

SPAINSIF
STUDY
2018

SUSTAINABLE AND
RESPONSIBLE
INVESTMENT
IN SPAIN

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A LETTER FROM OUR SPONSOR

ESG investment shifts into a higher gear



Steffen Hörter
Global Head of ESG
Allianz Global Investors

The rate at which responsible investment is becoming a mainstream concern has accelerated into 2018. While sustainable asset flows continue to grow, I have personally observed passion and decisiveness about ESG integration at last year's "PRI in Person" conference, been at the centre of AllianzGI's programme to promote sustainability across asset classes, and enjoyed interacting with our clients on such issues worldwide.

Investors are recognising the relevance of ESG factors to financial performance, while responsibility for integrating them is shifting from niche concern to being on every CIO's agenda. Companies that recognise and manage this are increasingly attractive to investors, while those that ignore it can be perceived as riskier. The paradigm is shifting.

And it's not just equities: in our 2017 study ESG factors - why they matter for sovereign bond portfolios, we turned the spotlight to Turkey nearly a year before political and economic challenges emerged, showing how identifying ESG tail risks is crucial to protecting investment performance.

Climate change is a good example of the broader societal risks and opportunities that ESG strategies account for. With an urgent need to transition to a low-carbon economy to curb the impact of global warming, there are opportunities to invest in new products (such as green bonds or renewable energy infrastructure) or companies that are considered climate leaders. We have developed our product range to include both over the last two years.

We are proud to have received an A+ for Strategy & Governance in the PRI's Assessment Report for the second year in a row. It strengthens our conviction that ESG factors can be important performance drivers when adopting an active approach to asset management. More importantly, feedback from our clients shows they value this expertise and the transparency with which we use it to help them achieve their financial - and extra-financial - goals.

The responsible investment movement has shifted gear, and it's great to see the opportunities and solutions it offers to global, real-world challenges.

A LETTER FROM OUR CHAIRMAN AND GENERAL DIRECTOR



Jaime Silos Leal
Chairman



Fco. Javier Garayoa
General Director

We present this year's review of SRI in Spain in the hope of meeting the expectations for information on the entire group of businesses that are committed to sustainable and responsible investment, who we must not disappoint.

We are talking about both market operators that comprise the supply of products and institutional investors and individual savers, without forgetting key players such as regulatory and supervisory bodies, the academic world, civil society and trade union representation.

As new features added to this review, we can highlight that, along with the analysis of the assets managed under SRI strategies in Spain, following the European and global methodology of Eurosif and the GSIA, we can add, among other contents, a statistical evaluation that considers aspects as important as a comparison between general indexes and of sustainability, showing the progress of investments that apply ESG criteria compared to those that do not.

Without wishing to be complacent in our conclusions, given that we still have a long road to travel, we can at least be optimistic regarding the market trend, to the extent that in recent years highly significant volumes have been consolidated with growth maintained, and, above all, with a clear improvement in with a clear improvement in the quality of sustainable investment, growth in best-in-class strategies and the inclusion of ESG rather than exclusion, which is the result of greater demand in the fiduciary mandates of the owners of institutional assets and a greater awareness in the demand of individual savers/investors, although in this case the response is still only symbolic.

At Spainsif, as a forum representing sustainable investment, we are pleased with the result and evaluations shown in this review, which encourage the association and all groups involved to continue working to make sustainable investment gain influence in the asset management market and representation in the investment policies of the financial and insurance sector.

We would like to take this opportunity to repeat that the sustainable investment market in Spain needs to achieve its rightful importance, and to do this the commitments of the financial sector to sustainability must be realised, by backing the support required so that the global objectives related to energy transition, COP21, and the directives established by the United Nations regarding sustainable development goals, SDGs can be achieved in the 2020-2030 period.

We would not like to end without highlighting the fact that we are at a moment of change that is clearly favourable to sustainable investment, both because of the trend of global markets and because of the commitment of European bodies, as shown by the Sustainable Finance Action Plan of the European Commission, which understand that in order to achieve the financial stability of European markets and channel savings towards sustainable investments, environmental social and governance criteria must be accepted and internalised.

We would especially like to thank our associates for the support they have provided and the related organisations and institutions for their contributions.



ASSOCIATED MEMBERS



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EXECUTIVE SUMMARY

Sustainable and responsible investment (SRI) is understood as the philosophy that through a long-term approach integrates environmental, social and governance criteria (hereinafter ESG criteria) in the process of the study, analysis and selection of securities in an investment portfolio.

It is a combination of fundamental analysis and active management, “engagement”, including an evaluation of ESG factors in order to achieve greater long-term profitability for investors, thereby benefiting society through the influence it has on the behaviour of companies¹.

This definition, agreed by the various European sustainable investment forums is a starting point to understanding that sustainable and responsible investment is a broad concept that encompasses various ways of investing.

Therefore, sustainable and responsible investment includes traditional ways of investing such as investment funds and pension plans (which take ESG criteria into account in their investment policies), new aspects of products that are widely used such as green, social and sustainability bonds (debt products used to finance projects related to the green, social or sustainable economy) and new approaches, such as impact investing (this type of sustainable and responsible investment seeks to achieve both competitive financial returns and produce a significant environmental and/or social impact).

The numerous ways in which sustainable and responsible investment can be applied could make investor and/or savers frightened by the amount of information that they can access about this type of investment and its applications, being unable to differentiate an SRI product from another kind of investment related to the green or social economy, philanthropy or solidarity investment products.

To solve this problem, INVERCO (the Spanish Association of Collective Investment Schemes and Pension Funds) published a circular², with the cooperation of the Government and Spainsif, about the application of ESG criteria in the investment policy of collective investment schemes (CISs) and pension funds. This circular considers sustainable and responsible investment strategies applied by Eurosif (the European association for the promotion of sustainable investments) and the GSIA (the Global Sustainable Investment Alliance).

¹ European SRI Study 2016. Eurosif 2016.

² Circular on the application of environmental, social and corporate governance (ESG) criteria on the investment policy of collective investment schemes (CISs). INVERCO 2014.

Nowadays, this type of investing is becoming increasingly important, because of the international Initiatives related to the fight against climate change (Paris Agreement³) and to sustainable development (Sustainable Development Goals and the 2030 Agenda of the United Nations⁴).

These are actions that, as well as including direct references to the amount of financing required to carry them out, are also being used to promote initiatives related to the development of a sustainable financial system. Some examples of these initiatives are the Task Force on Climate-related Financial Disclosures, the Principles for Responsible Investment, the Principles for Sustainable Insurance, the development of an initiative on sustainable banking by the UNEP FI, or the Action Plan on Sustainable Finance of the European Commission.

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Because of this trend it has become necessary to monitor and evaluate the sustainable and responsible investment market in order to discover if both the managers and owners of assets are aligned with these initiatives and, therefore, with the SRI market.

In this review, we look more deeply at how national organisations are promoting the development of a sustainable financial system in Spain, through the integration of the various SRI strategies into their investment policies.

We also analyse how the sustainable financial products belonging to collective investment schemes are growing, both domestic and foreign, that are marketed in Spain, as well as the growth of pension plans, both individual and employment plans that include SRI strategies in their investment policies.

We include a comparative review between the performance of sustainability indexes and leading stock market indexes at a national and European level, as a consequence of the increasingly greater presence of passive management products with ESG criteria.

In conclusion, the sustainable and responsible investment market in Spain continues to follow the path of growth as shown in previous years, between 2015 and 2017 recording a growth rate of 10%, thereby reaching 185.614 million euros, which represents a share of the domestic market for collective investment institutions and pension funds of 46%.

Regarding the sustainable and responsible investment strategies most widely used, exclusion (9% growth rate) continues to be the main strategy for managed assets. However, there has been a striking change in a trend towards more advanced SRI strategies, such as best-in-class (250% growth rate) or the integration of ESG criteria (97% growth rate). The positive growth is shown in all strategies except that of norm-based screening (-44% growth rate) there being a diversion towards more advanced strategies.

Regarding sustainable and responsible investment funds marketed in Spain by collective investment schemes, both domestic and foreign, there are over 30 billion of assets being managed, with a growth

³ Paris Agreement. UN 2015.

⁴ Sustainable Development Goals. UN 2015.

rate in the last two years of 32%, a figure that is higher than the total figure for the investment funds market, which grew by 20% in the same period. This growth trend, with a leading role being played by investment funds owned by foreign institutions, has spread to domestic collective investment schemes, whose number of ESG investment funds being marketed has grown by 53% in the last year, reaching 23 investment funds.

The results obtained in this analysis are very positive for the sustainable and responsible investment market in Spain, because, on one hand, domestic institutions are making great efforts to advance in their investments strategies with ESG criteria, as shown by the changing trend in the SRI strategies used, and also because it has been observed how the demand for investment products that include these criteria is growing at a rate that is far quicker than that of the general market.

This demand that, although it is being channelled through investment funds belonging to foreign institutions, which tend to have more highly developed ranges of ESG investment products, is making domestic institutions broaden their supply of this type of product in order to satisfy the demand from their clients.

Regarding the pensions market, individual ESG pension funds are starting to be marketed in Spain, with a purely symbolic presence both in terms of assets and number of funds, recording a growth of 4.18% in recent years, which represents a total of 1.25 billion euros of assets being managed.

The situation of employment pension funds is completely different, which continues to be a key player in the domestic SRI market, where 72% of the total include ESG criteria, representing equity worth 28 billion euros.

As a complement to the above studies, we have developed a comparative analysis between the FT-SE4GOOD Ibex Index and the Ibex 35 and Dow Jones Sustainability Europe Index and the STOXX 50 Index, where statistically significant differences have been observed in returns in favour of sustainability indexes.

The main conclusion of the review is that sustainable and responsible investment in Spain is at a turning point where its growth rate is becoming consolidated and the quality of SRI, in terms of growth through strategies, has taken a qualitative leap forward, which is a sign of the greater maturity of the Spanish SRI market.

Concerning the products marketed in Spain with ESG criteria, we would highlight the positive work carried out by foreign institutions, which provide their experience to international markets, and the growing activity in the supply of products by domestic institutions as a response to a growing trend in the demand for ESG investment products.

WARNING: This review includes and presents information and evaluations arising from them, but, under no circumstances, reflects the opinions or stance of Spainsif or of its associates.



1. INTRODUCTION

The progress of the world economy closed 2017 with growth of 3%, which according to the United Nations (hereinafter the UN) “represents strong growth compared to the meagre 2.4% of 2016 and constitutes the highest global growth rate since 2011”, maintaining the favourable forecasts for 2018 and 2019.

For its part, the Spanish economy has been growing for four years, since it managed to come out of recession in 2014. In the last years, Spain has consolidated its growth at above 3%, achieving rates above the global growth rate and that of the eurozone, which closed 2017 with growth of 2.4%.

At a global level, the investment conditions have improved due to the low instability, reduced weakness in the banking sector and generally low financial costs. Regarding Spain, its growth has been based on domestic demand, thanks to the favourable credit conditions, the improvement in household confidence and the good outlooks for the labour market. These favourable conditions have meant that the financial saving of Spanish households closed 2017 at around 2.1 trillion euros (182% of GDP)¹.

Regarding collective investment schemes (CISs) and pension funds, at the close of 2017 at a global level it was estimated that there was invested equity of 41.1 trillion euros in CISs and invested equity in pension funds of 26.1 trillion euros. In 2017 in Spain, the CIS market represented 14.8% (463.886 million euros) of all financial saving, while the pension fund market represented 5.7% (111.077 million euros) of all financial saving. These markets also experienced the highest growth rates in recent years, beating the deposit market share, the reference used in Spain, with a share of 37.3% of all financial saving².

The good performance of both the economy and the financial markets, especially of collective investment schemes and pension funds, together with increasingly greater support from investors, international institutions and countries for matters related to sustainability (economic, environmental and social criteria), mean that it is possible to forecast positive progress for the socially responsible market on a global level, and also on a domestic level, both in terms of quantity and quality.

Therefore, institutional investors are increasingly more committed to investment with socially responsible criteria. One example of this is the international support from the owners of assets and managing institutions for the Principles for Responsible Investment (hereinafter PRI).

¹ World Economic Situation and Prospects 2018. UN 2018.

² Collective Investment Schemes and Pension Funds. 2017 Report and 2018 Prospects. INVERCO 2018.

PRI is an organisation whose objective is to create and support an international network of investors that are in agreement with the incorporation of environmental, social and good governance (ESG) criteria in their investment decisions.

At the beginning of 2018, this organisation had 1,961 signatories, which represented equity of 16.3 trillion euros, with a growth rate between 2016 and 2018 of 28%. The support for this initiative has shown that there is an increasing number of institutional investors committed to incorporating ESG criteria in their investment decisions.

Also, there is growing interest by individual investors in including sustainability criteria in their Investment decisions. Regarding this group, in 2017 the asset manager Schroders published the results of an independent online survey given to 22,100 people from 30 countries from around the world, such as Australia, Brazil, Canada, China, France, Germany, India, Italy, Japan, the Netherlands, Spain, the United Kingdom and the United States². At the time of answering, those surveyed were active investors, having made changes in their investments or having invested at least 10,000 euros (or its equivalent) in the last ten years.

The results, on a global level, established that 78% of those surveyed placed greater importance on sustainable and responsible investments than five years previously. Also, 42% stated that they often invested in products that complied with these criteria.

The results were also positive in Spain, as 81% of the surveyed investors stated that they placed Greater importance on sustainable and responsible investments than five years previously.

Of these, 61% said that they had increased their investments in sustainable funds and 35% said that they often invested in these types of products.

Initiatives concerning sustainability related to sustainable and responsible investment

The increase in interest from investors, both institutional and individual, in sustainable and responsible investments, coincides with initiatives of the international community to promote the development of environmental and social policies connected to the transition to a low-carbon economy and corporate responsibility.

Because of their implications, the two most important initiatives are the Paris Agreement on climate Change and the Sustainable Development Goals of the United Nations (SDGs).

Regarding the first, since 1995 the United Nations has held an annual Conference of the Parties (COP) participating in the Framework Agreement of the United Nations on Climate Change (FAUNCC).

These conferences are the governing body of the FAUNCC, in which the United Nations, its specialised bodies and the parties, that is the member countries of the Treaty. The goals of the COP includes the duties of developing the negotiation process for the commitments adopted concerning climate change and of supervising and examining the application of said commitments. This conference has approved agreements such as the Kyoto Protocol (1997) and the Paris Agreement (2015).

The 2015 Paris Agreement is considered the most important binding agreement on climate change in

³ Global perspectives on sustainable investing 2017. Schroders 2017.

history and has been ratified by 96 countries and the European Union, which represents over 55% of greenhouse gas emissions worldwide.

The objective of the agreement is to limit the global average temperature increase to below 2°C compared to pre-industrial levels until the end of the 21st century. It also seeks to increase the ability to adapt to climate change and align the financial market with the process of transition to a low-carbon economy. All of the above in the context of sustainable development, the eradication of poverty and food security.

To achieve the objectives established in the agreement, an investment of 1.3 trillion euros a year will be required until 2030, according to the United Nations Environment Programme.

In the case of the SDGs, these provide continuity to the achievements of the previous initiative, the Millennium Goals. The main objective of the Millennium Goals was the fight against extreme poverty, which, although they achieved unprecedented progress regarding the reduction of inequalities and poverty by countries through international cooperation, were not able to align themselves with the private sector.

Since their origin, SDGs have provided initiatives to integrate the corporate, private and financial sector in the development and achievement of these objectives. Therefore, SDGs are negotiated between the 193 member states of the UN, with the participation of civil society, the corporate sector and other interested parties. The 17 resulting goals, divided into 169 targets, are broad in scope and cover elements that are inter-connected with sustainable development, such as economic growth, environmental protection and social inclusion.

Regarding the private financing required to achieve these goals, according to the Business and Sustainable Development Commission, 10 billion euros a year will be required until 2030.

The Sustainable Finance Action Plan of the European Commission

Concerning sustainable finances, there is a new Sustainable Finance Action Plan that the European Commission set up in the first quarter of 2018. The objective of this action plan is to improve the role of finances in the development of an economy that is aligned with the goals of the Paris Agreement and the agenda of the European Union for sustainable development based on SDGs.

