

ETFs: a new route to sustainable investing

Passive management
at the heart of
transformation

Embrace ESG

ESG Lunch – Frankfurt, October 2018

LYXOR etf
SOCIETE GENERALE GROUP



Why ETFs are fit for ESG investing?

▶ **Passive and engaged**

Vote, shareholder engagement, reporting

▶ **“Listed impact”**

Adds to private impact, liquidity brings scale

▶ **Generational**

Strong behaviour convergence, millennials, digital

▶ **Democratise**

Market access, cost

▶ **Transparency**

“Know what you buy”, portfolio disclosure

▶ **Data**

At the heart of both ESG and passive

▶ Passive management is **consistent** with the SRI approach

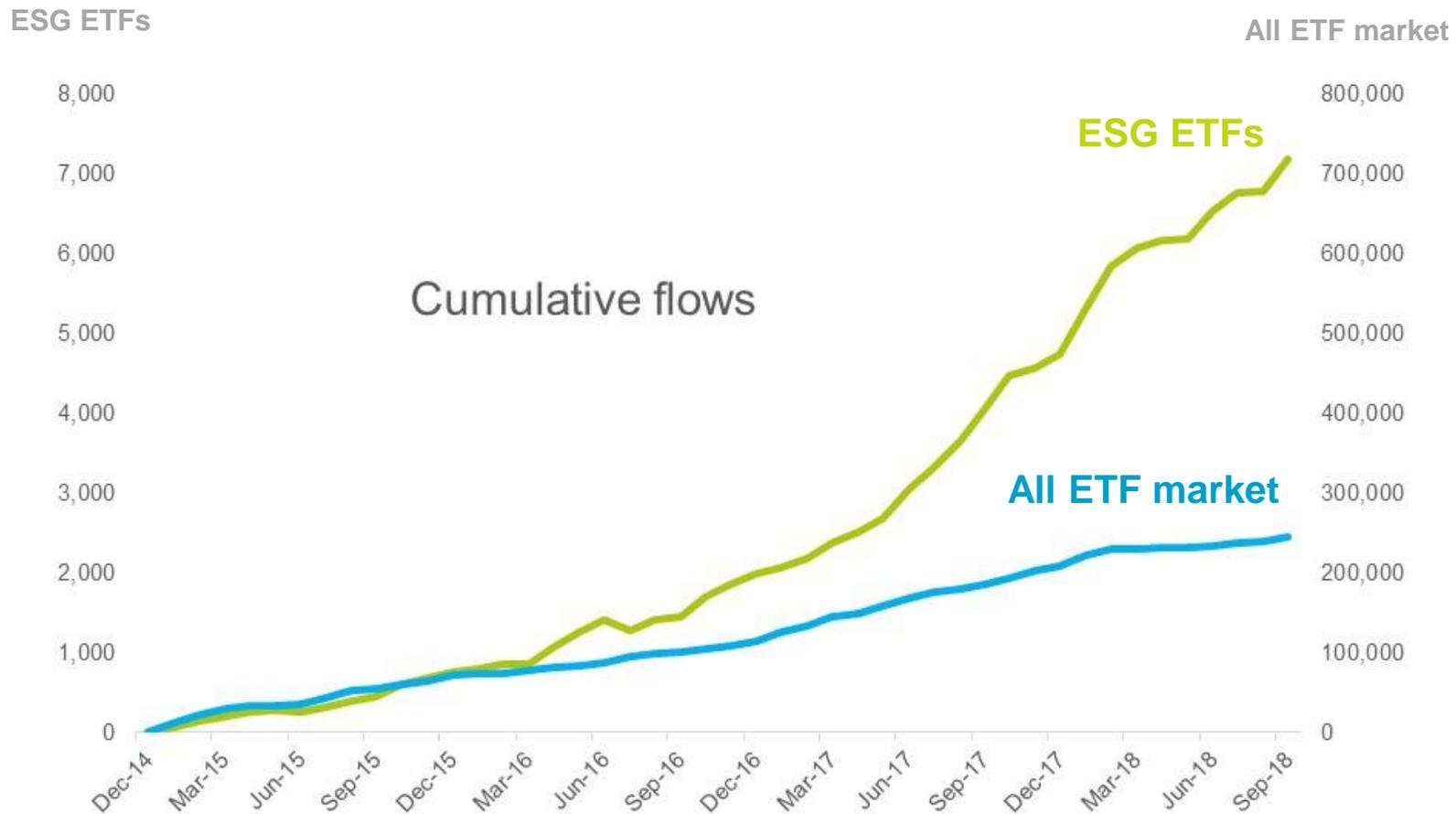


