

TIME TO INTEGRATE ESG IN ASIAN FIXED INCOME INVESTMENTS

Income Partners has been focused on Asian fixed income markets since its foundation in 1993. During these three decades we have seen numerous shifts in Asian fixed income landscape, including the establishment of Asian credit as a standalone asset class and the opening of the onshore Chinese bond market.

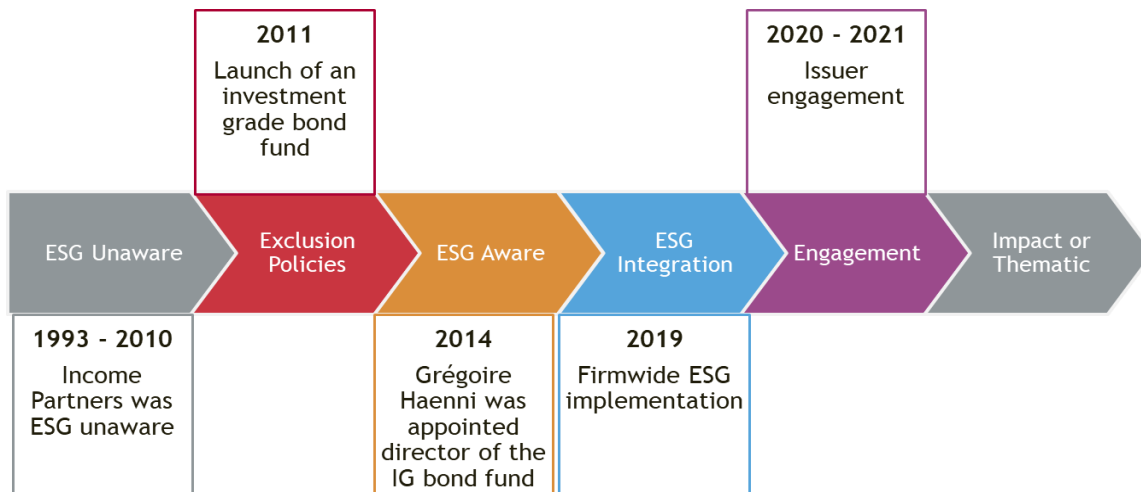
We believe that integration of Environmental, Social and Governance (ESG) factors in investment decision making is another significant shift. There has been a growing realization that asset owners must be responsible investors. By increasing the importance placed on ESG factors, corporates and other issuers can be influenced and persuaded to operate in more sustainable manners.



More importantly, our research has shown that performance and sustainability are not mutually exclusive. On the contrary, we are believers in the long-term value of being able to identify companies with improving ESG characteristics, which will be better equipped to attract capital and avoid potential financial risks down-the-line. We believe that a company's commitment to sustainability (including good corporate governance) will allow it to better avoid defaults, and outperform its peers in the long run.

DEVELOPMENT OF INCOME PARTNERS ESG COMMITMENT

Prior to 2011, Income Partners was ESG unaware, though corporate governance has always been a significant factor in our credit analysis.





In 2011, a Swiss-based pension fund seeded an investment grade bond fund managed by Income Partners. Then CIO of the pension, Mr. Grégoire Haenni, has always been a proponent of responsible investing. Under his guidance, Income Partners embarked on a sustainable investing journey starting with exclusion policies among certain mandates.

After joining a Geneva state pension fund in 2014, Mr. Haenni also became a board member of the investment grade mandate, thus becoming our firm's de-facto adviser in ESG. During 2014 - 2018, Income Partners continued to evolve our ways around ESG awareness and recognized the positive contribution ESG considerations can make to investment outcome.

In 2019, we started to formalize our policies on ESG by integrating it into our investment process. This resulted in the documentation in 2020 of our ESG objectives and principles as a firm in our ESG Responsible Investing Policy. In 2021, we further enhanced our commitment by becoming a signatory of the Principles of Responsible Investment ("PRI") and also became a member of the Asian Investors Group on Climate Change ("AIGCC"). We also established an ESG Committee to oversee our ESG policies and procedures and have started developing our internal ESG rating system, in which our issuer engagement is key.



Today, we embrace ESG in not only our investment processes, but also in our commitment to engage issuers we invest in. We believe we can drive positive change in sustainability through continual dialogue with issuers, which allows us to gain a deeper perspective on the company that would otherwise be lacking without a broader ESG angle.

Over the past two years, we have put increasing emphasis on issuer engagement and proprietary ESG research.

WHY ACTIVE ENGAGEMENT?

It is our belief that, by active engagement with issuers to improve their ESG disclosures and practices, we as asset owners create value for both investors and corporations we invest in. Engagement leads to a better flow of information and quality of understanding between companies and investors, thereby enhancing issuers' value and, ultimately, investment returns.

Engagement involves communicating with issuers to understand their ESG practices, initiatives and challenges, and then encouraging issuers to improve their ESG related disclosures and practices. Subsequently, we will follow up with issuers to monitor the implementation of suggestions.



All steps of the issuer engagement are documented in our internal research systems.

From time to time, we seek to collaborate with other asset managers to influence corporate behavior when opportunities arise. This could be through ad hoc groupings or through formal organizations. We are currently a signatory of the UN Principles for Responsible Investment (UNPRI) and a member of the Asia Investor Group on Climate Change (AIGCC).

We have not focused on impact or thematic ESG investing primarily due to a seemingly un-balanced supply / demand dynamics in such investment securities. For example, the Asian green bond market and issues from certain ESG aligned sectors tend to see excess demand hence relatively rich pricing.

