FNG – the German, Austrian and Swiss Sustainable Investment Forum

Sustainable Investments in Switzerland

Excerpt from the Sustainable Investment Market Report 2014

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Introduction

This publication contains an English version of an excerpt from the chapter on Switzerland in Marktbericht Nachhaltige Geldanlagen 2014 – Deutschland, Österreich und die Schweiz [Sustainable Investment Market Report 2014 – Germany, Austria and Switzerland]. It is the latest in the series of annual publications on the sustainable investment market in Switzerland previously produced jointly by the consultancy firm onValues and FNG Switzerland.

The data on which this publication is based covers sustainable investments which are managed from Switzerland. The following asset classes are covered:

- Equity
- Sovereign Bonds
- Corporate Bonds
- Monetary/Deposit
- Private Equity/Venture Capital
- Hedge Funds
- Real Estate/Property
- Commodities

The following sustainable investment strategies are included:

- Sustainability-themed investment
- Best-in-class investment selection
- Norms-based screening
- Exclusion of holdings from investment universe
- Integration of ESG factors in financial analysis
- Engagement on sustainability matters
- Voting on sustainability matters
- Impact Investment

Definitions of the various investment strategies can be found in following table.

Overview of investment strategies

Best-in-Class	Approach where leading or best-performing investments within a universe, category, or class are selected or weighted based on ESG criteria.
Engagement and voting	Engagement activities and active ownership through voting of shares and engagement with companies on ESG matters. This is a long-term process, seeking to influence behaviour or increase disclosure.
Exclusions	An approach that excludes specific investments or classes of investment from the investible universe such as companies, sectors, or countries.
Impact Investment	Impact investments are investments made into companies, organizations, and funds with the intention to generate social and environmental impact alongside a financial return. Impact investments can be made in both emerging and developed markets, and target a range of returns from below market to market rate, depending upon the circumstances.
Integration	The explicit inclusion by asset managers of ESG risks and opportunities into traditional financial analysis and investment decisions based on a systematic process and appropriate research sources.
Norms-based screening	Screening of investments according to their compliance with international standards and norms.
Sustainable themes	Investment in themes or assets linked to the promotion of sustainability. Thematic funds focus on specific or multiple issues related to ESG.

Source: Eurosif, European SRI Study 2012, page 64 (http://eurosif.org/images/stories/pdf/1/eurosif%20sri%20study_low-res%20v1.1.pdf).

The sustainable investment market in Switzerland

During 2013, the positive trend in the sustainable investment market in Switzerland continued. As at 31 December 2013, the total volume of sustainable investment funds mandates and structured products stood at CHF 56.7 billion[1], representing an all-time high. This sum can be described as the volume of SRI or core SRI in Switzerland.

Asset overlays

Asset managers are increasingly applying exclusion criteria to all or some of their invested capital as asset overlays. In Switzerland, exclusion overlays are applied to assets totalling CHF 1.91 trillion. However, the increase compared with the previous year, when the volume stood at CHF 739 billion, is only to a small extend due to actual growth in asset overlays. Rather, the significant increase is attributable to the fact that this year, more comprehensive data on asset overlays has been provided.

All asset overlays include an exclusion criterion covering cluster munitions and anti-personnel mines, with asset managers generally referring explicitly to the Convention on Cluster Munitions. Biological and chemical weapons are also excluded by asset investments totalling approximately CHF 130 billion. CHF 30 billion of assets exclude investment in vital basic foodstuffs such as soya, wheat, rice and maize.

In the vast majority of cases, exclusion overlays comprise just a single criterion – predominantly cluster munitions and anti-personnel mines. A second exclusion criterion is added in only a few cases. For this reason, exclusion overlays are not viewed in this report as SRIs, but rather as broad SRIs or responsible investments.

