Asset Management

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E-commerce is driving up demand for logistics and warehousing facilities.

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Their strengths and the reasons for their outperformance.

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A sense of proportion more important than ever

Michel Degen

Head of Asset Management
Switzerland & EMEA

The glut of news about COVID-19 caught market participants off guard and led them to make short-term decisions. Such reactions are understandable since a crisis affects all areas of our existence, as futurologist Matthias Horx aptly writes.

Alexandre Bouchardy, Head of Asset Management Investment Strategy Switzerland & EMEA, advises ignoring forecasts and instead looking to a medium to long-term investment horizon. Furthermore, investing with discipline, sticking to a plan, plays an extremely important role.

At the same time, investors are well advised to be open to new developments and spot the opportunities. In this edition of Scope we take a look at various trends that could be accentuated in the next few years and, as a result, present attractive investment opportunities. Without doubt that includes investment solutions that take account of ESG criteria and are guided by the Principles for Responsible Investment (PRI). In addition, we believe that logistics real estate offers good prospects for benefiting from growth in e-commerce. Finally, it might be worthwhile taking a look at emerging market bonds, which have experienced a real renaissance of late.

Our article about family firms underlines the fact that they regularly achieve better results than other companies. The historically strong performance of listed family companies also makes them attractive to outside shareholders.

I wish you a stimulating read.

Michel Degen

COVID-19 has significantly changed the short-term priorities of investors. The dramatic stock market movements of 2020 reflect the nervousness of many market participants, as well as a certain degree of helplessness on their part. Irrespective of the pandemic, however, the spectrum of investment opportunities has actually widened further. This makes selection criteria even more important.

A world full of opportunity

The Scope interview with Alexandre Bouchardy, Head of Asset Management Investment Strategy Switzerland & EMEA

The pandemic has not sparked new trends, but has accelerated trends that were already in place. This makes taking a long-term view more important now than ever.

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ESG investing

Investing in a way that meets environmental, social, and governance criteria is no longer a niche discipline. It represents a constructive solution to the problems faced by our planet, while at the same time offering a better risk/return profile than traditional strategies.

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Emerging market bonds

Important emerging markets have freed themselves from their debt burdens and undergone reforms; something that has triggered a renaissance in emerging market debt. Emerging market bonds can once again enliven a portfolio or stand on their own as a source of return.

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Credit Suisse is putting all its weight behind the development of ESG investments.

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The opportunities for investing with a robust ESG approach are on the rise.

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“Staying level-headed beats hectic day trading”

Interview with Alexandre Bouchardy

Head of Asset Management Investment Strategy
Switzerland & EMEA

Alexandre Bouchardy

Alexandre Bouchardy has been Head of Asset Management Investment Strategy Switzerland and EMEA since May 2020. Prior to that, he was in charge of Asset Management Fixed Income Asia and Equity Asia, as well as Asset Management Singapore. From 2005 to 2012, he was responsible for infla tion linked solutions. Before joining Credit Suisse, Alexandre Bouchardy worked for Banque Pictet & Cie and J.P. Morgan in Geneva and Paris. He holds a Master’s degree in Economics from the Faculty of Business and Economics (HEC) at the University of Lausanne.

Frequently noisy day-to-day newsflow gives investors countless reasons to keep shifting their portfolios. In the long run, though, it doesn't pay off to invest in this way. Investors can achieve greater potential returns by focusing on long-term trends and prudent judgments.

Mr. Bouchardy, you advise investors to back long-term trends. What exactly does this mean?
Alexandre Bouchardy: We don't issue forecasts and are guided by our finding that adopting a level-headed approach beats hectic day trading. We keep a general eye on performance to date and the reasons behind these trends. We then assess how likely it is that this performance will be maintained. Although risk premiums fluctuate in the short term, they're fairly stable over the longer run. A medium- to long-term investment horizon enables higher risk-adjusted returns to be achieved. The low or even negative interest rates in Europe provide a concrete example of this. We believe we'll still be experiencing a low interest rate environment in three to five years' time.

It makes sense to consider ESG criteria as part of the investment process because …
"… these criteria widen the risk assessment process and boost the long-term quality of investment decisions."

Why do you expect interest rates to remain low in Europe even on a medium-term horizon?
There are several reasons for this. One key factor relates to the structural differences in competitiveness between the northern and southern member states of the European Union. To understand this we have to rewind a few decades. Before the introduction of the euro in 1999, excessively wide variations were avoided via the valuations of the national currencies, as reflected in exchange rate movements. To take one example, Italy stayed internationally competitive by steadily devaluing the lira in the decades prior to the euro's launch, while the German mark was one of the hardest currencies in the world at times. This mechanism has stopped working since the launch of the euro as a single currency. A process of alignment that brings southern European countries whose economic growth is generally "below potential," such as Italy or Spain, under the umbrella of a single currency together with nations whose growth is "above potential," such as Germany or the Netherlands, can only be achieved via relative inflation.

So this means the European Central Bank has to keep interest rates low even in Germany, even though this is unnecessary for the country's domestic economy.
Yes, that's correct. The result is that the German economy posts growth rates that are above potential. This in turn leads to asset inflation.

In recent years the differences in economic growth between northern and southern Europe have repeatedly sparked calls to split the single currency area into northern and southern euro zones. Is there any chance this could still happen?
No, the announcement by the EU in June 2020 of its intention to embark on a cautious path toward a fiscal union probably means that a division of the euro area is now conclusively off the table.

How do the major phases of interest rate cuts over the past two decades differ?
Interest rates were lowered on a massive scale between 2001 and 2003 in order to stimulate what were structurally low growth rates and persistently low rates of inflation. At the time this did not entail the expansion of central bank balance sheets. Rates were also cut in 2008 and 2009, but this time the central banks' balance sheets ballooned. The interventions conducted at present are on an even bigger scale. They entail low or negative interest rates, even greater expansion of central banks' balance sheets, direct purchases of government bonds, and, in some cases, direct lending to businesses. In monetary terms, there is undoubtedly greater tolerance of inflation today.

What do you advise those who only want to invest their money for the short to medium term?
In the short term they have no choice but to use cash. If they have a certain amount of risk appetite and can accept some price volatility, they can put some of their wealth into equities and gold. This at least gives them a chance to preserve the value of their assets even though a portion may be subject to negative interest rates.

The advantage of long-term investment trends is that …
"… they don't create any market noise and therefore lead to better decisions."

Should external shocks such as coronavirus-related lockdowns prompt investors to significantly reallocate their portfolios and back different trends?
No, this is unlikely to prove a smart move in the long run. In fact, the pandemic has not sparked any new trends at all. Instead, it has accelerated certain trends that were already in place. Working from home is a good example in this regard. This option was already available before the pandemic hit, but only for a limited group of people with specific working arrangements.

The least useful piece of stock exchange wisdom that I hear again and again is …
"… sell in May and go away."

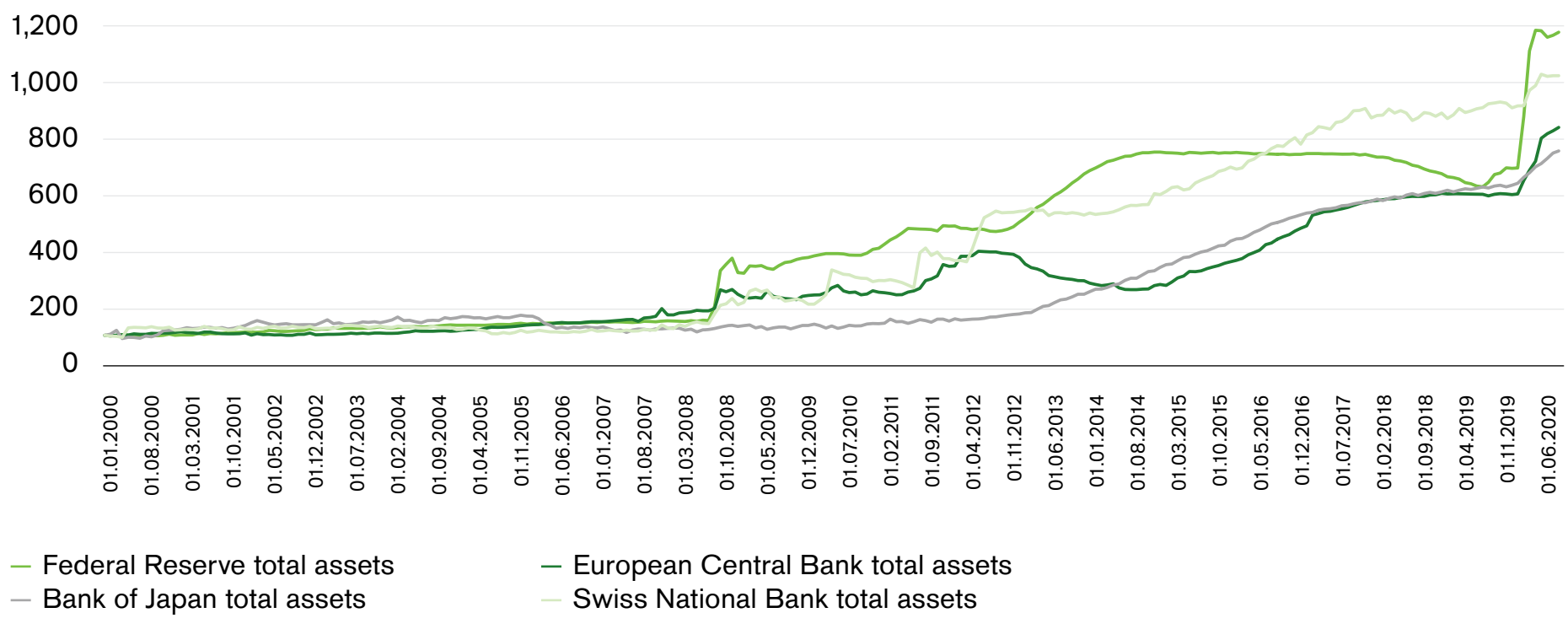
The outbreak of the pandemic and the subsequent lockdown meant that most employees' homes suddenly became their workplaces almost overnight.

On account of the energy transition and the promotion of renewable energies, the oil price too was already under pressure before the coronavirus emerged. Covid-19 has simply accelerated the fall in oil prices, though admittedly this drop has been very sharp at times.

As far as shopping online is concerned, the coronavirus shock prompted a huge surge in internet retail across the world. Having said that, this strong growth began years before the pandemic, enabling providers such as Amazon or Zalando to grow their revenues at above-average rates. Even if some of these online sales return to bricks-and-mortar stores, the digitalization trend in retail will continue unabated.

Central banks' balance sheets (indexed)

The various waves of interest rate cuts implemented by central banks since 2008/2009 have gone hand in hand with expanding balance sheets. The curves have seen an especially sharp rise since spring 2020. Index 100: January 1, 2000



Sources: Credit Suisse, Bloomberg

I make the best investment decisions for myself when …
"… I've found the perfect blend of intuition and analysis."

Can we extrapolate these trends?
No, this would be risky as in two or three years' time we expect conditions in many areas to have returned to nearly the way they were before the pandemic. People will be going to the opera, the cinema, soccer stadiums, festivals, and parties once again. They'll want to travel, hold celebrations, and have fun in large and small groups. There'll also be a return to business meetings and events, which will take the place of some of the virtual formats that people are currently using to interact.

What are the chances of a return to normal?
The biggest opportunity would be a pro-cyclical economic recovery. Despite all the imponderables stemming from Joe Biden being elected president of the US and the growth in the number of virus cases, we on the Investment Committee are generally positive that we'll see a trend characterized by the gradual normalization of the global economy based on nation states doing their utmost to avoid any more hard lockdowns.

The stimulus unleashed by fiscal, monetary, exchange rate, and lending policy should provide a sustained boost to large parts of the economy and trigger attractive upside potential for equities. By the way, if inflation does actually materialize, the value of equities has consistently proven to be more stable than that of other asset classes such as bonds. Selected real estate investments should also benefit from inflation. And the economic rebound could of course pick up speed and strength if new treatment methods for those suffering from Covid-19 and new and effective vaccines become available.

What do the following terms call to mind?

