New York Life Investments
Guide to Sustainable Investing
REACHING YOUR GOALS BY INVESTING FOR GOOD
WHAT IS SUSTAINABLE INVESTING?

In recent years, “sustainable investing”—meaning investment strategies that incorporate environmental, social, and governance (ESG) factors alongside traditional financial analysis—has grown considerably in attention and assets under management (AUM). According to a 2018 study, more than $12 trillion in assets in the U.S. alone were managed in a sustainable process, compared to $639 billion in 1995.1 Many strategies fall under the term “sustainable investing,” although there’s an almost dizzying number of other names, including “responsible investing,” “impact investing,” “ethical investing,” “green investing,” “mission-related investing,” and “values-based investing,” among others. While each approach has nuanced differences, for our purposes, we’ll use the umbrella term “sustainable investing” to refer to these strategies, as that appears to be the broadest and most accepted name for this category in the industry. Here we will explore the evolution of sustainable investing, the advent of “ESG integration” and look to the road ahead.

THE ORIGINAL APPROACH: SOCIALLY RESPONSIBLE INVESTING (SRI)

“SRI” (or “socially responsible investing”) strategies generally follow an exclusionary approach—eliminating exposure to certain sectors or companies involved in businesses such as tobacco, alcohol, gaming, and weapons, or avoiding all exposure to companies in specific countries. This approach has a long history that extends back to at least the 18th century, as religious groups sought to align their investments with their worldview. For instance, the Methodists and Quakers refused to invest in entities affiliated with the slave trade. In more recent times, it’s generally acknowledged that the widespread boycotts of South African companies during the 1970s and 1980s helped end Apartheid. Broadly speaking, modern SRI approaches are considered exclusive, or negative, as they rely on screens to filter out categories of investments that an investor wishes to avoid in their portfolio. Investment performance is often not the main objective of this approach. Rather, investors generally want to avoid investing in companies that do not align with their values or ethics, and the decision to avoid specific sectors and countries aims both to do good in terms of social impact, as well as to serve as a prudent investment decision.
THE NEXT EVOLUTION: ESG INVESTING

“ESG,” which stands for “environmental, social, and governance,” entered the mainstream in 2005 as part of a United Nations-sponsored initiative, which served as the first step in establishing environmental, social, and governance as key components of analysis, processes, and decision-making in investment management. While SRI investing takes a primarily exclusionary approach—seeking to avoid sectors or countries—ESG investing is an inclusionary approach based on the idea that companies with strong environmental, social, and governance practices may provide a source of long-term value that cannot be captured by traditional financial analysis. To oversimplify, SRI generally represents the past approach to sustainable investing, while ESG integration represents the present.

While SRI strategies may have missed opportunities if they excluded “bad” sectors or countries that happened to perform strongly, ESG strategies tend to seek out “good” companies that embrace positive environmental, social, and governance factors as another alpha source. Investment managers following an inclusive ESG approach aim to capitalize on the idea that “good” companies can help their clients do well.

What does ESG stand for?

Since ESG investing is comprised of a range of issues, below is a general summary of what each term entails:

**Environmental**—Issues relating to the quality and functioning of the natural environment, including areas such as: greenhouse gas (GHG) emissions, climate change, renewable energy, energy efficiency (i.e. air, water or resource depletion, or pollution), and waste management.

**Social**—Issues relating to the rights, well-being and interests of people and communities, including areas such as: human rights, labor standards, workplace health and safety, employee relations, diversity, consumer protection, and controversial weapons.

**Governance**—Issues relating to the governance of companies and their stakeholders, including topics such as: board structure, size, diversity, skills, and independence (i.e. executive pay; shareholder rights; stakeholder interaction; disclosure of information; business ethics; bribery and corruption; internal controls and risk management).

