

Press Release

London, Nice, Paris, March 30, 2021

New EDHEC-Risk Institute paper explores the impact of ESG factors on risk and return of sovereign bonds

In the last decade, sustainable and responsible investing have become more important and gained in popularity among investors. With global ESG assets in mutual funds and ETFs doubling in the five years to June 2020¹ and reaching almost USD 1.7 trillion by the end of 2020,² there is growing recognition that the financial system has a crucial role to play in the transition to a low-carbon and climate-resilient economy.

In a new publication titled “Measuring and Managing ESG Risks in Sovereign Bond Portfolios and Implications for Sovereign Debt Investing”, EDHEC-Risk Institute, with the support of Amundi ETF, Indexing & Smart Beta, **develops a formal framework for incorporating environmental, social and governance (ESG) criteria into risk management and investment decisions involving sovereign bonds.**

The main objective is to assess whether it is possible to incorporate ESG constraints through a significant improvement of the portfolio ESG score without a substantial increase in absolute and relative risk budgets, or a substantial decrease in expected performance.

The authors of the study draw four major conclusions:

1. Higher environmental scores for developed countries and higher social scores for emerging countries are associated with lower costs of borrowing for issuers and consequently with lower yields for investors.
2. Negative screening leads to more diversified portfolios and lower levels of tracking error, while positive screening leads to higher levels of improvement of ESG scores, at the cost of an increase in absolute and relative risk budgets.
3. A dedicated focus on absolute or relative risk reduction at the selection stage allows investors to reduce the opportunity costs along the dimension that is most important to them.
4. ESG momentum strategies in sovereign bond markets can be used to further reduce some of the aforementioned opportunity costs.

The results suggest that sound risk management practices are critically important in allowing investors to incorporate ESG constraints into investment decisions at an acceptable cost in terms of dollar or risk budgets.

Specifically this research confirms that improvement of the ESG attributes of sovereign bond portfolios comes at a measured cost in terms of active risk, and that ESG momentum strategies can reduce opportunity costs. Ultimately this validates ESG as a significant risk management tool in sovereign bond analysis.

¹ Broadridge, *ESG: Transforming asset management and fund distribution*, September 2020

² FT.com, *ESG funds defy havoc to ratchet huge inflows*, 6 February 2021

Commenting on this research, Lionel Martellini, Professor of Finance at EDHEC Business School and Director of EDHEC-Risk Institute, said “This paper contributes to the ESG-investing literature on the importance of ESG considerations across asset classes by exploring the impact of ESG factors on the risk and return of sovereign bonds from an investor perspective and, in particular, investigating how to measure and manage ESG risks in sovereign bond portfolios and their implications for sovereign bond portfolio strategies.”

Commenting on the results of the survey, Laurent Trottier, Global Head of ETF, Indexing and Smart Beta Management at Amundi, said “Supporting EDHEC-Risk Institute on this research harnesses Amundi’s expertise in fixed income indices and leadership in sustainable investing. With passive investors increasingly seeking to incorporate ESG into their fixed income allocations, this research identifies important practical implications which address sovereign bond investors’ need for a more systematic approach to determining their exposure and the potential investment risk of ESG factors.

You can access an exclusive 2-page summary of the publication outlining the authors’ main insights here: <https://risk.edhec.edu/measuring-and-managing-esg-risks-sovereign-bond>

You can access the full publication here: “[Measuring and Managing ESG Risks in Sovereign Bond Portfolios and Implications for Sovereign Debt Investing](#)”.

This research was supported by Amundi as part of EDHEC-Risk Institute’s “ETF, Indexing and Smart Beta Investment Strategies” research chair.



Contact:

For more information, please contact: **Maud Gauchon**

Tel.: +33 493 187 887 – E-mail: maud.gauchon@edhec-risk.com

Visit our web site: <https://risk.edhec.edu>

About EDHEC-Risk Institute

Academic Roots & Practitioner Reach

Since 2001, EDHEC Business School has been pursuing an ambitious policy to produce academic research that is both practical and relevant. This policy, known as “Research for Business” and now labelled “Make an Impact”, aims to make EDHEC an academic institution of reference in a small number of areas in which the school has reached critical mass in terms of expertise and research results.

