CAPCO

SUSTAINABLE FINANCE

THE BIG PICTURE

SUSTAINABLE FINANCE: THE BIG PICTURE

The financial sector is vital to fund the structural changes necessary for the transition towards a zero-carbon sustainable economy as set out in the Paris Agreement[1]. Regulatory actions such as the EU Action Plan on Sustainable Finance, as well as shifts in consumer attitudes, have driven firms around the globe to integrate sustainability concerns into their business models and strategies.

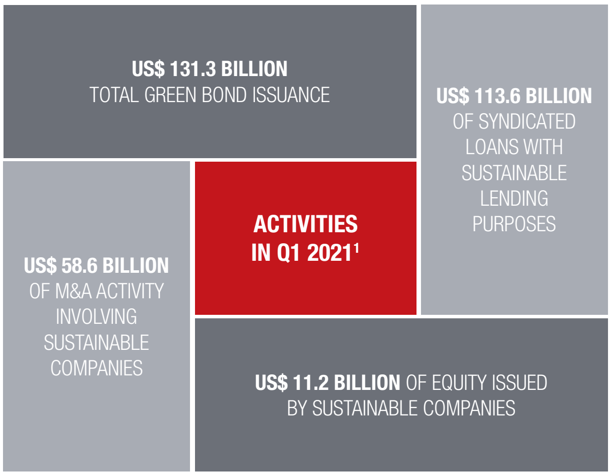
As ESG encompasses a wide variety of issues, ranging from the carbon dioxide footprint to diversity in the board of directors to corruption, the spectrum of financial products targeting these is diverse and complex. This paper provides an overview of the global market for sustainable financial products, highlights regional disparities, and explores the rationale for integrating sustainability matters in the investment selection process.

1 UNFCCC: The Paris Agreement

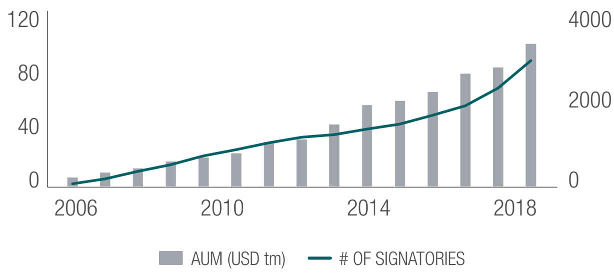
HOW DO FINANCIAL MARKETS REFLECT THE GROWING AWARENESS OF ESG MATTERS?

The market for sustainable financial products has seen significant growth in recent years, developing from a niche phenomenon to a major force in the overall financial market. The chart below provides an insight into the importance of the market for sustainable financial products:

SUSTAINABLE FINANCE MARKET OVERVIEW



NUMBER OF PRI SIGNATORIES AND AUM IN US$ TRN[2]



The Principles of Responsible Investment (PRI) are a voluntary set of investment principles that offer possible actions to incorporate ESG issues into business practice. As of 2020, 3038 asset owners and investment managers with US$ 103,4 trillion AUM were signatories of the UN PRI (Source: UN PRI, 2020).

US$ 53trn
expected global ESG AuM in 2025, representing more than a third of projected total AuM, according to Bloomberg.[3]

US$ 6.9 trn
estimated annual investments necessary up to 2030 to meet climate and development objectives (Source: OECD, 2018)[4]

79%
of global sustainable fund flows are located in Europe, showing the strong European leadership in the marke, according to Morningstar.[5]

Source: [1]Refinitiv: Reports 2021 Q1 – Sustainable Finance Review; [2]UN PRI (2020); [3]Bloomberg Intelligence (2021); [4]OECD: Financing Climate Futures: Rethinking Infrastructure Policy Highlights (2018); [5]Morningstar: Global Sustainable Fund Flows: Q1 2021 in Review

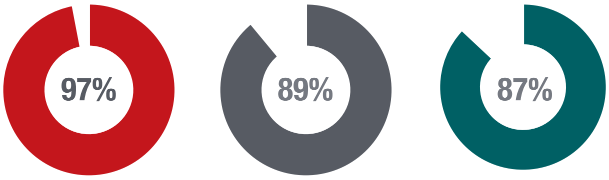
With the expected US$ 53 trillion of global ESG assets under management by 2025[2], sustainable finance presents a major opportunity, which is also demonstrated by the growth of market volumes across asset classes. The volume of sustainable finance bonds issued in Q1 2021 was US$ 286.5 billion, representing a 186 percent increase compared to Q1 2020. Similarly, the sustainable loans volume also more than doubled between these periods. Furthermore, equity issued by sustainable companies was at an all-time high in Q1 2021, with issues amounting to US$ 11.2 billion[3].