Source: Adapted from the United Nations Principles for Responsible Investing (UNPRI).
THE ROAD AHEAD: IMPACT AND THEMATIC INVESTING

Impact investing (sometimes referred to as “II”) is an extension of ESG investing and a growing area of interest for investors. Impact investing goes a step further in that impact investments are made with the explicit intent to generate positive, measurable social and environmental effects in addition to a financial return. According to the Global Impact Investing Network, the impact investing universe represented more than $500 billion in assets globally at the end of 2018. Examples of impact investing include “green bonds,” which may fund projects that aim to combat global warming and “social bonds,” whose proceeds are dedicated to projects aimed at improving social welfare or helping disadvantaged populations, among other initiatives. Thematic investing, which is investing along broad macroeconomic trends across sectors, can sometimes overlap with impact investing. Thematic trends are often aligned with ESG themes—for example, a thematic fund focused on climate change could invest in companies involved in renewable energy, recycling, or that have lower carbon emissions. While impact investing represents a relatively small portion of the global investment universe, there’s a lot of room for these assets to grow.

Impact investing also encompasses thematic ESG investing, which focuses on effecting change through broader macroeconomic themes—for example, a fund which invests in companies, across sectors, that contribute to fighting climate change.

Sustainable investing uses various approaches

<table>
<thead>
<tr>
<th>Negative Selection</th>
<th>Positive Selection</th>
<th>Positive Selection</th>
<th>Purpose</th>
</tr>
</thead>
<tbody>
<tr>
<td>Negative Screening</td>
<td>ESG Integration</td>
<td>Best-in-class Screening</td>
<td>Thematic / Impact Investing</td>
</tr>
<tr>
<td>Exclude companies in controversial industries and/or companies that don’t meet societal or environmental norms</td>
<td>Consider ESG factors in financial selection and investment decisions</td>
<td>Select the highest-rated ESG companies in their sector</td>
<td>Target investments aiming for social or environmental good alongside financial returns, often aligned with ESG themes</td>
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Engagement: Direct private dialogue with companies; shareholder activism

Source: New York Life Investments
WHY SUSTAINABLE INVESTING NOW?

After several years of steady growth, sustainable investing is now part of the financial mainstream. Initially adopted in Europe, U.S. institutional investors have blazed the trail on this side of the pond over the years. For instance, in 2001 the California Public Employees' Retirement System (CalPERS) voted to divest from tobacco company stocks in its portfolio. Public pension plans in states ranging from California to New Jersey have considered excluding companies in entire countries—such as Brunei, Cuba, Iran, Saudi Arabia, Sudan, and Turkey—from their portfolios due to poor human rights records and potential ties to terrorism.

Now individual investors have many options when committing assets to ESG strategies. The number of new ESG funds launched in 2018 (both open-end and exchange-traded funds) was at an all-time high. Total assets invested in these types of strategies reached record levels in 2019.

Sustainable strategies have shown strong growth in AUM and positive asset flows

ESG STRATEGIES MAY OFFER GREATER RETURN POTENTIAL

The most common objection investors cite for avoiding sustainable investment solutions is concerns about performance. This “performance trade-off” myth — the perception that investors must sacrifice returns in order to invest following ESG principles — is a deeply entrenched misconception about sustainable investing. Recent returns for sustainable investment strategies are challenging this notion. For example, in 2018, a majority of ESG funds ranked in the top half of their Morningstar category for total return. In addition, 41 of 56 Morningstar ESG categories (73%) outperformed their non-ESG counterparts in 2018. In fact, there is growing evidence that ESG strategies can help mitigate volatility in negative markets, suggesting that characteristics such as sound governance, sustainable practices, durable supply chains, and a focus on environmental factors can help companies perform well in a market downturn and build resilience in investor portfolios.

41 of 56 Morningstar ESG categories (73%) outperformed their non-ESG counterparts in 2018

<table>
<thead>
<tr>
<th>Quartile</th>
<th>All Funds</th>
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<th>Fixed-income</th>
<th>Allocation/alternatives</th>
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Source: Morningstar Direct, 12/31/18.
**SUSTAINABLE STRATEGIES ARE AVAILABLE ACROSS ASSET CLASSES**

Many investors think a sustainable approach is limited to equity investing, but in reality, other asset classes are increasingly incorporating ESG analysis into the investment process. As shown below, more than half of global sustainable assets were in publicly listed equities, and as of 2018, fixed-income assets represented more than a third of these assets. Alternative assets, including real estate, private equity, venture capital, and hedge funds, among others, represent more than 10% of sustainably managed assets.8

**Integration of global sustainable investments across asset classes (as of 2018)**

![Pie chart showing asset allocation]

Source: Global Sustainable Investment Alliance, “2018 Investment Review.” NOTE: “Other” includes hedge funds, cash, commodities, infrastructure, and unclassified assets. It does not include asset breakdown for Australia and New Zealand.