In 2001, EDHEC Business School created EDHEC-Risk Institute, a premier academic centre for industry-relevant research in investment management, which has developed a portfolio of research and educational initiatives in the domain of investment solutions for institutional and individual investors.

The institute, in partnership with industry leaders, boasts a team of permanent professors, engineers and support staff, as well as affiliate professors and research associates. They have gained very significant expertise in the areas of **retirement investing** and **sustainable investing**. Its philosophy is to validate its work by publishing in international academic journals, as well as to make it available to the sector through position papers, published studies, online courses, on-campus workshops and global conferences.

To ensure the dissemination of its research to the investment industry, EDHEC-Risk also provides professionals with access to its website, <https://risk.edhec.edu>, which has more than 120,000 visitors and is devoted to asset and risk management research, with a focus on investment solutions. Finally, its quarterly newsletter is distributed to over 100,000 readers.

Building on the cutting-edge research of the faculty, EDHEC-Risk Institute creates programmes to help executives level up their financial expertise on topics of considerable interest in the asset management industry: factor investing, goal-based investing, sustainable investing, data science and machine learning.

EDHEC-Risk's mission is to give participants an edge in today's fast-changing landscape, with programmes designed to guide them towards converting theoretical concepts into practical results. Courses are run in different formats to match the market's needs: 100% on line, on-site, blended or bespoke programmes. To date, 2,500 professionals have chosen EDHEC-Risk Institute to help them address their challenges.

As part of its policy of transferring know-how to the investment industry, EDHEC-Risk Institute set up Scientific Beta, an original initiative to boost the take-up of the latest advances in smart beta design and implementation by the whole investment industry. On 31 January 2020, Singapore Exchange (SGX) acquired a majority stake in Scientific Beta, a transaction that vindicates the school's "Make an Impact" model and its focus on producing research that is useful for both students and businesses.

EDHEC-Risk Institute also contributed to the launch of EDHEC Infrastructure Institute (*EDHECinfra*), a spin-off dedicated to benchmarking private infrastructure investments. *EDHECinfra* is now a provider of research and indices on unlisted infrastructure investments.

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EDHEC-Risk Institute
393 promenade des Anglais
BP 3116 – 06202 Nice Cedex 3
France
Tel: +33 493 187 887

EDHEC-Risk Institute – Europe
10 Fleet Place, Ludgate
London EC4M 7RB
United Kingdom
Tel: + 44 207 332 5600

About Amundi

Amundi, the leading European asset manager, ranking among the top 10 global players³, offers its 100 million clients – retail, institutional and corporate – a complete range of savings and investment solutions in active and passive management, in traditional or real assets.

With its six international investment hubs⁴, financial and extra-financial research capabilities and long-standing commitment to responsible investment, Amundi is a key player in the asset management landscape.

Amundi clients benefit from the expertise and advice of 4,700 employees in nearly 35 countries. Created in 2010 and listed on the stock exchange in 2015, Amundi currently manages nearly €1.700 trillion⁵ of assets.

Amundi ETF, Indexing and Smart Beta

With more than €158 billion* in assets under management, Amundi ETF, Indexing and Smart Beta is one of Amundi's strategic business areas and is a key growth driver for the Group.

Amundi ETF, Indexing and Smart Beta business line provides investors – whether institutionals or distributors – with robust, innovative, and cost-efficient solutions, leveraging Amundi Group's scale

³ Source IPE "Top 500 asset managers" published in June 2020 and based on AUM as of end December 2019

⁴ Boston, Dublin, London, Milan, Paris and Tokyo

⁵ Amundi data as at 31/12/2020

and large resources. The platform also offers investors fully customized solutions (ESG, Low Carbon, specific exclusions, risk constraints, etc.).

With over 30 years of benchmark construction and replication expertise, Amundi is a trusted name in ETF & Index management among the world's largest institutions. The team is also recognized for its ability to develop Smart Beta & Factor Investing solutions, with a more than 10-year track-record.

*All figures and data are provided by Amundi ETF, Indexing & Smart Beta as of end December 2020