February 2021

Learning about ESG

The fight against climate change

Learning about ESG is an educational series that connects **environmental, social and governance** topics with investing. Join us each issue to see how global developments can have implications for investors. The better we understand ESG, the bigger the role it can play in our everyday lives – and investment portfolios – contributing to a better world.

Key takeaways

- Renewed focus on **climate change in the US** – the world's third largest carbon emitter – is a significant step in its pledge to be 'net zero' by 2050
- Climate change is a global focus within the set of ESG factors; to incorporate **ESG factors into investment strategies** is a methodology of sustainable investing
- Sustainability has **become essential to the investment world**, with demand already topping USD30trn in developed countries alone

HSBC

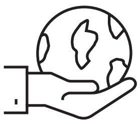
Together we thrive

What has happened recently?

Climate change is back on centre stage in the US since last year, with **renewed plans citing significant investment toward clean energy infrastructure**. Now with a new administration in place, executive orders were immediately issued with the mandate to control carbon emissions across the country. We believe that the US can now play a pivotal role in the global fight against this pressing issue.

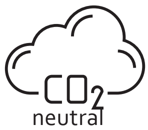
Climate change, global warming, net-zero carbon – these terminologies again have elevated priorities on the world agenda. **Our long-term average weather patterns are changing over time, caused by the planet's temperature rise, which in turn is fueled by atmospheric heat-absorbing gases such as carbon emitted from human activities** (e.g. fossil fuel burning for energy).

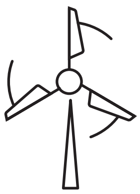
Achieving **net zero carbon, or the balance of carbon emissions vs absorption in our atmosphere**, requires global awareness and action. The US has unveiled plans to reach net zero carbon including key pledges[1] such as:



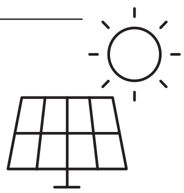
Re-entry into the **Paris Agreement**[2]

Net zero emissions by 2050

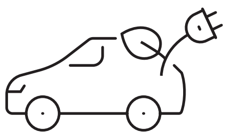




Invest **USD400bn** in clean energy and deliver a zero-carbon power sector by 2035



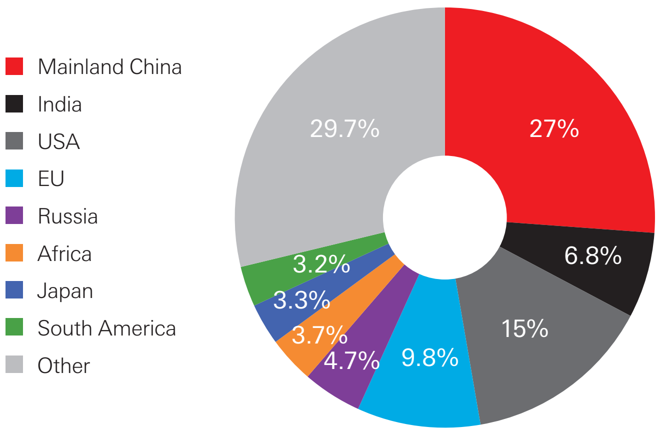
Reduce energy sector **carbon emissions** by half by 2035



Zero emission vehicles, clean rail, biofuels innovation, clean aircraft fuel

The US' commitments are significant to the world as it's the **third largest emitter of carbon dioxide (CO_2)**, accounting for 15% of global emissions – see Chart 1.

Chart 1: Global CO_2 emissions by geography



Source: Our World in Data

CO_2 is a major component of greenhouse gas emissions – gases that trap heat in the atmosphere, causing global warming and contributing to climate change.

Like the US, other top CO_2 emitters, including the European Union with 9.8% and Mainland China with 27%, have also committed to carbon neutrality by 2050 and 2060, respectively. Combined, these three economies account for more than half of the world's CO_2 emissions and are **working towards a common goal to be fully decarbonised by mid-century**.