Figure 1 shows how this action plan has developed and how it will develop in the future.

The action plan is divided into three main objectives that will be achieved through ten specific actions. The objectives are

- To reorient capital flows towards a more sustainable economy
- To mainstream sustainability in risk management
- To foster transparency and long-termism in the financial sector

The European Commission has already put in motion the first legislative proposals associated with the action plan, in order to:

1. Develop regulations that will include a classification of sustainable activities to generate a common language concerning sustainable finances.

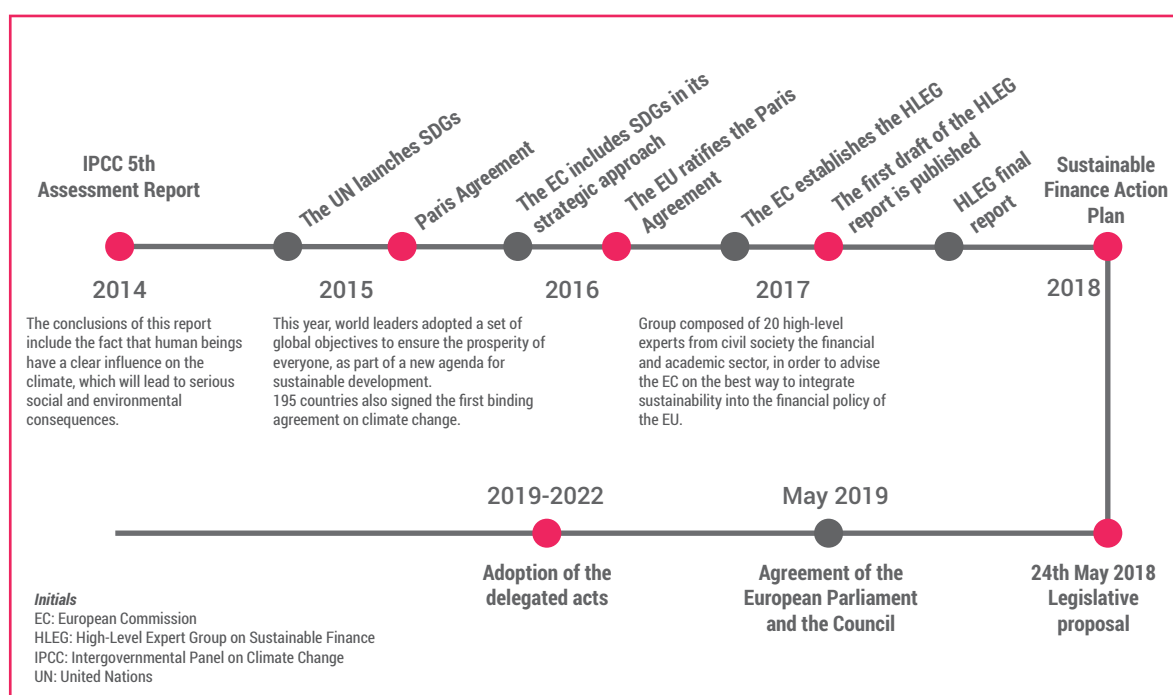


Figure 1: Progress of the Sustainable Finance Action Plan of the European Commission. *Source: Spainsif.*

2. Draft regulations that will establish obligations for asset managers, institutional investors and financial institutions, with the objective of integrating ESG criteria into investment decision-making processes.
3. Develop regulations in order to incorporate ESG criteria into financial advisory processes and the distribution of insurance products, so that both advisers and distributors will be obliged to be informed about the preferences of their clients concerning ESG criteria in the product selection process and their suitability assessment.
4. Draft regulations that will include low-carbon indexes and positive carbon impact indexes as new categories in leading stock exchange indexes.

National initiatives concerning sustainability related to sustainable and responsible investment

Legislative initiatives are also being prepared nationally regarding sustainable development and the transition to a low-carbon economy. Regarding SDGs, the Spanish Government has submitted a national evaluation report to the United Nations containing a first set of priority policies regarding sustainable development. Most of these policies are in their consultation or discussion phase, and all of them are in line with economic development that will consider environmental protection and social values.

These policies are focused on the prevention of and the fight against poverty, inequality and social exclusion, sustainable regional and urban development, the circular economy, climate change and

energy transition, sustainable scientific/technical development, the social economy, the development of open government and international cooperation.

Finally, concerning climate change and energy transition, the Spanish Government is aligned with the Paris Agreement and is preparing a climate change and energy transition law in order to promote a fair and supportive transition of the Spanish economy, by making the most of opportunities and identifying the guidance measures required that will improve Spain's resilience to the impacts of climate change.



2. GLOSSARY

Sustainable and responsible investment: An investment philosophy that integrates environmental, social and good governance criteria into the study, analysis and selection process of securities in investment portfolios.

Environmental Criteria: Objectives that are related to any aspect of the activity of a company that affects the environment positively or negatively. For example, greenhouse gas emissions, renewable energies, energy efficiency, the exhaustion of resources, chemical pollution, waste management, water management, impact on biodiversity, etc.

Social Criteria: Social questions include everything from aspects related to the community, such as improvements in health and education, to questions related to the workplace, including complying with human rights, non-discrimination and the involvement of stakeholders. Examples of social aspects include those related to work legislation (on supply chains, child labour, forced labour), relations with local communities, the management of human talent, controversial commercial practices (arms, conflict zones), health legislation, freedom of association, etc.

Good Governance Criteria: Questions of good governance refer to the quality of management, the culture and the risk profile of companies, among other characteristics. These include the accountability of boards of directors, work and strategic management on social and environmental performance, the principles of transparent information and management that is free of abuses and corruption. Examples of good governance include all aspects of corporate governance, such as the remuneration of executives, shareholder rights, management structure, corruption, dialogue with stakeholders and lobbying activities.

Sustainable Finance Action Plan of the European Commission: This is a road map with the objective of strengthening the role of finances in building an economy that will make it possible to achieve the objectives of the Paris Agreement and of the agenda of the European Union (EU) for sustainable development.

Paris Agreement: A global agreement concerning climate change, which is legally binding, through which all signatory countries undertook to participate in global reductions of greenhouse gases.

Sustainable Development Goals: A universal call for the adoption of measures to put an end to poverty, to protect the planet and guarantee that all people will enjoy peace and prosperity. This is an initiative developed by the United Nations.

Green, social and sustainability bonds: A financial product that is similar to a traditional bond, the only peculiarity of which is that the capital invested is used to finance projects related to environmental protection, social well-being and sustainability.

Private Equity: An activity carried out by specialised institutions that consists of the temporary supply of financial resources in exchange for a holding in non-listed companies with high potential growth.

Crowdfunding: A mechanism for financing projects through small economic contributions by a large number of people.

Investment Fund: This consists of equity composed of the contributions of a variable number of investors, called participants. The fund is created by an institution, the manager, which is the institution that jointly invests these contributions in various financial assets (fixed income, variable income, derivatives or any combination of these, etc.) following guidelines that are established in advance.

Active and passive management: Active management means that one or more managers are responsible for the management of the fund. Passive management replicates the composition of a certain stock market index.

Collective Investment Schemes: Schemes that gather funds, assets or rights to jointly invest and manage them in financial or non-financial assets.

Microfinance: Financial services for people with low incomes, including micro-enterprises, entrepreneurs and the self-employed.

Pension plans and funds: A pension plan is a contract through which the saving related to retirement is channelled. Their main features are that they are privately contracted and voluntary (through individual savings) and they are complementary in nature, because under no circumstances do they replace state pensions. A pension fund is independent equity where the contributions of people that have contracted a pension, called participants, accumulate.

Acronyms

ESG	Environmental, Social and Governance criteria
CNMV	The Spanish Stock Market Commission
COP	Conference of the Parties (Conventions on climate change)
UNFCCC	United Nations Framework Convention on Climate Change
DGSFP	The General Directorate of Insurance and Pensions
ETF	Exchange-Traded Fund
GSIA	Global Sustainable Investment Alliance
CIS	Collective Investment Scheme
INVERCO	Spanish Association of Collective Investment Schemes and Pension Funds
SRI	Sustainable and Responsible Investment
SDGs	Sustainable Development Goals
SIF	Sustainable Investment Forum
UNEP FI	The United Nations Environment Programme - Finance Initiative



3. OBJECTIVE AND METHODOLOGY

Due to the growing interest of both investors and by international institutions and countries regarding sustainability, it is becoming increasingly essential to carry out research that monitors how this interest is being translated to the financial industry. That is why Spainsif and its associates within the European (Eurosif) and global (GSIA) investment forums has carried out market research biennially, since its founding in 2009.

This history means that the reviews on the sustainable and responsible investment market, both by Spainsif and by Eurosif and GSIA are global benchmarks when providing reliable information about the volume and quality of sustainable and responsible investment.

Therefore, the main objective of this review is to carry out in-depth analysis of the sustainable and responsible investment market in Spain, both from the perspective of financial savings and from the perspective of investment products managed in investment and pension plans.

To do this, we have used various methodologies in order to achieve the broadest possible picture of the progress of the SRI market between 2015 and 2017.

Data compilation

Data compilation has varied according to the information requirements of the various types of analysis carried out in this review.

The analysis of managed assets is based on the results of a survey given to leading financial institutions, asset managers and owners of assets living in Spain, representing 75% of the equity managed professionally in Spain.

For information about investment funds, we have used the Spainsif fund platform, whose information is provided by VDOS, MSCI and Morningstar. The list of ESG investment funds belonging to institutions domiciled in Spain was provided by the NSMC and the list of ESG investment funds belonging to institutions domiciled outside of Spain and individual pension plans has followed an internal verification process by Spainsif, based on the match of investment policies with the INVERCO SRI circular¹.

¹ Circular on the application of environmental, social and governance (ESG) criteria on the investment policies of collective investment schemes (CISs). INVERCO 2014.

The information on employment pension funds was supplied by the General Directorate of Insurance and Pensions of the Ministry of Economy and Business.

The comparative data, both on national financial savings and on equity managed by collective investment schemes was collected by INVERCO.

Finally, sometimes the compilation of information has been completed by using available public information from the institutions studied or public bodies, both national and international.

We have not carried out any extrapolation processes in any of the analyses, and it is therefore likely that the results obtained undervalue the real size of the SRI market in Spain.

Data analysis and processing

The analysis of managed assets has been carried out based on the methodology used at European (Eurosif) and international (GSIA) level.

In order to preserve the comparison between reviews, we have considered some guidelines:

Firstly, because the figures included in the survey are added by strategies, the same volume of assets could be recorded in several of them.

To avoid this, we only recorded the volumes of assets in one of the SRI strategies.

Secondly, we have only considered financial groups located in Spain, because the high internationalisation of the asset management industry means that there are cases in which SRI funds are domiciled in one country, managed in another and sold in another.

Regarding the limitations of the scope of this review, although we have carried out a verification process, searching in detail for complementary information from other sources, it could be, due to the methodology used, that the results undervalue the actual size of the market in Spain.

Regarding the analysis of investment funds, we have used the average annualised returns

For each main investment category (variable income, fixed income and mixed income) in order to compare them to the total of the investment funds market traded in Spain.

We carried out the investments by strategies of employment pension plans by using weighting, based on information provided by the General Directorate of Insurance and Pensions, compiled by the pension funds themselves as compliance with legislation.

Finally, we carried out a study of stock market indexes, taking as our reference the returns on 1st January 2011, at base 100. Using R software for the calculation of the various statistics used.

Equation 1: Growth rate

$$TC = \frac{V_n - V_{n-1}}{V_{n-1}}$$

V_{n-1} : value at the time $n-1$

V_n : value at the time n

Equation 2: Compound annual growth rate

$$\text{CAGR} = \left(\frac{V(t_n)}{V(t_0)} \right)^{\frac{1}{t_n - t_0}} - 1$$

$V(t_n)$: Time value n

$V(t_0)$: Initial time value

$t_n - t_0$: Number of years between $V(t_n)$ and $V(t_0)$



4. ASSETS MANAGED UNDER SRI STRATEGIES

Since 2003, the association for the promotion and advancement of sustainable and responsible investment in Europe (Eurosif) has issued a biennial report on the progress of professionally managed assets using environmental, social and governance (ESG) criteria in Europe.

In this chapter we will categorise managed assets according to their various sustainable and responsible investment strategies. The strategies are used to include ESG criteria in asset management and are as defined globally by the Global Sustainable Investment Alliance (GSIA), an alliance that brings together all associations devoted to the promotion of sustainable and responsible investment, including Eurosif and Spainsif. The latter has been working with Eurosif since its founding to provide information about assets managed under ESG criteria on the Spanish market.

Globally, the assets managed professionally under these strategies amounted to 21 trillion euros, of which 52.6% were from Europe, according to the GSIA study on sustainable and responsible investment published in 2017¹. This equity represents 26.3% of all professionally managed assets in the world.

Assets managed under SRI strategies in Spain. Progress 2015-2017

In this section we present information on the progress of assets managed under ESGs in Spain between 2015 and 2017. This information is comparable to the information published by other SIFs, Eurosif and GSIA, because, except for minor exceptions, the methodology used is similar.

In this review, institutions that represented 299.744 billion euros of professionally managed assets completed the questionnaire, which represents 75% of all assets managed professionally by institutions domiciled in Spain.

In general terms, the managed assets that follow SRI strategies have been experiencing constant growth in Spain, since records first began in 2003.

¹ Global Sustainable Investment Review 2016. GSIA 2017.

Between 2015 and 2017, assets managed under ESGs in Spain amounted to 185.614 million euros, with growth in this period of 10%, 2.4% higher than the whole of the Spanish economy² and 3.7% higher than the leading stock exchange in Spain, the IBEX35³. This equity also represented 62% of the professionally managed assets of the surveyed institutions.

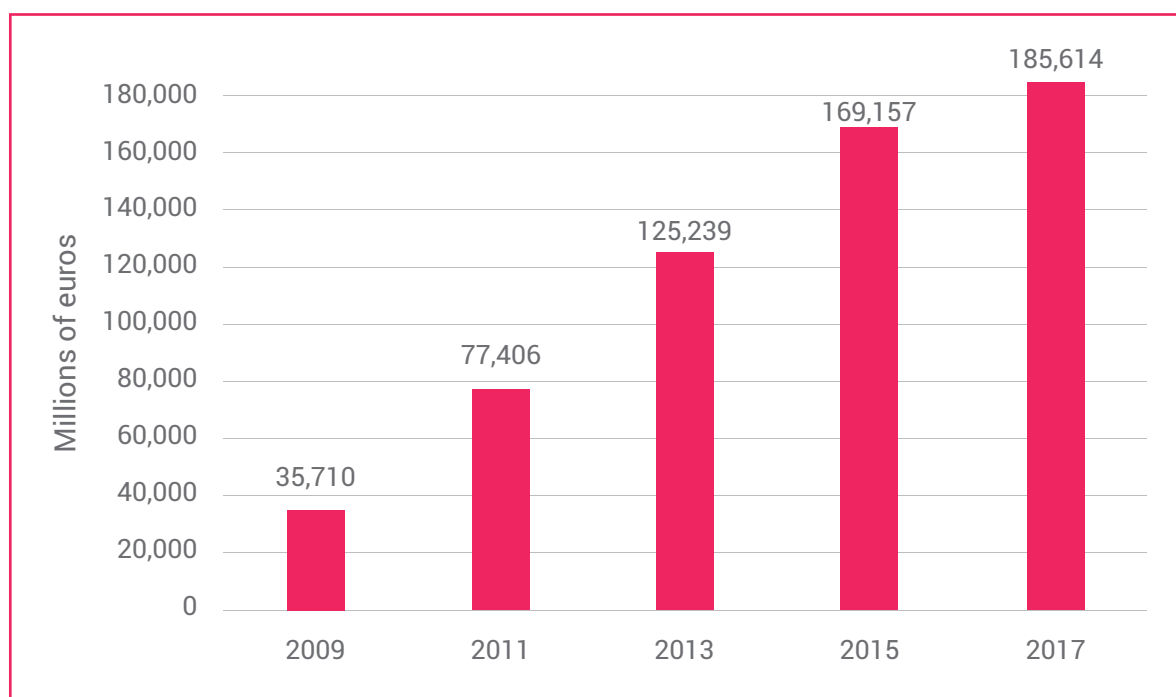


Figure 2: Progress of managed assets using ESG criteria by domestic financial institutions.

