

**One of our core beliefs** is that genuinely embedding ESG at the core of our investment decision-making process contributes to the generation of superior long-term risk-adjusted returns. This year again, we have further improved our scoring and integration processes. We notably focused on two priorities: making our proprietary assessment more holistic and rolling out our virtual sector teams to develop analytical frameworks across sectors.

## Enhancing sustainability measurement

Introduced by the European Commission in 2019, the bulk of the implementation of the Sustainable Finance Disclosure Regulation (SFDR) rolled out in 2022. SFDR aims to improve transparency in the market for sustainable investment products and prevent 'greenwashing'. Under this regulation, sustainable investment has been defined as investment that generates net-positive environmental and/or social outcomes. The resulting market-wide challenge has been around measuring individual holdings' environmental and social contribution, while ensuring that positive contributions do not come with negative side-effects – i.e. adverse impacts.

Our proprietary sustainable investment assessment enables these calculations. Over recent years, our methodology has grown from seeking historical revenue alignment to sustainable development goals, to a more holistic view that considers business models, operational activities, and ambitions. This scope enlargement better reflects the company's commitment and actions to address the sustainability challenges. In addition, the assessment also includes a 'Do No Significant Harm' (DNSH) test while considering good governance. This test includes the consideration of principal adverse impacts (PAI), as required by the SFDR regulation. PAI consists of a list of

environmental and social factors to be taken into account and reported – these include, among others, greenhouse gas emissions and intensity, carbon footprint, emissions to water or gender pay gap. For example, thermal coal revenue is used as an DNSH exclusion screen to indirectly address the greenhouse gas emission related PAIs.

For all these items, data accuracy and data suitability are key to deliver a comprehensive picture of both positive and negative impacts associated with our investments. Our ESG Research team selects the appropriate data and work with operational teams to deliver the implementation. Importantly, the process is dependent on one third-party ESG data vendor, and whilst using such data, the team constantly challenges the results. In some cases, a different conclusion is reached as a result of the analysis conducted internally, emphasising a more forward-looking view.

SFDR is one of many regulatory regimes we have incorporated into product development. It has been an important feature of solutions design, both in terms of investment process and reporting. To ensure an up-to-date understanding of fast-changing regulation and a successful implementation of our constantly enhancing processes, we conduct regular internal training sessions and workshops across the entire investment platform.

## Virtual Sector Teams: aligning sustainability and value creation

Building on our 20+ year experience in ESG integration, one of last year's focuses was to set up a 'materiality matrix' enabling us to capture the most financially relevant ESG criteria. In December 2021, we set up 12 Virtual Sector Teams (VSTs) aimed at leveraging ESG knowledge and establishing greater granularity in our Risk Scoring process across all asset classes and geographies. Acting as sector-focused centres of excellence, their role is to define and assess sector/industry-specific ESG materiality frameworks which form the first steps of our proprietary ESG scoring definition.

Overall, our VSTs are made up of 120+ investment professionals in various offices (including London, New York, Paris, Dusseldorf and Hong Kong). The geographical diversity of the VST initiative optimally combines 'on-the-field' expertise and quantitative rigour. This includes deeper analysis into the ESG risk drivers, a reweighting of E, S and G pillars as well as a specific sector overlay.

Beyond SFDR and other sustainability regulations to come, the whole purpose of ESG integration is to make better-informed investment decisions across all geographies, industries, and asset classes.

- **Xavier Desmadryl**, Global Head of ESG research, HSBC AM



## Virtual sector teams: 12 teams regrouping 120+ investment professionals<sup>7</sup>

	Energy	Materials	Aerospace & Defense	Industrials	Consumer Goods & Services	Auto & Transport	Food & retailing	Healthcare	Financials	Tech Media Telecom	Utilities	Real Estate
<b>Equity</b> (no. of portfolio managers & analysts involved)	5	6	/	7	10	8	6	8	4	11	6	5
<b>Credit</b> (no. of portfolio managers & analysts involved)	7	15	4	11	8	10	7	7	18	10	11	11
<b>Responsible Investment</b> (no. Of specialists from ESG Research, Stewardship and RI Investment involved)	3	4	5	3	5	4	5	2	4	3	4	2

7. Each investment professional can be involved in more than one Virtual Sector Team. Source: HSBC Asset Management, March 2023.