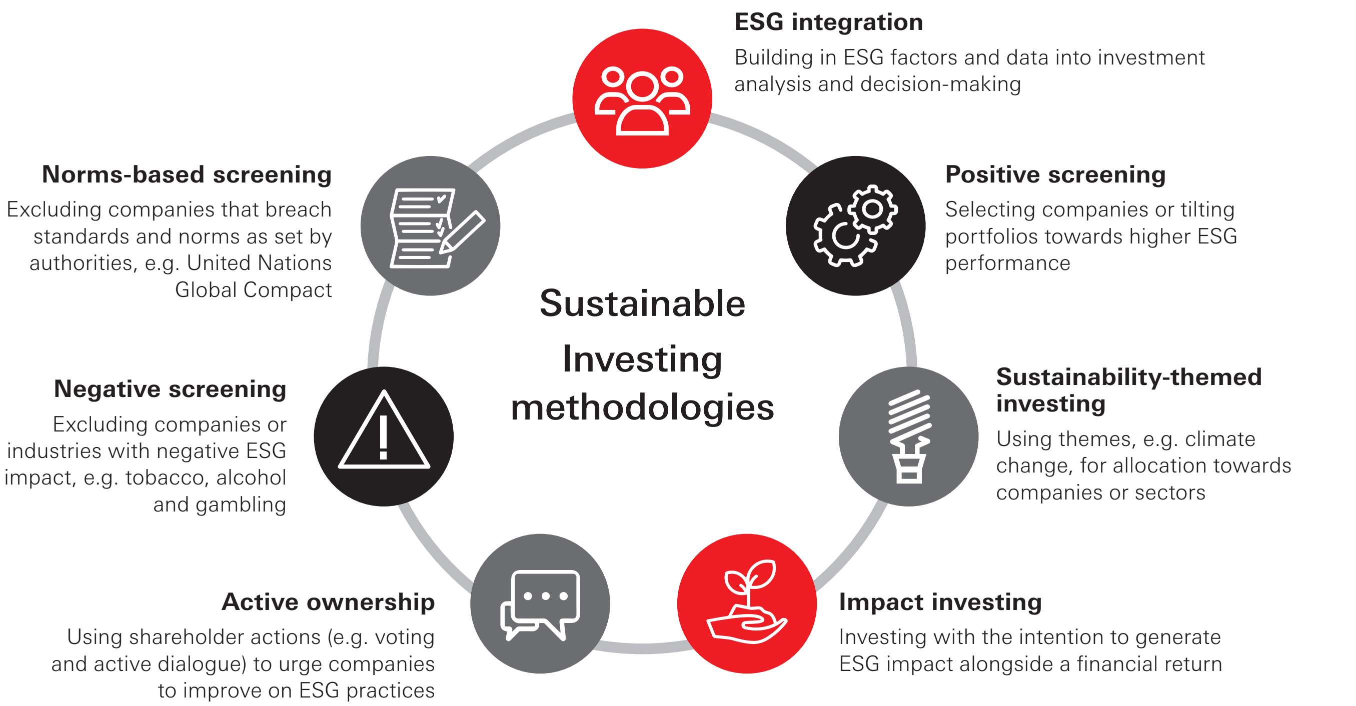
1. The Plan for a Clean Energy Revolution and Environmental Justice; joebiden.com
2. UN Framework Convention on Climate Change; an international treaty ratified by 189 territories globally to keep temperature rise to below 2 degrees C

What does climate change mean for investors?

As a global citizen, climate change can influence daily life such as becoming more energy efficient. As an investor, climate change presents material company risks that can impact share prices, but also opportunities for those companies who take measures in reducing carbon footprint. **Understanding ESG risks leads to sustainable investing, a practice with the objective to generate long-term financial returns and contributing positively to environment and society.**

Capital deployed for wealth creation can be used to tackle great challenges threatening our world today. As central banks are starting to include green bonds in quantitative easing policies, retail banks and other financial institutions have a role to play in the transition to a low-carbon economy. **Sustainable investing focuses on long term capital growth. Integrating ESG issues in investment decisions can help manage risks and unlock new investment opportunities.**

Every investor has a unique set of priorities to consider when making investment decisions. There are **many investment strategies available and often used in combination.** Investors can exclude specific companies or industries, include companies with higher ESG performance, or use sustainability themes to form as a basis for portfolio allocation. **Some common strategies** defined by Global Sustainable Investment Alliance are:



Source: Global Sustainable Investment Alliance, 2019 Report

Sustainable investing has become more essential and the **demand for solutions with positive impact is rapidly growing**: assets in sustainable funds have hit a record high of USD1,652 billion as of end 2020.

2. Source: Morningstar, "Global Sustainable Fund Flows: Q4 2020 in Review", 28 Jan 2021

What opportunities can investors explore?

At HSBC, **our sustainable investing offerings have integrated methodologies** and span across mutual funds, structured products, green bonds, etc. They are broadly categorised as:

- **ESG-enhanced**: products that invest in companies based on ESG performance (relative to a benchmark)
- **Thematic**: products that focus on themes and sectors dedicated to solving sustainability challenges and growth trends
- **Impact**: products that focus on a direct, positive and measurable impact on society and/or the environment, alongside financial returns

New opportunities could also emerge as **the finance industry embraces ESG issues**. In the US, where the green bond market is pre-dominantly Euro-denominated bonds, could change under the new administration. The Paris Agreement has also been a catalyst for increased assets flowing into climate specific funds; climate ETFs alone have quadrupled in number during the past year.

We can help you **understand how ESG issues can create and protect long-term value**. Speak to our relationship managers to explore sustainable investing opportunities that could help meet your goals.

Glossary

ESG: a set of Environmental, Social and Governance criteria that investors can apply to analyse and identify material risks and growth opportunities in investments

Green bond: a fixed income instrument issued by private companies, financial institutions and governments to fund projects with environmental and/or climate benefits

Net zero: the balance between the amount of greenhouse gases produced by society and the amount removed from the earth’s atmosphere (e.g. re-forestation to absorb carbon dioxide)

Sustainable investing: investing with the objective of generating long-term financial returns while contributing positively to environment and society

The Paris Agreement: an international treaty on climate change with a goal to keep global temperature rises in this century to below 2 degrees Celsius above pre-industrial levels; it is ratified by 189 countries and territories worldwide

Thematic investing: an investment approach that focuses on predicted long-term trends

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