[Discipline] "The key to achieving a good performance over the long run." **[Recession]** "A necessary evil on a temporary basis to trim excess capacity in an economy and enable long-term prosperity." **[Emotions]** "They're essential to our survival but can also be dangerous." **[Deglobalization]** "This has the potential to become a trend over the next decade."

ESG – Investment for a brighter future

Climate change and pollution, people working and living under repressive conditions, with mismanagement and corruption adding fuel to the fire. These are the challenges that impede human development and progress. Investors and asset managers are done with being idle bystanders or even inadvertently making things worse.

ESG (environmental, social, and governance) investing is done playing a niche role. Promising a constructive approach to the problems besetting the planet while at the same time offering better risk/return characteristics than traditional strategies, ESG is a new paradigm in asset management. As such, it should be seen less as a trend than as a path to the new normal. Already widely adopted by many institutional investors, it is currently continuing its expansion into the portfolios of private and additional institutional investors. In fact, portfolio managers and investors are actively pushing to introduce ESG into more and more segments and markets – recognizing both their own responsibilities vis-à-vis the greater good, and hoping to reap the benefits of the approach on a broader front. In this environment, Credit Suisse Asset Management has formulated ambitious goals of not only managing practically all investment funds according to strict ESG criteria, but also of nudging peers and investee companies onto more sustainable paths.

A way forward with strong drivers
The two aspects of ESG investing – collective responsibility and enhanced risk/return – are not totally independent. A society that values sustainability will tend to reward companies that act accordingly. Such companies will be able to avoid the reputational risks that come with being a polluter or treating various stakeholders poorly. But the effects go deeper, and companies with more diverse, better treated workforces, or rigorous environmental policies – both of which would enhance an ESG score – will also have sounder business models, more sustainable earnings, and be better suited for the challenges of the future. In this way, a high ESG rating becomes a factor for any portfolio manager in determining the potential of an investment.

This foundation, consisting of the determination to preserve a livable planet for future generations while engaging in a prudent and profitable investment strategy, has transformed sustainable investing into a generational and paradigm-shifting phenomenon. In many ways, it remains in its early stages, marked by a kind of pioneering atmosphere that is heady and dynamic on the one hand, yet can be confusing and overwhelming on the other. An example of the latter is a dearth of standards and labels that would enhance transparency and make decisions easier for all participants, individual investors as well as companies. Many regulators have not yet defined what they consider to be a sustainable or ESG-conforming investment, let alone that such definitions would be aggregated up to a regional or even global level. But some standards, or at least guidelines, exist. Most prominent among these are the Principles for Responsible Investment (PRI), formulated by the United Nations in 2005.

Steps in the right direction
Generally, it is important to have a clearly defined framework for proxy voting and engagement principles and activities to act in the best interest of clients. In addition, we also exercise our voting rights at globally active, large multinational companies. Looking to 2021, we will be further extending our coverage to Asia-Pacific as well as North America. As of today, for Swiss companies we have a coverage ratio of almost 100% for SMI shares and roughly 50% for SPI shares.

In terms of engagement we have also ramped up our activities:

- **Thematic engagement:** Conducting dialogue with companies about the current priorities of our ESG initiative – food loss and waste on the social side, as well as climate change measures and risk considerations within listed real estate companies are two examples.
- **Individual engagement:** Pertaining to company-specific issues.
- **Engagement in relation to proxy voting:** Proxy voting is not an isolated action. It is accompanied by a dedicated engagement plan.
- **Public policy engagement:** Participation in industry-wide efforts to influence our peers or the regulatory framework.

We work together with companies to set clearly defined KPIs for quantitative goals that are tracked and monitored over time. For qualitative issues, we use our proprietary questionnaire to evaluate the progress a company is making. All engagement activities are normally undertaken via one-on-one meetings or conference calls in which we mostly meet with the chairperson and/or BoD members, or in some cases with investor relations.

As an asset manager, it is desirable to join collaborative engagement initiatives such as Climate Action 100+, which is devoted to net-zero emissions in investing and represents USD 47 tn in assets. Membership in this and similar initiatives represents an opportunity to leverage and enhance influence. Readers are encouraged to find out more about this important initiative on the website. It is always fashionable, to a certain degree, to decry the influence of money in society. This is an example of making it a force for good.

The “Principles for Responsible Investment”

In the last 15 years, over 3,000 professional asset managers, including Credit Suisse, representing over USD 100 tn in assets have committed themselves to the PRI. In other words, the PRI have become the closest thing to a global standard for sustainable investing in existence, **and this makes them worth quoting in full:**

While they are mostly self-explanatory, some important aspects are worth pointing out. The principles acknowledge that making the financial world is a work in progress, and that cooperation, active engagement, and transparency are essential to success. The principles are also expressed at a very high level, leaving much of the concrete implementation to individual investors.

Principle 1

We will incorporate ESG issues into investment analysis and decision-making processes.

Principle 2

We will be active owners and incorporate ESG issues into our ownership policies and practices.

Principle 3

We will seek appropriate disclosure on ESG issues by the entities in which we invest.

Principle 4

We will promote acceptance and implementation of the Principles within the investment industry.

Principle 5

We will work together to enhance our effectiveness in implementing the Principles.

Principle 6

We will each report on our activities and progress towards implementing the Principles.

Sustainable portfolios

In the end, and most importantly, the increasing inclusion of ESG in decision-making processes affects the portfolios of funds and mandates. This effect varies by asset class, sector, and region. In some segments, data quality is a big issue, and understanding actual sustainability risks and opportunities in combination with traditional financial analysis is the right way to go. Therefore, it is important to work with specialized data providers while retaining the ability to cross-check and test the plausibility of both data and results. In line with with a consistent and comprehensive ESG framework in which some segments are entirely excluded from sustainable portfolios. On the active ownership side, companies are influenced to take a more sustainable direction and transparency is writ large, e.g. via dedicated ESG reporting.

The most profound effect has been seen in the emerging market space. These markets have lower levels of transparency and are institutionally less stable than their more developed counterparts. Under these conditions, the inclusion of ESG criteria in investment decisions is an invaluable tool to determine the quality of a company's leadership, its risk structure, and the solidity of its business model. While the phenomenon of ESG improving the quality of a portfolio is significant almost across the board, it is most visible in the emerging markets, which can be seen in the performance of sustainable emerging market equity indices compared to their traditional parent indices.

At this point, the question is no longer: Can I afford to invest sustainably? It is: Can I afford not to? And the answer is no. Both because of the environmental, social, and governance problems facing global society, and because investors want a solid return on investment.

Sustainable China

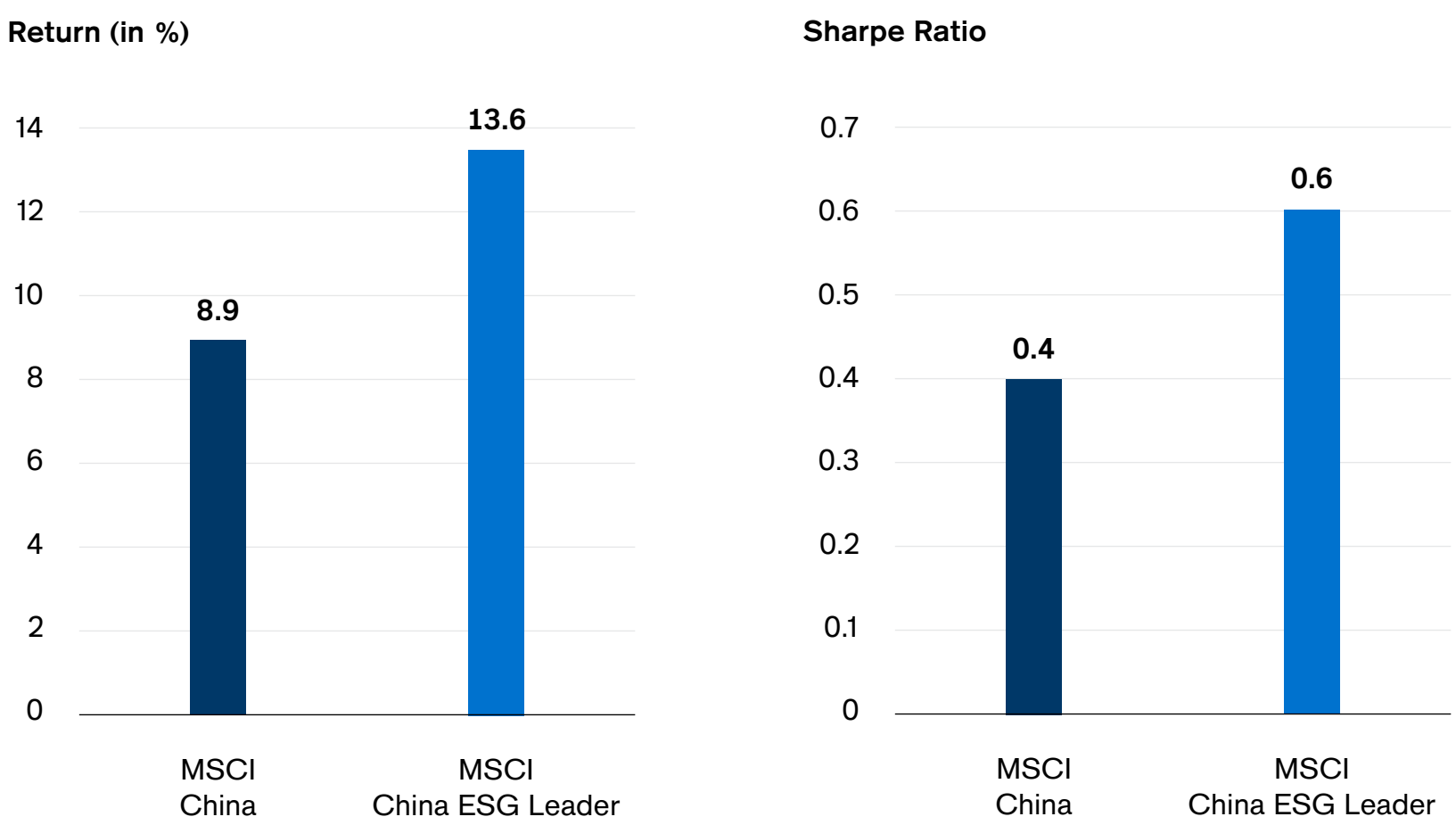
Over the past decades, China has followed a path of growth and development unparalleled in human history – lifting untold millions out of poverty and creating a dynamic modern economy. And the country has set its sights on an even more ambitious future. Issues such as environmental stewardship, transparency, and labor rights have not always been a high priority.

Expanding their lead

China is the leading manufacturer of solar energy panels worldwide and taps into environmental challenges to accelerate technological change.

ESG is a key component of many investment approaches. At the same time, one of the biggest stories in investing is the rise of China. At first glance, this puts many modern investors between a rock and a hard place. But things are on the move, and today, Credit Suisse Asset Management sees an opportunity to invest in China applying a robust ESG approach, thereby reaping the benefits of enhanced alpha and risk-adjusted returns – *see chart below.*

Better risk/return characteristics of China ESG indices compared to standard indices



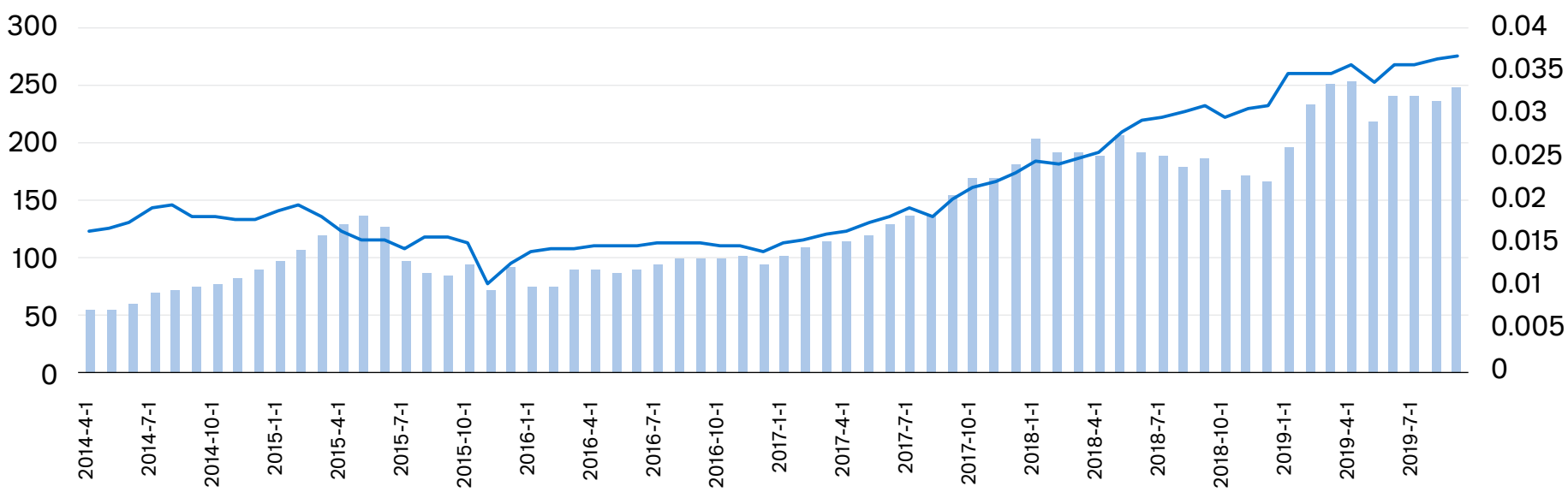
Sources: ESG and alpha in China, PRI, 2020
Note: Summary statistics, China strategies based on MSCI. Data from June 28, 2013 to June 28, 2019. All risk and return figures are annualized, based on gross daily index total returns in USD.

