In our Topical News section, we bring you extracts from a recently published article by Morgan Stanley (13th October 2023) , which gives us an insight into the key trends for sustainable investing.

Morgan Stanley (2023) in its recent web report, summarizes that sustainable investing is facing a period of new strategic thinking for business, increased demand for more sustainable resources, and a heightened regulatory environment:

Key takeaways

- Expect a greater diversity of sustainable investing strategies across assets and themes, partly driven by growth trends among Millennial investors.
- The net-zero transition will change approaches to land use, in order to satisfy demand for renewable power, metals and minerals and nature-based solutions.
- A proliferation of regulations and voluntary standards across the world will reshape corporate strategies, disclosures, and availability of data.

(Morgan Stanley 2023)

According to Morgan Stanley (2023), assets under management (AUM) for sustainable equity and fixed-income funds reached a record 7.9% of global total AUM in the first half of 2023, reflecting the growth in and adoption of sustainable finance globally:

> When Morgan Stanley started the Institute for Sustainable Investing to accelerate the growth and adoption of sustainable finance, few market participants understood its importance for the environment, society, and corporate bottom lines. Today, as the Institute marks its 10th anniversary, sustainability is reshaping investing: Assets under management (AUM) for sustainable equity and fixed-income funds reached a record 7.9% of global total AUM in the first half of 2023.

But the urgency for even more capital at scale to finance innovative sustainability solutions is clear, as companies race toward a net-zero energy transition and demand grows to finance additional and interrelated issues important to global economies, such as gender equity or ocean conservation. In the coming decade, investors and companies will need to tackle the increasingly complex terrain of sustainable finance in order to make informed decisions, mitigate risks and seize emerging investing opportunities. “Navigating the Next Decade: 10 Demand Signals for the Next 10 Years of Sustainable Finance,” the most recent report from the Institute, highlights many of these trends, including:

1. the growing diversity of sustainable investing products and strategies.
2. surging demand for land, minerals, and new technologies to facilitate the net zero transition.
3. increasing global government regulations that will affect corporate playbooks, disclosures, and data.

(Morgan Stanley 2023)

Current trends point to greater diversity in sustainable investing, both in terms of investor profile and demographics, and the types of companies and projects targeted for investment. The Morgan Stanley (2023) website expands on these developments, highlighting the growth in demand from millennial investors:

Demand from Millennial investors—paired with new government incentives and regulations—will likely fuel the presence of sustainable investing in new asset classes and themes in the next 10 years. Essentially, all surveyed U.S. Millennials (99%) indicated they were interested in sustainable investing, according to a 2021 report from the Institute. If that demographic follows through on its intention to invest, there will likely be a greater breadth of solutions across the market.

At the same time, sustainable investment opportunities are likely to branch out from public markets to other areas such as private equity. Private equity investors may seek growth opportunities with sustainable brands, which 62% of younger generations in the U.S. say they prefer to buy from, as companies may seek efficiencies in energy, inputs, and materials, as well as potential acquisitions of sustainability-oriented companies.

Finally, investors should expect growing interest in themes beyond climate action. These include nature and biodiversity, transition finance (which funds companies’ transition to net zero) and inclusive finance (which offers financing to underrepresented people and communities). Social issues should also continue to gain prominence on investor agendas, with growing attention to issues such as the privacy and ethical implications of artificial intelligence; racial, gender and LGBTQ+ diversity; access to affordable housing, healthcare, and education; and the disproportionate social implications of physical climate events.

(Morgan Stanley 2023)

According to Morgan Stanley (2023), the race to a net zero carbon targets globally, will alter company strategies and divert more capital to projects targeting climate change. There will need to be a change of approach to land-use in particular, as demand for land increases as a result of the greater focus on sustainable investment, e.g., solar farms and hydro-power stations:

> The race is on to decarbonize and reach key 2030 interim targets. Companies will need to reorient business models and corporate practices, while long-term investors will need to decide how to put their capital to work to meet global climate targets. One area of focus will be ensuring productive and efficient land use with growing demand for renewable energy and conservation efforts. Hydropower and some types of solar power can require up to twice as much land needed for coal, and up to 30 times as much as gas. The amount of land used for electricity production globally could increase by 60%. As competition for land grows, companies in all industries will need to ensure they use it sustainably. To ensure long-term climate-positive outcomes, land use should include reforestation and afforestation, which involves planting trees on land not previously forested; landscape restoration; and biodiversity protection.
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> Meanwhile, demand for metals and minerals such as copper, lithium, nickel, cobalt, graphite, zinc, and rare earth metals is set to increase as demand for renewable energy expands and electric vehicle production ramps up, since a typical electric vehicle requires nearly six times more mineral inputs than a conventional vehicle. Estimates suggest that demand for these minerals could rise between two- to six-fold by 2040, generating a battle for access to limited sources of these key commodities. The rapid growth in demand could lead to a shortage of key mineral and metals unless companies increase investments in mining exploration and outputs. The Energy Transitions Commission estimates that companies would need to invest $70 billion per year through 2030 to expand supply, yet annual capital investments have averaged only $45 billion in the last two decades. Additionally, it will be important to ensure that these resources are mined sustainably, with appropriate environmental and social standards to limit the negative impact on the physical environment and local communities.
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> (Morgan Stanley 2023)

Morgan Stanley (2023) highlights how important expertise in sustainability is becoming for finance companies and professional investment communities and how regulated the area is becoming with new legislation and policy directives coming down the tracks:

> Companies should expect to navigate an increasingly complex web of regulations and policy directives aimed at driving the transition to a net-zero global economy. One that is already due to start in 2024 is the EU's Corporate Sustainability Reporting Directive, which will require more than 50,000 companies globally to disclose numerous ESG factors. Regulations will reshape the corporate playbook, ensuring sustainability is a fundamental component of business strategy, operating models, and financing plans.
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> For investors, more robust corporate ESG disclosures means that specific and standardized information will be in the public domain to use when evaluating a company's sustainability performance, including around revenues, corporate practices, and supply chains. ESG data will likely also improve significantly as modelling techniques using artificial intelligence are applied to the space.
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> This evolution will likely require more sustainability-focused finance professionals at companies and in the investing community. Demand for sustainability skills in finance has soared, with a remarkable 17% increase in hires between 2021 and 2022 in the U.S. and EU. But there remains a critical talent gap, and in some cases, companies are already starting to pay talent premiums for people with ESG and sustainability skills.
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> (Morgan Stanley 2023)

Morgan Stanley (2023) concludes that the road ahead will be challenging for business and investors alike if they are to meet net zero targets in the next 10 years. They note that there is a lot of work still to be done and stress how stakeholders must come together to overcome obstacles for a sustainable and financially sound future:

> Though companies and investors understand that making the global economy more sustainable and inclusive will be a priority in the next 10 years, it will not be an easy route ahead. All stakeholders will need to collaborate to find appropriate ways to finance the transition in a manner that considers the complex interdependencies of many key environmental and social issues.
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> (Morgan Stanley 2023)

References

Morgan Stanley (2023) 'Trends for the Next Decade of Sustainable Investing', October 13th.
Available at: https://www.morganstanley.com/ideas/sustainable-investing-10-year-outlook (Accessed 26 October 2023).