**Each VST** is chaired by a member of the ESG research and integration team acting as the coordinator and the catalyst to ensure global consistency and cross-fertilisation of best practice. Each virtual team also benefits from the support of stewardship and engagement specialists tasked with defining a set of specific engagement questions which help gather valuable investment insights and refine our understanding of the investment case.

In terms of outputs, the VSTs focus on developing analytical frameworks for each of the sectors analysed, identifying the most critical and or financially/material ESG issues. The VSTs also act as the primary forum for reviewing, checking, and assessing the actual level of ESG accuracy of controversial companies. This encompasses assessment of UN Global Compact breaches, involvement in controversial and banned weapons, thermal coal involvement and negative impact on biodiversity.

In addition, we are now developing our ability to convert each issue into a score through identifying representative metrics and data points. We started with an approach to climate and net zero issues, which will combine greenhouse gas emissions data, physical risk and transition risk indicators and net zero commitments. Progressively, all ESG issues will be approached in the same manner whether these belong to the E, S or G pillars. The methodology applied to build these scores will be consistent, but the nature of the data considered will be substantially tailored.




## Looking forward

After climate and net zero, our next focus will be on utilities. This industry is certainly among the most impacted by all kinds of ESG issues, and as such will be a useful testbed for the implementation of the ESG framework and scoring approach which will extend to cover all sectors and industries.

Simultaneously, we are developing scoring frameworks which will be updated automatically, on a monthly basis, before feeding our reporting systems. To achieve this, we will leverage our cloud platform combined with the data aggregation and back-testing facility, which we will use for data aggregation, score building and back-testing.

Finally, our ambition for the months to come is to further explore emerging themes like the just transition, diversity, equity & inclusion and biodiversity. These themes are fully aligned with those adopted by our Stewardship team through engagement. Our primary objective is not to develop academic or fundamental research, but rather to develop usable insights that will inform our investment decision-making processes.

## External recognition

 Exemplary multi-level ESG research on companies, sectors but also selected topics with the aim of both supporting investment teams in their ESG due diligence and providing ongoing training.

- HSBC Asset Management ranks #5 in Scope's ESG Integration Study<sup>6</sup>

## Our commitment in numbers

Our virtual sector teams bring together **120+** investment professionals carrying out sector-specific ESG research across our investment platform

### Since 2010, ESG

considerations have been systematically integrated into our equity, fixed income and multi-asset capabilities and are being increasingly applied in liquidity and alternatives, with our proprietary ESG database now covering more than **19,000** financial instruments.

6. [Scope's ESG integration study: notable differences between asset managers](#) (July 2022)  
Source: HSBC Asset Management, January 2023.



For Professional Clients and intermediaries within countries and territories set out below; and for Institutional Investors and Financial Advisors in Canada and the US. This document should not be distributed to or relied upon by Retail clients/investors.

The value of investments and the income from them can go down as well as up and investors may not get back the amount originally invested. The capital invested in the fund can increase or decrease and is not guaranteed. The performance figures contained in this document relate to past performance, which should not be seen as an indication of future returns. Future returns will depend, inter alia, on market conditions, fund manager's skill, fund risk level and fees. Where overseas investments are held the rate of currency exchange may cause the value of such investments to go down as well as up. Investments in emerging markets are by their nature higher risk and potentially more volatile than those inherent in some established markets. Economies in Emerging Markets generally are heavily dependent upon international trade and, accordingly, have been and may continue to be affected adversely by trade barriers, exchange controls, managed adjustments in relative currency values and other protectionist measures imposed or negotiated by the countries and territories with which they trade. These economies also have been and may continue to be affected adversely by economic conditions in the countries and territories in which they trade. Mutual fund investments are subject to market risks, read all scheme related documents carefully.