2 Bloomberg: ESG assets may hit $53 trillion by 2025, a third of global AUM (2021)
3 Refinitiv: Sustainable finance continues surge in Q1 2021

WHAT ARE THE MAJOR DRIVERS OF GROWTH FOR THE SUSTAINABLE FINANCE MARKET?

There are several factors for including sustainability concerns in the investment decision-making process. Besides the alignment of investments with organizational values, there are also pecuniary reasons for the integration of ESG information. The following chart provides an insight into the perception of issuers and investors of sustainable investing:

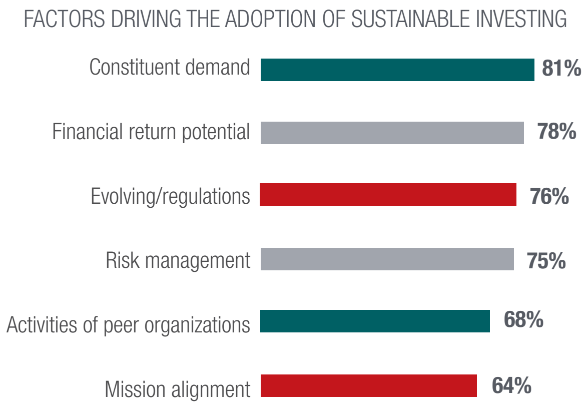
MARKET PERCEPTION OF SUSTAINABLE INVESTING



Almost all issuers of securities expect to redeploy capital in response to environmental and social challenges and opportunities over the next five years (HSBC Survey, 2020)[1].

The vast majority of investors perceive environmental and social issues as important or very important (HSBC Survey, 2020)[1].

The majority of investors perceive that the COVID-19 pandemic has changed how they consider ESG issues in their investments (HSBC Survey, 2020)[1].



Percentage of asset owners considering the factor extremely or somewhat important (Morgan Stanley, 2020)[2]

Perceived materiality of ESG information[3]

97%
The vast majority of investors deem non-financial information material to investment decision making because it affects a company´s reputation and brand.

93%
Perceive non-financial information as material for investment decision making as it exposes potential threats of litigation and regulatory intervention.

85%
Agree that non-financial information signals a company´s long-term approach to business strategy and is thus material.

Sources: [1]HSBC Sustainable Financing and Investment Survey 2020, [2]Morgan Stanley: Sustainable Signals: Asset Owners See Sustainability as Core to the Future of Investing (2020); [3]Amel-Zadeh, Amir, and George Serafeim. "Why and How Investors Use ESG Information: Evidence from a Global Survey." Harvard Business School Working Paper, No. 17-079, February 2017

As evidenced by 76 percent of asset owners citing evolving policy and regulations as an important factor driving the adoption of sustainable investing[4], the regulatory focus on the risks associated with climate change is a major contributor to the increasing significance of sustainable financial products. As pointed out by the Bank for International Settlements (BIS), climate related risks and the associated so-called "green swan" events can potentially be extremely disruptive for the financial sector, jeopardizing the stability of the financial system.[5] Thus, future regulation will continue to focus on sustainability matters and thereby fuel future growth of the market.

Moreover, the steadily increasing quality of sustainability reporting is of substantial importance for the sustainable finance market, as currently 53 percent of investors interested in allocating their assets based on ESG criteria perceive poor data quality

4 Morgan Stanley: Sustainable Signals: Asset Owners See Sustainability as Core to the Future of Investing (2020)
5 Bolton, P., Despres, M., Da Silva, L. A. P., Samama, F., & Svartzman, R. (2020). The green swan

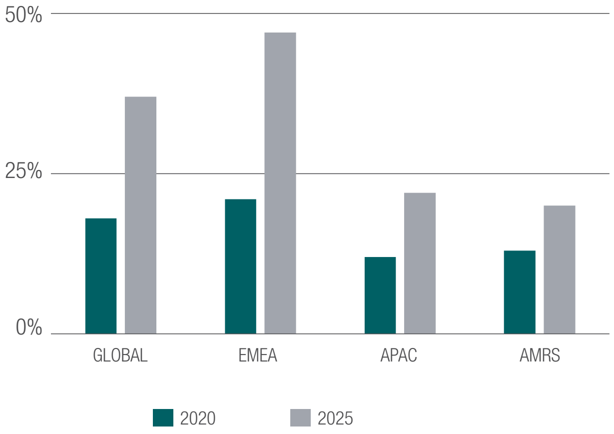
or availability of ESG data as a major challenge.[6] With the EU progressing the regulatory framework for sustainability disclosures with the proposed reform of the Non-Financial Reporting Directive (NFRD), data quality and availability will increase substantially in the near future. Other geographies are also making significant progress on the reporting of non-financial information, with more than 1,500 organizations globally supporting the Task Force on Climate-related Financial Disclosures (TCFD) recommendations. The increasing availability of ESG data represents a significant opportunity for investors as it allows to reliably measure and compare the ESG performance of companies.