Many individual Chinese companies have recognized the opportunity sustainable investing represents. They are interested in expanding their investor base internationally, and displaying the requisite progress and transparency on ESG matters is key to success. And products in the ESG space have enjoyed robust global demand, and these companies have responded. As a result, China is now the leading manufacturer of solar energy panels, electric cars, and other technologies that are crucial in bringing the world economy to live within its means.

On a collective level, there has also been support for such efforts. In 2016, China published guidelines for a sustainable finance and investment policy framework, based on the PRI. Building on this, various initiatives have helped companies offer ESG products and services and provide the necessary information. As foreign investor interest in China continues to grow, these efforts are likely to accelerate – *see chart below.*

The percent of foreign holdings in the Chinese stock market is still low, but growing. This will be a key driver in the accelerating compliance with various ESG criteria by Chinese companies.

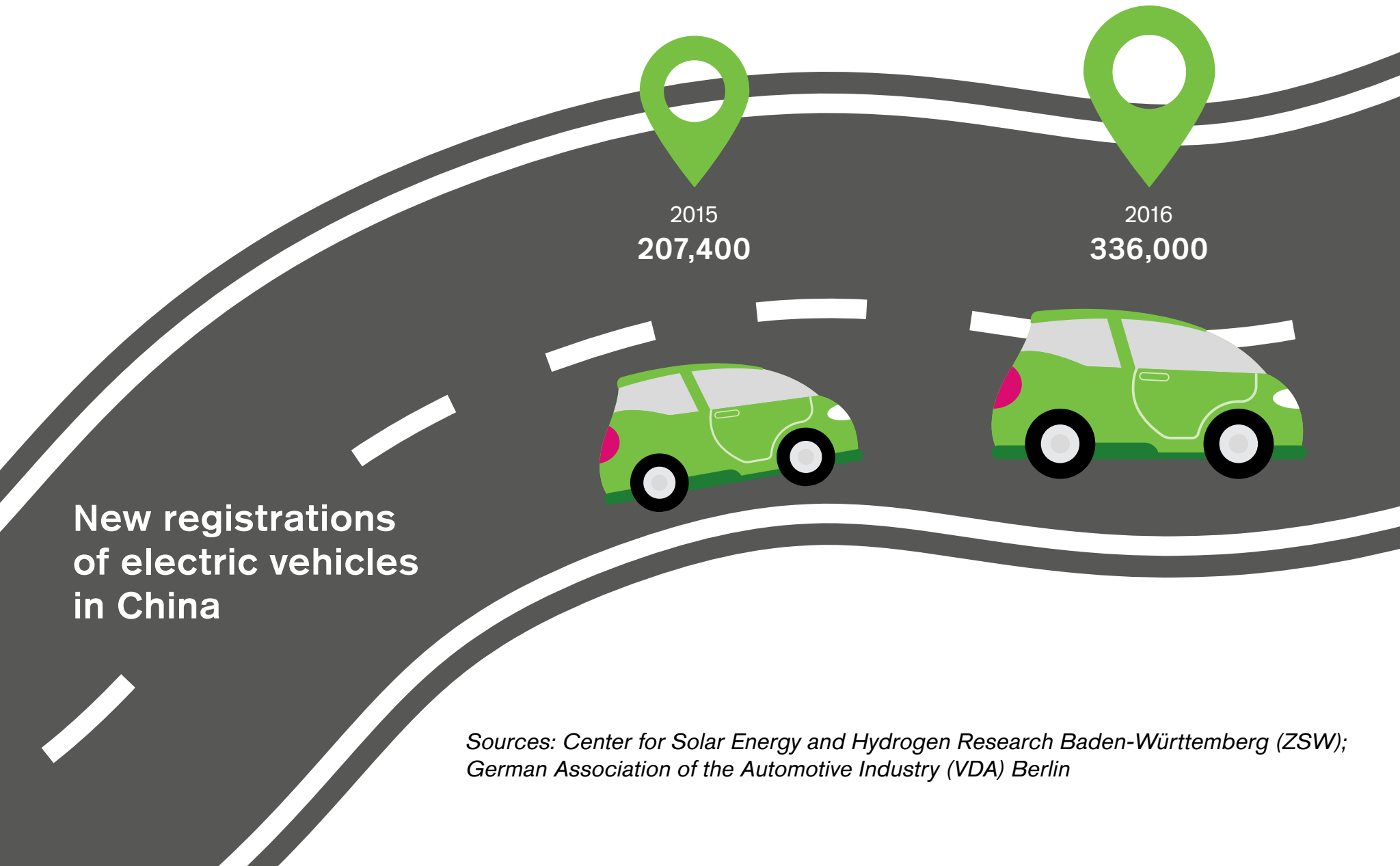
Percentage of foreign ownership of Chinese equities



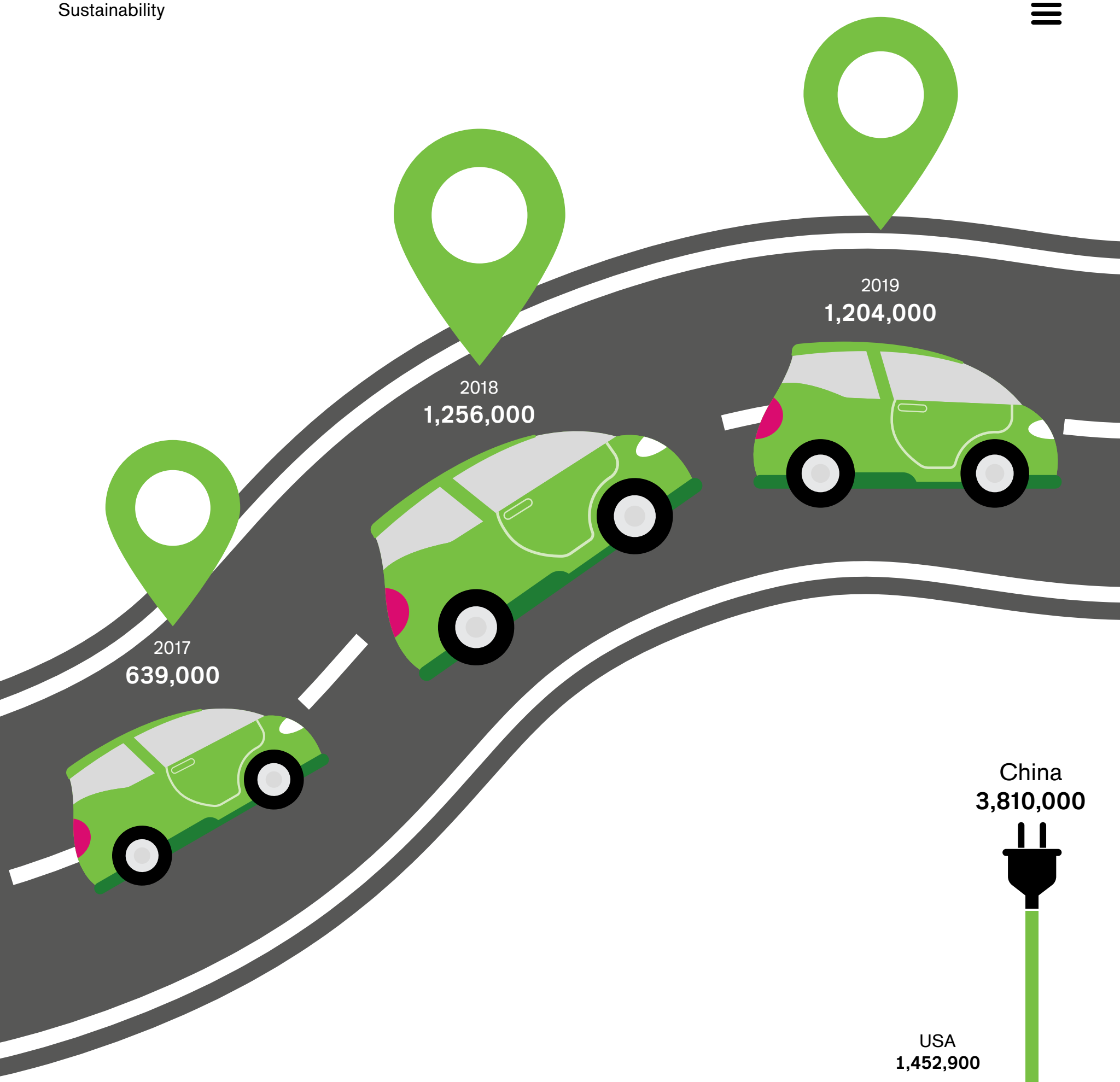
Source: Bloomberg

China
World leader in electric vehicles

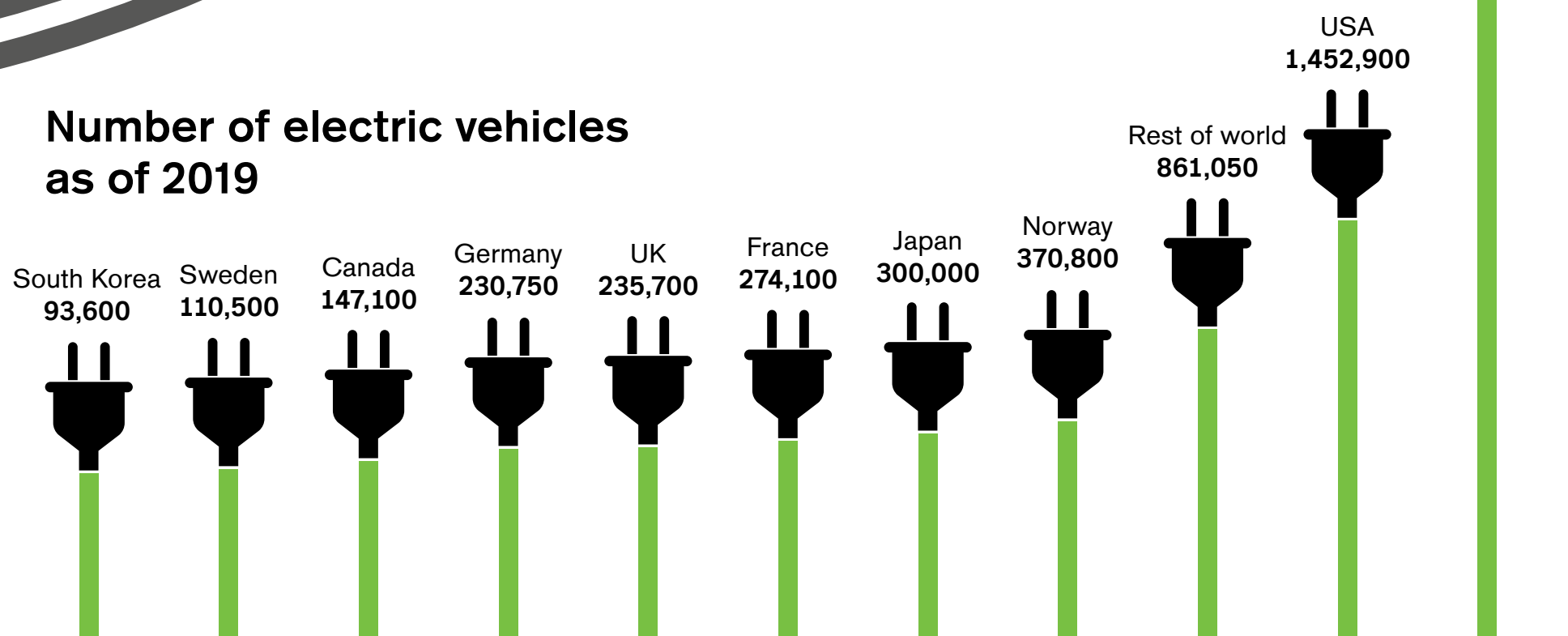
Of the 7.9 million electric vehicles that were registered last year worldwide, 3.8 million were in the People's Republic of China – approximately 2.6 times more than in the US. In China, electric mobility has benefited from government subsidies since 2014.



