BPS (SUISSE)

Striving to achieve increasingly Sustainable Finance

Opinions, considerations and prospects of your trusted Bank

Third Newsletter
February 2023

IMPRESSUM

Editing:
BPS (SUISSE)
Marketing Service
Piazza Indipendenza 2
6830 Chiasso

marketing@bps-suisse.ch

The evolution of BPS (SUISSE) in the field of the **"sustainability of investments"**

2022 was a highly unusual year for the financial markets: the sudden and higher-than-expected rise in interest rates led to a sharp drop in all bond indices, and the stock markets also reacted negatively due to the numerous external elements that increased uncertainty amongst institutional and private investors. For balanced portfolios, 2022 was therefore the worst year for several decades.
How did sustainability-oriented investments perform in this scenario?
Unfortunately, neither the orientation towards environmental sustainability (E), nor the attention to social issues (S) and governance (G) guaranteed stability of the values in the period in question. In fact, in the past year, there has been a general decline in financial assets, without much discernment in terms of orientation towards sustainability. Indeed, certain sectors which are traditionally underweighted or absent from these strategies, such as energy or base metals, outperformed the broader indices.
The question is this – is the paradigm of sustainability in investing therefore overrated or ineffective?
If we lengthen the investment horizon and analyse the medium-term results, the answer is no. The extraordinary negativity of 2022 has combined quantitative and qualitative assessments across stocks, sectors and indices in an unsuitable way, bringing back certain parts of the market which were previously underweight in global portfolios and deflating others that have been excessively exaggerated by trend effects, rather than from real expectations of growth and returns.
The basic problem is that the concept of sustainability is often misinterpreted, and is identified as a guarantee of profitability and investment security, when in reality it should be interpreted as a third and significant aspect of the portfolio: risk, return and sustainability.
The question you should be asking yourself is: having chosen a risk/return profile, what degree of sustainability do I want for my portfolio. In this sense, the role of client advisor is fundamental and in this edition of the Newsletter we hear from the regions in which the Bank is active, to highlight client preferences and our responses.
While considering the journey towards the sustainability of investments and whether these are effective or not, we must also consider regulation. The regulatory uncertainty that arises due to excessive regulation contributes to increasing confusion, both among financial services producers and among private and institutional investors. The fear of greenwashing while trying to comply with the rules has led some major asset managers worldwide to be more cautious when putting their offers together. We will speak to Alberto Stival – representative for Italian-speaking Switzerland of Swiss Sustainable Finance – to learn more.
BPS (SUISSE) is committed to providing investment services that include ESG logic in order to be able to meet the needs of both current and future clients. In 2022, we strengthened our investment process with regard to the ESG component and introduced analysis integration elements for traditional management mandates that take these aspects into account. We publish ESG investment concepts every quarter with the aim of promoting this investment philosophy in a simple and understandable way. For 2023-2024, we have plans to broaden our range.
Thinking Sustainable is not just a slogan, it's an approach to wealth management that we apply day in, day out, 365 days a year.

Roberto Mastromarchi, CFA, CESGA
Vice President Executive Board,
Head of the Front Office Division BPS (SUISSE)

ESG, INFLATION AND LATEST TRENDS

2022 was one of the worst years for fixed income investors, mainly due to the persistent rise in inflation and attempts by central banks to contain it.

The integration of environmental, social and governance factors into investment decisions has not been one of the most topical issues, but in reality, as highlighted by an interesting article by NordSIP, the analysis of ESG issues can help to evaluate more studied inflationary trends and those of interest rates, providing a contribution to the management of bond investments.
After all, central bankers are already doing this. As Christine Lagarde, president of the ECB, recently stated: "Our task of preserving price stability must include further work to understand how climate change affects our role. We need to incorporate climate change into everything we do: our models, data, projections and analyses".

In fact, looking to the future through ESG parameters can provide food for thought on inflationary effects due to the energy transition, greater social consideration and the relevance of sustainability mandates within central monetary institutions.

Energy and food, traditionally the most volatile elements of inflation and two of the items behind many of the recent price increases, are closely linked to climate change. Extreme weather conditions is one of the main issues affecting crops and therefore food markets in general. Research by Ghent University in Belgium estimates that exogenous fluctuations in the prices of food products represent 25% to 30% of the volatility of the harmonised index of consumer prices developed by the ECB. If we then analyse the costs of the materials needed for electrification worldwide, we see that these are gaining importance and the prices of many technologies such as photovoltaic modules and wind turbines have recently exhibited an upward trend. However, given that other renewable energy technologies have low and overall stable marginal costs, the energy transition may be inflationary initially and then help make inflation more stable at a later stage.