Other major forces driving future growth of the market for sustainable finance are the varying attitudes towards sustainable investing and the generational wealth transfer. Whilst 74 percent of millennials want to achieve a positive social impact with their investments, only 68 percent of baby boomers agree on that[7]. Considering that for the US in Q4 2020, 52.7 percent of household wealth was owned by baby boomers, and only 4.8 percent by millennials[8], the difference in attitudes might have a significant impact on the market for sustainable financial products, once wealth is passed down through the generations.

HOW DOES THE PERCEPTION OF ESG DIFFER AMONG GEOGRAPHIES?

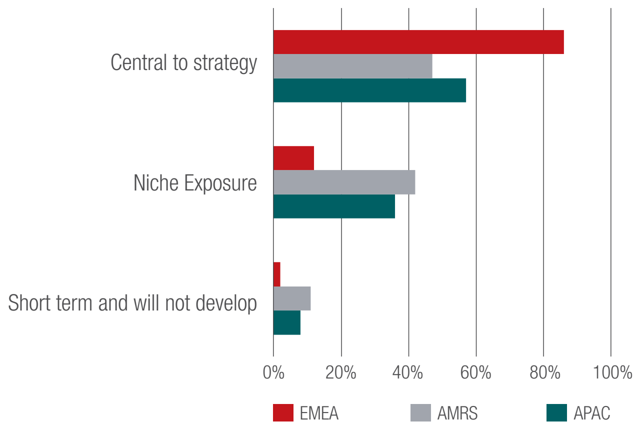
The perception of investors and issuers of securities on the future importance of sustainability matters differs strongly across geographies, with some market participants perceiving the development as only a short-term trend, whilst others expect the development to be of a long-term nature. The chart below illustrates how market participants in different geographies perceive the importance of sustainable investing:

PERCENTAGE INVESTED SUSTAINABLY



Sustainable investments defined as portfolios with a distinct ESG objective, applying exclusionary screening criteria or optimizing towards ESG (Source: BlackRock 2020 Global Sustainable Investing Survey)

LONG-TERM DIRECTION OF SUSTAINABLE INVESTING



There are strong regional differences in the perception of long-term sustainable investing. Importantly. Globally only 5% of investors believe that sustainable investing is only a short-term trend, showing the long-term perspective most investors take in these matters (Source: BlackRock 2020 Global Sustainable Investing Survey).

6 BlackRock 2020 Global Sustainable Investing Survey
7 Natixis 2021 ESG Investor Insights Report
8 Federal Reserve: Distribution of Household Wealth in the U.S. since 1989

The regional disparities for sustainable finance become evident when analysing the expected share of sustainable investment. Whilst American investors expect this share to be at 20 percent in 2025, EMEA investors expect 47 percent of their investments to be made with consideration of ESG aspects.[9] One major reason for this is the regulatory attention the EU devotes to sustainable finance. Channelling private investment into areas driving the transition towards net-zero emissions is one key element of the European Green Deal, aiming to make the EU climate-neutral by 2050.

However, President Biden's Executive Order on Tackling the Climate Crisis[10] will impact investments made in sustainable finance by US investors. In particular, the US Climate Finance Plan[11], which aims to mobilize capital to assist developing countries in their transition towards a climate-resilient, sustainable economy might create major opportunities in the global sustainable finance market. Notably, 11 percent of American investors still consider sustainable investing as a short-term trend that will not develop further, standing in stark contrast to the direction the regulation is taking[9].

HOW CAN ESG MATTERS BE REFLECTED IN THE INVESTMENT APPROACH?

As the size of the sustainable finance market has grown, several approaches for including ESG information in the investment strategy have emerged in the financial industry, ranging from exclusions based on norms or other criteria to impact investing with the goal of achieving ecological or social effect in addition to financial returns. The chart below illustrates the most important approaches investors follow:

SUSTAINABLE INVESTING APPROACHES

EXCLUSIONARY SCREENING

- Excluding investment projects that do not comply with social or environmental criteria
- Avoiding investments in companies engaged in undesirable activities
- Examples may include exclusions of companies in the tobacco or gambling industry

US$ 19.8 trn

ESG INTEGRATION

- Inclusion of ESG issues in the investment analysis
- Assessing the impact of material ESG factors on future cash flows, growth rates and competitive position
- Examples may include vulnerability to climate change, board diversity and labor relations

US$ 17.5 trn

BEST-IN-CLASS SCREENING

- Selecting those investment opportunities, where the company performs better for selected sustainability criteria
- There is a possibility that projects are selected, which, viewed in an absolute context, would not be considered sustainable