▶ There are strong **common values** between ETFs and SRI

European ESG ETF inflows

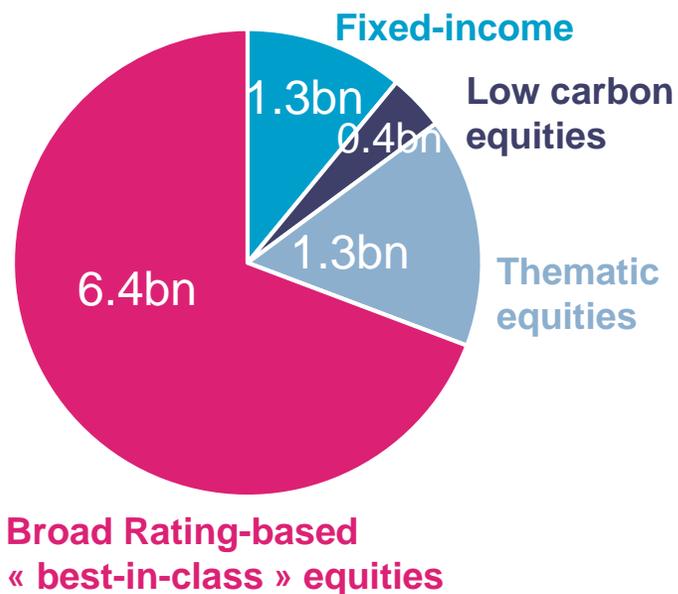
Flows 2015-2018 in € million

- ▶ Still a small portion of the ETF market, however it **grows significantly faster**



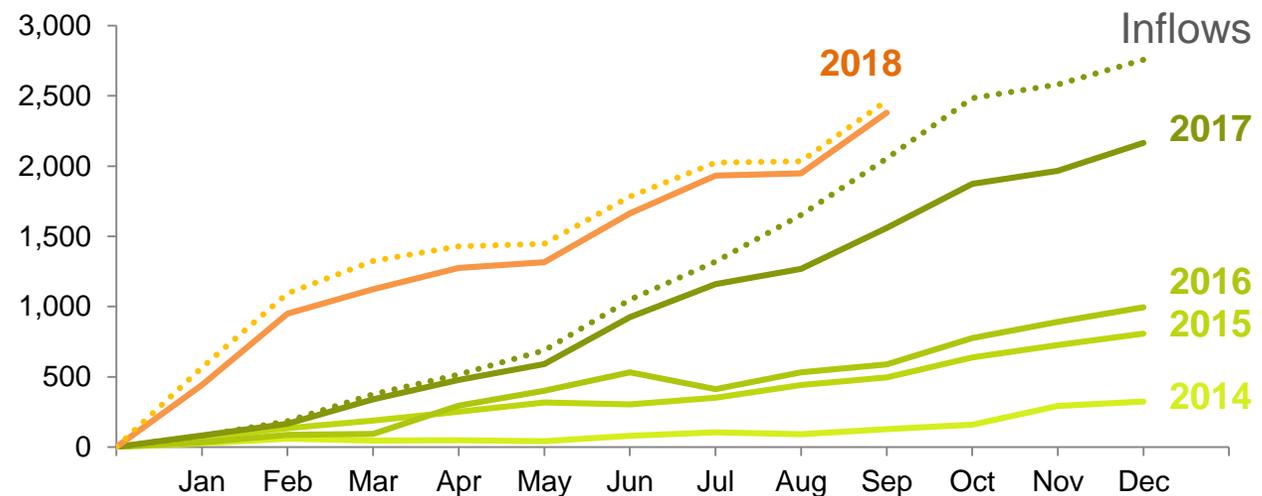
European ESG ETF market – Sep 2018

Assets under Management (€)



► AuM **€ 9.4 billion**
1.4% of total European ETF market

► Net New Assets 2018 YTD **€ 2.5 billion**
6.5% of total European inflows



..... Incl. Ex-controversial weapons ETFs

Positive carbon impact

“Financing Sustainable Growth”

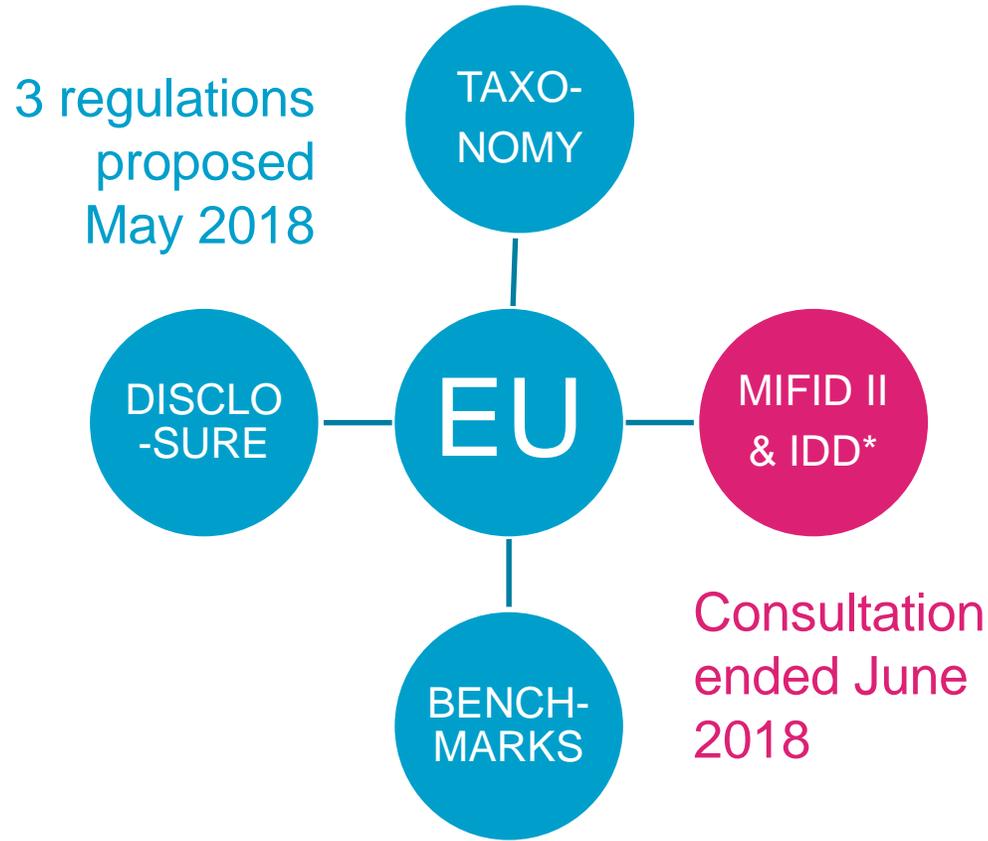
(the EU’s Action Plan - March 2018)

