

EARTHDAYpr
Jackie VanderBrug
Bank of America
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Joe Quinlan: Hello, this is Joe Quinlan, Head of Market Strategy in the Chief Investment Office. I'm joined today by Jackie VanderBrug, Head of Sustainable and Impact Investment Strategy for the Chief Investment Office, as well as Haim Israel, Head of Thematic Investing for BofA Global Research.

As a backdrop, we believe sustainability is a core strategic driver in our business because our clients demand it, because it's the right thing to do, and because it makes economic sense. With that as a segway, Jackie, how did we get here? Can you take us through kind of the historical backdrop?

Jackie VanderBrug: Yes, absolutely, Joe. Thanks so much. It's a really good year to reflect back, as 50 years ago, Earth Day gave voice to what was then an emerging environmental consciousness, was galvanized by the impact of a significant oil spill in California. Twenty million people engaged and that year saw the creation of the passage of the Clean Air and Water Acts, and of the EPA. Now, Earth Day is marked by over a billion people globally and last year four million people participated in global climate strikes in response to what they see as overwhelming evidence that climate change is no longer theoretical. In 2019 alone, we saw record-setting fires ravage California, Australia, and the Amazon; hundred-year floods destroyed crop yields in the Midwest; Category 5 hurricanes threaten the U.S. Southern and Eastern Coastlines; and record-setting heatwaves around the

world. NOAA estimates that every five years, climate events are costing the U.S. \$300 billion to \$500 billion and that doesn't account for economic loss in the affected areas.

We are seeing responses from individuals and governments and nonprofits but also from the corporate sector. Specifically in the past year, stakeholder capitalism emerged with a definitive claim that it is in the long-term interest of companies to be accountable to all of their stakeholders – that's their shareholders, their employees, their customers, and the communities in which they operate.

Joe Quinlan:

So, Haim, let's pick up from there. I want to ground us in the moment we are in, so can you talk about the shift in mentality you've seen in investors and companies over the last two years regarding climate crisis, climate change, and what have they done, really, so that they demonstrated the severity of the situation?

Haim Israel:

Sure, Joe, thank you very much. And yes, there has been a big shift in clients' interest, focus about, and engagement in climate change and all those, and sustainability issues.

First of all, the numbers are clear. We are actually surveying our clients and see how they look at all of our themes, including climate change, and I can tell you that in our survey that we've done on our Transforming World Conference back in November, this was the number one issue according to our clients. While a year before that, it was actually number four or five. So there has been a big shift in focus around climate change. That's one thing.

Second thing, I see that clients starting to understand that it is coming with an economic cost, and the economic cost is here and now. And it's not just that we have a problem globally and one day our sons or our grandkids are going to have to deal with it. This is something, this is happening here and now, and starting to impact companies.

The third point which we are seeing from clients is that the shift of asset which are starting to focus on all those themes. The ESG asset (ESG being environmental, social, and governance assets), we estimated in our research \$20 trillion worth of assets which will follow ESG by 2025. Just to give a number behind that, \$20 trillion is give or take four times the S&P 500. That number keeps increasing all the time.

Joe Quinlan:

Very good, Haim. Thank you. And I want to just say from Bank of America's perspective, the bank has been focused on sustainability and our relationship with the planet for a long time now, and our commitment to sustainability is broad and deep and includes our environmental business initiative which we committed \$445 billion to lower carbon-sustainable business activities since it was initiated in 2007. In 2019, Bank of America was ranked eighth on the Fortune's 'Change the World' list which looks at companies that are using creative tools of businesses to help the planet and tackles society's unmet need. And then in January of this year, we achieved our goal of carbon neutrality ahead of schedule, which is very impressive.

So, Jackie, we've seen the most persistent volatility in our lifetimes in the past 45 days. So in a time when market swings have become common,

sustainable investing or interest in the environmental, social, and governance data really has become important, so take us through some of the numbers and some of the things you're seeing.