US$ 1.8 trn

THEMATIC ESG INVESTING

- Identifying investment opportunities best positioned to profit from structural trends such as water management and climate change
- Focusing on specific issues (investments could have weak performance on other ESG criteria)

US$ 1 trn

IMPACT INVESTING

- Aiming to achieve social or environmental effects in addition to financial returns
- Impact measurement based on defined objectives and performance targets

US$ 444 bn

Market Volumes as of 2018, Source: Global Sustainable Investment Alliance, 2018 Global Sustainable Investment Review

9 BlackRock 2020 Global Sustainable Investing Survey
10 White House: Executive Order on Tackling the Climate Crisis at Home and Abroad
11 US International Climate Finance Plan

Interestingly, despite the widespread use, investors perceive negative screening as the least investment beneficial, with the integration of ESG matters into the investment analysis process and best-in-class screenings considered to be more beneficial.[12] As investors implementing negative screening refrain from investing in certain industries such as gambling or tobacco, they do miss out on the higher expected returns these so-called "sin" stocks achieve.[13]

Research on how integrating ESG concerns into the asset allocation decision process affects performance does not provide a definite answer. El Ghoul and Karoui (2017) provide two competing hypotheses on how integrating ESG concerns in the investment decision-making can affect returns. On the one hand, screening by ESG factors reduces the number of investment opportunities and increases monitoring costs, reducing returns. However, on the other hand, by targeting sustainable companies, fund managers may be selecting firms with strong financial fundamentals, resulting in better fund performance. One study suggests that an increase in the level of corporate social responsibility comes at the expense of reduction in risk-adjusted performance for mutual funds, however investors in more socially responsible funds are less sensitive to performance.[14]

HOW IS THE EQUITY MARKET AFFECTED BY ESG?

With more than US$ 11.2 billion of equity issues by sustainable companies[15], the market for equity issued by companies with a sustainable business model is still rather small, when compared to the overall volume of equity issuances of US$ 348 billion in Q1 2021[16]. However, the interest of the stock market in issuances such as the US$ 2 billion capital raise by Plug Power[17], a company developing fuel cell systems for e-mobility, clearly shows that there is a demand for equity by sustainable companies. More important, however, is the effect ESG matters can have for the overall market.

Currently, scientific research does not unanimously agree on whether ESG factors affect corporate financial performance positively or negatively. However, a meta study combining the findings of more than 2000 empirical studies found a non-negative relation between ESG criteria and corporate financial performance in 90 percent of the reviewed findings.[18]

For instance, Cheng et al. (2014) show that firms which perform better for CSR metrics face lower capital constraints.[19] The authors argue that this relation materializes via two distinct mechanisms. Firstly, as better CSR performance is associated with superior stakeholder engagement, managers adopt a long-term rather than a short-term orientation, reducing potential agency costs. Secondly, public disclosure of CSR activities decreases informational asymmetries between investors and firms, reducing perceived risk. In addition, Lamont et al. (2001) show that capital constraints affect firm value because a financially constrained firm is unable to finance all potentially profitable investment projects, resulting in lower returns.[20]

Khan et al. (2016) show that when differentiating between investments companies made in material and immaterial sustainability issues, firms with good performance on the material

12 Amel-Zadeh, Amir, and George Serafeim. "Why and how investors use ESG information: Evidence from a global survey." Financial Analysts Journal 74.3 (2018): 87-103.
13 Hong, Harrison, and Marcin Kacperczyk. "The price of sin: The effects of social norms on markets." Journal of financial economics 93.1 (2009): 15-36.
14 El Ghoul, Sadok, and Aymen Karoui. "Does corporate social responsibility affect mutual fund performance and flows?." Journal of Banking & Finance 77 (2017): 53-63.
15 Refinitiv: Sustainable finance continues surge in Q1 2021
16 S&P Global Market Intelligence: Q1 2021 M&A and Equity offerings report
17 Plug Power Press Release Details
18 Friede, Gunnar, Timo Busch, and Alexander Bassen. "ESG and financial performance: aggregated evidence from more than 2000 empirical studies." Journal of Sustainable Finance & Investment 5.4 (2015): 210-233.
19 Cheng, Beiting, Ioannis Ioannou, and George Serafeim. "Corporate social responsibility and access to finance." Strategic management journal 35.1 (2014): 1-23.
20 Lamont, Owen, Christopher Polk, and Jes s Saa -Requejo. "Financial constraints and stock returns." The review of financial studies 14.2 (2001): 529-554.

sustainability issues outperform those with poor performance on these issues, suggesting that investments in sustainability issues can be shareholder-value enhancing. Moreover, it is shown that investments in immaterial sustainability issues have little positive or negative value implications.[21]

Following Cornell and Damodaran (2020)[22], we propose a more nuanced view on investments in sustainability matters. For some firms, investment in corporate social responsibility offers tangible financial benefits, whilst for others they only create additional costs with no offsetting benefits. Therefore, the discussion on whether an investment in sustainability matters is financially viable needs to be done on an individual project and firm basis.