OUR PROPRIETARY ESG RESEARCH

Similar to our credit research processes, we supplement external ESG analysis and data with our own proprietary research. Our team of ESG professionals and credit analysts jointly analyze ESG factors, challenges, risks and practices for issuers that we cover. This includes analysis of public disclosures and management interactions.

Typical factors which we consider in our ESG analysis include:

Environmental	Social	Governance
<ul style="list-style-type: none">• Environmental responsibility• Climate Change (including related physical, transition and liability risks)• Greenhouse Gas (GHG) Emissions• Pollution and contamination of land, air and water• Eco-efficiency and resources efficiency• Waste management• Natural resource scarcity• Biodiversity	<ul style="list-style-type: none">• Equal opportunity independent of gender, race or religion• Influence over local communities and other stakeholders• Maintenance of working conditions that surpass basic health and safety standards	<ul style="list-style-type: none">• Maintenance of good corporate governance standards• Anti-bribery and corruption measures• Business ethics• Transparency and accountability

The results of our internal ESG research and engagement efforts are then summarized in issuer ESG scorecards. Certain issuers with extremely high ESG risks, lack of disclosure or poor engagement records could be placed on watch lists for exclusion.



Portfolio managers would use the ESG factor analysis, internal ESG scorecards as well as external ESG data as important factors in deciding inclusion and weightings of credits in portfolios, in addition to traditional factors of credit worthiness, relative valuations and technicals.

WHAT IS IN ESG ASIAN FIXED INCOME FOR INVESTORS?

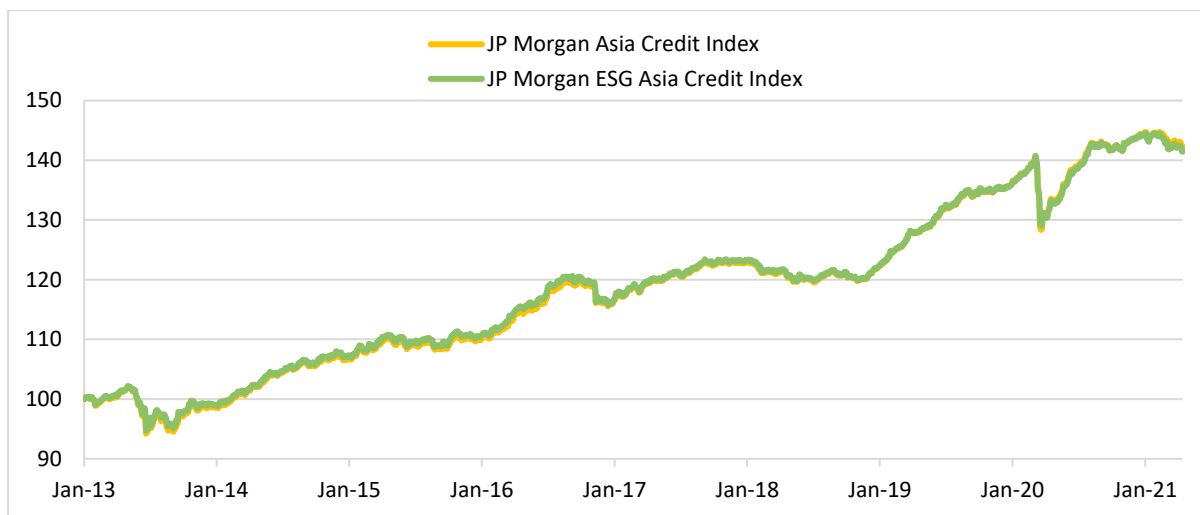
While many investors often fear that ESG investing can hurt returns, diminish diversification and can be difficult to implement when constructing a portfolio, we believe that these assumptions are untrue and that ESG investing can instead help investors achieve better overall performance.

Competitive returns

It is true that green bonds and certain thematic securities may trade with relatively tight valuations, potentially leading to lower returns in the long term. However, this is offset by potentially reduced risks emanating from better ESG management and also lower volatility given supportive technicals.

The chart below compares the performance of the JP Morgan Asia Credit Index (JACI) with the JACI ESG index, and shows that there has been little differentiation between the two indices in terms of total returns over the past 7 to 8 years.

JACI vs JACI ESG Index Total Return



Source: JP Morgan, April 2021

We believe that good ESG quality can help companies to develop competitive advantage and avoid potential liabilities, which can then drive outperformance in corporate financials and, ultimately, lead to better returns for investors.



Diversification benefits

Integrating ESG principles needs not sacrifice diversification. According to an MSCI report, one way to do so is by increasing the weights of companies with strong ESG profiles while minimizing exclusions to a core group of objectionable sectors. The back-testing result of the Income Partners investment grade bond strategy adopting such approach clearly validates this thesis.

ATTRACTIVENESS OF THE INCOME PARTNERS APPROACH

We believe that it is a misconception that only equity holders can influence management behavior regarding ESG matters. As a matter of fact, issuers tend to approach bond markets more frequently than equity markets. As more investors integrate ESG considerations in their investment processes, improved disclosures and practices could lead to lower funding costs. Conversely issuers with poor ESG ratings would face rising funding costs. At the extreme, companies with extremely poor ESG records, could be shut out of bond markets.

Armed with 27+ years of Asian credit research experience and strong commitment to ESG investing, with investment research teams in both Hong Kong and Shanghai, Income Partners is well positioned to deliver strong value proposition to ESG Asia bond investments. We invest in a large pool of regular securities of fixed income issuers with strong or improving ESG characteristics, in addition to solid fundamentals and attractive valuation, therefore investors' return and diversification goals are not compromised with ESG investing.



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