The contents of this document may not be reproduced or further distributed to any person or entity, whether in whole or in part, for any purpose. All non-authorized reproduction or use of this document will be the responsibility of the user and may lead to legal proceedings. The material contained in this document is for general information purposes only and does not constitute advice or a recommendation to buy or sell investments. Some of the statements contained in this document may be considered forward looking statements which provide current expectations or forecasts of future events. Such forward looking statements are not guarantees of future performance or events and involve risks and uncertainties. Actual results may differ materially from those described in such forward-looking statements as a result of various factors. We do not undertake any obligation to update the forward-looking statements contained herein, or to update the reasons why actual results could differ from those projected in the forward-looking statements. This document has no contractual value and is not by any means intended as a solicitation, nor a recommendation for the purchase or sale of any financial instrument in any jurisdiction in which such an offer is not lawful. The views and opinions expressed herein are those of HSBC Asset Management at the time of preparation, and are subject to change at any time. These views may not necessarily indicate current portfolios' composition. Individual portfolios managed by HSBC Asset Management primarily reflect individual clients' objectives, risk preferences, time horizon, and market liquidity. Foreign and emerging markets. Investments in foreign markets involve risks such as currency rate fluctuations, potential differences in accounting and taxation policies, as well as possible political, economic, and market risks. These risks are heightened for investments in emerging markets which are also subject to greater illiquidity and volatility than developed foreign markets. This commentary is for information purposes only. It is a marketing communication and does not constitute investment advice or a recommendation to any reader of this content to buy or sell investments nor should it be regarded as investment research. It has not been prepared in accordance with legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of its dissemination. This document is not contractually binding nor are we required to provide this to you by any legislative provision.

All data from HSBC Asset Management unless otherwise specified. Any third party information has been obtained from sources we believe to be reliable, but which we have not independently verified.

HSBC Asset Management is the brand name for the asset management business of HSBC Group, which includes the investment activities provided through our local regulated entities. HSBC Asset Management is a group of companies in many countries and territories throughout the world that are engaged in investment advisory and fund management activities, which are ultimately owned by HSBC Holdings Plc. (HSBC Group). The above communication is distributed by the following entities:

- ◆ In Argentina by HSBC Global Asset Management Argentina S.A., Sociedad Gerente de Fondos Comunes de Inversión, Agente de administración de productos de inversión colectiva de FCI N°1;
- ◆ In Australia, this document is issued by HSBC Bank Australia Limited ABN 48 006 434 162, AFSL 232595, for HSBC Global Asset Management (Hong Kong) Limited ARBN 132 834 149 and HSBC Global Asset Management (UK) Limited ARBN 633 929 718. This document is for institutional investors only, and is not available for distribution to retail clients (as defined under the Corporations Act). HSBC Global Asset Management (Hong Kong) Limited and HSBC Global Asset Management (UK) Limited are exempt from the requirement to hold an Australian financial services license under the Corporations Act in respect of the financial services they provide. HSBC Global Asset Management (Hong Kong) Limited is regulated by the Securities and Futures Commission of Hong Kong under the Hong Kong laws, which differ from Australian laws. HSBC Global Asset Management (UK) Limited is regulated by the Financial Conduct Authority of the United Kingdom and, for the avoidance of doubt, includes the Financial Services Authority of the United Kingdom as it was previously known before 1 April 2013, under the laws of the United Kingdom, which differ from Australian laws;
- ◆ in Bermuda by HSBC Global Asset Management (Bermuda) Limited, of 37 Front Street, Hamilton, Bermuda which is licensed to conduct investment business by the Bermuda Monetary Authority;
- ◆ in Canada by HSBC Global Asset Management (Canada) Limited which provides its services as a dealer in all provinces of Canada except Prince Edward Island and also provides services in Northwest Territories. HSBC Global Asset Management (Canada) Limited provides its services as an advisor in all provinces of Canada except Prince Edward Island;