Source: Spainsif.

However, the growth of all the equity invested in collective investment schemes and pension funds between 2015 and 2017, excluding foreign collective investment schemes, was 2% higher than the growth rate of the sustainable and responsible investment market, with the market share remaining at 45% (Figure 3).

Assets managed with ESG criteria were mainly allocated to shares in companies (51% invested in variable income), 20% to corporate bonds in private institutions and 20% to bonds in public institutions (for fixed income, the asset allocation was 40%) (Figure 4a).

Also, the vast majority of investments were made in Europe, representing 78% of asset allocation.

In Spain, investments of assets managed with ESG criteria represented 23% (Figure 4b).

Comparing this asset allocation with the investment categories that INVERCO publishes, the portfolio of assets managed with ESG criteria would be a Euro Mixed Variable Income portfolio.

Regarding the VDOS investment categories, the portfolio would be in the Global Mixed Moderate category, and according to the Morningstar categories it would be a Euro-Global Mixed Moderate portfolio.

² National Institute of Statistics (NIS). NIS 2018.

³ Ibex 35. Bolsas y Mercados Españoles 2018.

These categories have a ccumulated profit over the last three years of 0.67% in the INVERCO category, 0.44% in the VDOS category and 1.19% in the Morningstar category.

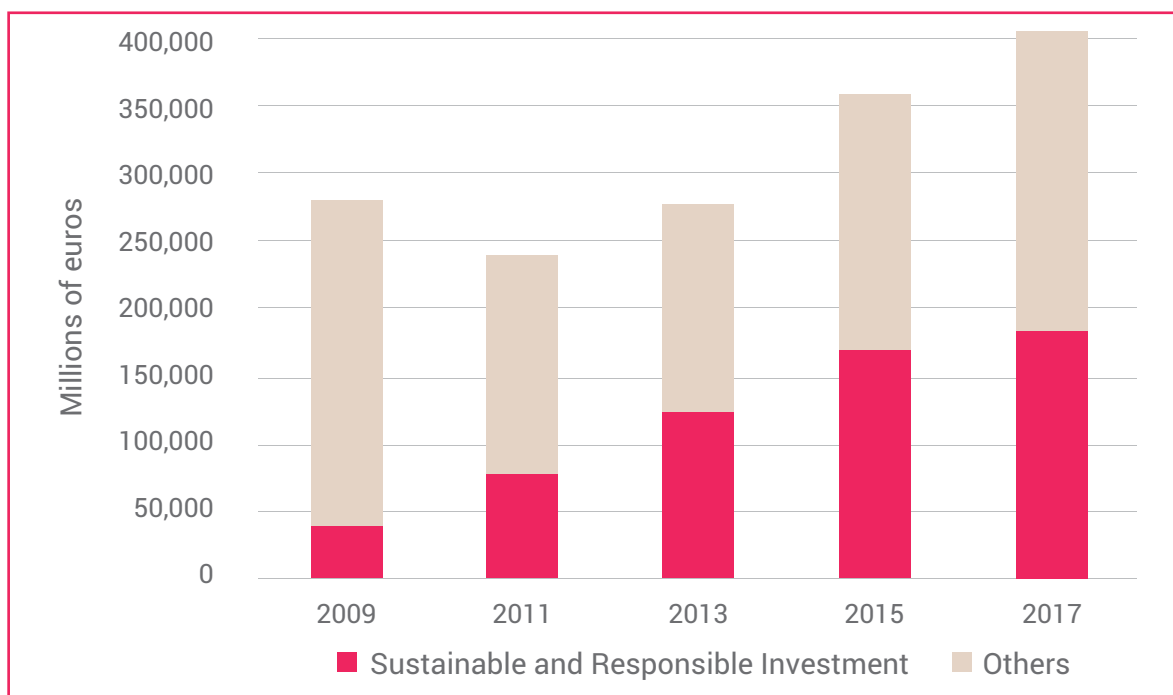


Figure 3: Comparison between ESG managed assets and all assets managed by national collective investment schemes and pension funds. *Source: Spainsif using INVERCO data.*

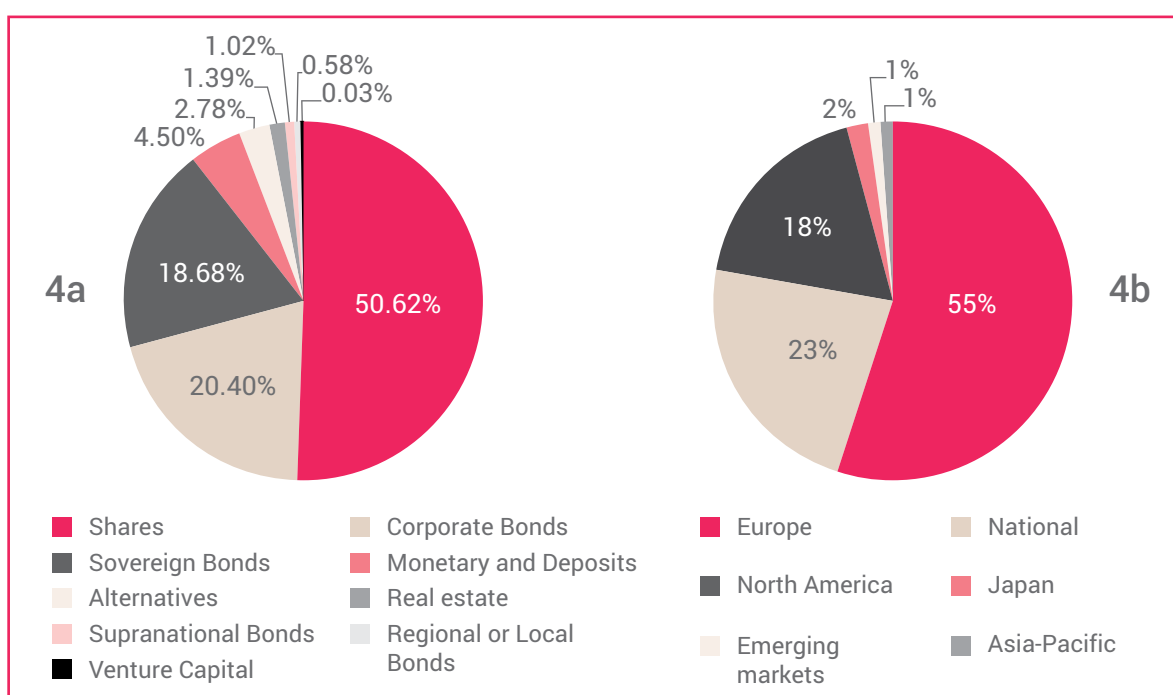


Figure 4: Allocation of assets managed with ESG criteria by type of investment (4a) and geographical distribution (4b). *Source: Spainsif.*

Sustainable and responsible investment strategies

Exclusion

This strategy is the simplest way to include ESG criteria in the management of financial assets.

It is based on finding among candidate institutions to be included in an investment portfolio, those companies whose activity is contrary to that defined in the investment policy.

Exclusion criteria differ from one financial institution to another, with the most common ones being arms, pornography, tobacco, nuclear energy and child exploitation.

Exclusion strategies have also started to be applied in recent years when investing in public debt. In this case, the most common exclusion criteria are applied to dictatorial regimes, the non-ratification of environmental agreements, institutional corruption, the violation of non-proliferation treaties, capital punishment or support for nuclear energy.

This strategy continues to be the most common globally today, representing 36% of all ESG managed assets.

Exclusion, therefore, should be understood as a strategy of minimums. A declaration of intentions by institutions committed to including ESG criteria in their investment strategies.

Norm-based screening

This strategy was conceived in northern European countries, as an evolution of exclusion and in order to give them a more regulatory character. In this case, it is not the institutions that manage assets that are responsible for deciding which securities to include in their portfolios and which to not. The process is based on whether the institutions comply with an external norm, usually international, or not, regarding environmental protection, labour rights, human rights or anti-corruption.

This is the natural step of an institution committed to sustainability in its investment process, ensuring that its sustainable and responsible investment strategy is in line with that of the various international bodies that issue these types of norms.

In general, the most commonly used norms are: The United Nations Global Compact, OECD guidelines for multinational companies, the norms of the ILO and the governing principles for companies and human rights. Globally, this strategy represents 15% of all ESG managed assets.

Best-in-Class

Best-in-class is characterised not by the exclusion of activities or sectors, it is characterised by the inclusion of those institutions that have better ESG performance within the various sectors and markets. This is the latest strategy that screens institutions when compiling their investment portfolios.

In this case, the applied strategy requires greater commitment by the institution managing the assets, because the ESG criteria to be evaluated and how these criteria are to be measured have to be defined. It is essential to produce a hierarchical list of the ESG performance of companies, including a system of weights according to the various ESG criteria that are considered.

The greater effort required to implement a best-in-class strategy characterises financial institutions and managers that take on greater commitment to sustainability in their investment policies.

A best-in-class strategy does not necessarily translate into high material and time costs, as it can be adjusted to the resources available. Firstly, there is an extensive and mature market of sustainable stock exchanges, which screen their members by region, sector, ESG or thematic performance, enabling passive management of portfolios (Dow Jones Sustainability, MSCI or Morningstar indexes).

Secondly, if there are greater requirements when managing assets, there are service providers that give information about the ESG performance of companies and countries depending on the needs of clients. In this case there would be companies such as MSCI, Sustainalytics and VIGEO-EIRIS.

Finally, for those institutions with more resources that wish to have total control of their best-in-class process, there is the alternative of having an ESG team within the institution that will extract, analyse and weight the ESG information of the companies to be selected, including the possibility to receive information from several service providers, indexes or ratings, thereby creating more innovative best-in-class strategies that will produce greater synergies in their investment philosophy, products and operation.

Overall, this type of strategy represents 2% of all assets managed with ESG criteria.

This strategy can be used as a bridge between negative screenings and integration, meaning that, in financial markets with sufficient ESG maturity, best-in-class screening usually progresses towards ESG integration.

ESG integration

This strategy is based on including the analysis of ESG criteria in the financial analysis that institutions make when making investment decisions.

ESG is the step after best-in-class. This exists in financial institutions and managers that have accumulated sufficient knowledge and experience in the definition and measurement of ESG criteria and have the ability to develop indicators that are comparable to those used in financial analysis, thereby achieving their integration without any need for an ESG screening.

The depth of detail and opportunities offered by ESG integration mean that many financial institutions and asset managers differentiate it from sustainable investment that applies other strategies.

ESG integration, although difficult to implement, has a high degree of adaptation according to the company, sector, type of investment and risk and opportunity management in the short and long term.

This strategy has the capacity to create advanced ESG criteria asset portfolios, with the possibility of beating competitors that operate in the same sector with weaker ESG qualifications.

The GSIA study concluded that ESG integration was already the second most used strategy overall, after exclusion, with 25% of all assets managed using ESG criteria.

Engagement and Voting

The voting strategy refers to the ability of shareholders to vote in shareholder meetings. There is increasing awareness that ESG criteria can affect reputations, as an investor, and the risk/profitability trade-off.

Investors are becoming increasingly active in the exercise of their rights, including questions related to ESG criteria in shareholder meetings and voting against certain decisions by boards of directors. The latter is known as shareholder activism.

Engagement is a strategy that is being increasingly applied by institutional investors, as negotiation prior to the exercise of shareholder rights or divestment as a consequence of not applying ESG criteria.

This strategy is focused on opening a line of communication between investors and companies, in order to avoid and resolve ESG disputes.

Globally, shareholders are carrying out engagement and voting activities regarding assets worth 7 trillion euros, according to data from the GSIA study.

Thematic investments

This type of sustainable and responsible investment, which are usually managed in variable income investment funds, focuses its strategy on the selection of securities that cover an ESG issue.

Therefore, there are thematic funds that solely invest in green bonds, funds that select companies and projects related to the responsible management of water, funds related to the low-carbon economy, focused on sustainable development goals, etc.

In order for thematic investments to be considered sustainable, it is necessary to consider all three ESG focuses, not just one of them.

Sustainable thematic investments are very useful investment vehicles, because they concentrate finance into specific areas, seeking to support sustainable markets that will generate financial profits for investors.

Impact investments

This is the most recently implemented strategy and adopts an additional focus to those we have seen, that of impact, as a result for society and a measurement of a return for investors.

The objective of this strategy is to achieve both a competitive financial performance and have a positive environmental and/or social impact.

The measuring of the impact must be quantifiable, in order to achieve significant changes in the solving of social and/or environmental problems.

Of course, for it to be considered a sustainable financial product it must meet ESG criteria. If it has social impact but damages the environment, it would not be a sustainable financial product.

Impact investments can be used to finance various types of projects, related, for example, to health, education, the environment or climate change.

The most important difference compared to other strategies is that impact investments quantify the profitability of investments, both in the form of financial returns and as environmental and/or social impact returns, meaning that investors have information about the effectiveness of their money in generating positive environmental and/or social changes.

For them to be successful, the predicted results of the investment must be identified and be specific and quantifiable before investors invest their capital in products within this strategy.

Analysis by SRI strategies

Regarding the progress of assets by strategies (figure 5 and table 1), we can see how exclusion

continues to be the most used strategy in Spain.

Table 1 includes two ways of measuring growth; through the growth rate (equation 1) and through the compound annual growth rate (equation 2). The latter is used in order to compare the growths with other studies such as by Eurosif and the GSIA, which use this methodology.

In Spain, it is the strategy of exclusion that is most influential. This situation is mainly due to the fact that most institutions surveyed have advanced strategies regarding sustainability and corporate social responsibility, in most cases having a strict code of conduct about the activities that the institution can carry out. Therefore, because of their general sustainability strategies, managed assets are subject to some kind of exclusion.

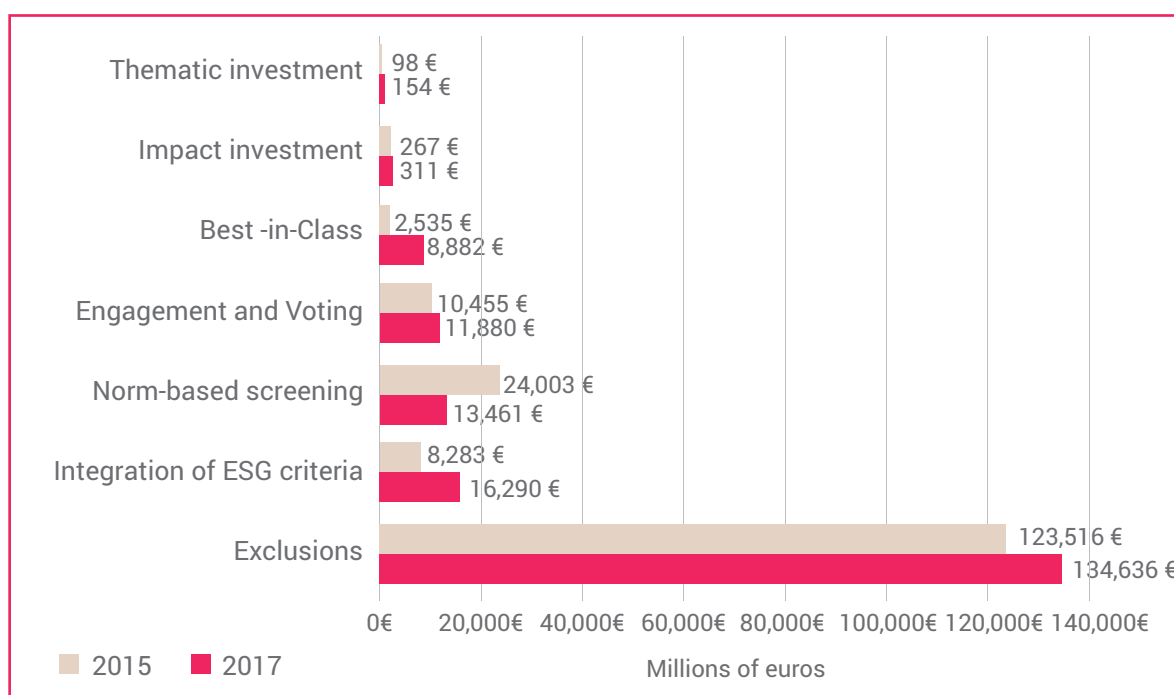


Figure 5: Managed assets by SRI strategy. Source: Spainsif.