"Determining whether the overall effect of ESG trends will be **inflationary** or **disinflationary** is therefore not a trivial exercise."

On the social front, as companies face higher expectations from investors and authorities, they are subject to increased hiring from more disadvantaged social groups and an overall increase in wages. This can improve companies' prospects by reducing the risk of fines and meeting the demand of ethical consumers but, in the short term, the costs can be passed on to consumers, thereby contributing to increased inflation.

We must also pay attention to the central banks' approach to sustainability, especially their asset purchase programmes. It is true that most institutions have now adopted, within their mandates, measures to improve the sustainability of economic growth. For example, last September the ECB published details on how it incorporates climate change into corporate bond reinvestments under the Corporate Sector Purchase Programme and the Pandemic Emergency Purchase Programme. The best issuers are rewarded with higher subscriptions while the poorest issuers are penalised, based on an internal ECB climate metric.

Determining whether the overall effect of ESG trends will be inflationary or disinflationary is therefore not a trivial exercise. The impact will also vary from country to country, depending on the energy mix and demographics. However, it is undeniable that the dynamics in terms of sustainability are intrinsically linked to the evolution of prices, and that analyses and investment decisions in the bond sector will be increasingly conditioned by those of an ESG nature.

Looking at the latest market dynamics, it can be seen that the share of ESG emissions in the European primary market has continued to grow. 36% of corporate issues last year were ESG, up from 26% in 2021 and 9% in 2020. From an issuer perspective,

rising investor demand makes ESG-labelled bonds an increasingly efficient form of funding. For investors looking at sustainable debt, after a period of great stress, it is plausible to expect some stabilisation in the bond market, whose prices now absorb a great deal of inflationary and monetary policy expectations. In the current context, it is possible to take advantage of more interesting valuation levels than in previous years and it is possible to find good-value opportunities even in the higher-quality and safer range.

Marco Romanelli, CESGA
Asset Management, Manager BPS (SUISSE)

THE REGULATORY COMPLEXITY OF THE **ESG WORLD**

As sustainable investing has grown, rules and regulatory complexity have also increased in recent years, reaching a staggering number of nearly 900 policies and regulations worldwide. Brakes on the diffusion of ESG investments or a guarantee of quality? We addressed this and other issues with Alberto Stival, representative for Italian-speaking Switzerland of Swiss Sustainable Finance.

ALBERTO STIVAL
representative for Italian-speaking Switzerland of Swiss Sustainable Finance

BIOGRAPHY

Alberto Stival has over twenty years' experience in the Swiss financial sector, in the fields of training and communication, and has worked with Swiss Sustainable Finance since 2014. He currently fulfils the role of training development manager as well as representative for Italian-speaking Switzerland.

He is president of pr suisse, the Swiss Public Relations Association, lecturer at SUPSI and founded his own consultancy company in 2019.

Mr Stival, in recent years, the number of policies and regulations relating to sustainable finance, both binding and non-binding, has increased significantly. It is estimated that almost 900 policies and regulations exist worldwide today, with over two hundred additions or revisions in 2021 alone. What do you make of this data?

The topic of sustainable finance has moved from niche to mainstream almost everywhere, which is, in itself, positive from my point of view. Therefore, the need to regulate everything relating to the world of sustainable investments is also understandable, in the interests of all those operating in the sector but also savers and investors, both private and institutional. It remains to be seen whether we are exaggerating here, in the sense that the bodies that issue rules and regulations are not always coordinated with each other and this risks making things more complicated rather than making things simpler.

Is there a common thread that links these regulations?

Yes, but like I said, there is no real coordination, sometimes even between organisations within the same country Everyone is more or less aligned on the interpretation of the concept of sustainability applied to finance, where more and more often a distinction is made between two fundamental concepts; on the one hand there are financial products whose final objective is to promote the resolution of social or environmental problems, and on the other we include financial products whose objective is simply not to have a negative impact on this social and environmental phenomena (according to the concept of "do no harm"). There is also a common effort by all financial supervisory authorities to correctly define and combat the phenomenon of greenwashing.