HOW DO ESG CONSIDERATIONS AFFECT M&A ACTIVITIES?

In Q1 2021, global M&A activity involving sustainable companies amounted to US$ 58.6 billion, clearly showing that transactions related to sustainable companies are of significant size.[23] However, when considering that the total value of M&A activities announced in Q1 2021 was at US$ 409 billion for North America alone[24], sustainable transactions currently account for only a small part of the overall market.

Nonetheless, ESG considerations are becoming increasingly important in M&A decision-making, in particular because poor performance for ESG metrics of a target company can pose significant litigation, regulatory and reputational risks for the acquiring company.

In a survey among private equity, asset management and corporate executives, 90 percent of respondents stated that they conduct an ESG due diligence as part of the M&A process, with 67 precent citing business risk including potential litigation as the most important motive for taking ESG into account.[25]

In the context of M&A due diligence, key ESG risks such as climate change, greenhouse gas emissions, diversity and labour practices are evaluated. Notably the list of risks included in the analysis continues to be extended as more ESG information becomes available. To mitigate the risks resulting from misconduct allegations, an increasing number of M&A agreements also contain so-called “Weinstein Clauses” requiring the target to disclose misconduct allegations before the acquisition is closed.

It is important to note that 77 percent of respondents stated that a negative assessment of ESG factors lowers the valuation significantly, demonstrating the need for the acquiring party to invest into restructuring and repositioning the acquisition target if it performs poorly on ESG aspects.[26]

21 Khan, Mozaffar, George Serafeim, and Aaron Yoon. “Corporate sustainability: First evidence on materiality.” The accounting review 91.6 (2016): 1697-1724.
22 Cornell, Bradford, and Aswath Damodaran. “Valuing ESG: Doing good or sounding good?.” Available at SSRN 3557432 (2020).
23 Refinitiv: Sustainable finance continues surge in Q1 2021
24 S&P Global Market Intelligence: North American M&A surges in Q1 to 2nd-highest deal volume this century
25 IHS Markit: ESG on the Rise: Making an impact in M&A
26 Ehlers, Torsten, and Frank Packer. “Green bond finance and certification.” BIS Quarterly Review September (2017).

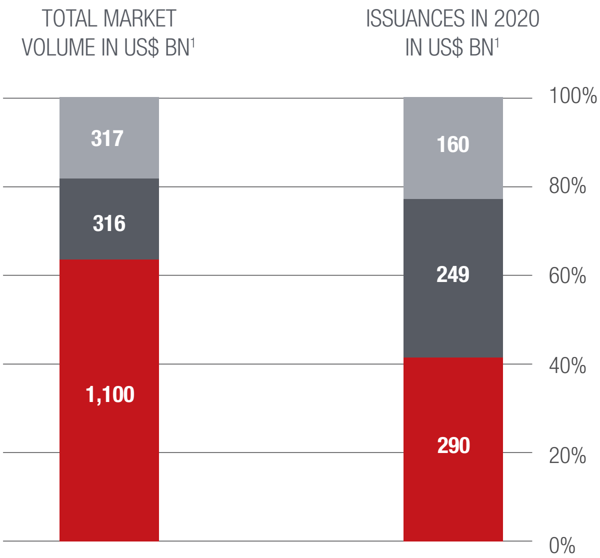
HOW ARE ESG MATTERS REFLECTED IN THE BOND MARKET?

The market for Green Bonds has seen strong growth in the recent years, with companies such as Volkswagen and Unilever issuing Green Bonds to finance their transition to a climate resilient business model. In addition, sovereign green bond issues by the Netherlands, France and Germany show the commitment of the national governments to stimulate the market with these issues certainly having signalling power for the wider financial markets.

