

Are ESG labels valid?

Or, are we seeing “Green-washing”?

Brenda Bloch-Young, November 3, 2021

ESG labels in investing

An investment theme almost everyone supports

- Who decides what investment deserves the ESG label?
- Are there defined standards?
- Should there be standards?
- Many funds have been rebranded as ESG with little or no change in the equities owned.
- Companies often judged on what they say rather than what they do.

ESG is overly weighted to tech and software

Underweight in healthcare

- ESG often has few employees
- Minimal plant and equipment
- No oil & gas, limited if any manufacturing
- Many clean energy ETFs are deemed as high risk due to size and financing
- The “E” is fairly easy to rate, but “S” and “G”?

Fig 22: Top 20 holdings (all funds)

| Company | Exposure |
|--------------------|-----------------|
| Microsoft | 2.98% |
| Apple | 2.42% |
| Amazon | 2.14% |
| Alphabet | 2.04% |
| Facebook | 1.33% |
| Tesla | 0.81% |
| JP Morgan | 0.78% |
| UnitedHealth Group | 0.75% |
| Visa | 0.67% |
| TSMC | 0.67% |
| Johnson & Johnson | 0.60% |
| Mastercard | 0.57% |
| Comcast | 0.55% |
| NVIDIA | 0.54% |
| Paypal | 0.53% |
| Netflix | 0.53% |
| Broadcom | 0.51% |
| Bank of America | 0.51% |
| Berkshire Hathaway | 0.51% |
| Home Depot | 0.49% |

Fig 23: Top 20 holdings (sustainable funds)

| Company | Exposure |
|-------------------|-----------------|
| Microsoft | 3.60% |
| Apple | 2.66% |
| Alphabet | 2.35% |
| Amazon | 2.13% |
| Mastercard | 1.20% |
| Adobe | 1.00% |
| Visa | 0.92% |
| Danaher | 0.89% |
| S&P Global | 0.86% |
| Tesla | 0.84% |
| TSMC | 0.82% |
| Deere & Co. | 0.73% |
| NVIDIA | 0.72% |
| Applied Materials | 0.70% |
| Verizon | 0.68% |
| Procter & Gamble | 0.68% |
| Facebook | 0.67% |
| Linde | 0.66% |
| Comcast | 0.65% |
| Texas Instruments | 0.64% |

SDG

Sustainable Development Goals

Securing economic development, social equity and justice, and environmental protection is the goal of sustainable development. Although these three factors can work in harmony, they are often found to conflict with one another.

Established by the United Nations in 2015 with 17 criteria hopefully achieved by 2030.

UN's Sustainable Goals

<https://www.un.org/development/desa/disabilities/envision2030.html>

[GOAL 1: No Poverty](#)

[GOAL 2: Zero Hunger](#)

[GOAL 3: Good Health and Well-being](#)

[GOAL 4: Quality Education](#)

[GOAL 5: Gender Equality](#)

[GOAL 6: Clean Water and Sanitation](#)

[GOAL 7: Affordable and Clean Energy](#)

GOAL 8: Decent Work and Economic Growth

GOAL 9: Industry, Innovation and Infrastructure

GOAL 10: Reduced Inequality

GOAL 11: Sustainable Cities and Communities

GOAL 12: Responsible Consumption and Production

GOAL 13: Climate Action

GOAL 14: Life Below Water

GOAL 15: Life on Land

GOAL 16: Peace and Justice Strong Institutions

GOAL 17: Partnerships to achieve the Goal

Morningstar Sustainable Investing

<https://www.morningstar.com/topics/sustainable-investing>

- New sustainable funds reached an all-time high in the 3rd quarter
- What is Green-washing?
- Top fund returns
- Morningstar's ESG framework

EU's definition of Sustainable Finance

https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en#next

“Sustainable finance refers to the process of taking **environmental, social and governance (ESG) considerations** into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects. **Environmental considerations** might include climate change mitigation and adaptation, as well as the environment more broadly, for instance the preservation of biodiversity, pollution prevention and the circular economy. **Social considerations** could refer to issues of inequality, inclusiveness, labour relations, investment in human capital and communities, as well as human rights issues. The **governance** of public and private institutions – including management structures, employee relations and executive remuneration – plays a fundamental role in ensuring the inclusion of social and environmental considerations in the decision-making process.

In the EU's policy context, sustainable finance is understood as finance to support economic growth while reducing pressures on the environment and taking into account social and governance aspects. Sustainable finance also encompasses transparency when it comes to risks related to ESG factors that may have an impact on the financial system, and the mitigation of such risks through the appropriate governance of financial and corporate actors.”

Current labels may be problematic

Contradictory opinions on the use of Sustainable versus ESG

- Your portfolio may already be biased toward ESG if your allocations weigh heavily on tech and software
- The EU is working on a measurable criteria for funds to use the ESG label
- Large fund firms generally vote proxies according to management recommendations for the shares they own - analysis of Vanguard proxy votes, only 43% were for climate initiative proposals.

Questions?

Sources: Util.co, Bloomberg, MIT Tech Review, Morningstar