Sources: Center for Solar Energy and Hydrogen Research Baden-Württemberg (ZSW); German Association of the Automotive Industry (VDA) Berlin



Number of electric vehicles as of 2019



Logistics. Logically.

The market for logistics properties is undergoing a significant and sustained period of global expansion. Spurred by changes in consumption patterns and technological progress, growth in the logistics real estate market presents investors with opportunities for strong risk-adjusted returns and portfolio diversification.

Logistics real estate – a growing market with strong potential

Several factors are converging to drive the expansion of the logistics real estate market around the globe, and this growth is creating attractive investment opportunities for investors seeking robust risk-adjusted returns. The primary factor is the continuing rise of e-commerce, a major contributor to demand for logistics properties, and this combined with a global scarcity of prime logistics space means the ingredients are present for investments in this segment to prosper.

Prior to the COVID-19 outbreak, Goldman Sachs Research's growth forecast for e-commerce was strong, with 14% average annual growth through 2022 predicted for that sector in the United States. Once the post-outbreak dust began to settle, explosive lockdown-driven growth saw this forecast revised upward to 22%.[1] E-commerce sales growth in Asia-Pacific is forecast to be even higher, while Western Europe rounds out the top three regions for e-commerce expansion. Globally, retail e-commerce sales are projected to rocket from USD 3.53 tn in 2019 to a staggering USD 6.54 tn in 2022, representing an 85% rise over that period.[2]

The link between growth in online shopping and the expansion of logistics real estate is rather straightforward. Besides better prices, consumers expect their e-commerce experience to deliver convenience. When choosing online retailers, shoppers also consider the delivery options offered, return policy, and delivery speed.[3] To satisfy these expectations, third-party logistics providers and online retailers are faced with the imperative of seeking out suitable locations for e-fulfilment centers and high-quality last-mile facilities located near major urban centers.

Crucially, online retailers require around three times the logistics space that traditional retailers occupy.

[1] *Credit Suisse Investment Strategy Department, "Logistics real estate: A post COVID-19 beneficiary," accessed 11.08.2020*

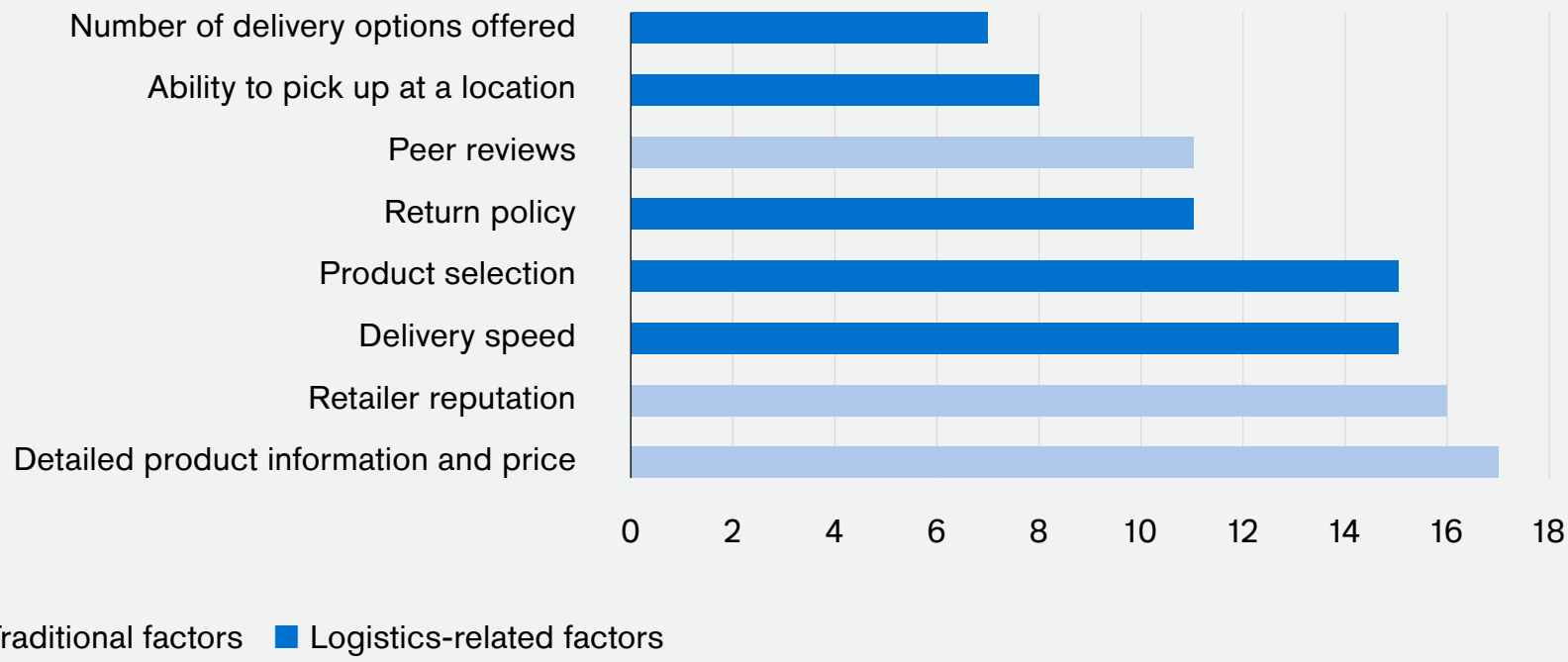
[2] *Statista, "Retail e-commerce sales worldwide from 2014 to 2023" https://www.statista.com/statistics/379046/worldwide-retail-e-commerce-sales/, accessed 27.08.2020*

[3] *Prologis research*

Changes in consumer behavior

E-commerce requires three times the warehouse space of traditional retailers, while consumers increasingly expect faster shipping, creating strong demand for well-located assets.

Considerations in choosing an online retailer (% of survey respondents)



Source: Prologis research

Sentiment is strong

This demand for quality logistics space in conditions of relative scarcity has led to a generally bullish outlook for the sector's prospects. In one recent survey involving 16 managers of logistics properties, 75% expected rental prices for logistics properties to increase in the next three years. Nearly half of those surveyed are planning to increase their purchases of logistics real estate properties over that same period.[4]

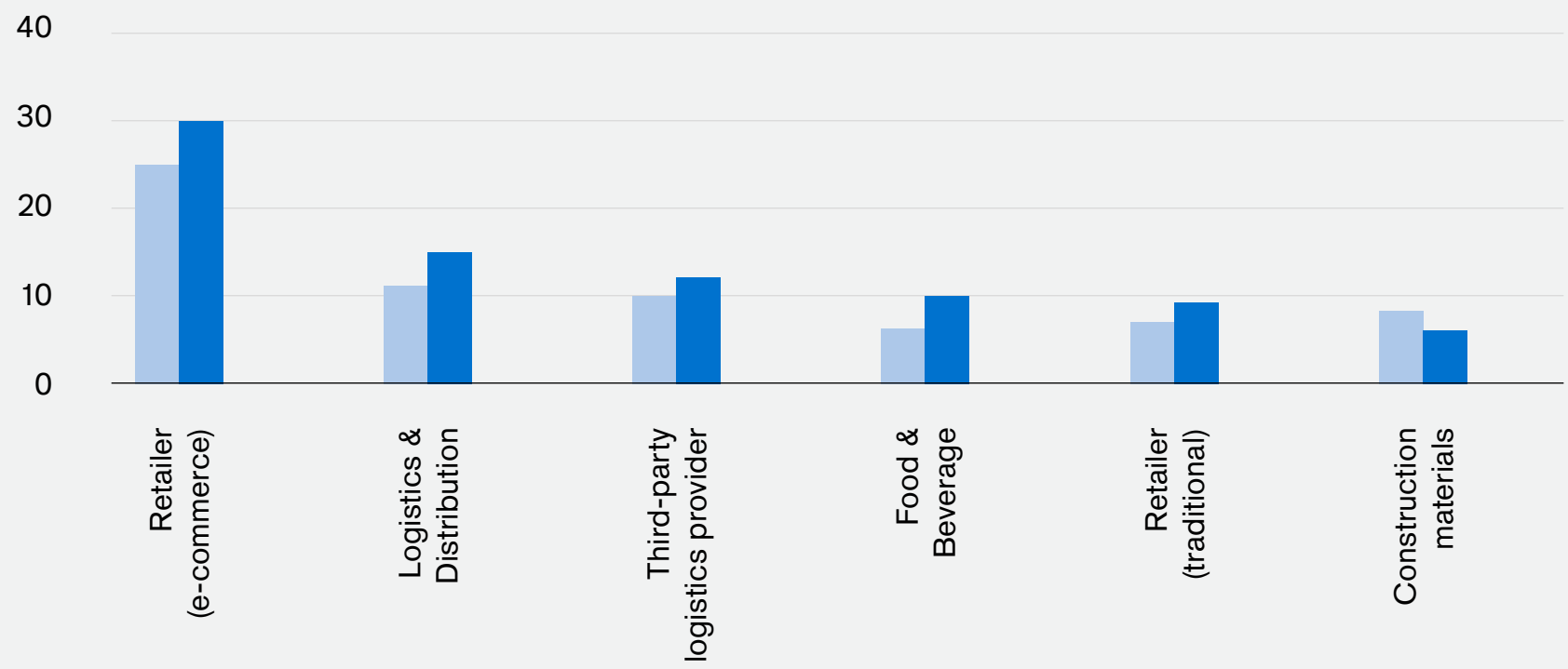
The high expectations of logistic real estate sector investors are already being borne out in the most recent data. From Q1 2020 to Q2 2020, e-commerce retailers in the US increased their volume of leased industrial floor space by roughly 20%.[5]

[4] *Scope Analysis "Logistics real estate market survey: Logistics properties as crisis winners – but with risks," https://www.scopeanalysis.com/?xyzallow#search/research/detail/164448ENEN, accessed 12.08.2020*

[5] *Credit Suisse Investment Strategy Department, "Logistics real estate: A post COVID-19 beneficiary," accessed 11.08.2020*

Higher US leasing volume in Q2 2020 despite lockdowns

Leasing volume of industrial floor space by category in mn sq. ft.



Q1 2020 Q2 2020

Sources: BofAML, JLL Research, Credit Suisse

Catella Research, in its August review, states that the same forces behind trends in logistics properties make “the European logistics market … the winner of the pandemic in the medium to long term”.[6]

Indeed, according to Sven Schaltegger, portfolio manager at Credit Suisse Asset Management, “The logistics property market seems on the cusp of a particularly large expansion. Asset managers with access to deal flow and a network of local logistics and industrial specialists are well-positioned to capitalize on this opportunity on behalf of their clients.”