Do you believe that regulatory complexity could hinder the diffusion of sustainable investments or, on the contrary, could it somehow favour its diffusion?

Like I said, regulation is absolutely necessary, but too many rules actually risk having the opposite effect. While for years, when I spoke of sustainable finance in banks, I encountered people who were very interested in the subject, I now meet more and more people who are mainly concerned with how to comply with the many new regulations while losing sight of the real objective, which is to contribute to a better and more liveable world for all. The Germans have a phrase, "Weniger ist mehr" (less is more), and I believe that this concept should also be applied to legislation on sustainable finance.

> "The bodies that issue **rules and regulations** are not always coordinated with each other and this risks making things more complicated rather than making things simpler."

You are responsible for training development and the representative for Italian-speaking Switzerland for Swiss Sustainable Finance. Can you briefly explain what role your association plays?

The association was founded in 2014 with the aim of promoting sustainable finance in Switzerland and consequently positioning the Swiss financial centre among the world leaders in this area. We currently have over two hundred members throughout the entire ecosystem: banks, financial management companies, insurance companies, pension funds and foundations, but also ESG rating companies, universities and research centres, public bodies, non-profit organisations etc. Few people know, but Switzerland has seen many pioneers in the field of sustainable finance, with the first players in the sector appearing in the 1980s and 1990s, so we have a solid tradition on which to build our present and future.

We have seen that there are many regulations, however the authorities are very attentive to the issue of so-called greenwashing. How do you explain this? And how can we combat this phenomenon?

Alongside greenwashing, there is also greenwishing, which is when you believe in good faith that an offering is for sustainable financial services and products, and only realise later that this was not actually the case. For example, this can happen when data used for the sustainability analyses for the companies you invest in is not of a high quality. The phenomenon of greenwashing must be combated by first of all promoting transparency in relation to products; if we think of an investment fund, for example, we must clearly specify which approach to sustainability was used to identify the securities in which to invest. We must also improve financial advisors' skills, so that they know how to properly explain the products in question to investors. The latest recommendations from SwissBanking point precisely in this direction.

In conclusion, how do you think or hope that the sustainable finance regulatory framework will evolve in the near future?

I hope that the phenomenon is consolidated, i.e. fewer rules which are clearer and easier to understand. But this won't be easy as the subject is constantly changing.

Interviewed by:

Fabio De Pasquale
Head of SICAV Development
Investment Advisory BPS (SUISSE)

Enrico Zadra CIIA, CAIA, CESGA
Head of Asset Management BPS (SUISSE)

RENEWABLE ENERGY

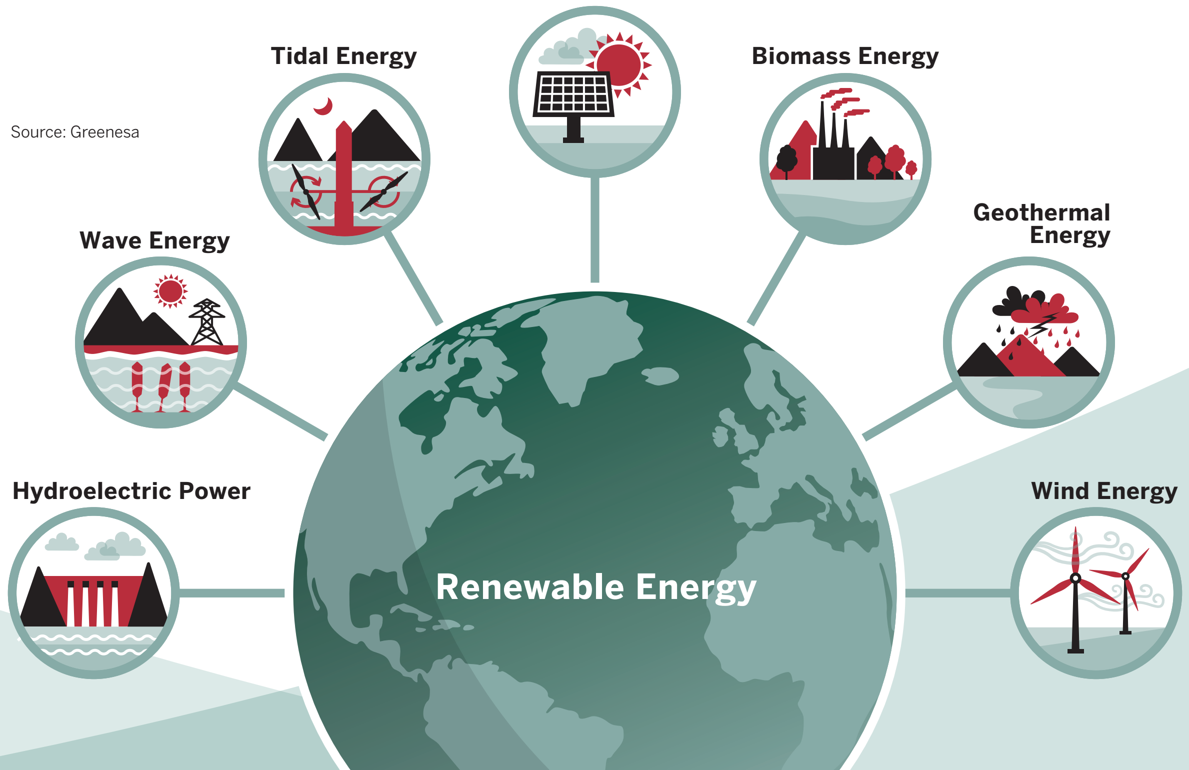
Today, we mainly use fossil fuels to heat our homes and power our cars. Coal, oil and natural gas are "conventional" energy sources, and are readily available to meet our needs. However, these are limited resources and the ever-growing demand for energy will inevitably lead to their depletion. Furthermore, we know that their use has a significant environmental impact, namely the greenhouse effect.