Jackie VanderBrug: Yes, it's interesting, Joe, because I feel like you could have this aspect where it seems like, with everyone glued to the market volatility and the COVID cases, sustainability would take a backseat. But, in fact, that is wrong. We're seeing this considerable data demonstrating that the crisis is an accelerant; that this moment, as Haim has said, is catalyzing the movement to integrating ESG into investment decisions. One way we think about it is it really does shift sustainable investing and the integration of ESG data from a nice-to-have to a need-to-have or a must-have.

Joe Quinlan: Well, Jackie, then how is – moderate sustainable investing markets have only existed in this bull market, right? Where are we now with the cycle, with the bear market? Some economic numbers globally in the United States and Europe, they're just unprecedented in terms of their ugliness, so where are we when it comes to sustainable investments?

Jackie VanderBrug: Yes, we have only a limited time span, to be clear, in terms of the current bear market. But, in our view, this extreme volatility, the market contraction has provided early evidence of what the hypothesis around sustainable investments was: that funds which are incorporating ESG data will demonstrate more risk mitigation than their peers.

Savita Subramanian with the BofA Global Research Team has written about this in a recent report 'Bull Market Phenomenon? Quite the

Contrary.’ They found that from the S&P’s peak to March 25, stocks in the top quintile ESG ranks outperform the market by five percentage points and this was not due, as some might have thought, to just an underweight in energy or small-cap exposure. The outperformance was there three to four percentage points even controlling for sector and size. This was also the case in the market selloff in 2018.

So the bottom line is that we see sustainable funds appears to have benefited from owning companies with stronger ESG profiles; those that are outperforming on environmental measures that have strong employee benefits, and relations, and impeccable governance. And sometimes, these are the features of what we might think of as future quality that may help companies weather dramatic changes and challenges in market like we’ve seen but also over the long-term. And it is that long-term performance that has always been and continues to be the motivating factor in sustainable investing.

Joe Quinlan: Very good. Thank you, Jackie. And then Haim, so from your point of view, what are you seeing in the midst of all this volatility and in headlines that we’re getting day-in and day-out?

Haim Israel: Sure. So the volatility right now, what we’re seeing is that there’s definitely an increase in interest in thematic investing and that included across the board in all of our themes which are including, of course, climate change and all the related topics.

Investors are starting to focus about what could be the black swan going forward and how that can impact investment in the near future. And

they're also starting to dig into the whole sustainability/climate change issue and start [to be] much more gradual work around that.

When we are talking about that, I think investors are starting to understand that this has a lot of different aspects, a lot of different layers that you need to start thinking about. If historically we just talked about climate change, now the world is getting hotter, there's a lot of mistakes on the back of that. If it's water that we're drinking, the quality of the waste that's been generated and, of course, the mission, no, there's also a lot of other things which we need to consider and that's what really investors are starting to focus right now.

We have published that the environmental issues, climate change has a big social impact and actually, when we talk about ESG, environmental, social and governance, we're seeing that the social side of things is really taking over the environmental side of things. The World Bank has put a projection that 140 million people will be climate change immigrants in the next five years. One hundred million people will go below poverty line. There's a lot of regulation which has to be involved in that and investors need to stop focusing around that as well.

One of the more interesting developments that we have seen is starting to understand how different generations are looking at climate change and how that pan out to investment opportunities around that. Gen Z, the new generation which is taking over, people that were born after the year 2000 are very much focused into sustainability. We have seen incredible numbers that millennials and Gen Z, the investment strategy, close to 90% is focused around the ESG factors and environmental issues so we're

definitely seeing the mindset in this volatility changing when people are starting to understand that the short term could be very much impacted by the long term, what we call it in our research is that actually the long term is the new short term.

Joe Quinlan: That's great, Haim, and I want to follow that up, Jackie, because as Haim laid out, I mean this is a big investment opportunity, front and center for a lot of – it doesn't matter what cohort institutional investor. So, given that we saw a lot of flows – new flows come in fourth quarter of 2019, has there been any change that you've seen, Jackie, that you can tell us about in the first quarter given the backdrop? Any change in the market environment? Are we going to continue to see the inflows? Will they abate? What do you think?