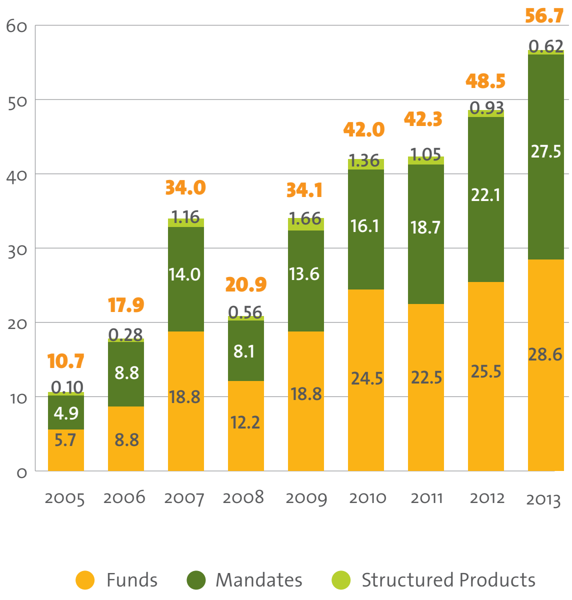
The volume of all Swiss SRIs – both core and broad, or sustainable and responsible investments, respectively – thus includes the asset overlays already mentioned, plus investment funds, mandates and structured products, minus any double counting. The total comes to CHF 1.92 trillion.

Investment funds, mandates and structured products

In 2013, the volume of the sustainable investment market rose to CHF 56.7 billion. The growth rate was thus 17 per cent.

The main contributors to this were mandates (CHF 27.5 billion), which attained almost the same volume as investment funds (CHF 28.6 billion). The growth in mandates continued the strong upward trend of 2012. The capital invested in sustainable investment funds increased in absolute terms by approximately CHF three billion. However, the net gain in these funds, at twelve per cent, fell far short of the strong growth of the mandates. By contrast, structured products saw a further decline, with a market volume of just CHF 621 million, compared with CHF 927 million in the previous year. This equates to a 33 per cent fall.

***Figure 1:** Investment Funds, Mandates and Structured Products*



Source: Forum Nachhaltige Geldanlagen

[1] The euro figures in this publication are based on conversions at the European Central Bank's exchange rate on 31 December 2013 (1 euro = CHF 1.2276).

Table 1: *Sustainable Investments in Switzerland 2012 and 2013 (in billion CHF – EUR)*

	2012		2013		Change 2012-2013
Currency	CHF	EUR	CHF	EUR	Calculated in CHF
Funds	25.5	21.1	28.6	23.3	12%
Mandates	22.1	18.3	27.5	22.4	24%
Structured Products	0.9	0.8	0.6	0.5	-33%
Total	**48.5**	**40.2**	**56.7**	**46.2**	**17%**

Source: Forum Nachhaltige Geldanlagen

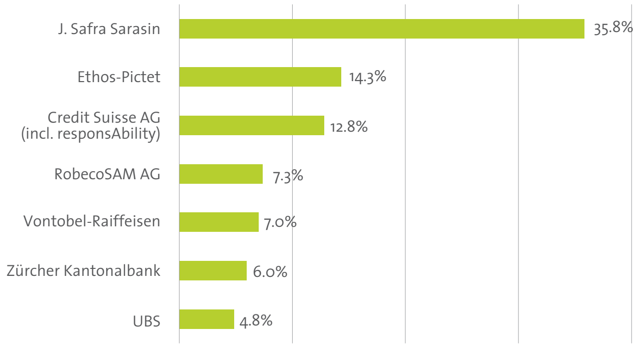
Overall, sustainable investments recorded a positive net inflow of funds in 2013, which was somewhat more marked in the case of mandates than in that of investment funds. However, the validity of this statement is slightly limited by the fact that the relevant data is not available for all the funds and mandates.[2] In December 2013, the overall volume of the Swiss fund market stood at approximately CHF 745.2 billion.[3] Sustainable funds' share of the total volume of the Swiss fund market in 2013 was thus 3.8 per cent, up 0.2 percentage points from 2012.

Overall, it can be stated that the sustainable investment market in Switzerland, with double-digit percentage growth, is continuing the upward trend which has been ongoing since 2005, interrupted only by the crisis year 2008. Since 2005, the volume of sustainable investments has grown by an annual average of 23 per cent.

Participants

25 financial players from Switzerland took part in this year's survey. Compared with the previous year, the market report therefore managed to gain four additional players, further increasing the already high market coverage of the survey. The following diagram shows the market shares of the major providers of sustainable financial products in Switzerland.