The events of recent months also highlight how vulnerable the conventional energy market is to geopolitical variables, bringing the issue of energy independence to the forefront of the political agenda of individual countries.
The global trend of looking to renewable energy as a primary energy source is therefore assuming increasing importance in order to mitigate the various problems deriving from non-renewable resources.

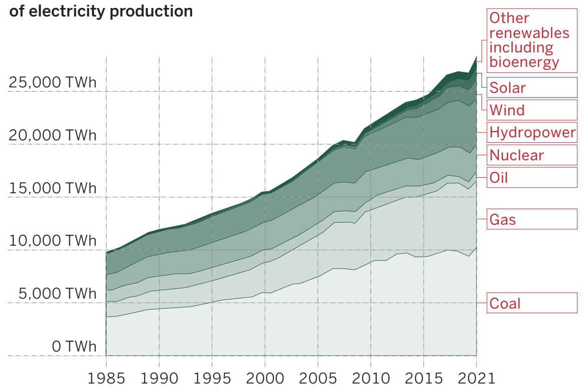
What are COP26's renewable energy and climate targets?
Natural sources, such as sunlight, wind, biomass, water, waves, tides and geothermal heat are sources of green energy. Unlike fossil fuels, these energy sources are renewable, infinite and renew themselves naturally.

In its study "Renewables 2021 – Analysis and forecast to 2026", the International Energy Agency (IEA) predicts that renewable capacity growth is set to accelerate over the next five years, accounting for almost 95% of the increase in global energy capacity by 2026. Forecasts have been revised upwards from the previous year, due to stronger political support and the ambitious climate targets announced for COP26 (United Nations Climate Change Conference). Globally, renewable electricity capacity is projected to increase by more than 60% between 2020 and 2026. Overall, China will remain the leader for the next five years, accounting for 43% of global renewable capacity growth, followed by Europe, the United States and India.

Sources of electricity production by source worldwide
About one third of the world's electricity generation capacity currently comes from low-carbon sources, of which 26% is from renewable sources and around 10% is from nuclear energy. The remaining two-thirds comes from greenhouse gas-emitting fossil fuels, such as coal, gas and oil.