[6] *Catella Research, https://www.catella.com/en/germany/research/catella-logistics-market-map-europe-2020, accessed 15.09.2020*

Diversification and value

Portfolio diversification remains as important as ever, and for those investors seeking to add a new asset class to their investments, logistics real estate deserves close attention. Real estate in general is traditionally viewed as a source of both respectable returns and capital protection, and given the market uncertainty brought on by the COVID-19 pandemic in an already record low-yield environment, it is enjoying popularity as a relative safe haven. Yet even before markets hit turbulence, logistics real estate in particular was picking up steam – for example, CBRE reported strong and sustained interest in high-quality logistics assets globally during 2018 while predicting robust growth in the next year.[7]

Returns on investments in the industrial real estate sector, which includes logistics properties, have long been attractive, and the forces behind expansion in the logistics sphere are set to continue driving this trend.[8]

There are a few elements to consider when compiling a global logistics real estate portfolio with a maximum risk-adjusted return at a certain level of risk. Firstly, it is paramount to have a solid understanding of the different risk-return characteristics offered by core, core-plus, and value-add investment opportunities. While core investments, i.e. standing assets in good locations with high-quality income streams from strong tenants, tend to be lower risk, their upside is typically also limited. Such core investments are helpful to add an element of stability to the portfolio, particularly due to their stable and long-term income returns, which in the case of logistics investments tend to be higher than for other real estate sectors. At the same time, a diversified logistics portfolio should include a development component seeking to unlock the premiums available from new facilities in today's strong and undersupplied market.

Of course it is crucial to manage the development risks carefully, for instance by limiting speculative developments, focusing on built-to-suits for strong covenants or using forward funding structures with best-in-class and well-capitalized developers. Scrutiny should also be applied to regional diversity, taking into consideration the fact that demand for logistics space is rising across the globe, and thus geographical weighting of a particular strategy is crucial.

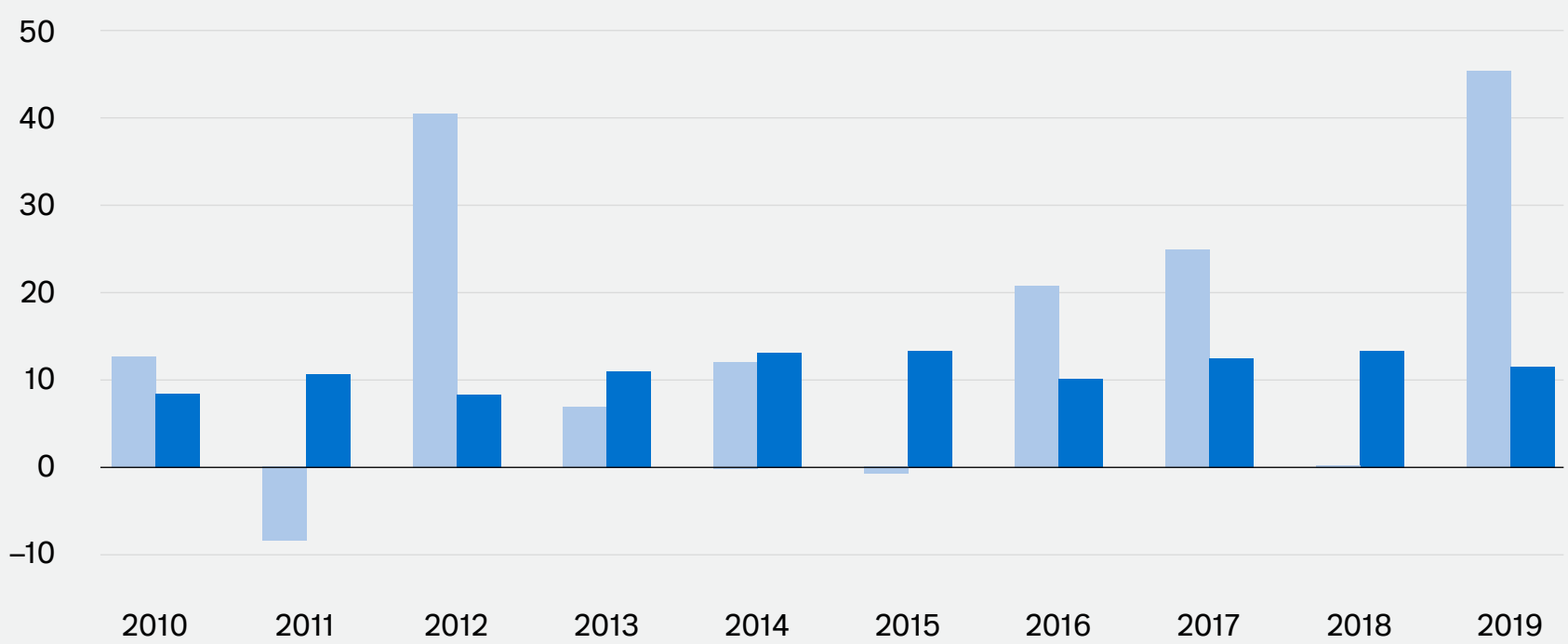
[7] *CBRE Research, "Global Industrial and Logistics Prime Yields 2019," https://www.cbre.com/research-and-reports/Global-Industrial-and-Logistics-Prime-Yields-March-2019, accessed 16.09.2020*

[8] *Bloomberg and MSCI*

Satisfying these criteria gives investors the opportunity to combine income derived from rising logistics property rents with capital appreciation as a consequence of active management, thereby providing the potential for overall long-term performance that outpaces many other asset classes in the current uncertain market environment. Naturally, investment selection is at the heart of a good strategy, and much depends on the ability of fund managers to source and execute on the right deals.

Annual total returns of the industrial sector

Listed and private real estate indices, in %



EPRA industrial sector (in USD, TR)
MSCI Global Annual Property Index – industrial sector (unfrozen; USD (fixed))

Sources: Bloomberg, MSCI

Partnerships key to good deals
In seeking attractive investment opportunities for logistics properties, it is difficult to overestimate the value of networks and partnerships. This is an important distinction from, for example, listed equities, where there are legal limitations on the kinds of material information investors are able to access. Real estate is a “people business,” and portfolio managers who understand this enjoy a significant edge in the fierce competition for high-quality logistics real estate investments.

Real estate investment professionals are deal makers. While they must possess a rich analytical skill set to grasp the economic fundamentals of a given opportunity, soft skills like network building are no less critical. Long-term relationships with experienced local logistics property partners are essential to building up an investment pipeline and deal flow that might not be visible to all market participants, and can also lead to attractive co-investment opportunities.

The key benefits are access to unique insights into local markets and the possibility of sourcing deals that are exclusive and not available to other, less well-connected investors. These can include joint ventures, funds, club deals as well as fund formation strategies by providing seed capital to new strategies.

Positive outlook

Real estate is a complex but sustained attractive investment space, and while some areas such as retail or offices are being challenged by market forces arising out of the COVID-19 crisis, these same forces are pushing up growth in sectors of the economy that need logistics space to thrive. And while the medium- to long-term outlook for this asset class is a bright one, care should be exercised in selecting a partner with an optimal strategy and the required expertise for logistics property investments.

the Digital Times

Credit Suisse Asset Management is successfully strengthening client retention in the era of COVID-19 thanks to entirely new, revolutionary digital formats that put content in the spotlight. The Digital Times takes a digital approach to making content king by creating streaming events in Italy, a specialized digital magazine, and a virtual club.

Let's be honest: a one-on-one meeting between two physically present people will always be the best type of dialogue. But this form of interaction has its drawbacks: it costs time, it limits the number of people you can reach, and can only take place during official business hours. In addition, pandemic-related restrictions prohibit or limit meetings with a larger number of participants. So, what's the solution?

Credit Suisse Asset Management searched for alternatives and came up with a suitable format called The Digital Times. The first of these innovative digital projects was undertaken in Italy with the aim of showing clients the benefits of theme funds. The Digital Times uses three tools to introduce participants to thematic investments: streaming events, a digital magazine, and a virtual club.

Streaming events

In streaming events, the facilitator meets with external guests (usually spokespersons from exciting companies or international experts on specific sectors) and the portfolio manager or specialist for the theme fund concerned to stage a debate resembling a TV talk show. The event takes place in a virtual space in which clients are introduced to the subject by means of video clips and a very interactive dialogue with the different speakers. Top-quality visuals, videos, and audio are used to highlight each speaker at the streaming event, in marked contrast to the clumsiness of many videoconferences.

The Digital Times's first event, powered by Credit Suisse Asset Management, debuted in July 2020 and was devoted to the topic of digital health. Participants included Lavina Talukdar, the head of investor relations at vaccine manufacturer Moderna Inc., Graziella Bilotta, the CEO of telemedicine provider Paginemediche, Roberto Ascione, the CEO and founder of healthcare technologies specialist Healthware Group, and Pascal Mercier, a product specialist for a Credit Suisse Asset Management fund focused on digital health.

The debut of the new format attracted 513 live participants from across Italy, and the invitation to the event on LinkedIn generated over 18,000 views. Streaming remained active for a full six months, enabling another 800 or so interested people to tune into the event at a time of their own choosing.

4,400

visitors joined the virtual club on digital health

513

live participants from across Italy

18,000

views

Digital proximity

As an alternative to physical contact with clients, Credit Suisse Asset Management has had good experiences streaming events in Italy. The facilitator welcomes the speakers and the clients from a virtual stage and leads them through the interactive event.

Digital magazine and virtual club
The new digital magazine produced by Credit Suisse Asset Management as part of this campaign, which consists of an editorial as well as four to five posts from leading international media, is dedicated to people who are interested in reading or hearing more about specialist topics and investment perspectives.

The contents of the magazine and much more are available through the Virtual Club hub, an innovative portal that visitors can access through their own personalized avatars and which allows them to navigate their way through a Credit Suisse Asset Management lounge to discover additional insights. No fewer than 4,400 visitors joined the virtual club on digital health and navigated for around five minutes on average to access videos featuring external speakers, the Credit Suisse Asset Management video, and podcasts from the digital magazine, or to also order product information.

The verdict is a big thumbs up: Credit Suisse Asset Management has positioned itself as a first mover for virtual campaigns in Italy and has made a real contribution to client retention despite having no physical contact. The Digital Times will never replace direct contacts and relationships, but it is clear that a combination of the two is the most effective way to disseminate stronger and wider messages and to grab the attention of a bigger audience. Clients' resounding appreciation of The Digital Times is evidenced by the number of participants and the number of clicks and views for the second focus event (31,000 views on LinkedIn for the digital magazine), which took place in October 2020 and was dedicated to the topic of safety and security.

Family bonus

Family firms are more successful on average. When times are good, they are more profitable; when times are bad, they use a more defensive strategy. The difference on the stock market is measured by "alpha." Investors would do well to take a closer look.