Jackie VanderBrug: Yes. You're actually right. In fourth quarter 2019 just flows into sustainable funds were over \$21 billion. That was a nearly fourfold increase over the previous calendar year, 2018, which was also a record year. Early indications are that this is holding up. The BofA Global Research team also found that the ESG ETFs, AUM was up 5% to date while the S&P 500 ETFs had seen corresponding AUM decline by over 30%. This kind of distinction and the beginnings of the flows that Haim mentioned at the beginning of the call that we anticipate over coming years is completely consistent with what we are hearing in terms of interest from clients as well as continued strategy innovation from asset managers. So, I just think that this trend should continue and potentially accelerate.

Joe Quinlan: Very good. Well, then, Jackie, let's bring in the elephant in the room and tie this together with everything you and Haim just laid out. From your perspective, give us the connection between climate change, ESG and then COVID-19. Where does this all fit in when we talk about the crisis at hand?

Jackie VanderBrug: Yes. At the most immediate level, the COVID crisis is showing the vulnerabilities of our economy and our healthcare system to large systemic emergencies, the type of black swan events that Haim is talking about that may arise from climate disasters showing us just how interconnected our supply chain and our economies really are. There are lots of connections – places where factors that drive health risk also drive climate risk. Harvard University's Center for Climate, Health and the Global Environment points out two that I would highlight, one being air pollution largely result of fossil fuel emitting sources but also is a key factor that worsens virus's impact on human health. The second being deforestation clearly linked to increased carbon dioxide emissions but also something that as it destroys wildlife habitat increases the risk of close human-animal encounters and the spread of disease. On the one hand, we can talk about this interconnection and the way in which, as Haim said, that the environmental factors are driving social factors. Social factors may mitigate or be exacerbated by environmental factors.

I think it's also important to take a look at the lessons that we're starting to see from the COVID crisis that we could apply to our thoughts in terms of the climate crisis. Here, I would point to four different things. The first is, as we talked about already, connection, how interconnected we are between our economy, healthcare, education, financial, political systems.

We have really a stark lesson that we are living through that creating economy based on our collective well-being is absolutely critical. The second is science. So, this COVID crisis like climate change was difficult for many to imagine. It hadn't happened in our lifetimes. It was easier to view it as something that was happening in a distant country and might stay there and yet, it wasn't unanticipated by many in the scientific community, Joe. We found that scientific data is an essential guide for us in navigating these crisis choices that we have and it should be for climate as well. Third lesson we have is around data, ESG data being more relevant to understand companies in a time of crisis whether that be COVID or climate. Then finally, I can't help but just say hope because the lesson from this crisis like others before it is that we can and will bond together as a global community to coordinate responses. I see our progress towards behavioral change in the face of this massive threat as a hopeful indicator of the kinds of activities which can be harnessed regarding the transition that we have in front of us to a lower carbon economy.

Joe Quinlan:

Well, Jackie, I hope you're right on that and I do agree with you. There's a lot to be optimistic about in terms of the crisis and how we handle it on the other side. Haim, every crisis has these unintended consequences and it's quite remarkable that we've seen global emissions decline. We've seen wildlife come back to urban areas and it's like the planet is getting a break, so to speak, from all the activities that we pump out day in and day out. Thinking about the relationship between the climate needs and the COVID crisis, what do you think? Where do you think we're going that's important to investors to look at?

Haim Israel:

Sure. I think that's quite important because I said for the short term, right now, there's less traffic, there's less industry, there's less pollution, there's less emission, less cars on the street and everything that might help climate change going forward. We need to think largely more long term here and there's a lot of questions we should be raising over here whether a world which is facing an economic crisis because of that whether governments which are right now expending trillions and trillions of dollars to fight COVID and the economic impact on the back of it, whether they're going to be able to promote climate-change-related regulations going forward, whether the plummet in oil prices eventually is going to change the balance between renewable energy and fossil fuel cost of production. We've been claiming in the past couple of times in our research pieces that today, it is cheaper to produce energy from renewable sources like wind or solar versus fossil fuel. However, we've seen a decline – a massive decline on fossil in the last couple of weeks so that's going to still remain a very big question.