Figure 2: *Market Shares of the Leading Swiss Asset Managers (in per cent)*



Source: Forum Nachhaltige Geldanlagen

The importance of HNWIs in the sustainable investment market in Switzerland

High-net-worth individuals (HNWIs) play a particularly important role in Switzerland. Around 280,000 individuals who own investable assets in excess of US$1 million are domiciled in the country.* The Confederation thus ranks in sixth place internationally. This is also reflected in the sustainable investment market. HNWIs account for almost 20 per cent (CHF 5.49 billion) of the sustainable mandates in Switzerland.

Sustainable investments are an increasingly attractive proposition for HNWIs, as Eurosif's 2012 HNWI & Sustainable Investment Study** has shown. For example, compared with past years an increasing number of HNWIs are investing a significant proportion of their portfolios – i.e. more than 20 per cent, or even over 50 per cent – sustainably. HNWIs cited as their chief motivation the desire to make a contribution to sustainable development. However, purely economic motives also play an important role: in second place, the HNWIs cited the goal of preserving their wealth for future generations, followed by the desire for stable returns.

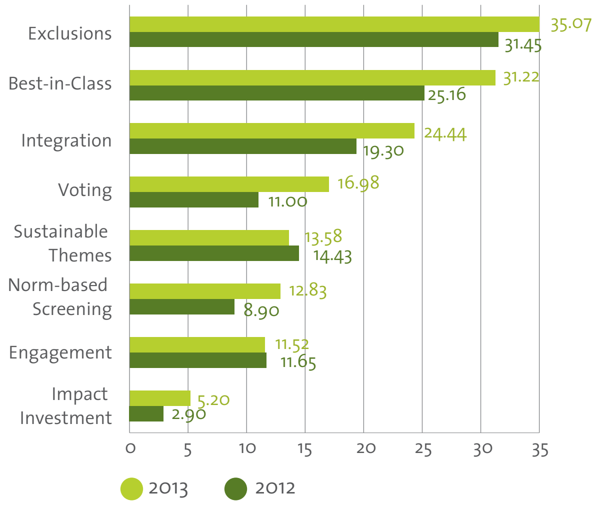
Their decision in favour of specific sustainable investment strategies also shows that HNWIs are living up to their reputation as particularly innovative investors who are keen to invest in new ideas and technologies. Compared with the sustainable investment market as a whole, they have a particular preference for themed and impact investments, according to Eurosif. Other sustainable investment strategies popular with HNWIs include norms-based screening, exclusion criteria and the best-in-class approach.

**Cf.: Capgemini/RBSC Wealth Management 2012: World Wealth Report.* ***Cf.: Eurosif 2012: High Net Worth Individuals & Sustainable Investment.*

[2] These figures are based on data relating to assets of CHF 30.2 billion, which equates to 53 per cent by volume of all investment funds, mandates and structured products.
[3] Cf.: Swiss Fund & Asset Management Association SFAMA 2014: fund market statistics 2013. http://www.sfama.ch/ (accessed 21.03.2014).

Investment strategies

__Figure 3:__ Sustainable Investment Approaches per end of 2012 and 2013 (in billion CHF)



Source: Forum Nachhaltige Geldanlagen

This year, the study is once again recording data on eight sustainable investment strategies. In the case of most sustainable financial products, several approaches are applied simultaneously.

With a volume of around CHF 35 billion, the use of specific criteria to exclude companies and countries remains the most important investment strategy, followed by the best-in-class approach, which has once again recorded significant growth following a slight decline in 2012. The integration of ESG criteria into traditional financial analysis also rose significantly (please see p. 7 for a case study on integration). Thematic funds, by contrast, are less strongly represented than in 2012. For the most part, these are multi-thematic funds, followed by water- and energy-based funds.

Voting, on the other hand, saw a sharp rise in 2013. This could be linked to the March 2013 "fat cat initiative". By voting for the initiative, a large majority came out in favour of pension funds having to actively exercise their voting rights at annual general meetings of Swiss companies on behalf of their members, among other things.

Starting from a relatively low level, norms-based screening showed significant growth, with an increase of 44 per cent. The providers that use norms-based screening take the UN Global Compact as a basis for assets totalling CHF 9.6 billion, followed by the core labour standards of the International Labour Organisation (ILO), for CHF 8.9 billion, and the Organisation for Economic Cooperation and Development's Guidelines for Multinational Enterprises, for around CHF 6 billion.