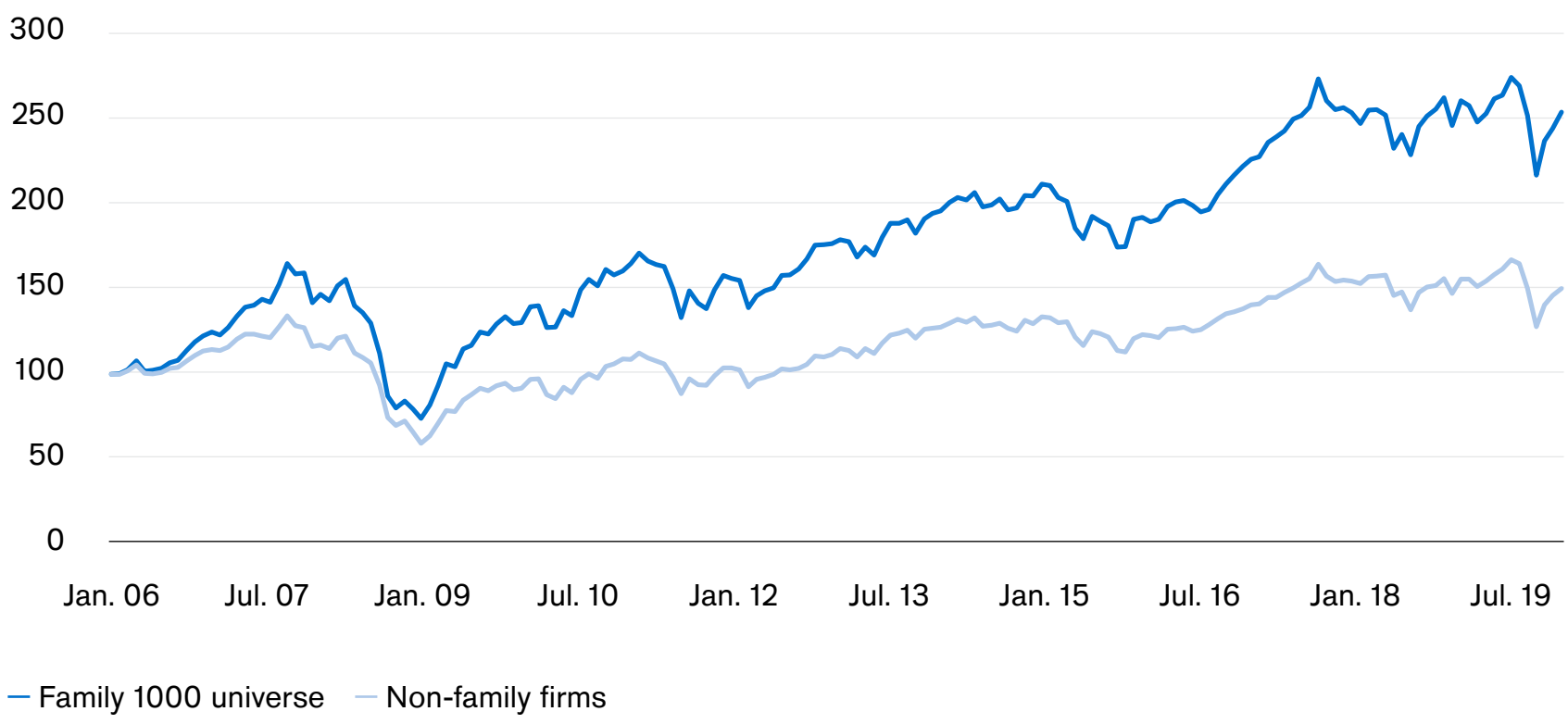
The numbers don't lie: Family firms regularly perform better than non-family firms do, as confirmed by the latest study of the Credit Suisse Research Institute.[1] For 14 years, the Institute has been following 1,000 publicly listed family firms. It includes companies whose founders and founder successors still hold an equity interest of at least 20% or control at least 20% of the voting rights. Among the top companies in the Credit Suisse Family 1000 universe are Alphabet, Facebook, Alibaba, Samsung, and Roche. The oldest firms in this universe are Norwegian conglomerate Orkla (founded in 1654), LVMH (1743), Bucher Industries (1807), Carlsberg (1847), and Davide Campari Milano (1860).

[1] *The Family 1000: Post the pandemic Credit Suisse Research Institute, Credit Suisse Group AG, September 2020*

Outperformance of up to 5%
On the stock exchange, these 1,000 companies generated an outperformance of 5.0% in Asia, 4.7% in Europe, and 2.6% in the US (on a yearly average). Investors can benefit from these differences, expressed as a company's alpha, by updating their portfolios to include individual securities from the Credit Suisse universe. Or they can take the simpler and more diversified approach of adding a fund that focuses on family firms.

Family firms are outperformers

Clear outperformance since 2006
Returns adjusted for sector, weighted by market capitalization; index with January 2006 = 100



Last data point: June 2020
Sources: Credit Suisse Research, Thomson Reuters Datastream

Historical returns and financial market scenarios are not a reliable indicator of future performance.

Passion and proximity
There are many reasons why family firms perform better on average. The amount of literature on the subject is manifold, and it's hard to get an overview. What successful family firms have in common, however, is passion for entrepreneurship and proximity to their stakeholders, namely their staff and clients. "Walk the talk" is not just an empty promise: it comes from the family tradition, not a management manual. Shareholders, analysts, and other representatives of the financial community are also important to family firms, but are not necessarily the top priority.

Sustainability is in their blood
The long-term horizon of family firms has a positive impact on sustainability. They perform slightly above average in the sustainability and ESG ratings. Compared with non-family firms, however, they lag behind somewhat in communicating about sustainability issues. This hesitance is most likely because family shareholders consider sustainability to be a matter of course in their corporate strategy and corporate management, thereby eliminating the need to communicate on this separately.

However, there is one area in which family firms do not tend to take the lead over their peers: governance. Thanks to voting right shares and similar tools, families are often the only authority figures, even though they hold just a minority interest. However, these types of situations are common, so external shareholders can carefully consider the pros and cons of investing in a family firm.

Interview

In conversation with Daniel Bossard, CEO of Bossard Holding AG in Zug, and Fabio de' Longhi, Vice Chairman of the Board of Directors of De' Longhi S.p.A. in Treviso.

Read the interview

The five typical strengths of family firms

1 Above-average sales growth

Since 2006, sales for the Family 1000 universe have grown by an average of 11.3% p.a. The benchmark universe of non-family firms achieved only average growth of 6.8%.

2 Higher profitability

The average cash flow return of family firms was 2% p.a. higher than the benchmark, which also meant an above-average return on capital. The earnings before interest, taxes, depreciation, and amortization (EBITDA) margins of family firms even showed an outperformance of 3% in 2019.

3 Greater emphasis on R&D

Family firms invest larger amounts and in a more sustainable and successful manner. This difference is strongest in Asia.

4 Less debt, higher return on equity

On average, family firms rely less on borrowed capital and reduce it more quickly in times of crisis than non-family firms, and they still generate higher return on equity.

5 Outperformance on the stock markets

Family firms also outperform on the stock markets, expressed as alpha. Average annual alpha since 2006 is 5.0% in Asia, 4.7% in Europe, and 2.6% in the US.

Historical returns and financial market scenarios are not a reliable indicator of future performance.

Sources: The Family 1000: Post the pandemic, Credit Suisse Research Institute, Credit Suisse Group AG, September 2020; Family Business, Weekly Viewpoints of Burkhard Varnholt, CIO Credit Suisse (Switzerland) Ltd., 11.09.2020

Fabio de' Longhi

Fabio de' Longhi,
Deputy Chairman of the
Board of Directors of
De' Longhi S.p.A., Treviso

Dr. Daniel Bossard

Daniel Bossard, CEO
of Bossard Holding AG,
Zug

Think long-term, act entrepreneurially

Daniel Bossard, CEO of Bossard Holding AG, Zug, and Fabio de' Longhi, Vice Chairman of the Board of Directors of De' Longhi S.p.A., Treviso, talk about their families' influence as well as the prerequisites for a successful future.

Well connected: The Bossard Group, Zug

The company was founded in 1831 by Johann Franz Kaspar Bossard in Zug. It got its start as a hardware store, eventually began to manufacture screws, and then expanded to include fasteners and connectors. Today, the company is a market leader for this segment in Europe, North and Central America, Asia Pacific, and South Africa. The product range consists of mechanical and electrical connectors like bolts, nuts, wash ers, and dowels. Its engineering and consulting services, along with automated parts management, enable the Bossard Group to help its customers increase their productivity. In 2019, the company generated net sales of CHF 876 mn, for an EBIT of CHF 95.7 mn and net profit of CHF 76 mn. It employs 2,500 at 80 locations around the world.

Bossard has been listed on the SIX Swiss Exchange since 1987. As of the end of 2019, family firm Kolin Holding AG and Bossard Unternehmensstiftung held 27.9% of the capital enti tled to dividend and controlled 56.3% of voting rights. Since 2019, group management has been back in family hands with Daniel Bossard. He succeeded David Dean, who managed Bossard very successfully for 14 years.

Coffee, nutrition and home well-being, family style: De' Longhi Group, Treviso

This family firm got its start in Treviso back at the beginning of the 19th century but it is in 1974 that De' Longhi start the production of oil filled radiators which would go on to achieve massive success. In the following years, the group expand its product range and its presence in the small domestic ap pliance sector, becoming a globally recognised player in the industry. Today, the group offers a wide range of coffee ma chines (including for Nespresso) and super automatic coffee machines under the De' Longhi brand, Kenwood small kitchen appliances, and Braun household appliances.

During the last 15 years the group has been successfully guided by Fabio de' Longhi and in 2019, De' Longhi's revenues were EUR 2.1 bn, with EBIT of EUR 210.9 mn and profit of EUR 161 mn. Worldwide, the Group is present in more than 120 countries with approximately 9,000 employees, about half of which are located in Europe.

Since 2001, De' Longhi S.p.A. has been listed on the Italian Stock Exchange, while is still controlled by the founding family. Founder Giuseppe de' Longhi is the chairman, and his son Fabio is vice chairman of the company. In April 2020, Massimo Garavaglia took the role of CEO from Fabio de' Longhi, who will continue to support the company by focusing on M&A (see the recent agreement to acquire Capital Brands Holding Inc.), innovation and strategic development. Garavaglia, Italian man ager with an outstanding track record, had worked for 16 years at the Swiss-based Barry Callebaut group, most recently as president of EMEA. In the future, the Company will focus on maintaining its leadership in the espresso coffee machines for the household segment and in selected categories of the food preparation, managing the continuous expansion of a pure multinational Group.

Daniel Bossard, Fabio de' Longhi – how does the family nature of your company manifest itself?

Daniel Bossard: The family nature is mainly reflected in our long-term thinking, which puts profit optimization before profit maximization and pursues a staff policy that's geared to the long term.

Fabio de' Longhi: For our group, the entrepreneurial spirit is a more important factor than its family nature. It's this entrepreneurial spirit that guarantees continuity and the desire to grow, as well as the willingness to tackle business challenges.

How much influence does the family shareholder vision have on the future of your company?

Daniel Bossard: The company is characterized by the values defined by the Bossard family holding company. These values are strategically and culturally integrated into the company by the Chairman of the Board of Directors and the CEO, both of whom are members of the family.

Fabio de' Longhi: The company's long-term strategy and vision are determined by the Board of Directors and implemented by management, with the general support of all shareholders. Family businesses are often characterized by the traditional values of their founders, but in a rapidly changing environment it's essential that these factors do not hinder future development.

"The family nature is mainly reflected in our long-term thinking, which puts profit optimization before profit maximization."

Daniel Bossard

How do you ensure your company stays a family-owned business?

Daniel Bossard: Through a family holding company, in which family topics are discussed and decided independently of the business.

Fabio de' Longhi: The family needs to motivate the management to take on new challenges, seize opportunities, and continually reinvent itself. Our group grew thanks to the courage and vision of my father in the 1970s, but the company has changed dramatically over time by facing new challenges. This willingness to change is fully embraced by our management team.

What does it take to ensure family shareholders and the CEO work well together?

Daniel Bossard: A clear division of powers and guidelines. For example, we have a family mission statement which governs how the family holding company communicates with Bossard. Communication takes place between the Chairman of the Board of Directors of the family holding company and Bossard. The Chairman of Bossard's Board of Directors then forwards the information to the CEO. We've also specified the conditions under which family shareholders can be involved in the management or operational leadership of Bossard.

Fabio de' Longhi: The group put in place the necessary governance at the time of the stock exchange listing in 2001. In recent years, we've also broadened our leadership and created a management structure with experienced, internationally oriented C-suite executives. The appointment of an external CEO is a further step towards a managerial approach.

"The family must allow the company to evolve and be prepared to change its role within the organization, while at the same time, it needs to uphold the firm's strategy and core values."

Fabio de' Longhi

How do you retain your innovative edge?

Daniel Bossard: In our case, innovation is part of our organization's DNA. Our values and management guidelines support entrepreneurship and the willingness of all our employees to experiment.

Fabio de' Longhi: Innovation is part of our corporate culture; indeed, we invested EUR 52 mn in research and development in 2019. These investments in tangible assets are complemented by our investment in human resources and the working environment, because the key to our innovative strength lies in our people.

Apart from your own company, how would you rate the development prospects for family firms?