There's one link which I think we need to ask ourselves in the future which we are still not asking ourselves enough. When you're talking about the connection between COVID and climate change, there's one missing link with how we tie that all together and that's the food, the food that we are eating. That's quite important that food process is one of the most important ESG factors over there. Probably, one of the things that we did not think about that 75% of all infectious diseases in the past decades were what we call zoonotic diseases meaning diseases which are transmitted between people and animal. We're not sure, of course, how COVID came, what is the source yet? There's no clear evidence but no disinformation about 75% of the influenza disease coming from animals, it's quite clear.

The second thing about food and health and how we tie that is also that today, agriculture emits more greenhouse gas than cars, trucks, airplanes and trains together.

Actually, just the dairy industry is in charge of 4% of global emission worldwide, so when we're talking about COVID and right now the short-term decline that we are seeing in emission today, we need to think long term. Are we going to eat in the same way? Are we going to produce food in the same way? Are we going to drive in the same way? How will our interactions going to be? Seventy-five percent of all emission is coming from urbanization from big cities. Is that going to be the case going forward? We are seeing social distancing. We are seeing a lot of trends right now because of COVID that we need to ask ourselves in the future whether those things will continue.

Joe Quinlan: Very true. A little commercial for Haim's team, could you tell us – you just put out a great food report. What's the name of the report again because it's fantastic?

Haim Israel: The report is...

Joe Quinlan: I remember [Crosstalk] that.

Haim Israel: Yes, the name of the report is "We Have to Stop Eating or Meeting like This." [Laughter]

Joe Quinlan: Very good, I like that. Jackie, bring this home for us. How does the planet impact the portfolio, and how does the portfolio impact the planet?

Jackie VanderBrug: Yes, take all of the themes that Haim has put out there, these questions about food, about renewables, about transportation, and we see clients looking to have that integrated into their portfolios to both understand where they can mitigate risk as there are significant disruptions in different sectors as well as where they can participate in huge opportunities where we're looking globally to solve challenges that we have. In addition, they're looking to make an impact, to contribute positively to the planet through their portfolio choices. They take different approaches to this, but we put them, Joe, in three categories. We talk about these as the ABCs, the ways in which clients are, in their portfolios, avoiding, so they're seeking to reduce negative environmental effects and manage risks. Maybe they're avoiding more carbon-intense industries or divesting or just overweighting companies that are less dependent on carbon-based fuel. The B is for benefitting. They're seeking to advance or support those companies that are ahead of others from environmental practices. They're looking to find companies that are using sustainability, that create competitive advantages, whether that might be, say, in a water supply chain or in an agriculture supply chain as Haim has mentioned. They're seeking to contribute, so they're looking for those companies that are innovating with new products and new services potentially in the renewable space but also companies that just are addressing issues in terms of resource use efficiency, water, waste, energy. That's A, B, and C. Clients may have a preference either avoiding, benefitting, contributing. Most clients do all three.

Joe Quinlan: Very good. Haim, what Jackie just talked about, in terms of portfolio, obviously requires good data, data we can trust, we can hang our hat on. I

know you've written a lot about this, so can you just tell us, what's the current state of green disclosure or transparency? Where are we? What do you see that impacts? Any regional differences you see when it comes to climate disclosure?

Haim Israel:

Yes, we're seeing big revolution in that, and thanks for raising that. That's actually one of the biggest revolutions we're going to continue to see in the capital market going forward. The new word that we want to talk about is TCFD, task force for climate change accounting standards, and that is still voluntary reporting how climate change is impacting my business including stress test, including very detailed information that companies have to disclose. Companies understand, big public companies, that if they will not give this information out, they will miss something from the market, so we are seeing that as being more and more standardized going forward and being more deepening going forward. That's one side of it, of course, the side of the buy side looking and the companies applying.