Source: Greenesa



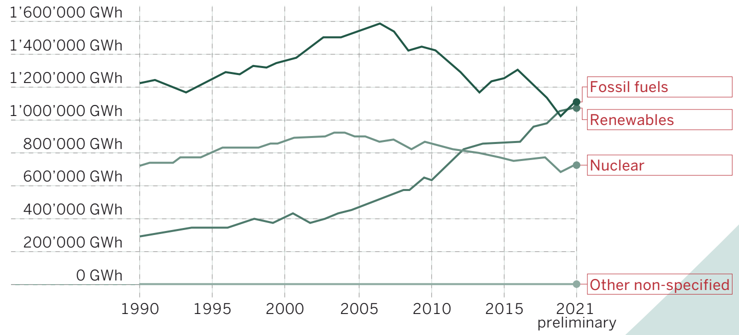
Source: Electricity production by source, World (ourworldindata.org)
Renewable energy is driving new electricity generation in the world's biggest carbon-emitting countries | World Economic Forum (weforum.org)

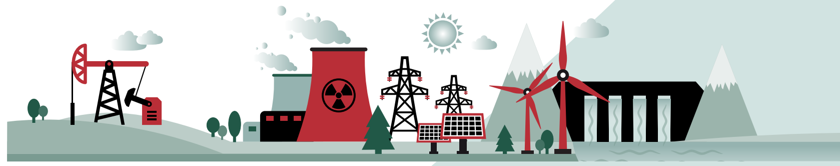
Renewable energy sources such as solar, wind and hydroelectricity need to become a much larger part of the global energy mix if governments around the world are to meet their net-zero targets.
Renewable energy now accounts for 26.74% of the total installed generating capacity in the United States. This is compared to 19.7% five years ago and 14.76% ten years ago.

> "The global trend of looking to **renewable energy** as a primary energy source is therefore assuming increasing importance"

China is also ramping up renewable energy production in an effort to meet climate goals and reduce dependence on external energy supplies. According to the International Energy Agency (IEA), China is the largest market in terms of increased renewable energy capacity, followed by the EU.

EU renewable energy: 37% of electricity
After a long period of restrictive measures introduced to contain the spread of COVID-19 in 2020, 2021 saw a recovery in economic activity and therefore energy use in many EU countries.
Following the massive decline in the consumption of petroleum products in 2020, 2021 estimates point to a 5% increase over the previous year, though still below pre-pandemic levels. Compared to 2019, the data for 2021 show an 8.1% lower consumption of petroleum products and are at the second lowest level since 1990. This evolution is expected, given the EU's goals for lowering carbon levels. Preliminary 2021 data show that around 37% of electricity is generated from renewable energies, with the largest increases in electricity being produced by solar energy (+13.0%) followed by solid biofuels (+9.6%).





Electricity generation in the EU
Fossil fuels led in electricity generation in 2021
Products Eurostat News - Eurostat ec.europa.eu/eurostat

How to invest in companies operating in the sector
As set out above, renewable energies are growing rapidly and companies active in this sector will be able to benefit from this trend. As the world moves away from fossil fuels, there is a market opportunity for companies to invest in clean or renewable energy sources.
There are several ways to profit from green energy prospects. The most direct way is to identify individual companies whose activities are based on the production of alternative energy technologies. However, researching individual companies can be time consuming and not all stocks are traded publicly. An easier way may be to determine a mutual fund or index fund with a large basket of green energy stocks. We recommend investing through investment funds, both "active", where the fund manager tries to beat the performance of the index through the selection of securities, and "passive" (ETF), which replicate the performance of the index. Due to the experience of the managers and the number of underlying assets, the funds make it possible to invest effectively whilst at the same time diversifying the risk, unlike investment in single shares.

Eric Elvio Mantovani CIIA, CESGA
Head of Investment Advisory and Product Management BPS (SUISSE)

ESG CONSULTANCY.
WHAT OUR CLIENTS SAY

We wanted to gather opinions with regard to sustainability from those in direct contact with our clients.
Our findings from interviews carried out with consultants Cedric Bürgin (Basel branch), Carlo Fiorillo (Neuchatel branch), Filippo Forcella (St. Moritz branch) and Guido Saccà (Lugano branch) are below.

2022 has been a particularly bad year for the world stock exchanges and even products with ESG characteristics have not been immune. Have you noticed a change in clients' attitudes towards sustainable finance as a result?

Before 2022, sustainable finance was a frequent subject of discussion with clients, who often decided to integrate ESG products into their investment strategy. However, Cedric Bürgin notes that in recent months the gap between two types of "ESG investors" has widened. The first type includes those who pursue sustainable investments with conviction and tenacity, and who are not discouraged by bad market phases, such as those that occurred last year. The second type, however, tends to opt for ESG investments in the hopes of seeing a positive return in the short term and, in years like the one that has just ended, tends to place less importance on this type of product, focusing on negative performance of stock exchanges, inflation and techniques for protecting assets, as Guido Saccà also points out.