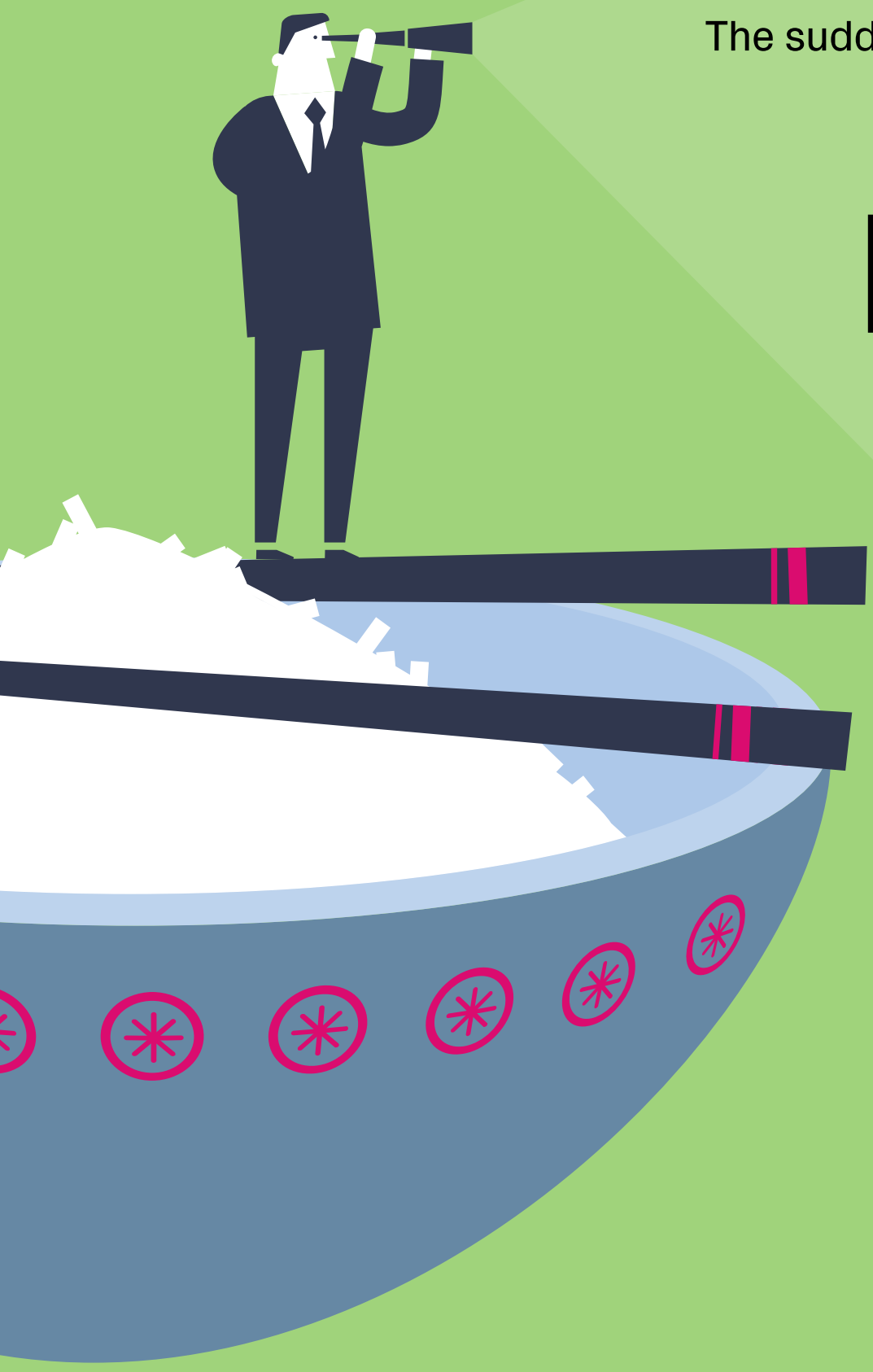
Daniel Bossard: Very good, but only if we're successful at playing the family card. The family is usually a good owner or a good operator. In our case it's both: Our structures have proved themselves. But if it transpires that the group of family shareholders cannot produce any professional managers, the family must ensure – as a minimum – that they remain a good owner.

Fabio de' Longhi: As long as they retain their entrepreneurial passion, willingness to innovate, and openness to new market developments, I believe the family can support the company along its journey. The family must allow the company to evolve and be prepared to change its role within the organization, while at the same time, it needs to uphold the firm's strategy and core values.

Why is it often easier for family firms to manage times of crisis better than publicly traded companies that are not family owned?

Daniel Bossard: Because family firms often operate on a more robust and sustainable footing. They normally have greater liquidity and employees who're more motivated, more loyal, and happier. The shared strength and long-term focus of family shareholders can be very useful in difficult situations.

Fabio de' Longhi: I don't have any data to confirm this thesis. But I do think families that play a central role in a company and support it in difficult circumstances represent a real point of reference for the whole community. This strengthens team spirit, and also fosters dialogue and mutual understanding.



The sudden reemergence of

emerging market bonds

Today, emerging market bonds are almost universally recognized as a dynamic and diverse asset class that can help enliven a portfolio or stand on its own as a source of return. This has not always been the case. A decade or two ago, many market participants were gun-shy. Too fresh were the memories of crises in Asia or South America that had wiped billions off balance sheets. As a result, the resurgence of the asset class went unnoticed for too long in many places, leaving current investors scrambling for expertise – and for solutions.

Latin American Debt Crisis. Asian Debt Crisis. These are words that can still strike terror in the hearts of investors of a certain age. The repercussions were felt for years. In the minds of many, the reputation for danger, instability and the risk of unpredictable and unstoppable domino-like collapse cast a pall on the asset class that lasted even as the fundamental strength and the advances in risk and crisis management no longer warranted it. This was one reason the renaissance of the asset class was missed by many.

An EM debt renaissance

Another was the almost hidden quality of its restoration. Earnest Hemingway famously described the way a person might slide into bankruptcy as “gradually, then suddenly.” Emerging market fixed income did the same thing in the other direction. Slowly going from strength to strength, it gradually improved its resilience and its fundamental solidity. Countries and entire regions dug themselves out of unsustainable debt, gaining ground in the rating agencies’ assessments as they did so. Institutions were reinforced with the introduction of independent central banks, the modernization of governmental and regulatory frameworks, as well as the integration into regional and then global markets. Emerging market governments have proven and continue to show an ongoing willingness to initiate and see through the necessary reforms. On the private side, globalization has forced companies, if they want to be internationally competitive, to hew to worldwide standards regarding financing, transparency, and accounting. Compared with the past, countries now have much less dollarized debt, corporates in emerging markets have less leverage than their developed market counterparts, and investors get a nice compensation for the risk taken.

Neglected capacities

However, in the aftermath of the crises and the doldrums that followed in their wake, many investment houses had let their capabilities in this asset class atrophy. Local branch offices were closed, specialists were reassigned and stopped training their successors. Expertise was lost, experience lay fallow. So even if the signs of regained strength and stability were there, very few were capable of picking them up and correctly interpreting them. Many missed the rebirth.

The result of all this was, for all intents and purposes, the sudden appearance, a few years ago, as if out of nowhere, of a new asset class that combined high-growth dynamism with reliable risk metrics and, for many Western investors, favorable diversification characteristics. Today, a truly global investor cannot afford to eschew emerging market fixed income. Many would welcome it as an interesting opportunity even outside the portfolio context, if they could just find the right solutions and/or a reliable partner with the requisite know-how.

Sprawling and diverse

So, what is the current lay of the land around emerging market fixed income? The first thing to emphasize is that this asset class is not one thing – and that its different segments can behave quite differently. It includes the full spectrum of credit qualities, all issuer types and sector varieties as well as a stunning geographic diversity. A further important distinction is between hard- and local-currency bonds, that is bonds issued in, say, US dollars that avoid the often significant exchange rate risks characteristic of emerging market, and these that do not. In other words, this is an asset class that includes sovereign and quasi-sovereign issuers in addition to Indonesian banks, Russian energy giants, and Mexican auto parts manufacturers, to name just a few. It comprises solid large-cap issuers with high ratings that do not significantly differ from their developed market counterparts except for the domicile of their headquarters, as well as stressed names struggling to find funding for their operations, perhaps due to institutional weakness of their market environment. Looking at it like this, the need for experience and expertise becomes clear.

The second thing to recognize is that, hidden in this complexity, a broad range of opportunities await the investor willing to seize them. The uneven coverage and idiosyncrasies of the asset class means that a guide – an expert, an active manager – can be the decisive factor for success.

For example, the coronavirus pandemic hit hard and fast in early 2020, and continues to impact both developed and emerging economies in various ways. Especially in that first phase of the crisis, information was lacking and market participants painted with a broad brush. Emerging markets took a dive across the board and spreads soared to historic and obviously unsustainable heights.

(Not just because of the perceived weakness on one side, but also because of the unprecedented support coming from the Fed-eral Reserve and some of its peers.) However, many emerging markets were successful in combating the virus, and this opened up opportunities for savvy and experienced observers.

In another typical phenomenon of this space, credit ratings for individual issuers are capped by the respective country ratings – i.e. corporates from a BBB rated country very rarely if ever attain an A rating, even if their fundamentals would allow it. This creates opportunity in high-quality issuers from shaky countries, for investors with the decisive information.

An active opportunity

Generally, an already complex interplay of risks – currency, rating, sector, region, etc. – interacts with limited information to create sudden opportunities – or sudden dangers – that an experienced active manager can navigate to deliver added value. But the problem remains: such managers are few and far between. Because of the aforementioned historic coverage and investment gaps, today's asset management infrastructure is not commensurate to the volume of the opportunities available. However, early movers in the space have been able to build an impressive capability and array of solutions.

Chances are that you, as an investor, are underinvested in emerging market debt as measured by its weight in international financial markets and by the weight of its home markets in the global economy. The scope of this imbalance becomes clear in the following simple juxtaposition – the GDP of emerging markets is currently more than 50% of global GDP, and yet the weighting of emerging market debt in the average institutional portfolio is nowhere near that. In other words, the typical institutional fixed income investor is massively underweight one of the most dynamic and fastest-growing segments of the world economy. To successfully remedy this, an investor must be able to access a deep well of expertise and experience. The right partner with the requisite know-how is crucial to successfully bringing a portfolio in line with the actual importance of this asset class, perhaps more so than in other areas of investment.

Underweighted

The GDP of emerging markets is currently more than 50% of global GDP, and yet the weighting of emerging market debt in the average institutional portfolio is nowhere near that. There is potential for performance here that can best be exploited with an experienced partner.

The virus is putting society to the **test**

Matthias Horx

Trend researcher and futurologist

The coronavirus crisis is fundamentally different from earlier crises. Not only is it posing challenges for the economy and politics, it is putting our society's entire value system to the test. It has paraded in front of our eyes what we are no longer able to ignore.

The thing I find most astonishing about the coronavirus crisis is that the global economy hasn't been brought completely to its knees. That we haven't experienced a lasting downturn, mass unemployment, or a stock market crash. What's happened instead shows us just how outdated our standard economic models are. In the midst of this major crisis, the stock markets are booming. How is that even possible? Maybe our economic systems are much more complex, flexible, and resilient than we've given them credit for.

Holism as a hallmark of the coronavirus crisis

The coronavirus crisis is different from other crises by virtue of its holism. It differs from major catastrophes such as world wars or natural disasters in that society, individuals, politics, and the economy have in principle retained their ability to take action. It is a crisis of decision-making ("krísis" is the ancient Greek word for "decision"). We can decide whether we wear a mask or not. Politicians can decide whether to impose strict measures or dismiss the whole thing as nonsense. Managers can seize the opportunity posed by the crisis to engage in innovation and reorganization. We can decide whether to take to the streets and protest against the "criminals in the control rooms". Or we can decide simply to wait it out and grumble until it's finally "over".

Broad array of threats

The coronavirus crisis, unlike subcrises such as the banking crisis or the refugee crisis, affects all aspects of our existence – our private lives, our day-to-day routines, our mobility, and our family life. Organizations are also affected – from healthcare to city administrations, media, politics, and the economy. These are the value systems that hold our society together. And all of this has been challenged, called into question, put to the test. Multilayer crises like these rip through the entire social fabric. The individual layers (or subareas) combine to amplify the effect.

Differing national repercussions
While the coronavirus crisis is a global phenomenon, its repercussions have been quite different from one country and one culture to the next. The virus is putting our society to the test; it is testing countries' and cultures' responsiveness and resilience and their ability to react to unforeseen challenges. This is much less about technological strength than it is about social coherence.

The countries that are emerging from the crisis in the best shape are those that have the most developed cooperative internal mindset. Alongside China, which has benefited from the strict policy controls it imposes on its citizens, this group primarily includes smaller countries with female or integrationist political leadership – New Zealand, Finland, Norway, Denmark, Estonia, and Iceland, for example. In these nations, the second wave has also been mitigated relatively successfully without the economy suffering any major damage. The "exceptional model" of Sweden is especially interesting in this regard because in certain respects it is the counter-model to China, fostering cooperation among individuals and in civil society, and consensus instead of control. In the US and Brazil, which are governed by autocratic populists, the coronavirus is, by contrast, exacerbating centrifugal forces in society – and leading directly to social catharsis. In Italy, meanwhile, the shocks have forged a new social cohesion. If you travel to Italy today and talk to Italians, their pride in how they have pulled together as a nation is palpable.