Impact investment showed particularly strong gains in 2013, growing by almost 80 per cent.

Impact investment

Of the 25 financial institutions which took part in the study, five offer impact investment products. Most of these products are microfinance investments, while other areas mentioned include sustainable agriculture, climate protection and SMEs, for example.

The financial players cited the desire to make a contribution to sustainable development as their main reason for impact investment. In second place was the idea of contributing to local community development. Stable long-term returns and alternatives to philanthropic motives also play a role in investing in impact instruments, but they are secondary to other motives.

As in the previous year, players cited reservations about risk and performance as the greatest obstacle to more extensive engagement in impact investment. One bemoaned the fact that there were too few suitable products and options in this area on the market.

Exclusion criteria

2013 saw yet another increase in the volume of investment funds, mandates and structured products applying exclusion criteria. While in 2012 the volume of assets invested using exclusion criteria stood at CHF 31.5 billion, in 2013 it had risen as high as CHF 35.1 billion. This represents growth of 11 per cent, so the 25 per cent growth recorded in 2012 has levelled out somewhat. It should be noted that a variety of different exclusion criteria are generally used in combination. For example, in practice, between five and ten exclusion criteria are often applied to a product. This means that considerably more criteria are used than in the case of exclusion overlays.

In 2013, the production of and trade in weapons once again constituted the most important exclusion criterion, followed by tobacco, nuclear power, pornography and gambling. Genetic engineering, alcohol, ozone-depleting substances, human rights violations (including child labour) and embryonic stem cell research also featured prominently. In contrast to the previous year, the "genetic engineering" exclusion criterion lost ground and now ranks sixth, behind gambling and pornography. The "embryonic stem cell research" criterion is a new entrant in the top ten.

***Table 2:** Top Ten Exclusion Criteria (bn CHF)*

1.	Weapons (production and trade)	32.7
2.	Tobacco	32.4
3.	Nuclear energy	27.8
4.	Pornography	26.6
5.	Gambling	13.8
6.	Genetic engineering	11.8
7.	Alcohol	8.9
8.	Ozone depleting substances	5.2
9.	Violations of human rights (including child labour)	4.1
10.	Embryonic stem cell research	3.6

Source: Forum Nachhaltige Geldanlagen

Case study: Vontobel's integration approach

As an investment strategy, integration involves integrating environmental and social opportunities and risks as well as aspects of good governance (ESG factors) into traditional financial analysis. The process focuses on the potential positive or negative impacts of ESG factors on companies' financial data. But how does this kind of investment process actually work in practice? We will illustrate this by examining the integration approach that Vontobel implements in its asset management of the equity funds it manages in Zürich.

The investment process starts with quantitative screening. What is important in this first phase of security selection are economic indicators such as market capitalisation, daily trading volume and – crucially – return on invested capital. The latter criterion makes it possible to identify companies which have achieved an above-average return on invested capital in the past – an indication that they are likely to continue to yield above-average returns. The team's approach does not include any provision for automatically excluding particular companies or sectors, with the exception of arms companies and tobacco producers.

The next stage comprises a fundamental analysis of all the securities which appear promising based on the factors mentioned above. The aim of this second step is to determine whether the companies will continue to yield above-average returns in future and whether they are attractively valued. To do this, the portfolio managers and sector specialists look out for the following factors: a sustainably high competitive advantage, consistently high rates of return and operating margins, the ability to generate above-average cash flow on a sustained basis, a strong balance sheet and – as an integral component – consideration of various ESG factors. Analysing environmental and social aspects makes it possible to identify other factors which may be crucial to the evaluation of a company. The ESG analysis also incorporates expertise from external service providers.

