SRI & Performance
by LFDE,
one year later...

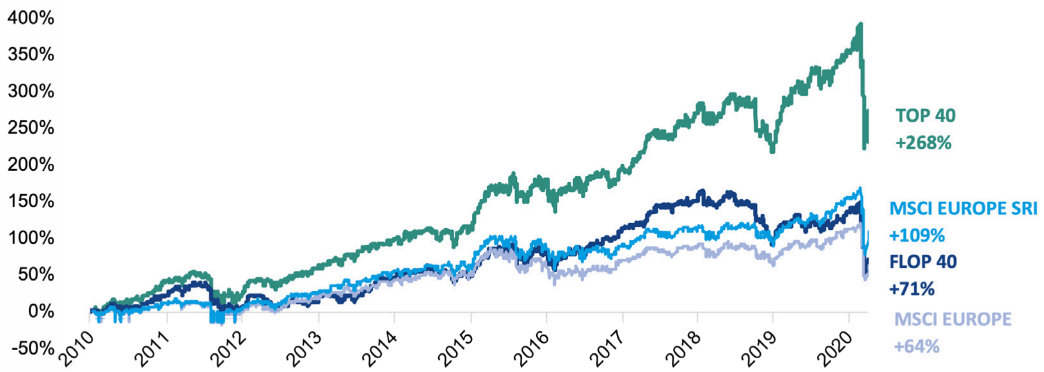
The SRI & Performance by LFDE study, facing the crisis

The updated study as of March 31, 2020

Financial markets recorded the fastest fall in their history in the first quarter of 2020 (-20% in just 20 days). The track record of our SRI & Performance study starts in 2010: this is the first time that our mock portfolios are subject to a crisis of this magnitude. The stock market reaction of the companies making up these portfolios in highly instructive on performance of Socially Responsible Investments (SRI) in times of crisis.

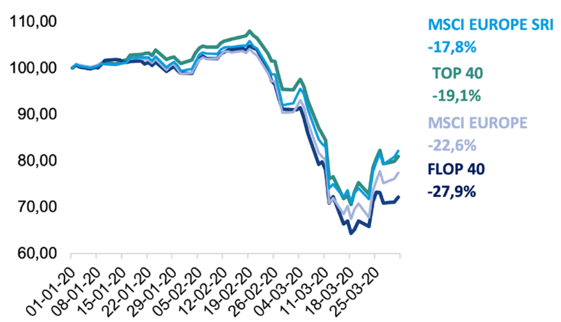
A foolproof outperformance!

The stock market crash confirmed our conviction on the resilience of companies with the best ESG profiles (Environmental, Social and Governance). Over 10 years, the portfolio of the best ESG profiles (TOP 40) generates a performance 3.8 times higher than that of the worst ESG profiles (FLOP 40). This gap has widened considerably, as at the end of 2019 it was 2.6 times.



Concerning risk, the risk/return ratio has remained stable. As in 2019, this ratio applied to the portfolio comprising the best ESG ratings is 2.3 times higher than that for the portfolio incorporating the lowest ratings.

Q1 2020 Performance



In the first quarter of 2020, the TOP 40 portfolio (-19.1%) significantly outperformed the FLOP 40 (-27.9%). In addition, as seen in 2019, the FLOP 40 was outperformed by the main European stock indices over this period.

How do we explain such resilience?

- We observe that companies with the best ESG profiles are mainly quality companies with solid balance sheets. Given the high level of risk liquidity, the market was therefore in favor of these companies, which were seen as safe havens.
- The proper identification and management of non-financial risks, which characterize responsible companies, are essential in the context of a health crisis: the protection of employees and customers allows these companies to bounce back faster and on a sustainable basis.
- Flows are increasingly directed towards companies with top ESG ratings, they have not dried up (+30 billion euros according to Morningstar*) and undoubtedly come to feed their stock prices.

