SRI-IMPACT INVESTING | BANOR | ESG

ESG, good practice equals better performance

- **According to the report, the determining factor is, without doubt, the one linked to good governance, while environmental and social factors seem to push in the opposite direction**
- **For Giancarlo Giudici of Politecnico di Milano, "It is therefore essential for asset managers to study the market and be ready for this new challenge."**

The latest study conducted by Banor Sim and the Politecnico di Milano School of Management gives a signal to the markets. In the European Bond Market, there is a close positive link between ESG criteria and high yields

The ESG rating has an effect on expected yield, even in the European bond market—especially so in recent years. And bonds associated with better sustainability practices have performed better, particularly so for high yield bonds. These are just a couple of examples of the evidence that emerges from the last study conducted by **Banor Sim** and the **Politecnico di Milano School of Management** on the relationship that exists in Europe between the bond market and ESG ratings.

Among the letters—and the criteria—that define ESG analysis (environmental, social and governance), **the most discriminating parameter is linked to good governance**, while the environmental and social factors seem to push in the opposite direction and seem to be perceived as less relevant for investors who are interested in reducing the risk of insolvency in the short term rather than long term sustainability and competitive advantage.

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“The results of the research are very interesting”, declared **Angelo Meda**, the manager in charge of research at Banor Sim. “Our hypotheses were in part confirmed. The study has also, in part, shed new light and 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 E, S and G variables are not in synch with each other was an unexpected result that we shall take into account in future**.” Meda continued:

“ESG topics are in the spotlight as never before. On the one hand, **investors increasingly demonstrate their desire to invest their savings, taking into account environmental sustainability, social and good governance parameters**, while on the other hand, European policymakers are introducing a series of training and information obligations”, **Politecnico di Milano Professor Giancarlo Giudici** emphasised. For Giudici,“It is therefore essential for asset managers to study the market and be ready for this new challenge”.

The report also confirmed the initial theory according to which, **over time, the market attributed a negative spread to issuers with a better ESG score**, considering them less risky in the short to medium terms. “This effect,” as the Banor and Politecnico researchers underlined, “seems to be limited to the advantage of adopting good practices in corporate governance which, for investors, can mean lower agency costs, lower risk of opportunistic behaviour and better monitoring.”

The analysis involved **536 bonds listed on European markets and issued by 146 medium to large companies between January 2014 and December 2018**, excluding convertible bonds and bonds placed by banks and real estate investment companies. Selection focused on bonds included in two State Street Global Advisors EFTs, the SPDR Bloomberg Barclays EU High Yield Bd UCITS ETF and the SPDR Bloomberg Barclays Euro Corp Bond UCITS ETF. For each bond, the prices on the Borsa Italiana, the financial statements of the issuer and the relevant ESG parameters were gathered. Upon reaching the availability of 424 indicators, each one was associated with one of the 30 classes of variables from the SASB matrix, which shows the relative importance of the ESG parameters for each sector.

The scores obtained were then normalised, and f**or each year, a final ESG score was calculated for each single issuing company as a weighted average of E, S and G** according to **SASB** recommendations. The issuers were then split into two groups as a function of their ESG score being higher or lower than the average. Subsequently, the Monthly Total Return Index of the bonds in the two groups was calculated, conducting separate analyses for investment grade and high yield bonds.

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