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A Banor sim research project illustrates the relationship between the performance of the bond market and ESG ratings in Europe

How important is good governance for corporate bonds?

BY ESTER CORVI

"ESG (Environment, Social & Governance, *Ed.*) rating has an effect on the expected yield of a corporate bond. From a comparison between the more liquid listed bonds and their performance, we noted that performance is higher for bonds that are linked with better ESG practices. A rule that holds true above all for high yield bonds," said Angelo Meda, manager in charge of the research at Banor sim. Of the three ESG factors, the determining parameter is without a doubt t linked to good governance, while environmental and social factors seem to push in the opposite direction. To conduct the research, "We adopted the same approach and the same methodology used by Harvard Business School Professor George Serafeim, who is an authority on Responsible Investment and who has been analysing the phenomenon and the correlation between ESG criteria and market performance for years," said Massimiliano Cagliero, founder and Managing Director of Banor sim, during the conference that took place yesterday in Rome.

"In 2018, we focused on analysing the stock market,
while this year, we wanted to explore the other side of the market, bonds, where our customers have traditionally always been very active," said Caglierò. Attending the convention, organised by Banor sim were George Serafeim from the Harvard Business School, Alessandro Tappi, the Chief Investment Officer of the European Investment Fund and Giancarlo Giudici from Politecnico di Milano School of Management, who coordinated the study. The analysis involved 536 bonds listed on European markets and issued by 146 medium to large companies between January 2014 and December 2018. The analysis shows that securities associated with good ESG practices perform better, above all in recent times, and particularly high yield securities. As already highlighted, the most discriminating parameter is linked to good governance, while the environment and social factors seem to be perceived as less relevant for investors who are interested in reducing the risk of insolvency in the short term. "Some of our hypotheses were confirmed, but the study has clarified some aspects. We did expect that the integration of ESG assessments in asset allocation could improve the quality of the value approach analyses that we follow, but, on the other hand, the fact that the three variables are not in synch with each other was an unexpected result that we shall take into account in future," emphasised Meda.

In the current phase of high turbulence in the markets due to the commercial war between the United States and China, international tension (Iran, Syria, Yemen, Saudi Arabia) and the unknowns linked with the results of the forthcoming European elections, Banor sim experts have adopted a prudent approach that favours liquidity, allowing for rapid movement, depending on the direction that financial markets will take.

The manager of Banor sim research concluded by saying, "ESG analysis is gaining increasing importance, so much so that it is adopted alongside the fundamental analysis to assess companies for the purpose of forecasting performance".