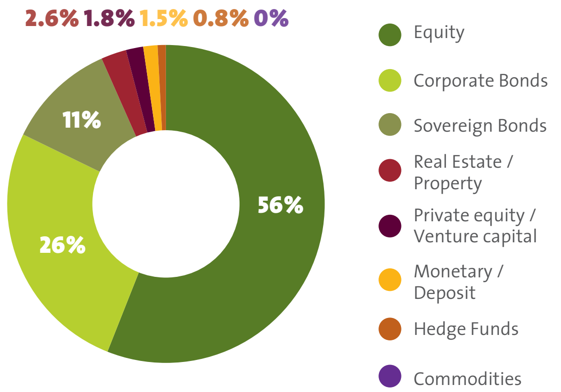
In addition, the financial analysts assess how well each company performs in terms of ESG issues. This is done by drawing up a rating matrix which will have different criteria and weightings depending on the sector involved. In the consumer staples sector, which supplies consumers with everyday products, relevant environmental issues include, for example, whether data on emissions and water consumption is published, what the position is regarding the environmental impact of products, and whether risks in the supply chain are assessed. Companies must achieve a minimum score in this rating in order to be recommended for purchase. The rating carried out by the sector specialists is reviewed by an external sustainability expert and then discussed with them.

If the results of the analysis as a whole show that the company has good prospects and is attractively valued, it will be recommended to the portfolio managers for purchase. Each portfolio manager holds around 30 to 40 items in his/her portfolio and regularly replaces securities with attractive new recommendations. If a security in the portfolio ceases to meet the stringent requirements, it will be sold. The same applies if its sustainability performance falls below the minimum value specified. Voting rights are actively exercised for all securities. In addition, Vontobel works together with a specialist company, which conducts an active dialogue with companies in Vontobel's portfolios on ESG challenges and risks.

Allocation of assets

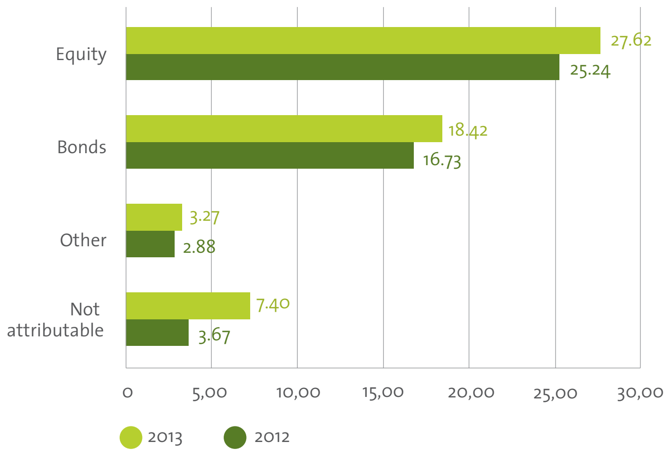
As far as the allocation of assets is concerned, absolute growth has been recorded in almost all classes, particularly in equities and bonds. In relative terms, however, very little has changed. As in the previous year, the proportion of equities stands at 56 per cent – a high level compared with the allocation in Germany and Austria. The proportion of bonds has also remained more or less constant. However, more differentiated data is now available for this segment for the first time: this year, corporate bonds and government bonds have been recorded separately in order to give a clearer picture of the bond market. This shows that corporate bonds account for 26 per cent of assets and sovereign bonds for 11 per cent. Other asset classes are still of little importance both in relative and in absolute terms. Of these, investments in real estate/property top the list with a market share of 2.6 per cent and have also shown significant growth compared with the previous year. By contrast, the proportion of private equity/venture capital declined slightly, and the monetary/deposit category remained unchanged at 1.5 per cent. Investments in commodities and hedge funds, accounting for less than one per cent, play only a very minor role.

Figure 4: *AuM Share of Different Asset Classes (2013 in per cent)*



Source: Forum Nachhaltige Geldanlagen

Figure 5: *AuM Share of Different Asset Classes in Switzerland 2012 and 2013 (in billion CHF)*