How new regulation will put passive management
at the heart of transformation

EU to accelerate shift

A game-changing package of measures announced by European Commission

► EU willing to act along 4 axis



ESMA should update the (MIFID) suitability requirements to include explicit provisions on the obligation to ask clients about their sustainability profile

HLEG (High Level Expert Group)
Recommendation to the European Commission, Final Report 2018



1) Disclosure – what you need to know

- ▶ **Obligation to integrate** ESG risks in investment decisions or in advisory
 - ▶ **Obligation to disclose how** ESG risks are taken into account in investment decisions or in advisory
 - ▶ **Obligation to disclose** how ESG risks are taken into account **at product level**
- 
- ▶ Pre-contractual information will disclose
 - Procedures for ESG integration
 - Estimated **ESG risks on returns** for proposed products
 - Pertinence of benchmark chosen and how it is built
 - ▶ **If** the product is marketed as **green investment**:
 - **Impact** of product through appropriate indicators



« **Financial market participants** » who benefit from a **mandate** from clients to take investment decisions integrate ESG criteria in their internal processes and inform clients

« **Investment firms and insurance intermediaries** » providing advice consider ESG as drivers of value in the advice given as part of their duties towards investors and provide investors with the related information

European Commission, Proposal for Regulation on disclosures, May 2018



2) Taxonomy – what you need to know

A framework to facilitate sustainable investment through a technically robust classification system, starting with a **taxonomy on climate mitigation**



- ▶ EU taxonomy will define “**environmentally sustainable**” economic activities
- ▶ Supporting an **EU Green Bond Standard**
- ▶ Taxonomy to underpin “**low carbon**” indices for use by asset and portfolio managers as a benchmark for low carbon investment strategies
- ▶ A common set of **metrics** allowing improved **disclosure on climate-related information**
- ▶ Obligations fixed for **labelling** a product as “**environmentally sustainable**”



6 broad objectives:

- Climate change mitigation
- Climate change adaptation
- Sustainable use and protection of water and marine resources
- Transition to a circular economy, waste prevention and recycling
- Pollution prevention and control
- Protection of healthy eco-systems



HLEG (High Level Expert Group) Recommendation to the European Commission, Final Report 2018



How is our Green bond ETF positioned?

- CBI is member of HLEG and working group
- TEEC label partly inspired by the CBI taxonomy
- Likely to underpin EU taxonomy and the European Ecolabel

3) Benchmarks – what you need to know

From Low carbon to Positive carbon indices

- ▶ Existing indices
 - ▷ Negative screening: **Fossil fuel free, Ex Coal**, exclusions from market cap benchmarks...
 - ▷ Best-in-class: **Low carbon** indices
 - ▷ Transition leaders: **green revenues**
- ▶ **Amendment to the European benchmark regulation**
- ▶ **“Sustainability benchmarks”**: the EU will start by defining **carbon specific benchmarks**, of two types
 - ▷ **Low Carbon benchmarks**
 - ▶ Objective: less CO₂ emissions than the market cap benchmark
 - ▷ **Positive Carbon Impact benchmarks**
 - ▶ Objective: foster carbon emission savings by companies
 - ▶ Still to be developed = > **next generation carbon indices** are a challenge



Impact benchmarks:
 “assets are selected on the basis that their **carbon emission savings exceed the asset’s carbon footprint”**

Proposed amendment of Benchmark regulation (EU) 2016/1011



Why we need positive carbon impact benchmarks

- ▶ **Climate action is #1 sustainable goal** for investors
- ▶ **Investors to shift portfolios** and step-up pressure on companies to cut emissions, disclose and oversee climate-related risks

**June
2018**

Climate Action 100+ / Open letter by investors representing \$10 trillion (list of signatories in the FT) urging companies to take tougher action on emissions, will submit resolutions in shareholders meetings

Call to G7 by a group of 288 asset owners and AMs representing \$26 trillions (public list) for the de-commissioning of coal production and coal use, and stop of any subsidies to fossil fuels

- ▶ Existing products focus on footprint, not on impact
- ▶ Objectives are clearly **shifting** from lowering carbon footprint **to generating a positive carbon impact** as measured by emissions avoided
- ▶ **European regulation** is a catalyst for positive carbon impact
- ▶ **The challenge: deliver carbon positive indices** (green revenues not enough, emissions avoided must be tracked)
- ▶ Will allow passive management to act at the heart of transformation