In day-to-day terms, which products or topics do clients show the greatest interest in?

According to Guido Saccà, in the current economic context, clients are leaning towards diversified products and strategies which make it possible to minimise the risk of incorrect timing and to minimise the effect of inflation on their assets.
The most popular products are therefore the investment fund savings plan, which allows you to diversify and distribute investments over time, and high-quality bonds, which allow you to stabilise the return on your portfolio. Technology (for example, electric vehicles), the pharmaceutical sector and the Swiss market in general continue to pique client interest despite volatility, adds Filippo Forcella.
However, in the ESG area, according to Carlo Fiorillo, the topics of greatest interest are climate change and respect for human rights.

"Those who pursue the path of **sustainable investments** with conviction are not discouraged by bad market phases"*

If we look at the next five years, what do you think are the essential elements to increase the diffusion of ESG products?

The latest climate data has again highlighted the precariousness of our ecosystem and the need to act quickly; to this end, all four agree that ESG products would make a significant positive contribution to the environment. As the theme of sustainable investments is relatively recent, the legislation currently appears generic and at times incomplete. To avoid the risk of "greenwashing", i.e. disclosing misleading information on how certain investment products are sustainable, clearer, more precise and more efficient regulations would be needed which are capable of enabling greater creation and diffusion of ESG solutions. As clients invest, in most cases, primarily to achieve a positive return, these regulations should not be excessively stringent and overly damaging to the performance of ESG products.

Interviewed by:

Fabio De Pasquale
Head of SICAV Development
Investment Advisory BPS (SUISSE)

Davide Muscionico
Investment Advisory BPS (SUISSE)

* Cedric Bürgin, Private Banking Advisor, Basel

SUSTAINABILITY TIPS

Switzerland is committed to a more sustainable economy (source: swissinfo.ch)

As a country, Switzerland is not rich in raw materials; however, it does consume a great deal and produces a large amount of waste – between 80 and 90 million tons per year. The annual volume of waste per person is around 703 kg – the third highest figure in Europe after Denmark and Norway.

Reasons for this are high per-capita income and continuous population growth. Our planet pays a very high price for the standard of living enjoyed by rich countries.

The current economic cycle is magnifying the shortage of raw materials, the issue of waste and environmental pollution. This situation requires a change of pace, something Swiss politicians are well aware of: the Swiss government is encouraging implementation of the circular economy, especially in certain sectors where levels of raw material use and waste are high. Although Switzerland recycles half of its waste and is committed to improving the recovery of raw materials, there is still a long way to go, with more than 5 million tons of asphalt, concrete and other materials not recovered. Textile fibres and plastics could also be reused more.

Focus on Africa: A continent paying the price for climate change (source: Bloomberg ESG news)

The continent hit hardest by climate change is the one that has contributed least to the problem. The industrialised world, which has been emitting the lion's share of greenhouse gases, may now be starting to see the consequences, while extreme weather conditions wreak havoc on African nations. The number of African migrants arriving at the Mexico–United States border is set to hit a record high in 2022. Many cite droughts and floods as at least part of the reason why they decided to fly to South America and trek thousands of miles north. These refugees highlight the environmental problems that Africa faces, despite being responsible for only 4% of the world's carbon emissions.

In 2022, the heaviest rains in at least six decades killed 459 people around the South African city of Durban, and the Horn of Africa is suffering its worst drought in 40 years. Rising seas threaten West African cities and Indian Ocean island nations, while storms batter Mozambique and Madagascar. While the United States fortifies its borders and the United Kingdom pays Rwanda to accept the asylum seekers that arrive on its shores, the rich world continues to fall short of its pledges to help finance the climate change adaptation that Africa desperately needs.

Michelle Moro, CESGA
Asset Management, Manager BPS (SUISSE)

Roberto Mastromarchi,
Vice President Executive Board,
Head of the Front Office Division

General Management
Via Giacomo Luvini 2a, CH–6900 Lugano

Head Office
Via Maggio 1, CH–6900 Lugano

Direct Banking
Tel. +41 58 855 00 60

Call Center / Free Call
00800 800 767 76

contact@bps-suisse.ch / esg@bps-suisse.ch
www.bps-suisse.ch

BPS (SUISSE)

Your Bank, your values