The strategy of exclusion grew by 9% between 2016 and 2018, more slowly than the historical growth rate (on average, exclusion has grown at a rate of 24% in the last five years).

This change in the trend is the first sign that the sustainable and responsible investment market in Spain is starting to mature, due to the fact that institutions are starting to actively include sustainable and responsible investment strategies beyond the exclusion of controversial sectors or activities.

Figure 6 lists the areas subject to exclusions, which are dominated by those related to the arms sector (controversial arms, weapons of mass destruction and arms manufacturing), followed by the areas related to traditional corporate ethical questions (tobacco, gaming and human rights).

We would emphasise that environmental issues (environmental legislation, nuclear energy and fossil fuels), with increasingly greater media and political impact (the Paris Agreement, the Sustainable Finance Action Plan of the EU), only represent 11% of all exclusions.

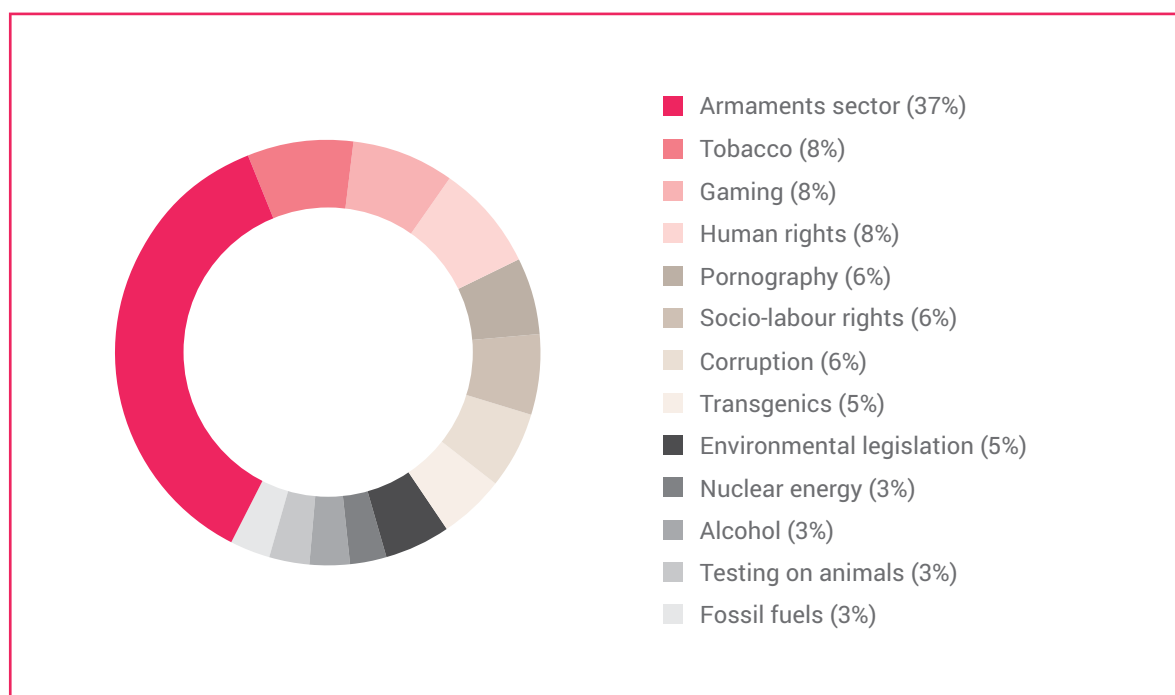


Figure 6: Areas subject to the strategy of exclusion. Source: Spainsif.

	2017	2015	%	CAGR
Exclusions	134,636 €	123,516 €	9%	4%
Norm-Based Screening	13,461 €	24,003 €	-44%	-25%
ESG Integration	16,290 €	8,283 €	97%	40%
Thematic Funds	154 €	98 €	57%	25%
Best-in-Class	8,882 €	2,535 €	250%	87%
Engagement and Voting	11,880 €	10,455 €	14%	7%
Impact Investment	311 €	267 €	16%	8%
TOTAL	185,614 €	169,157 €	10%	5%

Table 1: Assets managed with SRI strategies in millions of euros. Source: Spainsif.

Norm-based screening is the only one of the strategies that suffered a decrease in the period studied. However, this circumstance is due to a methodological question, because, in order to avoid the repetition of the attribution of assets to several strategies, assets managed under an SRI strategy are attributed only to the most advanced strategy.

Therefore, it is not the case that there has been a net decrease in assets managed under the norm-based screening strategy, the fact is that assets that two years ago were managed solely under this strategy are nowadays managed by other more advanced SRI strategies such as best-in-class or ESG integration, as well as norm-based screening, and therefore in order to avoid repetitions, the assets

have been attributed solely to the most advanced strategy.

In this period, both the best-in-class strategy and the ESG criteria integration strategy achieved a high growth rate, with a transfer of assets from norm-based screening towards best-in-class and ESG integration.

These data are interpreted in terms of how SRI is developing in Spain towards a more mature market, in which assets that were previously recorded in the norm-based screening strategy now use the best-in-class and ESG integration strategies.

In figure 7 we can see the development of these three strategies over the years. We can see in this figure that there is a turning point in 2015 for the three strategies. Looking more deeply at the results in figure 7, we can see how firstly norm-based screening experienced exponential growth between 2011 and 2015, while during these years there was almost zero growth in the other strategies

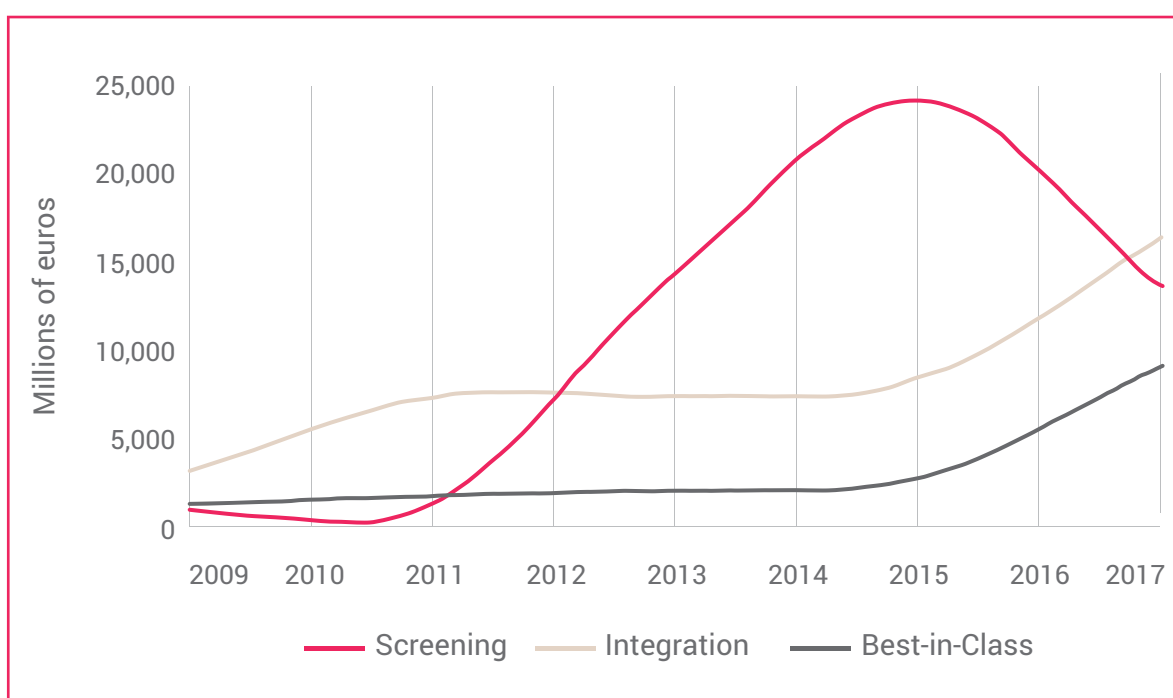


Figure 7: Comparison of assets managed under norm-based screening strategies. ESG Integration and Best-in-Class. *Source: Spainsif.*

Secondly, from 2015 we can see how the trend reverses, beginning a decrease in the norm-based screening strategy in favour of growth in ESG integration and best-in-class strategies.

The sharpest growth was in the best-in-class strategy, due to the fact that the adaptation process is simpler than in the case of ESG integration. Also, in this period, assets managed under the ESG integration strategy exceeded the assets managed with a norm-based screening strategy, something that had not occurred since norm-based screening began its growth in 2011.

This change in the trend, along with the deceleration in the growth of exclusions, is good news for the

domestic SRI market, in which institutions are reaching an advanced degree of development in their sustainability strategies. In coming years, this development will be encouraged, thanks to the new European regulatory framework and international trends.

Engagement and voting are the most difficult strategies to quantify, because they are not channelled into any kind of financial product, as their traceability is complicated.

The line between having conversations with companies, attending road shows and engagement is hard to trace, meaning that, in the survey, engagement is only considered to be what is included in the formal policy of an institution, and, therefore, there is a high likelihood that the assets that appear as managed under this strategy are lower than in reality.

In the case of voting, its traceability is more direct, as financial institutions know the equity that they have invested in each company and the shareholder meetings that they attend, as well as how they vote.

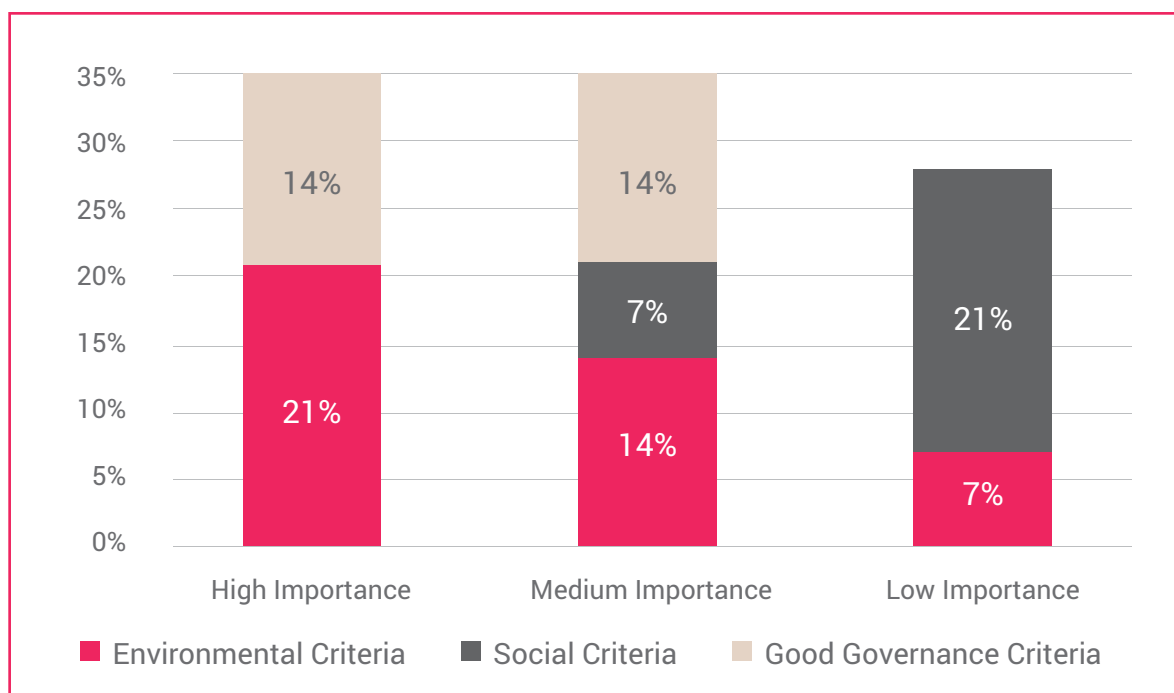


Figure 8: The importance of ESG criteria in the engagement and voting processes of the surveyed institutions. *Source: Spainsif.*

Figure 8 includes the percentage of those surveyed that place high, medium or low importance on environmental, social and good governance issues in their engagement and voting processes.

As we can see in this figure, the most used ESG criterion in the engagement and voting processes is the criterion associated with environmental issues, followed by the criterion associated with governance, with social issues being the least used criterion. Indeed, half of those surveyed stated that they take special consideration of issues related to climate change and the transition to a low-carbon economy in their engagement and voting processes.

Finally, regarding thematic and impact investments, growth is constant, although the size of the market continues to be very small.

However, an increase is forecast for impact investments in the coming years, because this category includes the issuing of green and social bonds by financial institutions, which in 2018 issued higher volumes than all the assets managed with this strategy between 2015 and 2017.

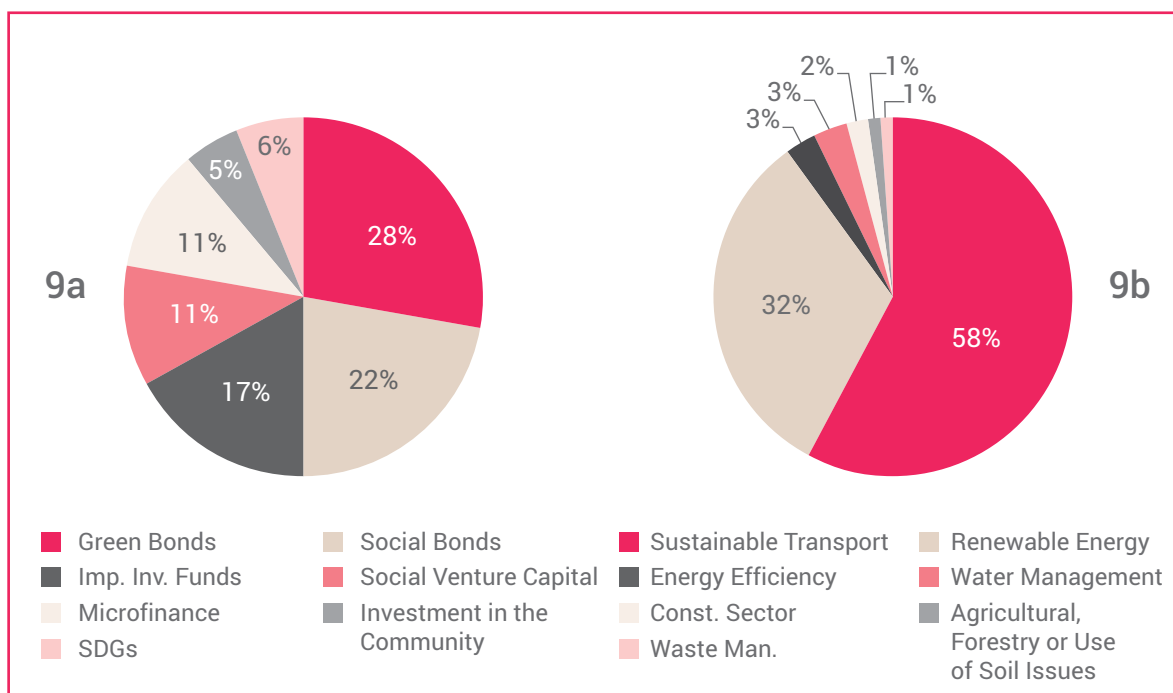


Figure 9: Percentage of assets managed by type of impact investment (9a) and percentage of assets managed by investment issue in thematic investment products (9b). *Source: Spainsif.*

In figure 9a we can see how green and social bonds now represent 50% of all assets managed under impact investments. It is surprising that, among the types of impact investment, there are no assets invested in social crowdlending or environmental and/or social entrepreneurs.

Figure 9b shows the issues upon which thematic investment is focused. This strategy, in the Spanish market, is dominated by sustainable transport and renewable energy. We can also see how all the issues with investments with this strategy are directly or indirectly related to the environment.

Qualitative analysis

Finally, in this analysis of assets managed under SRI strategies we include a section with qualitative evaluations about sustainable development, climate change, the key factors of the SRI market and its development in coming years. The most significant results and trends are shown below.