Accelerated glocalization
In the economy, too, Covid-19 has triggered significant countertrends. It appears that the dichotomy between "local" and "global" has given way to the integration of local into global. The result is being called "glocalization." Global just-in-time production, which sees millions of separate parts manufactured and shipped around the globe with perfect precision in order to put together a car in a high-wage country, has had its day. There are not only political but also systemic reasons for this that have become evident during the coronavirus crisis. What happens if entire classes of drugs are no longer deliverable if they are produced in a lone Indian factory? What about cobalt, which we (still) need for electric engines?

"The virus is testing countries' and cultures' responsiveness, resilience, and ability to react to unforeseen challenges. This is much less about technological strength than it is about social coherence."

Global production is currently being dismantled – and reconfigured – en route to a new type of sourcing in which the individual commodity and supply chains are becoming smarter. Outsourcing is increasingly being replaced by insourcing. Locally based production is booming, networks are being localized, and artisanship is experiencing a renaissance. In the process, individual countries, regions, and continents are becoming more self-sufficient and autonomous, and economic structures more complex. All of this also supports sustainability and upcoming decarbonization, which requires a realigned division of labor and a new appreciation of what is local. No, this emerging "slowbalization" will not put an end to globalization. But it will put it on a different footing. It will make the industrial production process and the global flow of goods and people a bit less hectic. This is perhaps the greatest impact of the coronavirus crisis: it has curbed the over-acceleration of our world.

Lasting memories

How will we remember the coronavirus crisis when we look back in a few years' time? The hot core, the real nucleus of the Covid crisis is how it has shone a spotlight on the status of human civilization. It has paraded in front of our eyes what we are no longer able to ignore: we are in an escalation crisis that is affecting EVERYTHING: flows of goods, products, energy, the money economy, the way we consume, the way we live, and the way we interact with one another. The escalation principle also encompasses the realms of information and communications, of affects and emotions – the hurtling universe of attention and stimulation that threatens to push us to the edge of reality with its hate culture and conspiracy theories.

"This is perhaps the greatest impact of the coronavirus crisis: it has curbed the over-acceleration of our world."

Covid-19 has sent us a polite – yet firm – reminder that our lives are still dependent on nature, that we cannot really leave behind the realms of viruses and bacteria from which we originate (50% of human DNA consists of virus DNA). Despite all the technology we have, we are still part of the biological, living world. We are and will remain social beings that depend on one another, despite all the (apparent) triumphs of technology.

Everything stays different

The crisis has laid bare what we already knew, or at least suspected: we have reached an invisible frontier, a tipping point for civilization. The images of burning Californian forests, the floods, and the landslides – never has their impact been more intense and dramatic than during these coronavirus times. Covid-19 has acted like a burning lens that has concentrated our focus on the true challenge facing us next, the real decision we have to make for our future: the decarbonization of our economy. It is not premature to speak of a semantic shift toward the great environmental and existential issue of our time. Today there are barely any major companies or financial providers that do not fly the flag of environmentalism and sustainability.

The coronavirus crisis has consolidated sensory overloads, shone light into dim recesses, and made things tangible that were previously diffuse. It demands clarifications – between the individual and society, and between the economy and nature. It demands in no uncertain terms that we INTEGRATE these ruptures and contradictions.

The “annus horribilis” of 2020 will, in retrospect, maybe not be so “horrible” after all. It has also honed our experience of managing situations and enabled us to live life with greater intensity. It has provided clarity. As long as we are in a position to accept such experiences, the future remains possible. But as soon as we refuse to accept them and insist that everything should go back to what it was like “beforehand,” whatever the cost, then we’ve lost our future. Then we’ll slide back into a false past where everything was supposedly better, even though the way things were going had no longer been sustainable for a long time. What was the name of that Swiss film again? “Alles bleibt anders”– everything stays different. So let’s get going.

Matthias Horx

Matthias Horx is one of the most influential trend researchers and futurologists in the German-speaking world. After a career as a journalist, he founded the Zukunftsinstitut in 1998. He advises numerous companies and institutions. His books *Anleitung zum Zukunftsoptimismus* and *Das Buch des Wandels* became bestsellers. As guest lecturer, he teaches prognostics at various universities. A passionate European, he commutes between London, Frankfurt, and Vienna, where he has lived with his family in the Future Evolution House since 2010.

futureday.network/details/matthias-horx

Indexed sustainable funds gaining in popularity

As investors increasingly demand products that satisfy their sustainability preferences, passive funds are gaining in popularity. These funds offer a broad range of benefits that make them attractive to investors of all stripes, while having the capacity to advance ESG objectives.

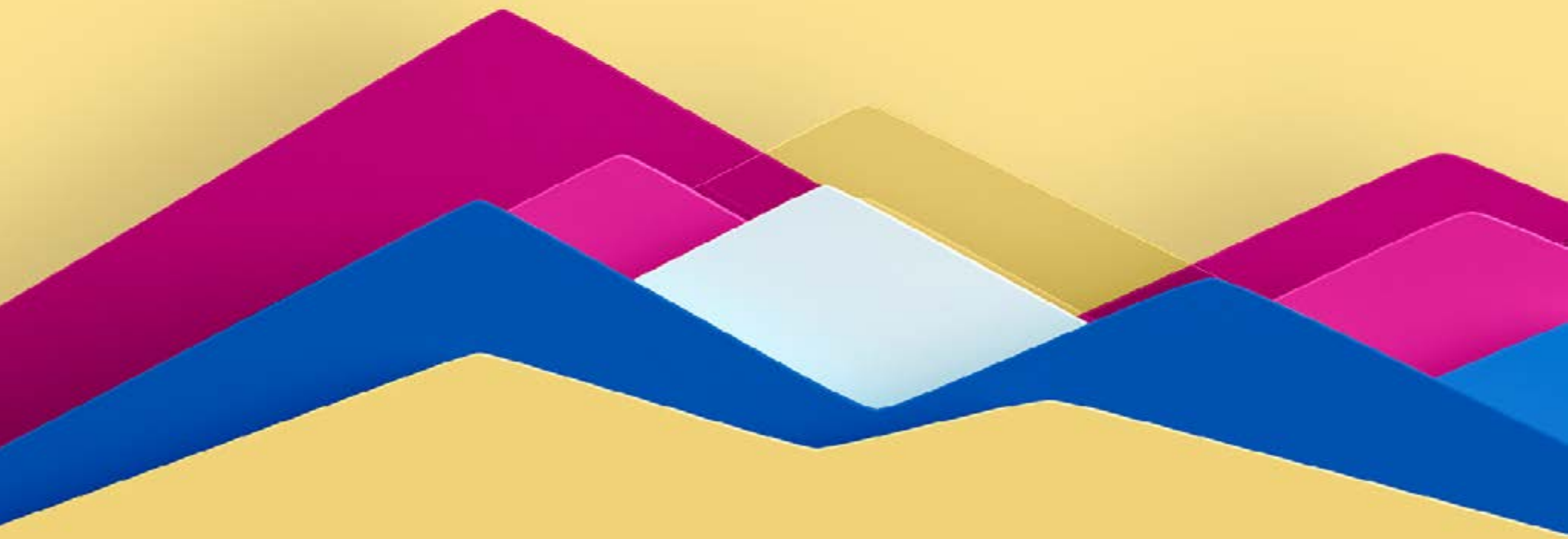
Sustainable investing has rapidly developed from a niche into the dominant paradigm in asset management. Broad social awareness of environmental, social, and governance (ESG) considerations combined with a concerted effort by the world's largest asset managers have brought issues of sustainability to the fore. Global sustainable investments have already smashed through the USD 30 tn barrier.[1] Sustainability criteria are applied across all asset types and classes, and passive sustainable investments, including exchange traded funds (ETF), are no exception, as detailed by Morningstar's September 2020 report "Passive Sustainable Funds: The Global Landscape 2020."

Passive sustainable funds with room to grow

At present, passive funds constitute 24% of the global fund market, yet passive sustainable funds make up a relatively small 12% of the general sustainable fund universe. That universe amounted to a total of over 3,400 funds as of September 2020.[2] As the majority of these funds are actively managed, this means that there is significant room for investment flows in passive sustainable funds to grow.

Indeed, interest in passive sustainable investments has long been following an upward trajectory. By one estimate, year-on-year growth of passive ESG fund assets in the period between 2014 and 2019 was 33%, an expansion three times greater than that of active ESG funds over that same period.[3]

Investors in passive sustainable funds benefit from the advantages that are common to all index funds – they obtain a cost-efficient solution for diversifying their portfolio with low benchmark tracking error. In addition, passive ESG funds in the main offer high liquidity, and they are suitable for both retail and institutional investors alike.



[1] *World Economic Forum, https://www.weforum.org/agenda/2020/02/sustainable-investment-gain-momentum/*
[2] *Morningstar report, "Passive Sustainable Funds: The Global Landscape 2020," September 2020*
[3] *Financial Times, "How index investing can drive sustainable finance transition," https://www.ft.com/content/65d307c4-7379-455e-bcb2-d821b670a90f*

ESG is moving the needle for passive funds

Environmental, social, and governance issues have rightfully occupied a prominent place in the minds of investors and asset managers. This shift is not the result of purely ethical or philosophical considerations, but rather of practical ones: "Stock-picking strategies based on 'ESG tilt' and 'ESG momentum' approaches beat the world index. Sustainable enterprises have a lower probability of running into financial difficulties."[4]

The simple fact of enhanced long-term profitability naturally impacts the passive sustainable funds sphere as well, encouraging fund managers to continually expand their offerings. There were three times as many passive sustainable funds in June 2020 as five years previous, while each year seems to bring a record number of passive sustainable fund launches.[5]

Rising inflows are leading to predictable and beneficial results. Fee premiums on passive sustainable funds, once considered prohibitive by all but the most idealistic investors, are dropping in the face of stiffer competition. At the same time, passive sustainable funds are beginning to offer exposure to new markets, including ones concentrated on specific objectives related to environmental and social issues.[6]

Strong asset flows across the globe are propelling growth in this segment – in Europe, the share of sustainable funds in passive assets has risen by over 80% since 2016, with positive quarterly net inflows going back a decade.[7] Within this category, ETFs are advancing on index funds, while fixed income funds remain underrepresented. While lagging behind Europe, the Unites States and the rest of the world are also making great strides in passive sustainable investments, and large institutional investors such as government pension funds are set to continue this trend.

It should also be noted that MSCI is the unquestioned leader in sustainable indexing, with around two-thirds of global assets invested in sustainable funds tracking an MSCI benchmark. As the world's largest ESG research provider, MSCI dominates over FTSE (6% of the global market) and Germany's Solactive (just under 6%).[8]

Selecting a partner

Broadly, when individuals and institutions seek to engage an asset manager in order to access passive sustainable funds, the same considerations apply as to all other forms of investment – you want a track record of performance and trustworthiness.

However, ESG investing requires a more comprehensive and in-depth approach. The right asset manager is one with an established framework that provides clear criteria for identifying and classifying investments by sustainability level. A robust ESG framework will be aligned with criteria set out in relevant legislation (the European Union being a leader in this sphere) as well as industry-recognized best practices.

Passive investing also facilitates engagement

Active ownership means that asset managers exercise their mandate via engagement and proxy voting in the interest of their clients, regardless of whether the underlying investment is an active or passive one. Contrary to what the name might suggest, passive sustainable funds are by no means passive as concerns engagement with the management of investee companies. ETFs, as long-term index-based investments, give investment managers the freedom to pursue sustainability goals with the same tools they use when managing active investments.

Passive sustainable investments to remain prominent

By combining the advantages of passive investments with a strong ESG focus, passive sustainable funds are poised to continue gaining in prominence. Increasing opportunities for investment vehicles designed to tailor exposure for demanding and ESG-conscious investors are sure to push asset flows even higher, thus giving reason to assume that there is a bright future ahead for them in the face of growing interest.

[4] *Nagy/Kassam/Lee (2015); Giese/Lee (2019)*
[5–8] *Morningstar report*

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