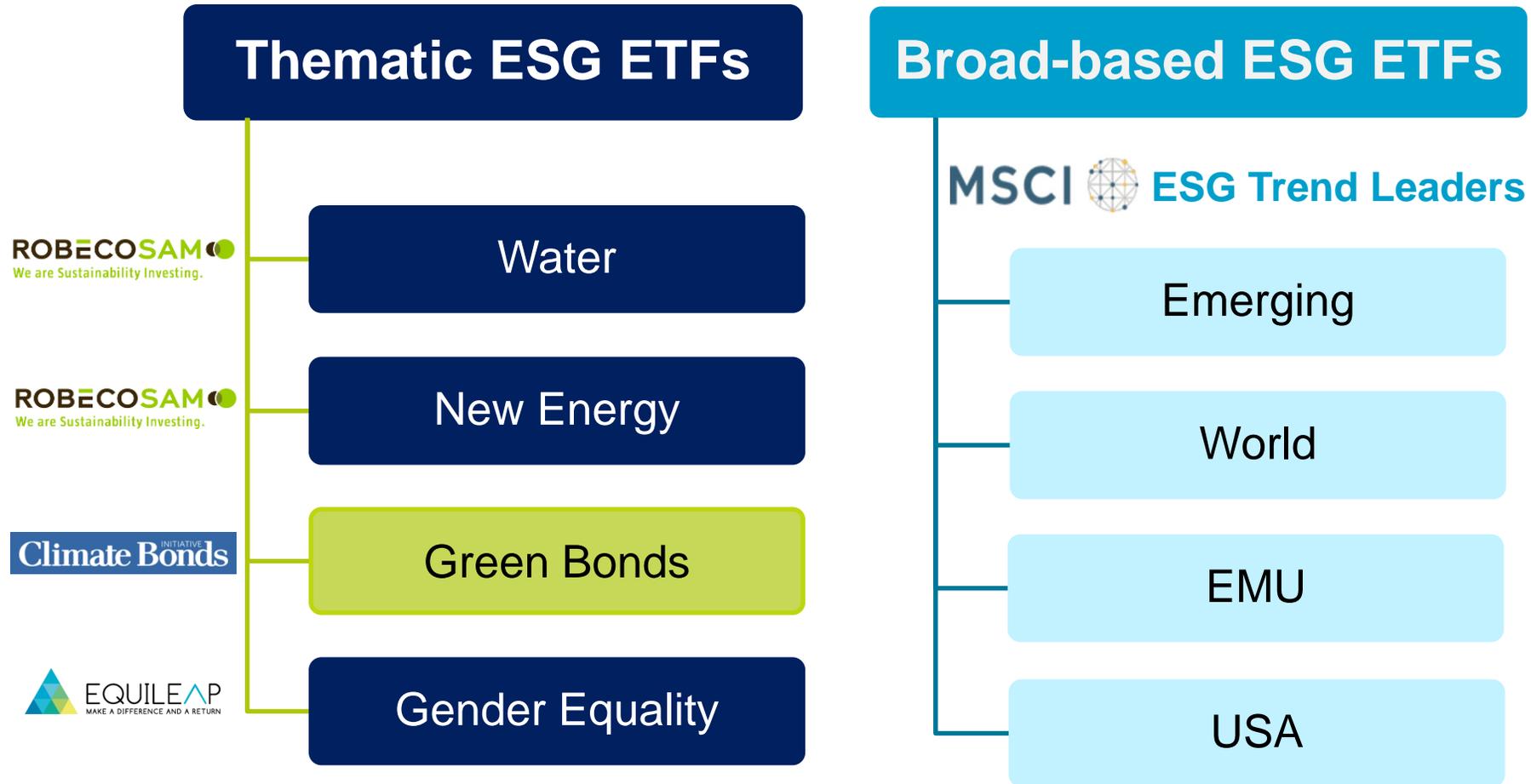
ETF solutions

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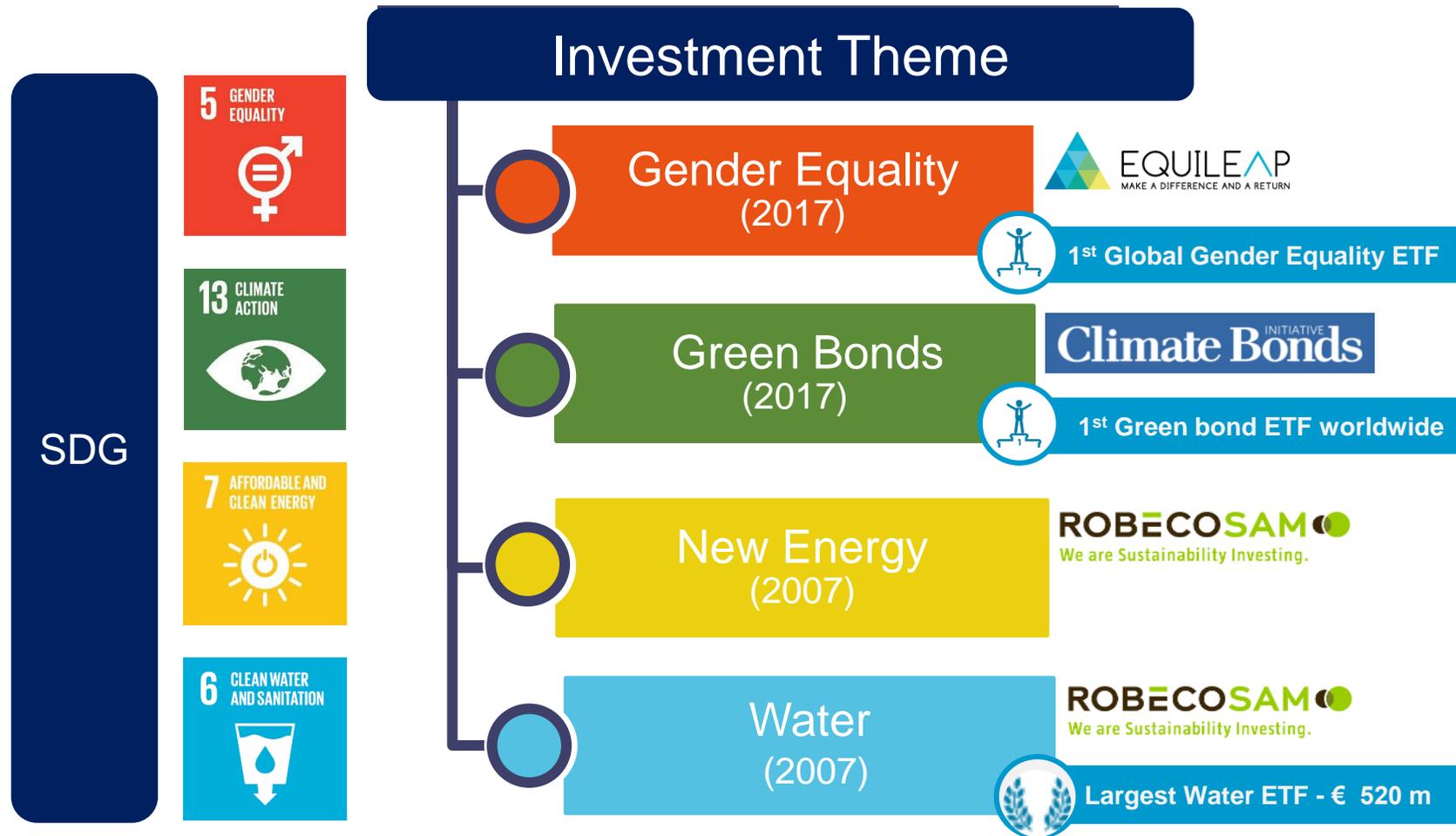


Our two pillars



Thematic ESG range

Lyxor ETF, unique range allowing to invest in alignment with four of the UN's SDGs*