Regarding strategies related to sustainable development and climate change that the surveyed institutions are implementing, it is striking that 21% of the institutions have now adopted strategies related to SDGs, which were launched in 2015, followed by green investment strategies and renewable energies (figure 10).

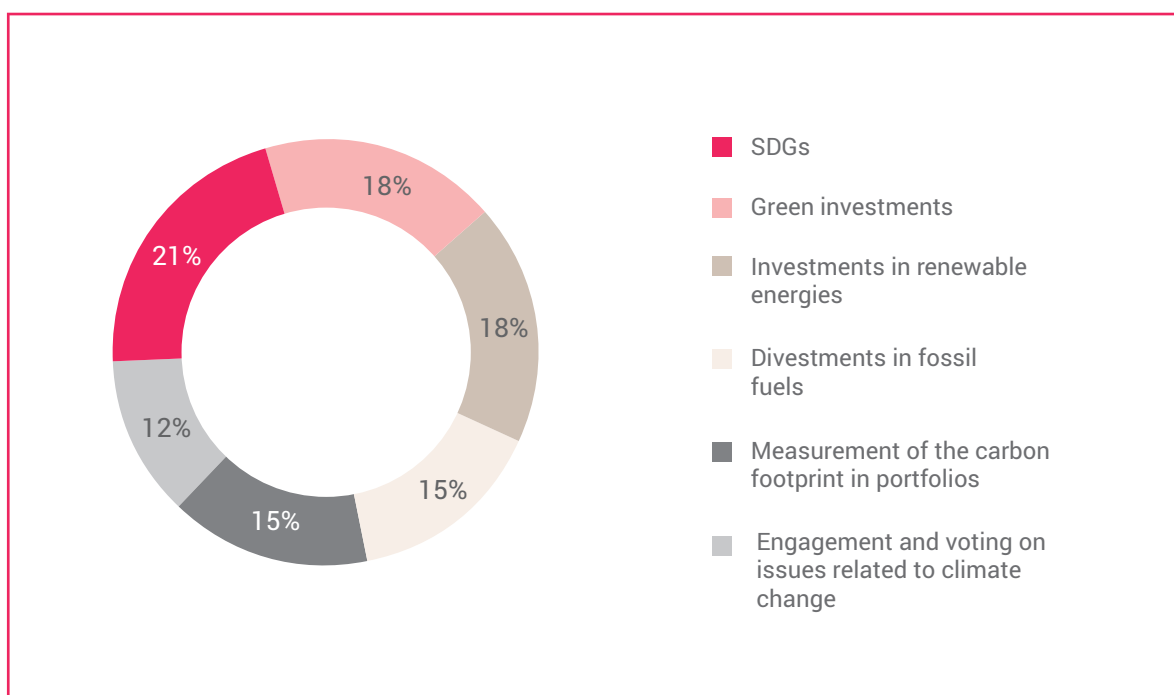


Figure 10: Strategies developed by the surveyed institutions regarding climate change and sustainable development. *Source: Spainsif.*

Among the key factors that will promote demand for sustainable and responsible investments in coming years (figure 11), those surveyed stressed the role that institutional investors and legislative initiatives will play in the development of the SRI market. This trend has now been set in motion on one hand, with the expression of widespread support for SRI by major Institutional investors and, on the other, with the implementation of the Sustainable Finance Action Plan of the European Commission.

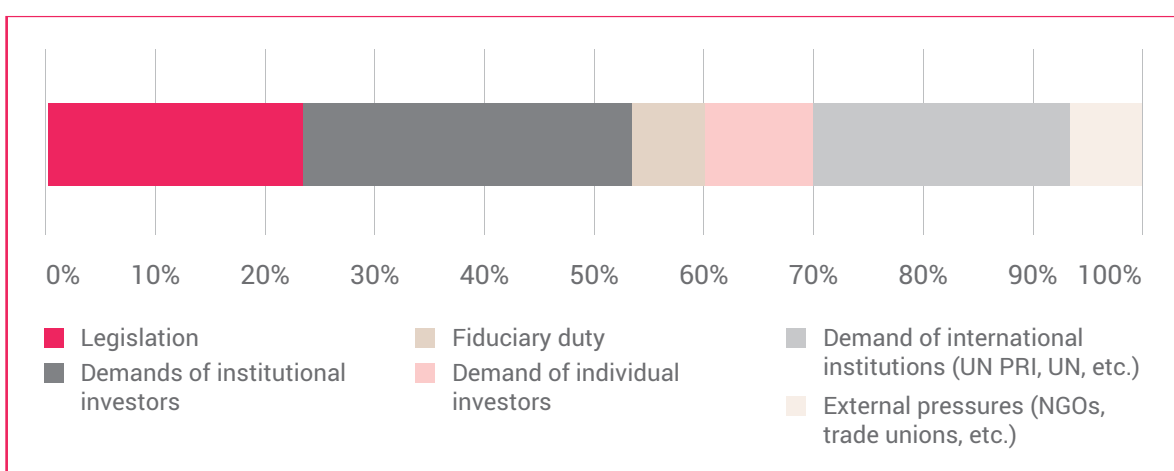


Figure 11: Key factors for development of the SRI market in the next three years. *Source: Spainsif.*

Regarding the SRI strategies that are most valued by the surveyed institutions, we would highlight the fact that ESG integration appears in first position, followed by best-in-class, agreeing with the results

of the quantitative analysis of this review. In contrast, norm-based screening is the only one of the strategies that those surveyed did not rate as of high importance for their clients (figure 12).

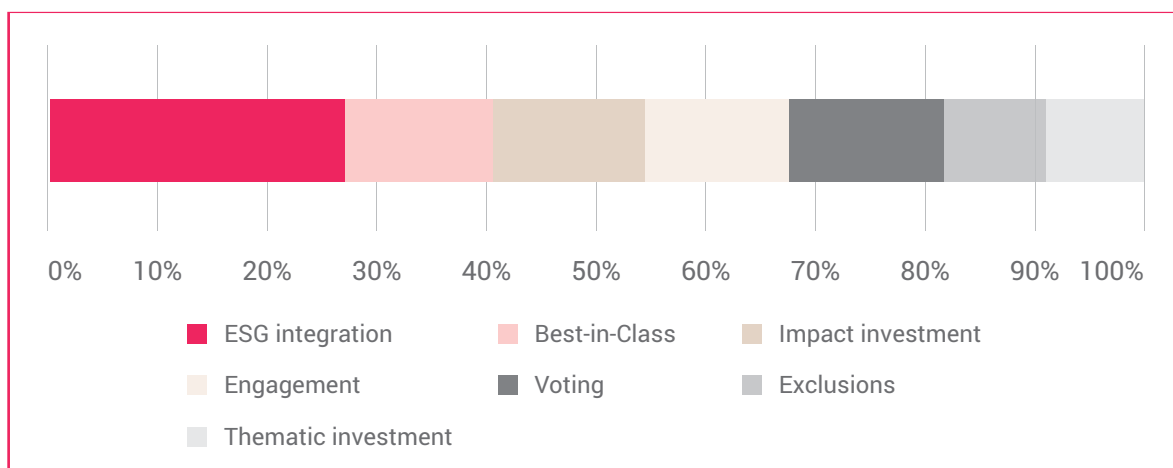


Figure 12: The ESG strategies rated as the most important by clients of the surveyed institutions.
Source: Spainsif.

The conclusion of this chapter is that, although in the studied years we have seen how the growth of the sustainable and responsible investment market has declined, this has been due to the greater participation of institutions in improving the quality of SRI.

The short-term perspective is that, once the SRI best-in-class and ESG integration strategies have been implemented, as promoted by legislative changes arising from the Sustainable Finance Action Plan of the European Commission, the domestic SRI market will again start to experience growth rates that are well above the average of the collective investment scheme and pension fund market, with the difference that, this time, growth will be accompanied by an improvement in the quality of the SRI.



5. ESG INVESTMENT

In this chapter we will discuss collective investment ESG criteria in Spain, including investment funds, individual pension plans and employment pension plans.

Unlike the previous analysis, in this chapter we will take all the collective investment products sold in Spain as a sample, from both domestic and foreign institutions.

For the purposes of this study, we will call ESG investment funds and pension plans those funds and plans that include in their investment policies an express mention of environmental, social and governance criteria (ESG criteria) in their investment decisions and risk management, following the definition agreed by Eurosif. Funds and plans that have a high sustainability rating and solidarity funds and plans, which under no circumstances can be considered SRI funds and plans, are excluded from our analysis.

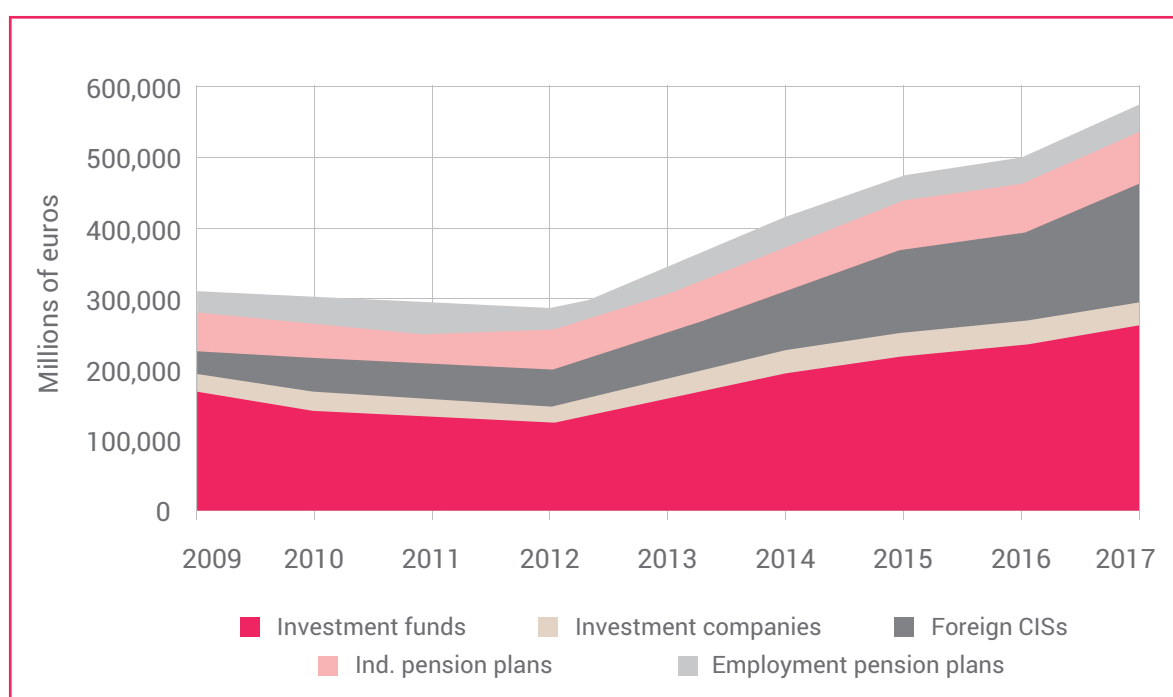


Figure 13: Equity managed by CISs and pension plans. Source: Inverco.

To put collective investment scheme (CIS) and ESG pension plan products in context, figure 13 shows the progress of the equity managed in collective investment schemes and pension plans, both individual and employment.

In this figure we can see how the managed equity has grown from 300 billion euros to almost 600 billion euros in recent years, with an average annual growth rate of 8%.

However, not all the asset categories have progressed at the same rate, with investment funds belonging to both domestic and foreign institutions being the ones making the greatest contributions. Indeed, foreign collective investment schemes, unlike others, have been the institutions that have accumulated the most equity during these years, achieving an average annual growth rate of 24%, which is much higher than that of domestic investment funds, which have experienced average annual growth of 6%.

ESG investment funds

Regarding ESG investment funds, the progress of their equity has followed the general market trend. In figure 14 we can see how the equity of investment funds that include ESG criteria in their investment policies has grown from 15 billion euros to 30 billion euros, with an average annual growth rate of 15%.

This growth has accelerated since 2013, after four years of stagnation. Currently, equity managed in ESG investment funds represents 7% of all the equity managed by collective investment schemes,

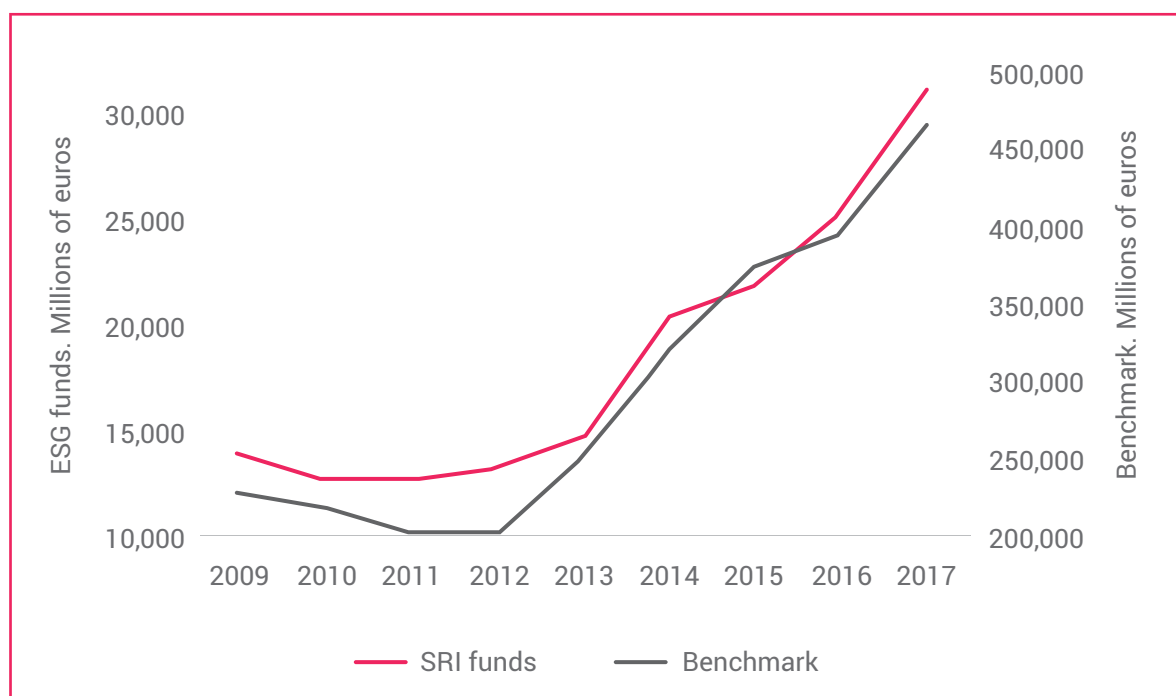


Figure 14: Equity managed by ESG investment funds marketed in Spain, compared with all the equity of investment funds marketed in Spain. *Source: Spainsif using information compiled by VDOS, Morningstar and Inverco.*

although it is now in line with other types investment vehicles, shown in figure 13, such as investment companies and employment pension plans.

The growth of the equity of investment funds with ESG criteria was 12% higher than the growth of the equity obtained by all the investment funds marketed in Spain. This is a great indicator of how demand for investment funds with ESG criteria has been accelerating in Spain, as the growth in equity in these types of funds is exceeding the total equity of the market.

As in the general case of the market, international collective investment schemes have been mainly responsible for the growth of equity during these years.

In 15 we can see that the ESG investment funds owned by international institutions represented, on average, 85% of all the ESG investment funds marketed in Spain.