* Citywire 28/04/2020 "European ESG funds attract €30bn amid wider selloff, report finds"

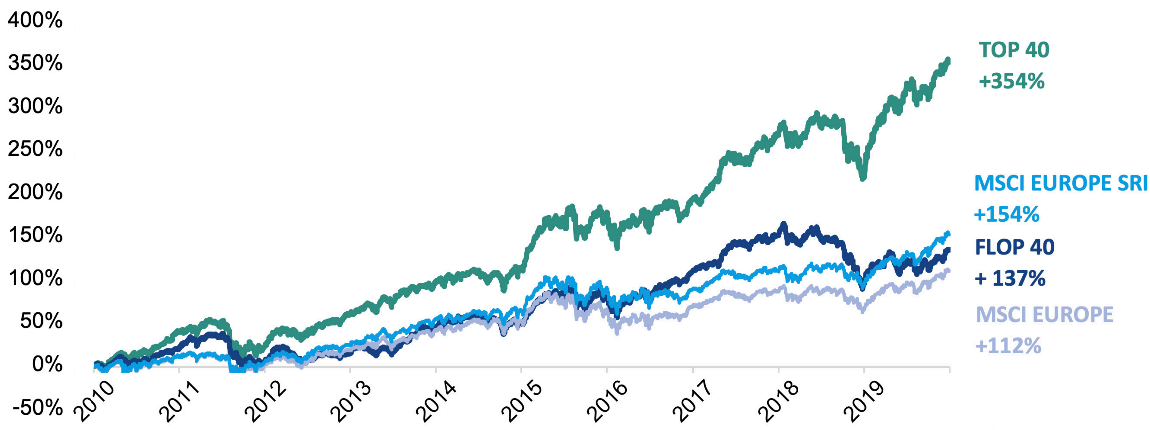
What happened in 2019?

Responsible investment and performance: death of a cliché

The first version of the SRI & Performance study by LFDE, published at the beginning of 2019, demonstrated that: far from destroying value, taking Environmental, Social and Governance (ESG) criteria on the contrary favors performance in the long term. This study highlighted the relationship between ESG ambitious companies and their stock market performance. At the time, over 9 years, the portfolio composed of the best ESG profiles (TOP 40) had generated a performance 2.3 times higher than that of the worst ESG profiles (FLOP 40).

A year later, the outperformance of the best ESG profiles has increased

The outperformance of the best ESG profiles is confirmed and accentuated. Over 10 years, the portfolio of the best ESG profiles generates a performance 2.6 times higher than that of the worst ESG profiles.



Concerning the risk, the indicators have not changed significantly. Over a 10-year period, the risk/return ratio of the portfolios composed of the best ESG ratings is 1.6 times higher than that of the lowest ratings. The TOP 40's 10-year risk-return ratio is excellent: it stands at 1.11 compared to 0.7 for the FLOP 40, 0.6 for the MSCI Europe SRI and 0.5 for the MSCI Europe.

The best criterion is still the Social

If taken separately, Environmental, Social and Governance criteria are all sources of long-term performance, as the first edition of our study demonstrated, the Social criterion remains the most creator of value. Over 10 years, the portfolio with the best social ratings performed the best (+ 333%), followed by the best governance scores (+ 262%) and the top environmental ratings (+ 233%).

The synergy effect between the three criteria E, S and G is confirmed

Out of all the simulated portfolios, the one that creates the most value over 10 years is the TOP 40 (+ 354%), followed by the portfolio of the highest social ratings (+ 333%). La Financière de l'Échiquier's unique weighting, which gives Governance 60% of the ESG rating, and the remaining 40% split between the Environment and the Social, is therefore creating value in the long-term.

The study confirms our extreme vigilance with regard to bad governance

Of all the portfolios tested, the one with the worst governance scores generated the worst performance over 10 years (+ 126%). Staying away from companies with the worst governance is therefore beneficial in the long run.

Focus on 2019's performance

The results are spectacular. The portfolio composed of the best ESG profiles (TOP 40) grew by nearly + 39% whereas the worst (FLOP 40) profiles increased by by just over + 20%. Against them, benchmarks performed better than FLOP 40, but less than the TOP 40: the MSCI Europe gained + 26%, the MSCI Europe SRI + 30%.