Green bond ETF

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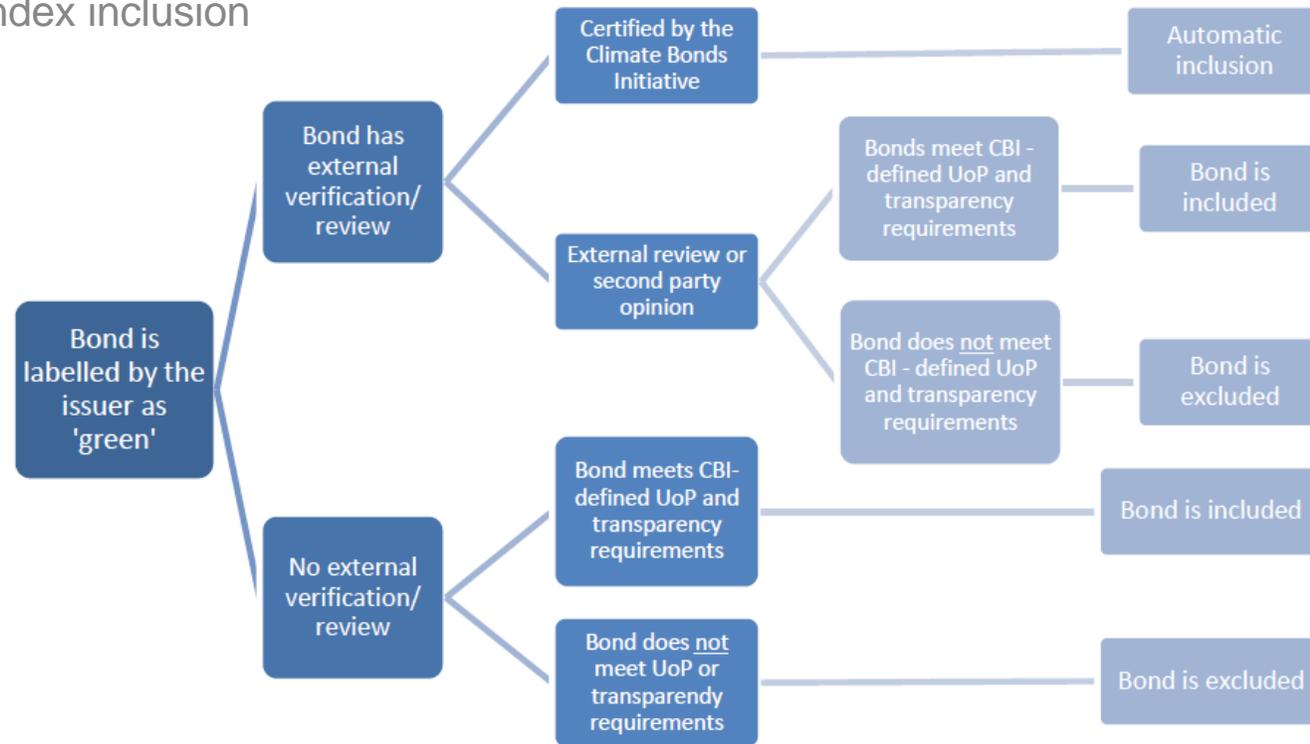
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Selecting 'real' green bonds for our index