However, particularly in light of the COVID-19 pandemic, social bonds have also gained in importance, as social differences have further increased. The chart below provides a more detailed illustration of the market for Green, Social and Sustainable (GSS) Bonds:

SUSTAINABLE DEBT

GREEN BONDS	SOCIAL BONDS	SUSTAINABILITY BONDS
• Proceeds are used to finance climate- or environment-related projects in the areas of: – Energy efficiency & renewable energy – Pollution prevention and control – Clean transportation • Major issuers: Daimler, Volkswagen, Unilever, Apple	• Proceeds are used to finance social welfare investments for an identified target population, projects funded may be in the areas of: – Affordable basic infrastructure / housing – Access to essential services – Employment generation • Major issuers: Bank of America, CaixaBank, LBBW	• Bonds financing a combination of both Green and Social projects, expected to provide both environmental and social benefits • Offer a greater flexibility to issuers as they include a more diverse set of eligible investment categories • Major issuers: Burberry, Alphabet, Starbucks



Source: [1]Climate Bonds Initiative: Sustainable Debt Global State of the Market 2020

Risk characteristics of a green bond are essentially identical to those of a conventional bond issued by the same organization, however the majority of studies show that issues of green bonds on average face lower spreads, as an increasing number of investors prefer holding green bonds due to their sustainability promises. However, not all green bond issues are priced at a premium, with some of them priced at spreads above the matched conventional bonds.[26]

Bachelet et al. (2019) demonstrate that for an issuer to realize lower funding costs, an established reputation or a verification of the sustainability claims is necessary, in order to reduce asymmetric information and to guarantee investors that no greenwashing is taking place.[27]

26 Ehlers, Torsten, and Frank Packer. "Green bond finance and certification." BIS Quarterly Review September (2017).

27 Bachelet, Maria Jua, Leonardo Becchetti, and Stefano Manfredonia. "The green bonds premium puzzle: The role of issuer characteristics and third-party verification." Sustainability 11.4 (2019): 1098.

HOW WILL REGULATION AFFECT THE FUTURE OF THE SUSTAINABLE BOND MARKETS?

Currently the Principles for green, social and sustainability bonds issued by the International Capital Markets Association (ICMA) play a major role as best-practice standards in the industry. However, the Principles issued by the ICMA are only recommendations to be adopted on a voluntary basis.

One important regulatory initiative impacting the market for sustainable bonds are the EU Green Bond Standards (EU GBS) proposed in the EU action plan on sustainable finance adopted by the Commission in 2018. The ultimate decision on how and in what legal form the EU GBS is implemented, will be part of the Renewed Sustainable Finance Strategy of the European Commission, which is expected to be published shortly.

Nonetheless, the report on an EU GBS by the Technical Expert Group (TEG)[28] on sustainable finance does give some indication on what the upcoming EU GBS might look like. The proposed EU GBS demand that the proceeds of an EU Green Bond issuance are invested into projects aligned with the EU Taxonomy. As the Taxonomy regulation already demands from companies disclosing non-financial information to include information on their Taxonomy-aligned activities, the insights gained from that analysis can be further processed when issuing EU Green Bonds, facilitating the classification of investment projects for issuers. Moreover, the alignment with the EU GBS needs to be externally verified, reducing the information asymmetry between issuer and investor.

Importantly, the proposal foresees that the EU GBS are voluntary standards, thus issuers not willing to use the term "EU Green Bond" are not obliged to follow the EU GBS, with non-EU issuers also having the option to issue bonds under the framework. Integrating the EU GBS within the EU framework for sustainable finance will certainly be beneficial for the green bond market within the EU, providing greater clarity and consistency on what constitutes a green project.

28 Technical Expert Group: Usability Guide EU Green Bond Standard

HOW IS THE LOAN MARKET AFFECTED BY THE INCREASING AWARENESS OF ESG CHARACTERISTICS?

ESG matters are also relevant for pricing loans, as severe ESG issues can result in financial distress, directly impacting a firm's ability to repay creditors. This hypothesis is supported by Goss and Roberts (2011) finding a premium averaging between 7 and 18 basis points for firms with below average ESG records. Especially for unsecured loans, lenders are more sensitive for CSR concerns.[29]

Particularly for investments in carbon-intensive industries such as the oil industry or manufacturing transitory risks play an important role for future profitability. Capasso et al. (2020) indicate that carbon-intense companies face a higher probability of default as their future cash-flows are likely to be affected by progressively stricter climate-related regulations.[30]

Following Ehlers et al. (2021), these risks of climate policy changes aiming to reduce Carbon dioxide emissions are reflected in the pricing of syndicated loans resulting in a loan risk premium for carbon-intensive borrowers. However, the risk premium is not sufficient to fully internalize the potential impact on repayment capabilities by the introduction of carbon taxes. Moreover, as only Scope 1 emissions are priced, the transition risks arising for companies depending on carbon-intensive inputs in their production process are not properly captured.[31]

In view of the unique access to information credit institutions have, taking sustainability information into consideration in loan pricing is necessary to mitigate and efficiently price the risks associated with ESG matters. Sustainability-linked loans offer the opportunity to integrate ESG concerns in the contractual terms of a loan by incorporate pricing mechanisms incentivizing improvements for specific sustainability metrics. In February 2021, Anheuser-Busch InBev announced a US$ 10.1 billion sustainability linked revolving credit facility, with pricing linked to improvements in the areas of water efficiency, recycling, renewable energy and reducing GHG emissions.[32]

