme, but also to seek an attractive financial return. Clients can choose to invest in this solution through a fund or a portfolio of direct holdings.

To find out more

Please get in touch with your usual Aberdeen Standard Capital contact or email **asc@aberdeenstandard.com***.*
Visit **aberdeenstandardcapital.com/responsibleinvesting**

Important Information

The value of an investment is not guaranteed and can go down as well as up. An investor may get back less than they invested. Past performance is not a guide to future.

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