Bonds must comply with the Climate Bonds Standard and Taxonomy

► Decision tree for index inclusion



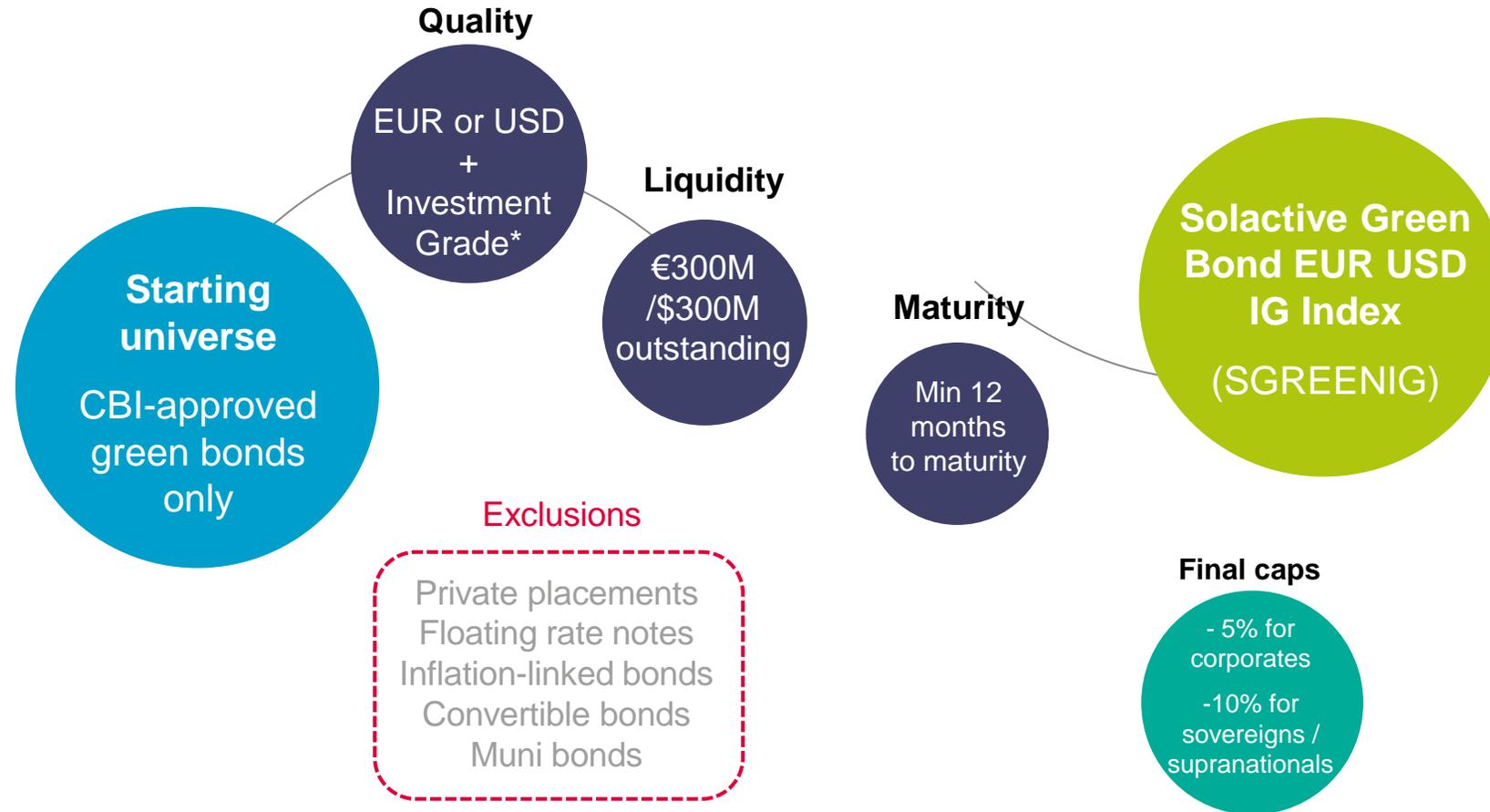
84.6% of green bonds in index have received a second opinion, or a CBI certification*

