

The forecast

# The rise of the environmental factor

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Francesco Castelli (Banor Capital): "When we talk about ESG criteria, the letter E (environment) will soon overtake G (governance), even in the bond market"

"Investors are becoming increasingly aware. They want to understand how environmentally sustainable a company is, considering who the bank lends money to. Is it a someone who pollutes the environment with coal-powered plants or someone who has wind turbines?" Francesco Castelli, European bond market manager at Banor Capital, an independent management company under British law founded by two Italians, explains the reasons which led them to embrace ESG criteria, the principles of responsible finance becoming increasingly widespread throughout the market. "The world of finance is not always home to the nicest of people," explains Castelli, "but everyone is coming to realise that investing in companies and governments that care about environmental, social and governance matters has an impact on portfolio performance".

While historical data suggests that investors in the bond market are more sensitive to the G aspect, namely a business' governance, according to Banor Capital, which manages assets of 8 billion euro, all that is rapidly changing. "The letter E, which stands for the environment, is gaining increasing importance, and we predict that it will soon become the dominant factor", Castelli notes. In fact, it will soon influence the entire system. "In 2024, I can confidently say that no bank will lend money to someone who wants to use it to build a coal-powered plant",

Castelli continues. "Credit institutions, in Italy and internationally, will lead the market to drive significant changes in this regard. We already have updated business plans from Italian and international banks, and all of them are applying ESG policies".

## THE SHIFT

In 2015, the governor of the Bank of England, Mark Carney, had already predicted that businesses with high CO<sub>2</sub> emissions could pose a problem for portfolios. "Their weaknesses are now exposed. and oil companies are valued as though they might disappear in a few years", states Castelli. The same is true in the USA. "Investors faced with a country known as a heavy polluter, like the United States, and one like Sweden, which has a different impact on the rising global temperature and is not considered a polluter, are more likely to choose the second option". Another example? "Volkswagen", offers Castelli, "which forgot the importance of the environmental aspect and, in doing so, made a very expensive mistake. Between September and October 2015, shares in Volkswagen fell by over 40 per cent". It is now trying to repair the damage. "It has revolutionised its platform and is one of the world's leading investors in electric technology".

It is wrong to talk about the environment as a whim. The market is unforgiving. "Non-life insurance firms are already seeing the negative impacts of climate change on their bottom lines", notes the expert. "Just think about the sudden spike in damage claims for fires in California. And

environmentalists say that this is only the beginning". Of course, analysing ESG criteria has its challenges. "Particularly when analysing governments", admits the analyst. "On the one hand, you need to focus on screening emerging economies. Then, you have to dedicate time to developed countries, where it is increasingly common to encounter problems such as how democracy is transforming with the internet. The re-emergence of populism has an effect on investors too".

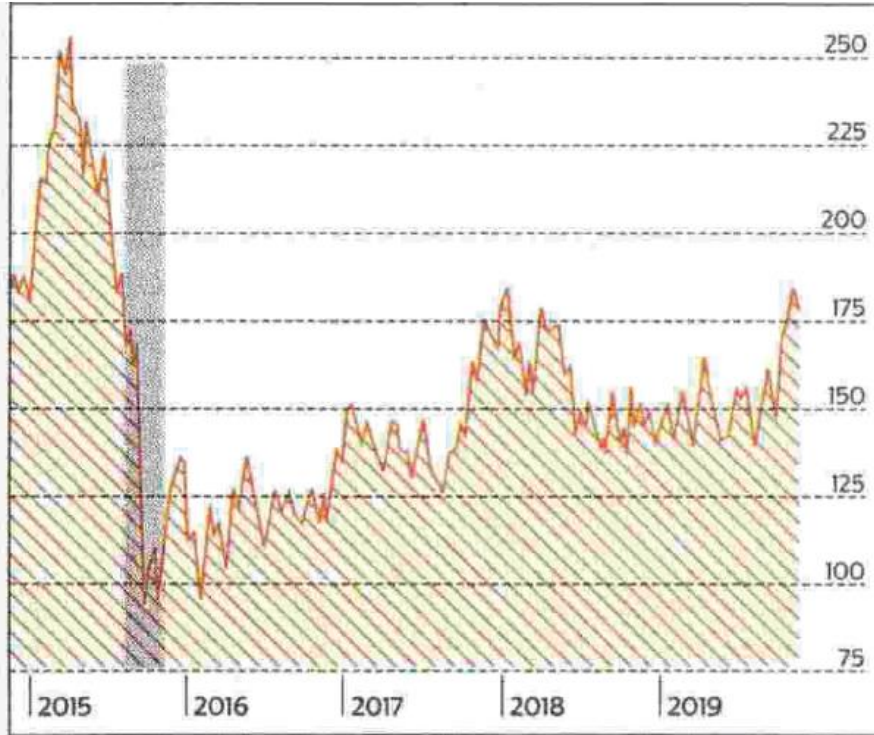
## BOND DIVERSITY

But why does governance traditionally have more bearing on the bond market than the environmental and social aspects? "The initial considerations are different", states Castelli. "Clearly, there are businesses which decide that environmental considerations are too costly and take shortcuts. Doing so might court environmental disaster but, as long as they aren't discovered, shareholders stand to gain". For bondholders it's different: "It's not the profit that interests them, but what the business generates with the invested funds", explains the analyst. This is another reason why the risk of non-compliance with environmental regulations has increasing weight. "Today, the market isn't asking you to give something back to the region", concludes Castelli, "but rather wants to know how much you're lending to high-carbon businesses. Investors are now asking for specific targets. This is an approach Banor Capital is pleased to pursue. ESG is more than a label".

**The numbers**

**VOLKSWAGEN ON THE STOCK MARKET**

THE NEGATIVE EFFECT OF THE COMPANY'S LESS "GREEN" MOMENTS



**Francesco Castelli**  
Banor Capital