- ◆ in Chile: Operations by HSBC's headquarters or other offices of this bank located abroad are not subject to Chilean inspections or regulations and are not covered by warranty of the Chilean state. Further information may be obtained about the state guarantee to deposits at your bank or on [www.sbif.cl](http://www.sbif.cl);
- ◆ in Colombia: HSBC Bank USA NA has an authorized representative by the Superintendencia Financiera de Colombia (SFC) whereby its activities conform to the General Legal Financial System. SFC has not reviewed the information provided to the investor. This document is for the exclusive use of institutional investors in Colombia and is not for public distribution;
- ◆ in Finland, Norway, Denmark and Sweden by HSBC Global Asset Management (France), a Portfolio Management Company authorised by the French regulatory authority AMF (no. GP99026) and through the Stockholm branch of HSBC Global Asset Management (France), regulated by the Swedish Financial Supervisory Authority (Finansinspektionen);
- ◆ in France, Belgium, Netherlands, Luxembourg, Portugal, Greece by HSBC Global Asset Management (France), a Portfolio Management Company authorised by the French regulatory authority AMF (no. GP99026);
- ◆ in Germany by HSBC Global Asset Management (Deutschland) GmbH which is regulated by BaFin (German clients) respectively by the Austrian Financial Market Supervision FMA (Austrian clients);
- ◆ in Hong Kong by HSBC Global Asset Management (Hong Kong) Limited, which is regulated by the Securities and Futures Commission;
- ◆ in India by HSBC Asset Management (India) Pvt Ltd. which is regulated by the Securities and Exchange Board of India;
- ◆ In Israel, HSBC Bank plc (Israel Branch) is regulated by the Bank of Israel. This document is only directed in Israel to qualified investors (under the Investment advice, Investment marketing and Investment portfolio management law-1995) of the Israeli Branch of HBEU for their own use only and is not intended for distribution;
- ◆ in Italy and Spain by HSBC Global Asset Management (France), a Portfolio Management Company authorised by the French regulatory authority AMF (no. GP99026) and through the Italian and Spanish branches of HSBC Global Asset Management (France), regulated respectively by Banca d'Italia and Commissione Nazionale per le Società e la Borsa (Consob) in Italy, and the Comisión Nacional del Mercado de Valores (CNMV) in Spain;
- ◆ in Mexico by HSBC Global Asset Management (Mexico), SA de CV, Sociedad Operadora de Fondos de Inversión, Grupo Financiero HSBC which is regulated by Comisión Nacional Bancaria y de Valores;
- ◆ in the United Arab Emirates, Qatar, Bahrain & Kuwait by HSBC Bank Middle East Limited which are regulated by relevant local Central Banks for the purpose of this promotion and lead regulated by the Dubai Financial Services Authority.
- ◆ in Oman by HSBC Bank Oman S.A.O.G regulated by Central Bank of Oman and Capital Market Authority of Oman;
- ◆ in Peru: HSBC Bank USA NA has an authorized representative by the Superintendencia de Banca y Seguros in Perú whereby its activities conform to the General Legal Financial System - Law No. 26702. Funds have not been registered before the Superintendencia del Mercado de Valores (SMV) and are being placed by means of a private offer. SMV has not reviewed the information provided to the investor. This document is for the exclusive use of institutional investors in Perú and is not for public distribution;
- ◆ in Singapore by HSBC Global Asset Management (Singapore) Limited, which is regulated by the Monetary Authority of Singapore;
- ◆ in Switzerland by HSBC Global Asset Management (Switzerland) AG. This document is intended for professional investor use only. For opting in and opting out according to FinSA, please refer to our website at <https://www.assetmanagement.hsbc.ch/> if you wish to change your client categorization, please inform us. HSBC Global Asset Management (Switzerland) AG having its registered office at Gartenstrasse 26, PO Box, CH-8002 Zurich has a licence as an asset manager of collective investment schemes and as a representative of foreign collective investment schemes. Disputes regarding legal claims between the Client and HSBC Global Asset Management (Switzerland) AG can be settled by an ombudsman in mediation proceedings. HSBC Global Asset Management (Switzerland) AG is affiliated to the ombudsman FINOS having its registered address at Talstrasse 20, 8001 Zurich. There are general risks associated with financial instruments, please refer to the Swiss Banking Association ("SBA") Brochure "Risks Involved in Trading in Financial Instruments";
- ◆ in Taiwan by HSBC Global Asset Management (Taiwan) Limited which is regulated by the Financial Supervisory Commission R.O.C. (Taiwan);
- ◆ in the UK by HSBC Global Asset Management (UK) Limited, which is authorised and regulated by the Financial Conduct Authority;
- ◆ and in the US by HSBC Global Asset Management (USA) Inc. which is an investment adviser registered with the US Securities and Exchange Commission

## NOT FDIC INSURED ◆ NO BANK GUARANTEE ◆ MAY LOSE VALUE

Copyright © HSBC Global Asset Management Limited 2023. All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, on any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of HSBC Global Asset Management Limited.

336\_AMFR\_CM\_2023\_03