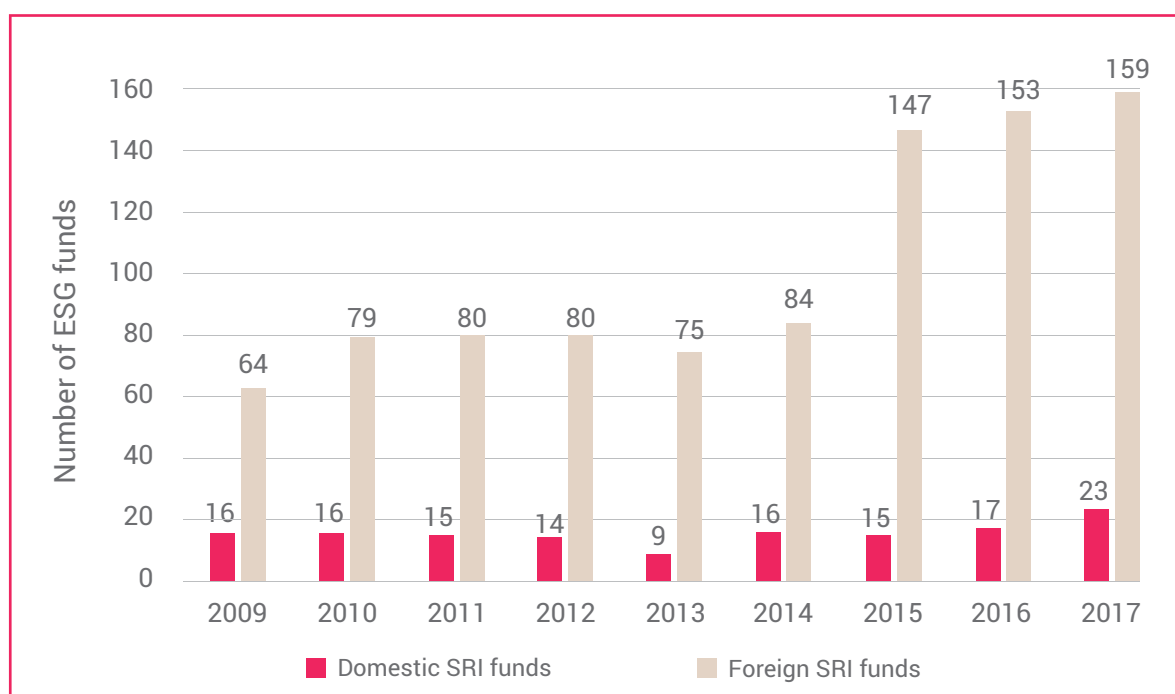


Figure 15: Number of ESG investment funds marketed in Spain, according to their origin. *Source: Spainsif.*

However, it appears that there is a change in the trend regarding domestic collective investment schemes, as growth in the number of these products between 2015 and 2017 was 53% and to date in 2018 it has been 30%, including the launch of seven new ESG investment funds.

Regarding the allocation of assets where these financial products invest them, we can see in figure 16 how ESG savers/investors have a wide variety of product categories where they can invest their money.

In figure 16 we can see how ESG investment funds that are invested in a variable income are the most common, followed by fixed income and mixed funds, in agreement with what we have seen in figure 4, for all assets managed with an SRI strategy.

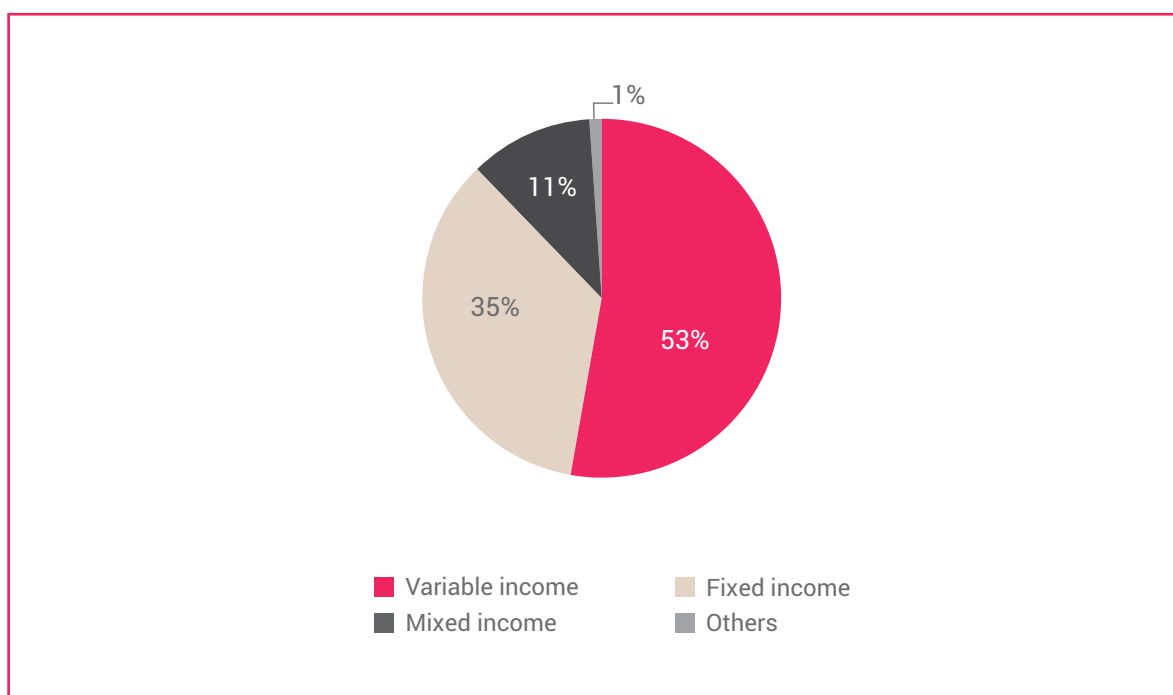


Figure 16: Asset allocation according to the portfolios of ESG investment funds. *Source: Spainsif using information compiled by VDOS and Morningstar.*

Table 2 shows the average annual profits per category, including an example portfolio that shows the weighting of categories according to the asset allocation of figure 16.

	PROFIT (%)			
CATEGORY	1 year	3 years	5 years	10 years
Variable income	11.25	4.98	7.17	1.7
Fixed income	0.05	0.11	1.83	0.77
Mixed income	4.03	1.27	2.65	0.54
Others	2.15	0.54	1.2	0.23
ESG Portfolio	6.43	2.82	4.74	1.23

Table 2: Annual average profit by category of ESG investment funds. *Source: Spainsif using information compiled by VDOS and Morningstar.*

The profit of the ESG investment fund is higher than the average profit of all the investment funds included in table 3, in all cases except when measuring the average annual profit over ten years. This could be due to the fact that most ESG investment funds were not marketed in Spain until ten years ago and therefore the profits in this timeframe are not representative.

INVERCO CATEGORY	WEIGHTED AND ANNUALISED AVERAGE PROFIT (%)			
	1 year	3 years	5 years	10 years
Monetary	-0.29	-0.11	0.32	0.95
Euro short-term fixed income	0.14	0.08	0.58	0.96
Euro long-term fixed income	0.65	0.63	2.53	2.68
Euro mixed fixed income	0.9	0.67	2.4	1.48
Euro mixed variable income	3.39	2.12	5.2	1.02
Euro domestic variable income	12.54	5.37	9.19	0.48
Euro long-term fixed income	-1.52	1.39	2.2	2.56
International fixed income	1.25	0.45	1.46	0.64
International mixed fixed income	3.15	1.41	3.51	1.58
Other euro fixed income	8.94	6.43	9.3	2.4
Europe international variable income	7.9	5.39	8.05	1.05
USA international variable income	10.59	8.55	13.82	6.77
Japan international variable income	14.55	10.53	12.97	3.11
Emerging international variable income	16.68	6.86	3.41	0.11
Other international variable income	10.08	7.96	10.8	5.05
Global	4.49	3.69	4.33	2.12
Guaranteed fixed income	0.66	0.32	1.65	2.26
Guaranteed variable income	1.51	0.94	2.24	1.46
Partially guaranteed	2.51	1.41	3.89	
Passive management	2.21	1.42	4.48	
Absolute return	1.44	0.65	1.25	
Hedge funds	9.88	7.39	9.29	
Total Funds	2.64	1.59	2.95	1.84

Table 3: Annual average profit by INVERCO category. Investment funds owned by domestic institutions. *Source: Inverco.*

ESG pension plans

Between 2015 and 2017, individual ESG pension plans in Spain grew by 4.18%, reaching equity of 1.25 billion euros (figure 17). This equity is divided into 56 pension plans belonging to ten pension funds, managed by four domestic institutions. Also, 53% of these pension plans are products that have been turned into ESG pension plans due to a change in the investment policy of the pension

funds, in which they chose to clearly consider ESG criteria when making investment decisions.

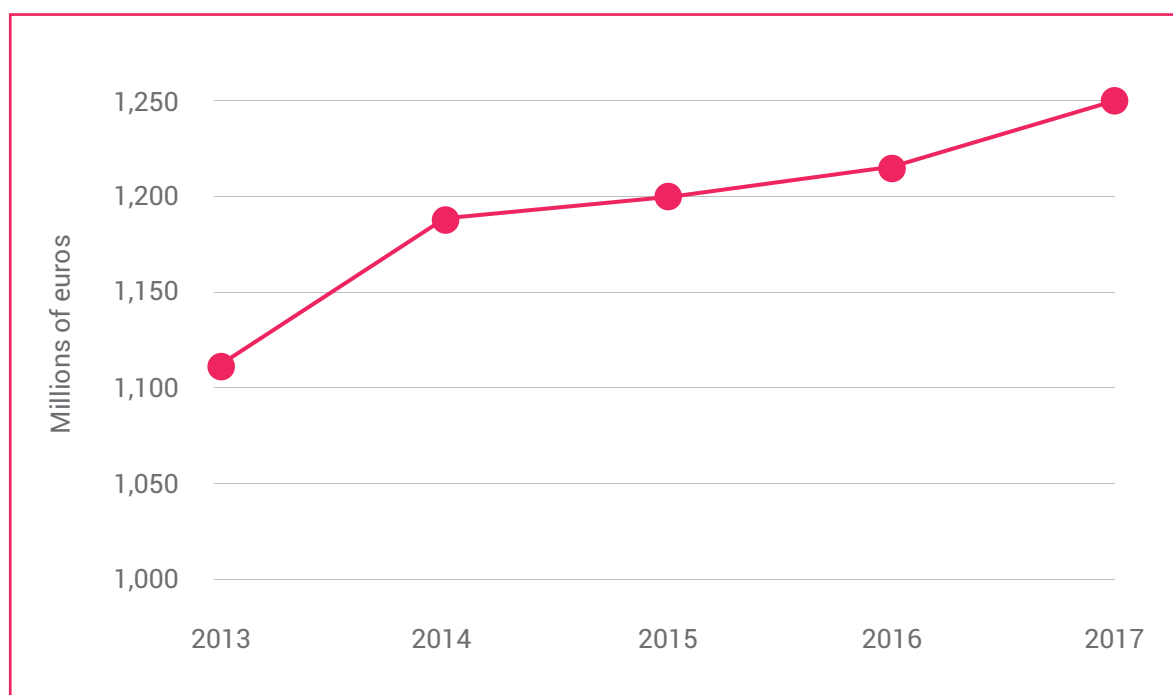


Figure 17: Equity of individual ESG pension plans marketed in Spain. *Source: Spainsif using information compiled by VDOS and Morningstar.*

This market is still at its initial stages in Spain, and ESG pension plans represent a very small volume of assets if we compare them with the 74.378 billion euros recorded by INVERCO in individual pensions funds at the close of 2017.

However, due to the fact that sustainable and responsible investment includes ESG criteria in its risk management, it has great potential to better manage investment risks in the long term. Future expansion is predicted in assets managed in individual pension funds with ESG criteria, as is already happening in investment funds and in employment pension funds.

In their control committees, employment pension funds include the representation of workers through trade unions. Therefore, they have been promoting investment policies with ESG criteria for years, being one of the main players in the inclusion of ESG criteria in the collective investment scheme and pension plan market in Spain.

This continued support for investment policies with ESG criteria has been used to begin to legislate concerning SRI in Spain. Regarding this, the 2/2011 Sustainable Economy Act of 4th March, in its final provision, number thirty-one, calls for regulatory development concerning the distribution of ESG information in the investment policies of pension funds.

This final provision was implemented in the 27/2011 Act of 1st August on the updating, adaptation and modernisation of the social security system, in which its final provision, number eleven, modifies the consolidated text of the Law on the Regulation of Pension Plans and Funds approved by Legislative Royal Decree 1/2002 of 29th November, a text that had a new section added in its

article 14, stating that control committees, together with managing institutions, must prepare a comprehensive declaration about the principles of their investment policies, which, in the case of employment pension plans, must mention whether extra-financial risks are taken into consideration in investment decisions.

This was implemented in the Regulations for Pension Plans and Funds, which was approved by Royal Decree 304/2004 of 20th February and modified by Royal Decree 681/2014 of 1st August, in which article 69, section 5 explains that employment pension funds, in their comprehensive declaration of the principles of their investment policies, must mention whether the extra-financial risks that affect the various assets that comprise the pension fund portfolio are taken into consideration or not in investment decisions.

On a European level, Directive 2016/2341 of 14th December 2016 on the activities and supervision of institutions for occupational retirement provision (IORP Directive II), includes a clear mention that employment pension funds must report whether they consider, in investment decisions, ESG criteria and how they form part of their risk management systems.

As we can see, domestic legislation has gone before European legislation in this case, which shows the importance that this type of financial product has in the development of sustainable and responsible investment in Spain.

Since 2015, the General Directorate of Insurance and Pensions of the Ministry of Economy and Business has published a report including the results of the ESG information provided by employment pension funds. This information has been standardised thanks to a voluntary information sheet prepared by Spainsif in 2016, which organises ESG information so that it increases the standardisation of data and thereby makes it easier to process.

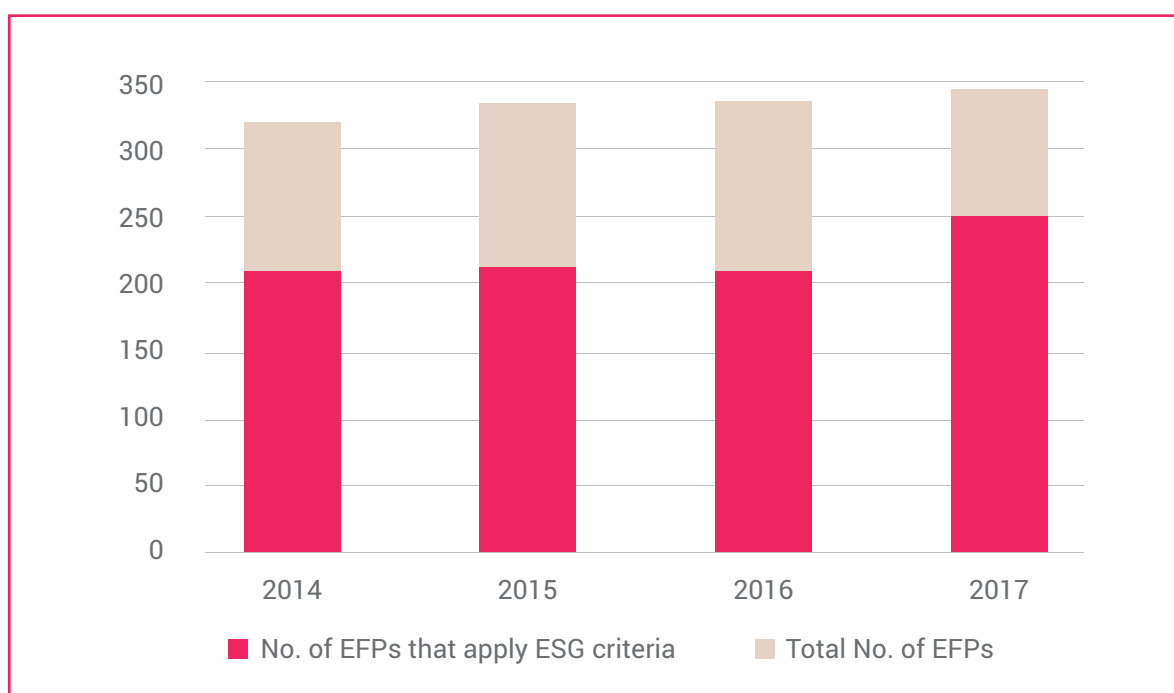


Figure 18: Number of employment pension funds that include ESG criteria in their investment policies. *Source: DGSyFP.*

In figure 18 we can see how the number of employment pension funds that apply ESG criteria amounts to 72% of all funds, which represents equity of approximately 26 billion euros.

Employment pension funds, as a complementary social welfare tool to retirement, have been one of savings instruments that have suffered the most as a consequence of the financial crisis of 2008.