29 Goss, Allen, and Gordon S. Roberts. "The impact of corporate social responsibility on the cost of bank loans." Journal of Banking & Finance 35.7 (2011): 1794-1810.
30 Capasso, Giusy, Gianfranco Gianfrate, and Marco Spinelli. "Climate change and credit risk." Journal of Cleaner Production 266 (2020): 121634.
31 Ehlers, Torsten, Frank Packer, and Kathrin de Greiff. "The pricing of carbon risk in syndicated loans: which risks are priced and why?." Journal of Banking & Finance (2021): 106180.
32 ABInBev Press Release

HOW DID THE COVID-19 PANDEMIC AFFECT THE MARKET FOR SUSTAINABLE FINANCE?

Social inequality was exacerbated by the COVID-19 pandemic, with the World Food Programme (WFP) indicating that the lives and livelihood of an additional 130 million people are at risk due to the effects of the pandemic, nearly doubling the number estimated prior to the emergence of the pandemic.[33]

In a Capco webinar on the regulatory perspective of ESG, Frank Pierschel, Chief Sustainable Finance Officer at BaFin (Germany's Financial Supervisory Authority) drew attention to this social risk dimension of the COVID-19 pandemic:

"Corona as a (massively materialized) social transition risk has clearly shown us that it can come much faster, entail massive policy decisions, and emerge in a materiality that threatens financial market stability."

As investors are increasingly taking the social and environmental implications of their investments into account, the rise in social risks as a result of the pandemic was reflected by a surge in the social bond market. The volume of issuances reached US$ 249 billion, representing a ten-fold increase on the prior year. Pandemic bonds substantially contributed to this, accounting for 34 percent of social bond issuances in 2020.[34]

Moreover, with several ESG exchange-traded funds and mutual funds outperforming the broader market during the COVID-19 pandemic[35], the business case for investing sustainably has gotten even stronger during the pandemic.

As the pandemic slowly begins to weaken with the vaccination campaigns taking effect, governments around the globe are concerned with the question of how the economic recovery from the pandemic-related losses should be carried out. The recent G7 summit expressed in their joint statement the need for recovery plans to address ESG issues:

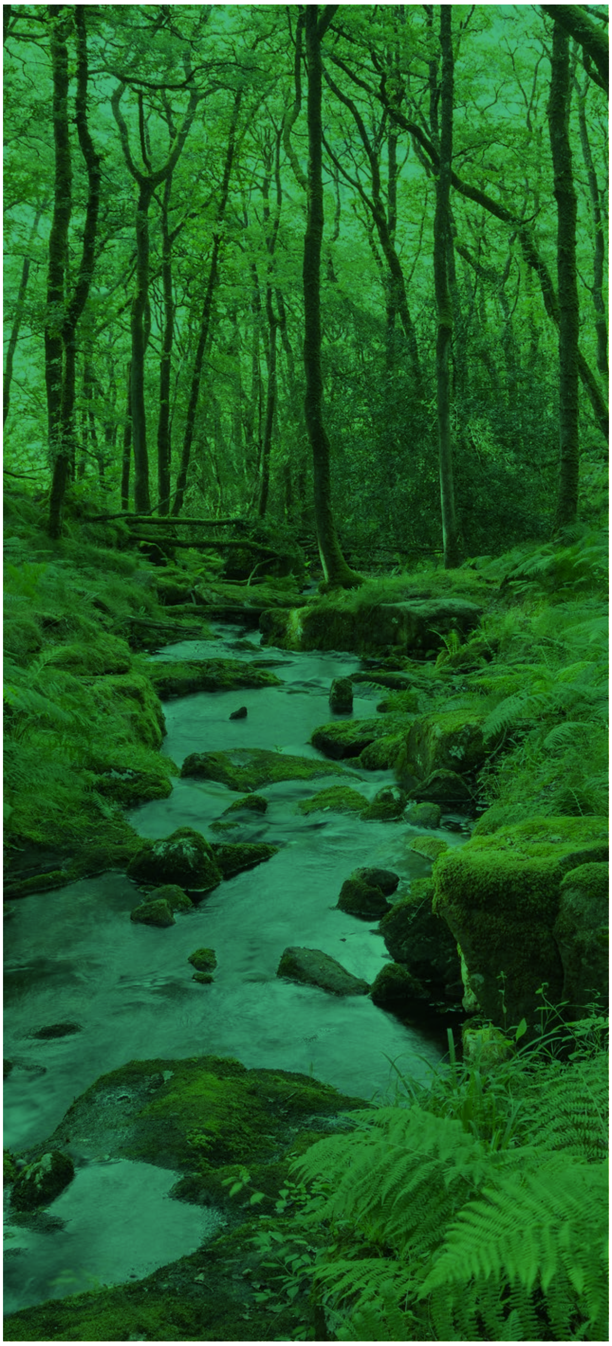
"Our plans for the recovery from COVID-19 need to put us on a path to strong, sustainable, balanced, inclusive and resilient growth by not only addressing the immediate challenges arising from the pandemic, but also the long-term shifts in the global economy and society, including demographic, technological, and environmental trends, and inequalities between and within countries, many of which have been magnified by the COVID-19 pandemic."