The cumulative 10-year performance of the portfolio with the worst ESG profiles (+ 137%) has fallen below that of the MSCI Europe SRI index (+ 154%) due to the underperformance of FLOP 40 in 2019 (+20.4% against + 29.7% for the index, or 9.3% underperformance). Yet, over the same period, the average ESG rating of the FLOP 40 portfolio deteriorated by 0.9 points - from 5.0 / 10 in 2018 to 4.1 / 10 in 2019 - due to the rating of new companies with bad ESG profiles. Our conclusions on the impact of ESG bad practices, captured by our rating, on the stock market performance of companies are therefore confirmed.

Who are the top contributors to performance in 2019[1]?

ASML

ESG rating: 8,1/10 | 2019 Performance: +95,3%

The manufacturer of lithography machines for the semiconductor industry has strong checks and balances through a board of directors composed of independent directors with relevant technical expertise (semiconductors, electronics, academic ...). The corporate culture is very strong and the group's environmental policy incorporates ambitious long-term numerical targets. The product life cycle is perfectly managed as 98% of the machines produced since the beginning in 1984 are still in operation.

sartorius stedim biotech

ESG rating: 7,6/10 | 2019 Performance: +69,9%

The manufacturer of products for the production of biomedicines (filters, membranes, disposable bags) has good governance, stands out for excellent results on its key environmental metrics, including water consumption, and perfectly manages the attractiveness and employee loyalty, two major challenges in this fast-growing sector. The group is working to develop products based on bioplastics to offset the increase in waste generated by its activity.

DSM

ESG rating: 7,7/10 | 2019 Performance: +66,2%

The sustainable dimension is at the heart of the strategy of this producer of vitamins and materials for human and animal nutrition and the pharmaceutical industry. This strategy integrates profits, the environment and people. DSM thus voluntarily set an internal carbon price that affected its investment decisions. On the HR aspect, its results are excellent: employee turnover is very low and the training rate is high.

What lessons can be learned?

In 2019, LFDE stepped up its commitment to responsible investment:

- 100%[2] actively managed assets integrate ESG criteria.
- 33% of SRI assets: 4 additional funds have obtained the French SRI label, bringing our labeled offer to 6 funds.
- Our 2 historical SRI funds, Echiquier Major SRI Growth Europe and Echiquier Positive Impact Europe, have obtained the Belgian (Towards Sustainability) and German (FNG with three stars) labels.

This commitment has also shone beyond our walls: L'École de l'ISR, an educational innovation by LFDE that includes in particular the results of the study, has trained more than 999 financial professionals since its launch.

[1] From the TOP 40
[2] Excluding: Systematic strategies and asset allocation funds

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Sources: La Financière de l'Échiquier, Bloomberg. Data as of 31/03/2020. The 2019 performances are calculated in total return (31/12/2018 to 31/12/2019).
Disclaimer: The analytical results presented in this document are based on the best sources available to us and on a proprietary methodology for analyzing environmental, social and governance criteria. Other criteria are taken into account in the performance of a share. Past performances are not a reliable indicator of future performances and are not constant over time. They therefore should not be the central factor in making any investment decision.
Methodological review: The study integrates all internal ratings produced by LFDE's management team between 1 January 2010 and 31 December 2019, representing a sample of 885 companies. Ratings concern the entire rating base without sector or normative exclusion. Since 01/01/2019, in addition to the internal ratings carried out by the SRI team, ESG ratings achieved in «ESG integration», that is to say a portion of the E and S ratings, are taken into account. may come from external rating agencies. The ESG integration program launched at the end of 2017 has now stabilized. The ESG coverage rate of all portfolios exceeds 90%. Only ratings evaluated for less than 3 years are taken into account. Beyond that, the rating no longer reflects the profile of the company, which has been able to materially change its ESG practices. These are listed companies of all capitalization sizes, predominantly European.
The portfolios are equally weighted, created solely from the filter of ESG ratings, they are 100% invested, composed solely of equities and rebalanced at regular maturity (from 2010 to end 2015, annual rebalancing then quarterly rebalancing since 01/01/2016). No management fees or ancillary fees are applied to performance which means dividends reinvested (Net Return).