Due to the vast size of the overall market, fixed income could offer the largest growth area for sustainable investing. While fixed-income assets managed following ESG guidelines still lag their equity counterparts, the recent growth of green bonds suggests expansion potential in this area. According to Bloomberg, $580 billion in green bonds were sold through 2018, with another $170–$180 billion estimated in 2019.4 While these totals represent a fraction of the vast fixed income universe, there is significant room for growth ahead.
OUR APPROACH TO SUSTAINABLE INVESTING

With over $550 billion in assets under management, New York Life Investments offers clients access to specialized, independent investment teams through our family of affiliated boutiques. Our multi-boutique business model is built on the foundation of a long and stable history, which gives our clients proven historical performance while managing risk through multiple economic cycles. With capabilities across virtually all asset classes, market segments, and geographies, our family of specialized, independent boutiques and investment teams allows us to deliver customized strategies and integrated solutions for every client need.

Our goal is to align with the six principles of the Principles for Responsible Investing (PRI) (unpri.org) and implement an investment approach that incorporates ESG factors into the decision-making process to manage risk and generate sustainable, long-term returns.

■ **We agree that:**
  
  — Including ESG factors in the decision-making processes provides us with even greater flexibility in ensuring that all relevant investment considerations are accounted for when assessing risk and return

■ **ESG-factor considerations may vary across our subadvisors and can include one or more of the following***:
  
  — Integrating ESG information into quantitative and qualitative analysis, which could result in making adjustments to areas as: selection, weighting, or asset allocation
  
  — Engaging with investee companies/entities about the ESG considerations identified as relevant to them—either individually or alongside other investors
  
  — Encouraging investee companies/entities to disclose information about ESG-factor considerations that do or could affect them
  
  — Monitoring overall ESG risk within the portfolio, including climate-related risks when reasonable
  
  — Contributing to the shaping of investor-relevant public policy and advocacy about ESG-related issues; and promoting wider understanding and use within the investment industry

*This list is not exhaustive
OUR ESG SOLUTIONS

At New York Life Investments, we understand there is not a one-size-fits-all approach to sustainable investing, which is why we offer a diverse set of ESG solutions that utilize a variety of approaches to sustainable investing, ranging from basic ESG consideration to direct impact investing.

A broad spectrum of ESG approaches can fit diverse investor profiles

**ESG Consideration**
- ESG consideration described in prospectus or investment objective
- ESG one of various factors driving investment decisions

**ESG Focus**
- ESG tilt to portfolio using full integration
- May use exclusions
- May engage in active ownership

**Sustainable Sector**
- Focus on “green economy” industries:
  - Renewables
  - Energy efficiency
  - Environmental services
  - Water
- May engage in active ownership

**Thematic/Impact Investing**
- Impact investments aim for social or environmental good alongside financial returns
- Thematic investments aligned with broad trends, often with ESG themes
- May engage in active ownership
## OUR SOLUTIONS

<table>
<thead>
<tr>
<th>ESG category</th>
<th>Fund</th>
<th>Negative selection</th>
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<th>Purpose</th>
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The content displayed above is subject to change. Please note that other asset managers/investors may categorize their products differently than what is displayed above.
5. Source: Randy Diamond, “CalPERS Decision to Divest from Tobacco is Costly,” Chief Investment Officer, 12/12/18.

**DEFINITIONS**

*Alpha* is the term used in investing to describe a strategy’s ability to beat the market or provide excess return.

**ABOUT RISK**

Consider the Funds’ investment objectives, risks, charges and expenses carefully before investing. The prospectus, or summary prospectus, and the statement of additional information include this and other relevant information about the Funds and are available by visiting IQetfs.com or calling (888) 474-7725 for IndexIQ ETFs and by calling 800-624-6782 for MainStay Funds®. Read the prospectus carefully before investing.

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