The so-called green recovery is already taking place, with the Organization for Economic Co-operation and Development (OECD) estimating that within COVID-19 recovery measures, US$ 336 billion have been allocated to environmentally positive measures.[36] This support by public policy measures will certainly further stimulate the market for sustainable finance.

33 WFP: Risk of hunger pandemic as coronavirus set to almost double acute hunger by end 2020
34 Climate Bonds Initiative: Sustainable Debt Global State of the Market 2020
35 S&P Global Market Intelligence: ESG funds beat out S&P 500
36 OECD: Focus on green recovery

CONCLUSION

Environmental issues are currently at the forefront of sustainable investing with 88 percent of investors prioritizing the environmental aspects of ESG in comparison to social and governance matters.[37] However, the COVID-19 pandemic has clearly shown the need for investments to be made with social objectives.



As we have demonstrated, ESG considerations will be relevant for all investors, regardless of whether they pursue sustainable investing as an objective or not. Higher cost of equity and debt capital for companies subject to exclusions due to environmental screens are an important driver of sustainable economic activities as they have the potential to cause companies to internalize their environmental externalities.[38] Mark Carney, the United Nations special envoy for climate action and finance emphasized in a speech at a European Commission Conference:[39]

"Financial policymakers will not drive the transition to a low-carbon economy. Governments will establish the climate policy frameworks, and the private sector will make the necessary investments."

Therefore, integrating sustainability considerations into the investment analysis process, business model and business strategy is key to capture the opportunities sustainable finance presents, but also to achieve the goals laid down in the Paris agreement.

Despite the many reasons for considering sustainability matters in the investment process, effectively implementing them in the investment decision-making process and in risk management remains challenging.

Contact us to learn more about how we can leverage the increasing availability of sustainability information for your institution and how to set up the necessary environment for data management and analysis. Take advantage of the opportunities that the shift towards sustainable growth offers your organization.

36 OECD: Focus on green recovery
37 BlackRock 2020 Global Sustainable Investing Survey
38 Chava, Sudheer. "Environmental externalities and cost of capital." Management Science 60.9 (2014): 2223-2247.
39 Carney, Mark. "A new horizon." Speech at the European Commission Conference: A global approach to sustainable finance, Brussels, March 2019.
38 Chava, Sudheer. "Environmental externalities and cost of capital." Management Science 60.9 (2014): 2223-2247.
39 Carney, Mark. "A new horizon." Speech at the European Commission Conference: A global approach to sustainable finance, Brussels, March 2019.

AUTHORS

Philipp Binz and **Marcus Fleig**

CONTACT

Dr. Olaf Clemens, Partner
T: +49 69 9760 9076
M: +49 172 746 7502
E: Olaf.Clemens@capco.com

ABOUT CAPCO

Capco is a global technology and management consultancy dedicated to the financial services industry. Our professionals combine innovative thinking with unrivalled industry knowledge to offer our clients consulting expertise, complex technology and package integration, transformation delivery, and managed services, to move their organizations forward.

Through our collaborative and efficient approach, we help our clients successfully innovate, increase revenue, manage risk and regulatory change, reduce costs, and enhance controls. We specialize primarily in banking, capital markets, wealth and asset management and insurance. We also have an energy consulting practice in the US. We serve our clients from offices in leading financial centers across the Americas, Europe, and Asia Pacific.

To learn more, visit our web site at www.capco.com, or follow us on Twitter, Facebook, YouTube, LinkedIn, Instagram and Xing.

WORLDWIDE OFFICES

APAC
Bangalore
Bangkok
Gurgaon
Hong Kong
Kuala Lumpur
Mumbai
Pune
Singapore

EUROPE
Berlin
Bratislava
Brussels
Dusseldorf
Edinburgh
Frankfurt
Geneva
London
Munich
Paris
Vienna
Warsaw
Zurich

NORTH AMERICA
Charlotte
Chicago
Dallas
Hartford
Houston
New York
Orlando
Toronto
Tysons Corner
Washington, DC

SOUTH AMERICA
São Paulo

WWW.CAPCO.COM