~85% of self-labelled green bonds get CBI approval

* Source: Lyxor International Asset Management.as at October 2018

From CBI accreditation to index inclusion

CBI approved green bonds only



Solactive Green Bond EUR USD IG Index

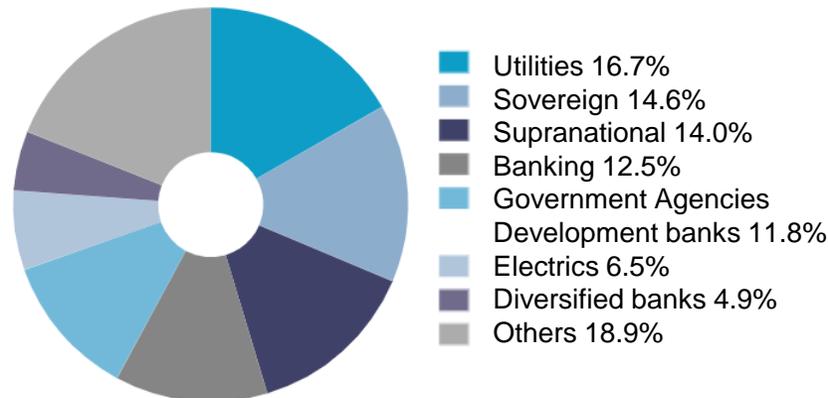
Investment grade Green Bonds with CBI approval

208
bonds

AA-
average rating

Green
CBI approved issues

Issuer breakdown by type*

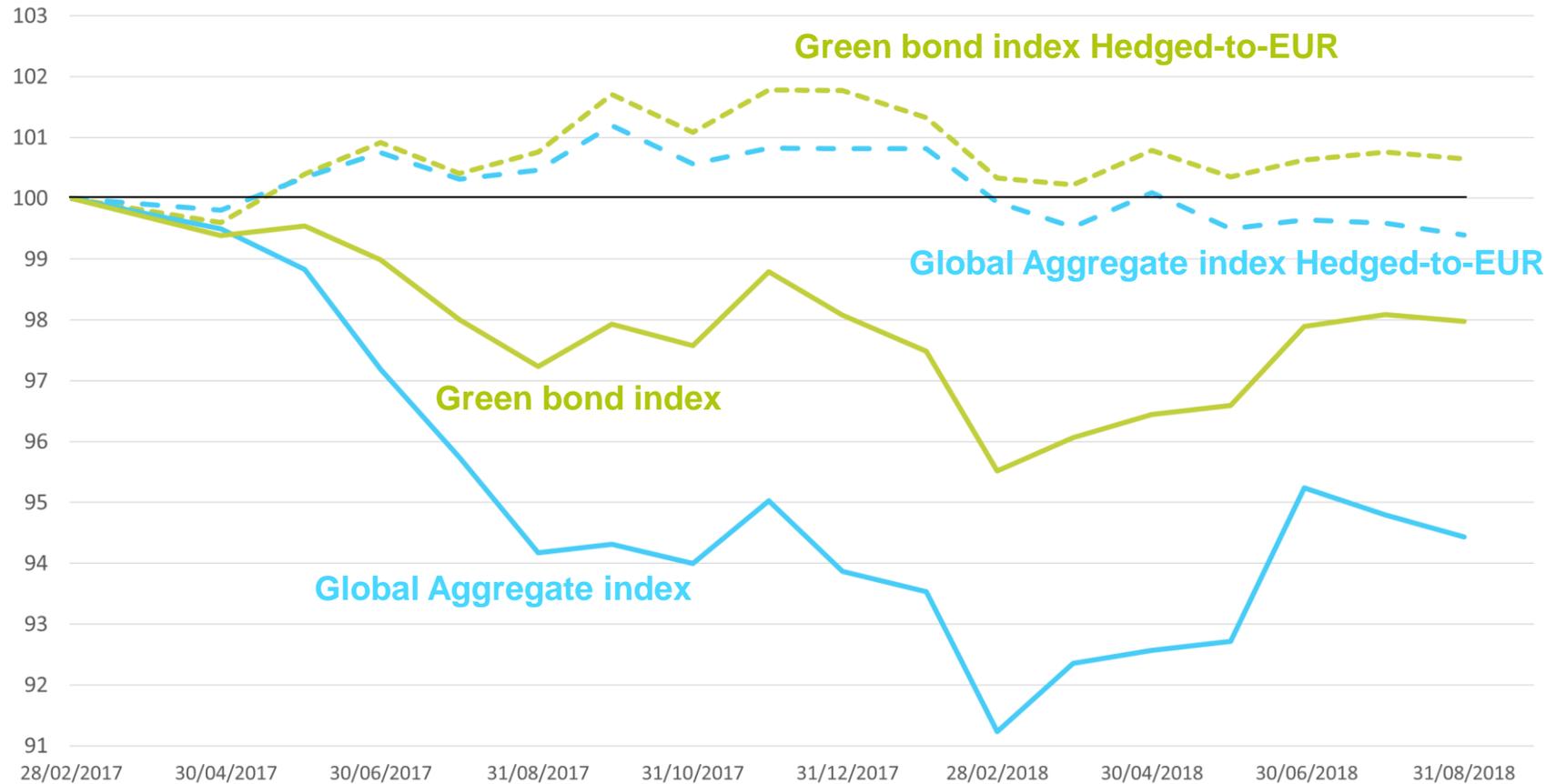


Index analytics*

The things you need to know	
Yield to maturity	1.7%
Duration	7.6
Avg. maturity	8.7 years
Avg. coupon	1.6%
# issuers	129
# bonds	208
Avg. rating	AA-
Currency breakdown	72% EUR, 28% USD
Rebalancing freq.	Monthly

How does it compare to the Barclays Global Agg?