Source: Forum Nachhaltige Geldanlagen

Investors

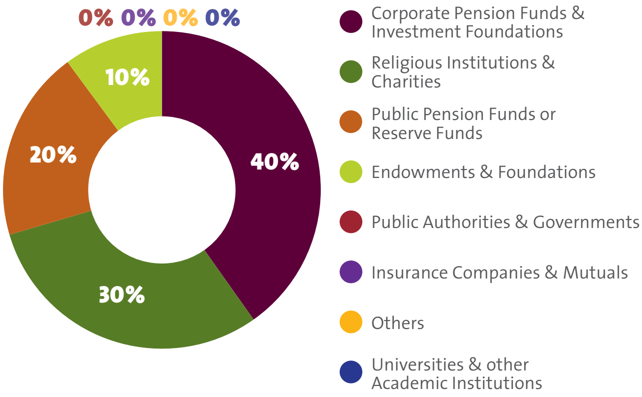
In 2013, institutional investors once again gained ground compared with private investors. Their share increased to 59 per cent, while private investors lost five percentage points compared with 2012, leaving them with just 41 per cent.[4]

Within the category of institutional investors, corporate pension funds and investment foundations continued to dominate, with a market share of 40 per cent (in the previous year it had been 36%). Religious institutions and charitable organisations also recorded growth and have now moved up to second place. Public pension and reserve funds, by contrast, lost ground slightly and are now ranked in third place, with a 20 per cent market share. Foundations and endowments are another major player, while other categories of institutional investors play only a negligible role.[5]

4 Details of the distribution of assets between private and institutional investors are available for assets totalling CHF 48.7 billion (for 14 per cent, no data is available).

5 This information is based on informed estimates provided by financial service providers in relation to assets of CHF 20 billion (no data available for approx. 30 per cent).

***Figure 6:** Typology of SRI Institutional Investors in Switzerland 2013 (in percent)*



Source: Forum Nachhaltige Geldanlagen

TRENDS

On the whole, the players on the sustainable investment market are positive about the future. Typically, the financial institutions are assuming growth in sustainable investments of between 20 and 50 per cent over the next three years. Those surveyed are of the opinion that the key driver of this growth will continue to be institutional investors, followed by legislation. Furthermore, they anticipate an increase in investments by private investors similar to that of the previous year.

By contrast, the influence of international initiatives, such as e.g. the PRI, and of non-governmental organisations is seen as being less significant. Respondents' answers differed most widely on the question of fiduciary duty. The participants in the study see the accounting principle of materiality as having the least relevance to further market growth.

***Table 3:** Key Drivers for Demand in SRI*

1.	Demand from institutional investors
2.	Legislative
3.	Demand from retail investors
4.	Notion of fiduciary duty
5.	External pressure (NGOs, media, trade unions)
6.	International initiatives
7.	Materiality

Source: Forum Nachhaltige Geldanlagen

Sustainability-oriented specialist banks in Switzerland

According to the specialist literature*, two banks in Switzerland come under the heading of sustainability-oriented specialist banks: Freie Gemeinschaftsbank and Alternative Bank Schweiz.

According to Freie Gemeinschaftsbank's website, the funds it manages are invested predominantly in projects which "stand up for humans, animals, plants and the Earth". It specifies its objective as being "to bring its entire cash flow into line with ethical/environmental criteria". Alternative Bank Schweiz describes itself as a social and environmental bank which works "for the common good, humanity and nature". Its high degree of transparency is the main factor distinguishing this bank from traditional banks; for example, when issuing loans, it publishes the recipient's name, the amount and the intended purpose of the loan.**

The customer deposits of these two specialist banks have continued to grow, and in 2013 amounted to approximately CHF 1.5 billion. This represents growth of eleven per cent compared with the previous year.

**Deml, Max/Blisse, Holger 2011: Grünes Geld. Das Handbuch für ethisch-ökologische Geldanlagen 2012/2013 [Green Money: an ethical/environmental investment handbook 2012/2013]. Stuttgart: Hampp Verlag. pp. 9.*
***Cf.: www.gemeinschaftsbank.ch and www.abs.ch.*

The financial service providers surveyed are also assuming that their sustainability teams will grow. The majority is planning to increase staffing levels.

The study participants also forecast positive developments over the next ten years. Several players anticipate strong growth, particularly in the integration of sustainability criteria into financial analysis. Some expect that factoring ESG criteria into company analysis will have established itself as standard within ten years. In contrast to the mainstreaming of sustainable investments, two market players envisage the parallel development of a niche market for specific sustainable investments offering particular social and environmental added value.

The study participants also anticipate a further growth surge in the engagement and voting investment strategies, and one anticipates a corresponding decline in the best-in-class and exclusion strategies. One study participant highlights the danger of greenwashing.