Due to wage cuts and workforce reductions, the assets managed through employment pension funds had a growth rate of 16% between 2009 and 2017, which is lower than that of all pension funds, which have grown by 30%, and well below the growth recorded in these years for all assets managed through collective investment (83%).

Although the growth in equity might be small, 1% between 2016 and 2017, the equity managed taking into consideration ESG criteria grew by 10% in this period, a circumstance which means that employment pension plans and their control committees will play a key role in the development of sustainable and responsible investment in Spain.

To end this section, we have included a section on the ESG information provided by employment pension funds through the information sheet prepared by Spainsif. In the information obtained in 2017 We can see that 75 employment pension plans (21.74% of the total), which represented equity of 15.492 billion euros (43.39% of the total), reported their ESG information by using the Spainsif information sheet. This sheet provides information beyond telling us whether the employment pension plan applies an SRI policy or not, helping us to discover in which category these principles are applied.

As a result, in table 4 we can see that 74% of all equity whose committees used the sheet, include ESG criteria, and how in the variable income categories this percentage reaches 95%. This situation is because the indicators to measure SRI in variable income categories are much more developed than for the other investment categories, which makes it easier to invest with ESG criteria.

Also, based on the information provided, we can classify this equity according to the sustainable and responsible investment strategies used by the employment pension funds. Figure 19 shows the assets managed according to the various SRI strategies.

In this figure we can see how the majority of employment pension funds use ESG integration as

TYPE OF ASSETS	EQUITY (MILLIONS OF EUROS)	% SRI
Sovereign fixed income	5,870	90%
Corporate fixed income	3,407	62%
Direct variable income	999	95%
Indirect variable income	2,718	95%
Alternative assets	899	89%
Other	1,599	11%
TOTAL	15,492	74%

Table 4: Equity of the employment pension funds by investment category and the percentage of SRI they apply. *Source: DGSyFP.*

their main SRI strategy and, in the case of assets invested in variable income, how the use of engagement and voting strategies is widespread.

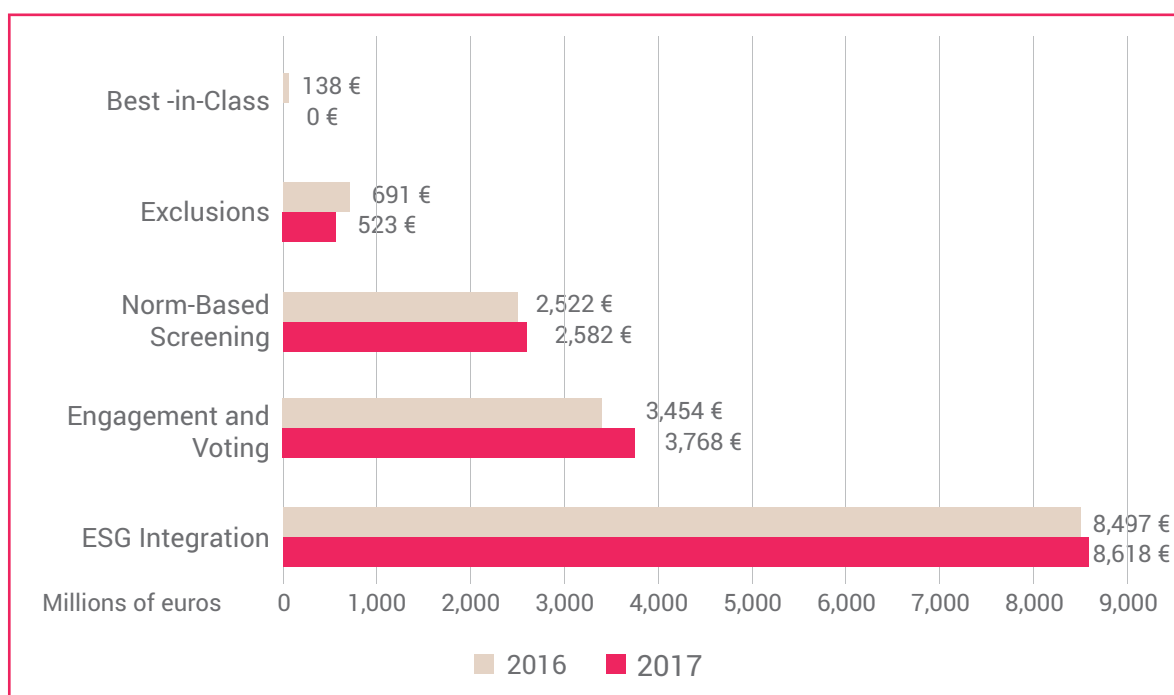


Figure 19: Managed assets by SRI strategy. Source: DGSyFP.

Comparing these results with those obtained in the previous chapter (figure 5), we can see how the strategies most used by employment pension funds differ from those included in the surveys and show the leading role played by employment pension funds as catalysts for high-quality SRI in the domestic market.

Finally, regarding the use of environmental, social and governance criteria, all of the surveyed employment pension funds included information about the ESG criteria with the same degree of importance.

The main conclusion of this chapter is that foreign collective investment schemes are the main driving force of SRI in the investment fund, although we can see how domestic institutions are now working on the development and marketing of these types of products.

Also, individual pension funds continue to play a fairly unrepresentative part, in contrast to employment pension funds, which are achieving a high share of assets managed with ESG criteria.

6. PASSIVE MANAGEMENT IN SUSTAINABLE AND RESPONSIBLE INVESTMENT

To complete the analysis made of sustainable and responsible investment, we include this chapter devoted to the management of ESG criteria based on sustainable stock market indexes, due to the increasingly used strategy of passive management and the boom in ETFs with ESG criteria.

Passive management is an investment strategy, the objective of which is to replicate a stock market index. The origin of this strategy goes back to the portfolio theory developed by Markowitz in 1952 and the CAPM (capital asset pricing model) developed by Sharpe in 1964.

Nowadays, the growing interest of investors in management fees, regulatory changes and advances in financial technology (as in the case of robot advisers) mean that passive management is evolving rapidly, in 2017 reaching equity in Europe of 1.3 trillion euros, with growth in the last year of 160 billion euros. This growth was to a large degree achieved thanks to the ETFs that last year brought equity of 670 billion euros to Europe¹.

This development affects sustainable and responsible investment, meaning that passive management's share of the SRI market went from 6% in 2013 to 12% at the end of 2017 globally, reaching 102 billion euros².

Passive SRI can take many forms, with one of the most developed methods being focused on replicating sustainable stock market indexes such as the Dow Jones Sustainability Index or the FTSE4GOOD Index. However, there are now alternatives when choosing the reference index for investment products, such as the MSCI ESG indexes or the Morningstar sustainability indexes.

This variety of indexes and products is positive, but it can create uncertainty, because all of them have different ways of evaluating ESG criteria. Therefore, countries are attempting to reduce this uncertainty through the official certification of sustainable products (ESG labels) and the creation of stock market indexes related to sustainability.

In response to this need to standardise the SRI market, the Action Plan of the European Commission proposes the creation of a stock market index focused on the transition to a low-carbon economy.

¹ A record year for ETFs in Europe. Morningstar 2018.

² ESG: Strong growth of passive funds. Morningstar 2018.

This boom in sustainable passive management is arising as a consequence of the comparable evidence that investing with ESG criteria generates more returns in the medium and long term.

To confirm this situation, we have included comparative analysis in this review between two sustainability stock market indexes, one at a domestic level and another on a European level.

We carried out this analysis based on the daily returns of the indexes (at base 100) between 2011 and 2017. We have also included inferential analysis to check whether the observed differences are statistically significant.

We carried out the latter based on three statistical tests, the first of which was used to check if the tests followed a normal distribution (Kolmogorov-Smirnov test), the second to discover if the samples were correlated (Spearman's rho) and the third in order to discover if the observed differences were significant (Wilcoxon signed-rank test).

FTSE4GOOD IBEX

Bolsas y Mercados Españoles (BME) and the FTSE Group created a sustainable stock market index in 2008, which enables responsible investors to identify and invest in those companies that comply with global sustainable and responsible investment standards. The reference index used was the IBEX 35.

The FTSE4GOOD IBEX Index is currently composed of 43 companies that are also present on other national stock market indexes such as the IBEX 35, the IBEX Medium Cap and the IBEX Small Cap.

In figure 20 we can see how the progress of the FTSE4GOOD IBEX Index has affected the progress of the IBEX 35 index over the years. On average, between 2011 and 2017 the sustainability index per-



Figure 20: Comparison of the performance of the FTSE4GOOD IBEX stock market index and of the IBEX 35 stock market. *Source: Bolsas y Mercados Españoles.*

formed 3% better than the reference index, achieving a difference of 6.9% in 2017.

In order to check whether these differences were significantly different, we carried out inferential analysis of the data show in figure 20, the results of which are included in table 5.

In the case of the normality tests, the significance had to be greater than 0.05 for the sample to be considered as having followed a normal distribution of their data.

In the case of the evaluated samples, we can see that neither of the two followed a normal distribution, as they did not have a significance of greater than 0.05.

Once we had confirmed that there was not a normal distribution, we used a correlation test to discover if the samples were related, Spearman's rho, the result of which is that there was a correlation of 97%, confirming that these indexes are closely related.

Finally, we used the Wilcoxon signed-rank test, in order to discover if the differences observed between the two indexes were due to chance. We used this test because the samples did not follow a normal distribution and the indexes were also related.

A significance greater than 0.05 would mean that the differences are due to chance, but in this case the observed differences were statistically significant, as the result of the Wilcoxon test gave a significance of less than 0.05.

STATISTICAL TEST	COEFFICIENT	RESULT
Normality test for the FTSE4GOOD sample	Kolmogorov-Smirnov Z test	4.387
	Significance	0
Normality test for the IBEX35 sample	Kolmogorov-Smirnov Z test	4.329
	Significance	0
Correlation test between the samples	Spearman's rho	0.971
	Significance	0.01
Statistical significance test between the samples	Wilcoxon signed-rank test	-24.832
	Significance	0

Table 5: Inferential analysis between the performance of the FTSE4GOOD IBEX index and the IBEX35 index. *Source: Spainsif.*

DOW JONES SUSTAINABILITY EUROPE

Since 1999, RobecoSAM has published the Dow Jones Sustainability index since 1999, which is a global sustainable stock market index. Since 2001, this organisation has also published a specific sustainable stock market index for Europe.

Each year over 3,400 listed companies from all over the world are asked between 80 and 120 specific questions about the industry, which are focused on relevant economic, environmental and social factors but that are not often investigated in conventional financial analysis.

The Dow Jones Sustainability Europe (DJSE) index includes the best 120 European companies in terms of sustainability, according to the information collected by RobecoSAM.

In this case, the reference index used was the Europe STOXX 50, which brings together 50 of the leading companies in the eurozone.

As in the previous section, in figure 21 we can see the comparison between the performance of the DJSE index between 2011 and 2017 and the performance of the Europe STOXX 50 for the same years.



Figure 21: Comparison of the performance of the Dow Jones Sustainability Europe index and the Euro Stoxx 50 index. *Source: Bloomberg and RobecoSAM.*

In the years studied, on average the sustainability index performed 10% better than the reference index, with this difference reaching 13% in 2017.

As in the previous case, in order to study the statistical significance of these differences we carried out the same inferential analysis as in the FTSE4GOOD IBEX case, and the results are summarised in table 6.

The samples do not follow a normal distribution on this occasion either, as can be seen from the Kolmogorov-Smirnov test. We therefore carried out a nonparametric correlation test through Spearman's rho, and found that the samples were closely related to each other, with a relation of 97% in the series. Finally, because of these previous results, we used the Wilcoxon signed-rank test to discover if the differences were statistically significant, obtaining a positive result.

From these two analyses it can be concluded that sustainable and responsible investment through the strategy of passive management is both possible and profitable. Sustainable stock market indexes achieve significantly better results than the reference stock markets.

We would emphasise that the differences between sustainability indexes and reference indexes are increasingly larger, which could be a sign that sustainability is being considered more and more, with leading companies in this field being the ones obtaining the best index results.

STATISTICAL TEST	COEFFICIENT	RESULT
Prueba de normalidad para la muestra del DJSE	Kolmogorov-Smirnov Z test	2.978
	Significance	0
Normality test for the Euro Stoxx 50 sample	Kolmogorov-Smirnov Z test	2.235
	Significance	0
Correlation test between the samples	Spearman's rho	0.97
	Significance	0.01
Statistical significance test between the samples	Wilcoxon signed-rank test	-36.182
	Significance	0

Table 6: Inferential analysis between the performance of the Dow Jones Sustainability Europe index and the Euro Stoxx 50 index. *Source: Spainsif.*



7. MAIN PLAYERS IN THE DOMESTIC SRI MARKET

The forum for sustainable and responsible investment in Spain (Spainsif) is a meeting platform and a benchmark concerning sustainable and responsible investment in Spain (created in 2009 by 32 organisations). The main objective of Spainsif is to promote the integration of environmental, social and governance criteria into investment policies through dialogue with various social groups, contributing to sustainable development and also raising awareness about and promoting changes in investment processes in the investment community, public authorities, companies and the general public.

It currently has the support of 65 highly respected organisations, both national and international, including banking institutions, insurers, asset managers, service providers, universities, business schools, not-for-profit organisations, foundations and trade unions.

Spainsif is part of the sustainable development forums international initiative and is a member of the European Sustainable Investment Forum (Eurosif), an organisation that brings together the main sustainable investment forums of neighbouring European countries (France, the United Kingdom, Germany, the Netherlands, Italy, etc.).

Spainsif's activity is focused on three main themes: the promotion of sustainable investment to increase the influence of SRI products on investment products, research and training to increase knowledge about sustainable investment, and dialogue with interest groups in order to facilitate the development of sustainable investment.

Therefore, Spainsif's associates are a benchmark in the sustainable and responsible investment market in Spain.

Below we will briefly summarise the points of view of some of them about the importance of sustainable and responsible investment to promote the creation of a financial market that is aligned with the fight against climate change and the Sustainable Development Goals of the United Nations.



By Javier Dueñas

*Sustainability Director of Grupo
Cooperativo Cajamar*

Grupo Cooperativo Cajamar brings together a group of organisations as a cooperative focused on sustainable local development, the

social economy and on support for local production systems. Because of its size and volume of assets, it is the largest group of credit cooperatives in Spain, and one of the leading organisations in the field of cooperative credit in southern Europe.

Sustainability, in its broadest sense, is one of the fundamental aims of Grupo Cooperativo Cajamar, which has integrated sustainable development goals and the sustainability agenda into its strategy and business model.

Sustainability is an issue that affects all society and perhaps that is why we can see how concern about climate change, environmental questions, how companies treat their workers, as well as corporate social responsibility are all growing. In the world of investments, these concerns are often connected to sustainable and responsible investment (SRI) and there are increasingly more investors interested in considering SRI criteria in their investment portfolios.

For many, their interest is based on their values. They wish to invest in companies whose activities reflect their concerns about sustainability. For others, including many asset managers that now include SRI in their investment processes, the interest is aimed at minimising social economic/financial or environmental risks and the reputational risk that is always present as collateral damage in these questions.

For all the above reasons, Grupo Cooperativo Cajamar has been a pioneer in the development of an ethical management system that shows its commitment to transparency, responsibility and integrity, all values that make up the corporate culture of the group, and to the development of sustainable and responsible investment in its investment policies and the management of its assets.

With Spainsif, we have found the best platform for the promotion of SRI, which is the common objective of all its members and associates that work together to raise awareness concerning sustainable and responsible investment.



By Enrique Garrido

Director of the Wealth Management Advisory Unit at Tressis

Tressis is a financial services company specialising in financial planning and wealth management. It is the leading independent

company in Spain, managing over four billion euros of wealth and with over eight thousand clients.

Since Tressis saw the light, 18 years ago, it has been closely connected to sustainable and responsible investment (SRI), launching new products and services as the asset management industry has evolved.

Therefore, as well as distributing the SRI investment funds of the main domestic and international managers, in 2014 it was a pioneer in the launch of a discretionary management service of sustainable and responsible investment funds, receiving the award for the "100 Best Ideas" for this initiative, given by the Actualidad Económica magazine in 2015. At the close of last August, 9.21% of the total volume managed by Tressis was done with SRI criteria. In March 2018 it launched the Tressis SRI Sustainable Portfolio fund of funds.