Returns since ETF inception to end Sept. 2018



ESG Trend Leaders

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Broad-based ESG range

Lyxor MSCI ESG Trend Leaders: the passive activist

- ▶ Captures the **ESG Trend** of companies: **rewarding issuers making efforts and penalising laggards**
- ▶ **Exclusions** based on **industries** and **controversies**
- ▶ **Top 50% best-in-class companies in each sector** selected for their combined ESG Ratings **and Trend**
- ▶ Like-for-like building blocks well suited for **core equity allocation** by region



Unique

Integrates companies' ESG Trends in the selection criteria



More impactful

Rewards those with improved ESG rating and penalises laggards



Diversified

880 stocks in World Trend Leaders vs. 1650 for parent index & 400 in conventional SRI equivalent



Effective

Moderate tracking error vs. parent indices as opposed to "MSCI SRI" Top 25% approach

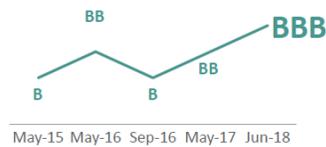
Capture the Trend

How well a company addresses ESG key issues vs. its industry peers

CASE STUDY #1

FRESENIUS - ESG RATING BBB

- ▶ GICS level 3 : Health Care Providers & Services
6 key issues (mainly Social and Governance)
- ▶ Weighted-average score: 4.5
- ▶ Industry Relative score : 4.9
- ▶ Positive Industry relative Trend



	Weight	Score	Quartile
Environment	5.0%	9.8	
Carbon Emissions	5.0%	9.8	●●●
Social	56.0%	4.6	
Labour Management	22.0%	0.9	●
Privacy & Data security	17.0%	7.1	●●●
Product Safety & Quality	17.0%	6.9	●●●
Governance	39.0%	3.6	
Corporate Governance	17.0%	4.1	●
Corruption & Instability	22.0%	3.2	●●●
Overall Score			
Weighted average key issue score		4.5	
Industry Relative score		4.9	

CASE STUDY #2

BMW - ESG RATING A

- ▶ GICS Level 3:Automobile,
6 key issues (mainly Social and Environmental)
- ▶ Weighted-average score: 5.0
- ▶ **Industry Relative score : 6.2**
- ▶ Negative Industry Relative Trend



	Weight	Score	Quartile
Environment	34.0%	5.6	
Opportunities in Clean Tech	17.0%	5.8	●●●
Product Carbon Footprint	17.0%	5.3	●●
Social	37.0%	5.6	
Privacy & Data security	20.0%	4.5	●●●
Labour Management	17.0%	6.8	●●●
Governance	29.0%	3.8	
Corporate Governance	15.0%	4.2	●●●
Business Ethics & Fraud	14.0%	3.3	N/A
Overall Score			
Weighted average key issue score		5.0	
Industry Relative score		6.2	

Why choose Lyxor for ESG?



Lyxor is a signatory of the PRI
(Principles for Responsible
Investment)



The only provider
in Europe to offer ETFs on
four of the UN's Sustainable
Development Goals¹



We can provide full
ESG metrics on *all* our
equity ETFs



We vote on a vast number of our
ETFs and engage in direct
dialogue with companies



We make the estimated
carbon footprint of *all* our
equity ETFs available on
our website

Important information

Key risks of Lyxor ETFs

It is important for potential investors to evaluate the risks described below and in the fund prospectus which can be found on www.lyxoretf.com

CAPITAL AT RISK

ETFs are tracking instruments: Their risk profile is similar to a direct investment in the Underlying Index. Investors' capital is fully at risk and investors may not get back the amount originally invested.

REPLICATION RISK

The fund objectives might not be reached due to unexpected events on the underlying markets which will impact the index calculation and the efficient fund replication.

COUNTERPARTY RISK

Investors are exposed to risks resulting from the use of an OTC Swap with Societe Generale. In-line with UCITS guidelines, the exposure to Societe Generale cannot exceed 10% of the total fund assets. Physically replicated ETFs may have counterparty risk resulting from the use of a Securities Lending Programme.

UNDERLYING RISK

The Underlying Index of a Lyxor ETF may be complex and volatile. When investing in commodities, the Underlying Index is calculated with reference to commodity futures contracts exposing the investor to a liquidity risk linked to costs such as cost of carry and transportation. ETFs exposed to Emerging Markets carry a greater risk of potential loss than investment in Developed Markets as they are exposed to a wide range of unpredictable Emerging Market risks.

CURRENCY RISK

ETFs may be exposed to currency risk if the ETF is denominated in a currency different to that of the Underlying Index they are tracking. This means that exchange rate fluctuations could have a negative or positive effect on returns.

LIQUIDITY RISK

Liquidity is provided by registered market-makers on the respective stock exchange where the ETF is listed, including Societe Generale. On exchange liquidity may be limited as a result of a suspension in the underlying market represented by the Underlying Index tracked by the ETF; a failure in the systems of one of the relevant stock exchanges, Societe Generale or other market-maker systems; or an abnormal trading situation or event.

Important information

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