The second thing is that companies, once they're implementing ESG standards and reporting, it gives them a much stronger tool of preparing, of future planning, of how to address all those issues. Jackie, as you have

mentioned earlier in the conversation, [we just] strongly support those companies with the high ESG scoring, are outperforming, have better [EPF], have premiums in multiples and so on. It all comes down to ESG really impacting my operation. Once we are going to see this reporting, it gives a powerful tool to management teams to stop referring, so that is something I would highly recommend to focus on going forward.

Joe Quinlan: Do you think the COVID crisis will cause some backtracking or not? They won't meet their goals by the end of this year or this is structural? This is going to happen?

Haim Israel: I think this is going to happen. This is a question where I said this still is not a regulated issue right now. It's more voluntary at best, but we are seeing it develop, and I think actually this current crisis will definitely focus what countries are doing in order to meet the social aspects, the environmental aspect, of course, definitely about regulation and all these things. We need to remember this is not just a health crisis, also a social one, so companies are going to be under the spotlight, and I think so. I think that no one really has an interest to postpone disclosure.

Joe Quinlan: Very good. Wrap up in the interest of time, I'll start with you, Jackie, and then, Haim, I'll ask you the same question. In times of global uncertainty, market volatility, the climate emergency is still in front of us, COVID crisis as well. Jackie, I'll start with you. What two things would you recommend to clients that they keep in mind amidst all of this volatility and uncertainty right now?

Jackie VanderBrug: Yes, the volatility and the uncertainty can clearly be confusing. What I would say is what we are seeing is that the use of ESG data through the ups and downs has emerged as an imperative. As Haim's saying, companies are committed. Timelines may shift, but they are seeing this as part of their long-term plan, and this moment is actually accelerate. We're moved past the point where sustainability is a luxury to it being an imperative. And then the second piece I would say, Joe, is that the issues at the forefront of minds of investors may and will continue to shift. It may be climate. It may be equal pay. Supply chain redundancy is something we're talking about a lot. Healthcare capacity, food security as Haim said, all of these things come in and out. Materiality is dynamic, but from a long-term perspective, those strategies that are fully integrating environmental, social, and governance data into their investment process for the long term, they're better able to assess these different material aspects that are emerging in a much faster pace than what we've seen in the past.

Joe Quinlan: Very good. Haim, what are two things that you would recommend clients keep as top of mind given where we are today?

Haim Israel: I so agree with Jackie on everything she said, and I want to go back to what I said in the beginning of my conversation. Clients need to understand that the long term is the new short term, and if you're going to focus only on the short term, you will miss something. Those environmental issues have been with us for a very long time. We actually call the 2010s "The Lost Decade" because nothing has been done and everything was pushed for us to do right now, and as a result, all those themes are not long term anymore. They are really short term. One of the

outcomes coming from this crisis, the COVID crisis we're seeing right now, is a lot of our themes are long term, five-year themes are materializing way faster than expected. Joe, as you said, it's with big data and AI. If it's the future human, future healthcare, it's definitely climate change, sustainability, and so on, so we need to focus on that. I'll give you one stat to really highlight all of that, we published that in our 2020s note back in November. If you would look at the US market, the last 90 years of the US market and add on a disclosure that was before the current crisis, you will notice something fascinating. Twenty-seven thousand companies were trading in the United States in the last 90 years. Ninety-six percent of these companies generated zero excess return, meaning the total return was T-bills, zero excess return. Four percent generated 100% of the net worth return on the market, 4%. Ninety-six percent were zero. Four percent were 100%, meaning if you want to be in those 4% – and that's what we all want, right? We all want to generate returns here. You will have to start thinking about the long term. Those companies always were the leaders, were the disrupters, were the companies that were seeing the long term. They are not just companies, and I have to say that upfront it's in each and every different industry. I think that's a very important lesson for investors.

Joe Quinlan:

Haim, that is very powerful. They are very powerful numbers. To wrap up, I want to go back to what I said at the outset. Sustainability is a core strategic driver in our business because our clients demand it, because it's the right thing to do, and because it makes economic sense. Jackie and Haim, thank you for taking the leadership role with bank and with the industry, and you're going to be hearing a lot more from these folks in the weeks, months, years ahead. Thank you, everyone.

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