As part of its commitment, it has signed the Principles for Responsible Investment (PRI) promoted by the UN and is a member of Spainsif, the leading platform for sustainable and responsible investment in Spain.

During this phase we have witnessed not only the evolution and sophistication of the various analysis and investment strategies using SRI criteria, but also the impressive increase in the volume of assets managed with these criteria.

Society in general is increasingly committed to environmental and social issues, and the owners of assets are transferring this concern to their managers and advisers. In this context, we have a dual objective. On one hand to be able to measure the impact that said assets have on society, on the environment and on the governance of companies. On the other, to make the long-term management of portfolios more efficient in terms of profitability/risk.

We should also not lose view that our ultimate objective is to influence companies and governments to create a more sustainable financial market, using both capital itself and the regulatory framework as springboards for change.

In this sense, initiatives such as that of Spainsif are key, because they bring together the various agents involved with different perspectives and interests: financial institutions, asset managers, trade unions, not-for-profit organisations and service providers. We therefore share points of view and concerns and provide solutions in order to achieve a common objective: for all investment policies to consider environmental, social and governance criteria.



By Joaquín Garralda

Dean of Academic Affairs at IE Business School

IE Business School is a business school That is part of IE University, and that, as an academic institution, has research as one of its

raisons d'être.

As well as having an academic department in the area of finance and another in social innovation, most of our master's programmes include specific courses that deal with SRI.

The market system does not deal effectively with the issue of externalities of companies, and although the regulator introduces rules in an attempt to resolve them according to social demands, the financial world has a greater capacity to make progress (following public expectations) concerning the negative results produced by the non-integration of social costs into corporate decisions.

Therefore, the role that the financial world plays to deal with major global challenges is fundamental.

One of the most noteworthy characteristics of Spainsif is its nature as a multi-stakeholder.

The consideration of SRI as a force that can drive development in society, makes it necessary for the main agents to participate in the ability to influence that Spainsif could have in the Spanish financial market. To this characteristic we should add that the coordination it has achieved with other European SIFs makes Spainsif an effective mediator in the evolution of SRI in the financial world.





By Manuel Álvarez

General Secretary of OCOPEN

The Organisation of Pension Consultants of Spain (OCOPEN) is a not-for-profit professional association, that brings together pension consulting companies, pension fund management

companies and insurance institutions for the development and consolidation of private social welfare in Spain, both within the field of industrial relations and in individual savings, as a complement to the state pension system.

OCOPEN is a meeting point for all professionals and organisations committed to the development and consolidation of social welfare systems as a complement to social security to provide, in an unbiased and independent way, recommendations and proposals in order to promote long-term retirement saving by the public so that their future well-being is safeguarded.

In the past, pension consultants used to focus on the calculation of commitments for defined benefit pensions, included in the liabilities of balance sheets. The transition towards defined benefit pension plans and the growth of investments in them caused a change in focus towards the monitoring of and advice concerning the assets of pension funds and other social welfare schemes. Since then, pension consultants have attempted to offer their clients the best practices in the field of management.

SRI forms part of these best practices, with pension consultants forming part of the backbone of the advice and investment processes of pension and mutual funds for social welfare in the present and even more so in the coming decades of energy transformation towards sustainability.

A significant part of future well-being comes from achieving a cleaner and more sustainable economy. Sustainability also minimises the climatic risks that long-term investments are exposed to.

The transition towards a low-carbon economy requires an enormous economic effort. The changes that need to be implemented are so large that institutional investors that channel savings towards productive investments must take a leading role in this process. That is why, in Europe, pension funds are key elements for the development of sustainable finances, and pension consultants form an important part of this turn towards investments, using ESG criteria in addition to the traditional criteria of profitability and risk.



By Mario E. Sánchez

Economist at CS CCOO

and Andrés Herrero

*Employment Pension Plan Officer at
UGT Confederal*

CCOO (the Trade Union Confederation of Comisiones Obreras) currently holds the Vice-Presidency of the 'grupo 5' (trade unions) in Spainsif, representing the UGT (General Union of Workers) and the CCOO. Both trade unions represent over 70% of workers in Spain.

Concerning SRI, the CCOO and UGT have participated in the incorporation in Spain of two questions into the legal system that are fundamental for the development of these policies in the second pillar (the obligation To exercise political rights and report on the consideration - or not - of what are known as ESG criteria - environmental, social and governance criteria).

In 2017 both trade unions prepared a joint document including SRI proposals for social welfare institutions in the employment system. We later participated in the Spainsif working group that as a result produced the document "Spainsif proposal for transparent SRI", which included many trade union proposals on the subject. The search for this consensus in associations composed of various interest groups, such as Spainsif, is also key in order to advance in the development of SRI.

For our organisations, an SRI policy means the exercise of social responsibility by control committees of employment pension plans and funds and by the boards of directors of social welfare mutual funds, both regarding participants and beneficiaries and society as a whole. SRI is perfectly compatible with the achievement of the profitability required to pay benefits, because its objective is the generation of long-term profits and the minimisation of risks through a more thorough analysis (financial and extra-financial). It also contributes to the creation of a sustainable financial system and to economic and social development.

Those responsible for implementing these policies are the members of the control committees and of boards of directors, many of them representing both trade unions, which are taking a leading role in what today occupies the employment system in the promotion of SRI in Spain. A result of this is that over 30% of the equity of employment pension funds have made a formal commitment to the Principles for Responsible Investment initiative, Supported by the United Nations through UNEP FI and the Global Compact. However, despite these preliminary and noteworthy advances, there is still much to do. One of the areas in which more progress should be made is in the comparison of the importance of the criteria contained in the "S" (social and employment) criteria compared to environmental and good governance criteria. To do this, the Committee on Workers' Capital (CWC), a committee promoted by the International Trade Union Confederation (ITUC), has prepared the Guidelines for the Evaluation of Workers' Human Rights and Labour Standards, which we hope will be gradually integrated into investment policies.



By Steffen Hörter

Global Head of ESG at Allianz Global Investors, and member of the Technical Expert Group on Sustainable Finance of the EU Commission

ESG is going mainstream because it's business-critical

Environmental, social and governance (ESG) factors are increasingly recognised as critical determinants in the success or failure of corporations of every stripe. Investors, too, are paying more attention to ESG factors because incorporating them into investment decisions can help manage risk and generate more sustainable long-term returns.

Intangible factors help determine market value

Analysing ESG factors is meant to be a supplement to, rather than a replacement for, more traditional research tools. While it is certainly always important to examine a company's balance sheet and public filings, a growing percentage of corporate assets today are of a more intangible nature.

These intangible assets include a company's reputation, intellectual property and brand value – and many are directly related to, or affected by, mainstream ESG factors:

- Environmental – climate change, pollution, water management, biodiversity
- Social – human rights, labour relations, health and safety, community relations, diversity
- Governance – board structure and accountability, executive pay, bribery and corruption

Companies grow increasingly attractive to investors if they recognise the ESG factors relevant to their enterprises, invest in them as business opportunities and manage them well. Conversely, poorly managed companies that ignore ESG factors may be riskier investments.

Intangible assets have grown increasingly valuable

Three ways to incorporate ESG

The growing interest in ESG is causing a paradigm shift in the investment world. While there are many approaches, ESG investments generally fall into one of three categories.

Socially responsible investing (SRI)

This approach typically aims to avoid companies or sectors with bad ESG practices or to create portfolios with a positive ESG profile. After applying negative screens or positive filters to their investable universes, SRI strategies are able to invest in only a portion of their benchmark indices. Since SRI strategies are a first-generation approach to ESG investing, dating back more than 20 years, they currently make up the bulk of the ESG market.

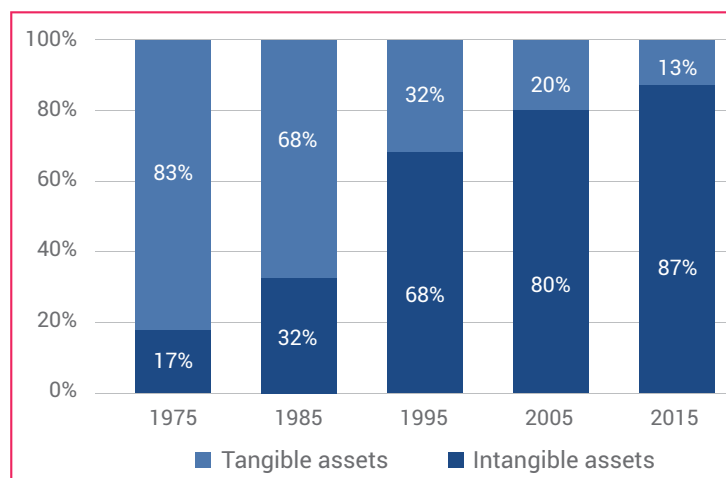
Impact investing

Part of the SRI landscape, impact investing aims to create a positive social and environmental impact along with a positive financial return. Impact investments frequently focus on topics such as

providing access to clean energy or clean water, but they can also focus on areas such as providing quality education and gender equality.

Integrated ESG

This is a “next-generation” approach that we follow at AllianzGI for our mainstream investment strategies. It is built around conducting deep, proprietary research on corporate ESG risks and opportunities. Integrated ESG portfolios are not constrained by ESG filters that narrow the investable universe; instead, portfolio managers make an educated ESG risk/return trade-off across all potential holdings – with a special focus on avoiding ESG tail risks. For example, a portfolio manager who wants to invest in a lithium company for exposure to the electric-vehicle revolution would need to consider whether its manufacturing operations could be shut down for safety or pollution reasons.



Components of S&P 500 market value.
 Source: Ocean Tomo (2015), "2015 Annual Study of Intangible Asset Market Value".
 For illustrative purposes only.

ESG and active investing

Corporate ESG issues are seldom black or white. That’s why in our view, the practice of packaging up complex issues into passive ESG indices by indiscriminately applying rules-based criteria and third-party ESG research holds relatively little prospect of success. Active investment strategies, on the other hand, can build ESG factors into a portfolio in a far more flexible way by allowing access to securities that are mechanically “screened out” by many passive sustainability strategies. We believe it is in this broader opportunity set where the most attractive investment prospects are often found.

Another benefit of an active approach to ESG investing is active engagement between portfolio managers and corporate management teams. Our integrated ESG approach aims to improve how companies perform on financially material ESG issues by emphasising strong stewardship, consistent proxy voting and regular, direct contact with management. In this way, we aim to help corporations move towards more successful business outcomes – and help our clients improve their performance potential over the long term.

8. CONCLUSIONS

Assets managed under an SRI strategy continued to grow between 2015 and 2017 at a rate of 10%, with a change in trend being observed towards higher quality.

This change in trend is due to the large growths recorded in sustainable and responsible investment strategies such as best-in-class (with growth of 250%) and the integration of ESG criteria (with growth of 97%), at the expense of other less advanced strategies such as norm-based screening (with a decrease of -44%).

These data show, on one hand, that sustainable and responsible investment continues growing both in times of market reduction and in times of expansion. They also show that institutions are evolving towards more sophisticated SRI strategies, as can be seen from growths in advanced SRI strategies at the expense of less evolved strategies.

The growth of assets under SRI management has managed to exceed some reference data, such as the growth of the Spanish economy or the growth of the IBEX35. However, it has remained below the growth experienced by the collective investment scheme and pension fund market (a market that has grown by 12% in the last two years, excluding foreign collective investment schemes).

Regarding the market share, sustainable and responsible investment has remained above 45% of all managed assets in collective investment schemes and pension funds, excluding foreign collective investment schemes.

Concerning the collective investment market as a whole, assets managed by foreign CISs have recorded the greatest growth, 34% in the last year compared to 12% recorded by domestic collective investment schemes.

There is a similar trend in the sustainable and responsible investment market, with growth in ESG investment fund equity of 32% between 2015 and 2017.

In this case, foreign collective investment schemes play an especially important role, as 87% of all ESG investment funds marketed in Spain belong to these institutions.

However, a change in trend can be seen in domestic institutions, as the number of ESG investment funds owned by these institutions has grown by 53% in the last two years, to a figure of 23 investment funds marketed today.

This growth in investor interest coincides with the initiatives of the international community to promote the development of environmental and social policies linked to the transition to a low-carbon

economy and corporate responsibility, such as the Paris Agreement or the Sustainable Development Goals.

In the case of individual pension plans, although movement can be detected in the inclusion of ESG criteria in the investment policies for this kind of product, both through the marketing of new products and through the inclusion of ESG criteria in the investment policies for existing products (53% of individual ESG pension plans come from changes in the investment policy of existing products), the equity level continues to be very low.

Regarding employment pension funds, since the modification to the Regulations for Pension Plans and Funds in 2014, which included a clause that obliged institutions to report on whether These products considered ESG criteria in their investment policies or not, the use of these criteria has grown by 7%, now amounting to 72% of all employment pension funds, which represents an approximate equity of 26 billion euros. Therefore, employment pension funds continue to be one of the main players in the SRI market in Spain, thanks to the commitment of their control committees to the inclusion of ESG criteria in their investment policies.

Regarding investment under passive management strategies, this reached equity of 1.3 trillion euros in Europe in 2017.

This growing investor interest in passive management is also being transferred to sustainable and responsible investment, a market in which this type of investment already represents 12% of all global investment.

Concerning passive management, we have carried out comparative analysis between sustainable stock market indexes and reference indexes between 2011 and 2017, in order to discover whether investing in these indexes is advisable for passive management investors. As a result of these analyses, we have confirmed that there is a significant positive statistical difference in the performance of sustainable stock market indexes. We have also confirmed that this difference has been increasing in recent years, a sign that leading companies in sustainability have an increasingly improved stock market performance.

The sustainable and responsible investment market in Spain is now at a turning point. The years in which sustainable and responsible investment based its growth on the exclusion of sectors, activities or based on international rules have been left behind.

This analysis has produced results of a lower growth rate than in the previous review, but with a strong change in trend towards improved quality, including extraordinary growth in ESG integration and best-in-class strategies.

In this review we can see the progression of the market of investment funds using ESG criteria, setting records in both the number of funds and in the managed equity.

Everything points to the fact that the sustainable and responsible investment market in Spain is at the gates of a new stage of consolidation, both in terms of volume and quality, backed by international initiatives, governments and demand from investors themselves.

USEFUL LINKS

Forum for Sustainable and Responsible Investment in Spain (Spainsif)

<https://www.spainsif.es/>

Sustainable Finance Action Plan of the European Commission

<https://www.spainsif.es/pa-finanzas-sostenibles/>

The European Association for the Promotion of Sustainable Investment (Eurosif)

<http://www.eurosif.org>

Global Sustainable Investment Alliance

<http://www.gsi-alliance.org/>

Principles for Responsible Investment (PRI)

<https://www.unpri.org/>

United Nations Environment Programme – Finance Initiative (UNEP FI)

<http://www.unepfi.org/>

Committee on Workers' Capital

<https://www.workerscapital.org/?lang=es>

The Spanish Stock Market Commission (CNMV)

<https://www.cnmv.es/portal/home.aspx>

Spanish Association of Collective Investment Schemes and Pension Funds (INVERCO)

<http://www.inverco.es/>

Main elements of the Paris Agreement

<https://www.mapama.gob.es/es/cambio-climatico/temas/el-proceso-internacional-de-lucha-contra-el-cambio-climatico/naciones-unidas/elmentos-acuerdo-paris.aspx>

Sustainable Development Goals

<http://www.undp.org/content/undp/es/home/sustainable-development-goals.html>

ACKNOWLEDGEMENTS

Spainsif is a not-for-profit association composed of institutions interested in promoting sustainable and responsible investment in Spain, by creating a platform that brings together financial institutions, managing institutions, SRI service providers, not-for-profit organisations connected to SRI and trade unions, currently comprising 65 associates.

The objective of the association is to be a meeting platform and a benchmark for the generation and distribution of knowledge about sustainable and responsible investment (SRI) and for raising awareness and promoting changes in the investment processes in the investment community, public authorities, companies and the general public.

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Project Supervisor: Francisco Javier Garayoa Arruti

Project Director: Adrián García Bruzón





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