Conclusion

In 2013, the market for sustainable investments once again showed strong growth, with a growth rate of almost 17 per cent. Institutional and private investors showed growing interest even though the growth rates of the early years were not maintained. Nonetheless, the sustainable investment market is still a niche market: sustainable investment funds still account for less than four per cent of the market as a whole, and have seen only minimal growth compared with the previous year. The optimism about the future displayed by players on the financial market gives reason to hope that there will be some movement here over the next few years.

Study participants

Below is a list of all the study participants who have consented to have their names included:

- ACATIS Fair Value Investment AG
- Bank J. Safra Sarasin
- Bank Vontobel AG
- Banque Cantonale de Genève – BCGE Asset Management
- BlueOrchard Finance S.A.
- Care Group AG
- CONINCO Explorers in finance SA
- Craton Capital Ltd
- Credit Suisse AG
- De Pury Pictet Turrettini & Cie S.A.
- Ethos Services SA
- Hauck & Aufhäuser (Schweiz) AG
- LGT Capital Management
- Migros Bank AG
- Notenstein Privatbank AG
- Pictet Asset Management
- Quantex AG
- Raiffeisen Schweiz Genossenschaft
- responsAbility Investments AG
- RobecoSAM AG
- Swisscanto Asset Management AG
- Symbiotics SA
- UBS
- Zürcher Kantonalbank

Swiss Sustainable Investment Market

million CHF / Euro	2012		2013	
Funds	25,494 CHF	21,118 €	28,630 CHF	23,322 €
Mandates	22,092 CHF	18,300 €	27,462 CHF	22,370 €
Str. Products	927 CHF	768 €	621 CHF	506 €
Total	**48,513 CHF**	**40,186 €**	**56,713 CHF**	**46,198 €**
Asset Overlays	739,049 CHF	612,201 €	1,911,777 CHF	1,557,329 €
Total including Asset Overlays*	**747,120 CHF**	**618,887 €**	**1,918,346 CHF**	**1,562,680 €**
Investment Approaches (multiple choice)				
Exclusions (including Asset Overlays)	747,129 CHF	618,894 €	1,917,480 CHF	1,561,975 €
Exclusions	31,451 CHF	26,053 €	35,066 CHF	28,565 €
Best-in-Class	25,158 CHF	20,840 €	31,216 CHF	25,428 €
Integration	19,299 CHF	15,987 €	24,441 CHF	19,910 €
Sustainable Themes	14,432 CHF	11,955 €	13,579 CHF	11,061 €
Engagement	11,647 CHF	9,648 €	11,519 CHF	9,383 €
Voting	10,996 CHF	9,109 €	16,982 CHF	13,833 €
Norms-based Screening	8,897 CHF	7,370 €	12,833 CHF	10,454 €
Impact Investment	2,901 CHF	2,403 €	5,195 CHF	4,232 €
Asset Classes				
Equity	25,244 CHF	20,911 €	27,618 CHF	22,498 €
Corporate Bonds	na	na	12,912 CHF	10,518 €
Sovereign Bonds	na	na	5,506 CHF	4,485 €
Bonds	16,728 CHF	13,857 €	18,418 CHF	15,003 €
Venture Capital/Private Equity	898 CHF	744 €	869 CHF	708 €
Alternative/Hedge Funds	779 CHF	645 €	414 CHF	337 €
Monetary/Deposit	680 CHF	563 €	717 CHF	584 €
Real Estate/Property	516 CHF	427 €	1,271 CHF	1,035 €
Commodities	2 CHF	2 €	3 CHF	2 €
Total	**44,847 CHF**	**37,149 €**	**49,310 CHF**	**40,167 €**
Not specified	3,666 CHF	3,037 €	7,403 CHF	6,031 €
Investor Types	**2012 CHF**	*in per cent*	**2013 CHF**	*in per cent*
Institutional	22,023 CHF	54%	28,624 CHF	59%
Retail	19,066 CHF	46%	20,042 CHF	41%
Total	**41,088 CHF**	**100%**	**48,666 CHF**	**100%**
Not specified	7,425 CHF	15%	8,047 CHF	14%

**Adjusted for double counting.*