Forging Hong Kong into an ESG Metropolis and a Zero-carbon Economy

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Recent years have seen Environmental, Social, and Governance (ESG) become a hot topic around the world. With various financial markets subject to the impact of the turbulent times, driven by the lust for high interest return, Hong Kong people have been flocking to buy green bonds. But how much do they actually know about the underlying meaning and economic effect of these such bonds?

This article attempts to explore Hong Kong's path to becoming a green financial centre in the following three areas: 1) Can sustainable financing create shareholder value? 2) the key to turning Hong Kong into a green financial centre; and 3) how can green financing be the way forward for the local young generation?

Triple-win strategy for companies, society, and citizens

ESG criteria refer to the decision making process integrating environmental, social, and governance factors into a company's holistic actions. Many companies used to believe that ESG and green initiatives were merely beneficial to society and the environment, thus regarding them as resource consumption and business expenses; quite the contrary, ESG and green finance can be sustainable investments.

As a business strategy, ESG is conducive to winning the battle for talent, establishing customer relationship, creating sound bites on social media, extending care and support to local communities, and cooperating with regulating authorities. All these are particularly important amid calls for wealth equality and common prosperity these days. Professor Theodore Levitt of Harvard Business School points out that the ultimate purpose of a business is to "get and keep" customers. To this end, companies must offer products or services to the satisfaction of customers so as to make consumers dependent on the products or services. What sets ESG apart is that it helps to maintain such a competitive edge, which not only involves an all-out marketing effort to drive home to consumers the merits of the products or services but also the alignment of the values and expectations of consumers with those of the company. At the same time, it is also designed to actively craft a positive corporate image in the eyes of the general public.

Hong Kong being Asia's third largest and the world's fifth largest securities market, recent years have seen a surge in debt-raising activities there, followed by the trend of green and sustainable financing. Featuring green bonds as a major financing tool for public institutions and private companies, the trend also covers better-known examples such as green bonds issued by the Airport Authority to fund the third runway development, green bonds launched by the MTR Corporation in connection with its new railway projects, etc. ESG evaluation has also been incorporated by the Hong Kong Exchanges and Clearing Limited (HKEX) as part of the Listing Rules while ESG reporting practices comprise the twin components of "Comply or explain" and "Recommendations". In other words, companies listed in Hong Kong should comply with the reporting requirements and disclose any non-compliance issues.

ESG as an asset rather than liability

In the deglobalization era, the business environment has been in a state of chaos. Being more active than ever searching for new directions and purpose, companies continuously evolve to survive and to transform. According to the Business Case for Purpose survey conducted by Harvard Business Review Analytic Services in 2015, there is a general consensus among senior business executives in the US that the fast-changing concept of purpose must go beyond shareholder value. Over 80% of executives surveyed believe that they share the same purpose with their employees; if the focus is not just on profit, they will have greater success in transforming their companies, more dedicated employees and loyal customers, as well as greater capabilities to innovate and transform. However, only less than half of companies surveyed are actively searching for a new purpose.

Many young people are willing to earn less to get a meaningful job so that they can make contributions to society while making a living. In this connection, companies committed to corporate social responsibility have lower staff turnover rates and are in a better position to help resolve the issue of youth employment. There are also research findings that, compared with similar companies without ESG, those with ESG tend to have higher stock value and better performance in cash flow and risk rating. While it is hard to prove "chicken or egg first", ESG criteria seem suitable as indicators of a company's management performance and can create value for shareholders.

Moreover, thanks to the support of ESG-oriented funds of ESG-tracking companies and that of Assets under Management (AUM), ESG-friendly stocks are in short supply, with prices soaring as a result. As pointed out by a report of Bank of America Merrill Lynch in 2019, over the preceding five years, ESG-related AUM has registered the highest growth among asset management strategies, boasting a CAGR (compound annual growth rate) of over 70%. Research by Allianz Global Investors indicates that as of 2020, ESG AUM is valued at more than US$35 trillion, i.e. for every US$100 worth of AUM, US$30 are ESG-related.

Take the MTR Corporation for example (declaration of interests: the authors have no collaborative relationship with the company). As per the disclosure requirement under the Environmental, Social, and Governance Reporting Guide, a sustainability report was also published together with the company's 2021 Annual Report. In addition, referencing the Global Reporting Initiative (GRI) Standards and the United Nations Sustainable Development Goals, the company has also set forth three primary objectives, namely Social Inclusion, Advancement and Opportunities, and Greenhouse Gas Emissions Reduction in order to coordinate ESG-related work.

In April 2021, the MTR Corporation released its Sustainability Report, which demonstrates improvements in several areas. For example, compared with 2020, water usage was reduced by 5% while the share of persons with disabilities employed rose from 3.4% to 3.7%. Although ESG arrangements in these areas are not at the forefront of profit generation, they help to mitigate the potential adverse consequences from different stakeholders and therefore will enhance the sustainability performance of long-term finance.

Furthermore, the rail giant also makes use of green financial products to create value added for its shareholders. As of the end of 2020, the company has issued a total of

15 green bonds, incorporating ESG into its financing and decision-making processes. For the majority of financing entities, the interest rate of issuing green bonds, which is less than that of issuing plain vanilla bonds, helps to reduce the financing costs. At the same time, since green financing requires companies to have certain ESG-friendly measures in place, green finance can bring about social value in addition to shareholder value. For instance, thanks to the environmentally-friendly design of the MTR Corporation's South Island Line (East), carbon emissions along the line are reduced by approximately 21,000 tonnes on an annual basis, thus contributing to the zero-carbon economy.

As another example, Standard Chartered Bank has launched a Sustainable Savings Account, which pledges to use the savings to support environmentally-friendly and sustainable development projects, including green finance and sustainable infrastructure. Through the Account, which offers a higher interest rate per annum, investors can benefit environmental conservation and society in the process of pursuing return on investment. Standard Chartered will be able to burnish its corporate image by capitalizing on the business opportunities that come with green finance, which appeal to new customers from the Z generation and the millennials. Coupled with higher-yielding investment in renewable energy and climate change new projects, this initiative will generate environmental benefits for the wider community and, as a result, achieves a triple-win result.

Towards transforming into a green financial hub

As one of the pioneering green-bond markets, Hong Kong is Asia's first signatory to the Green Bond Pledge, testifying to the SAR Government's environmental commitment.

For policymakers, requiring more ESG-related disclosures has become the order of the day for banks and financial investments around the world. Regulators should encourage more companies (both listed and unlisted) to make ESG disclosures part of their business strategy, reach out to the international market, and attract foreign investments. Hong Kong, as the nation's super-connector, should also contemplate how to bring in capital for the green finance listing of Mainland enterprises overseas.

With Hong Kong developing into a sustainable financing and economic centre, green finance as an emerging sector will enjoy ample opportunities in Asia. This will be conducive to good employment prospects characterized by upward social mobility and SAR's economic transformation.

There will be more companies looking to run on the sustainable-finance racetrack, where green finance, green investment, ESG reporting and auditing, community relations, and corporate social responsibility in supply chains, etc. will need a large pool of ESG professionals. According to the latest report of the International Renewable Energy Agency published in 2020, the renewable energy industry has created as many as 11.5 million jobs worldwide. It also predicts that employees in the sector will grow to 42 million by 2050. The HSBC Sustainable Financing and Investing survey 2021 reveals that 40% of institutional investors in Asia are held back from pursuing ESG-based investing because of a lack of expert knowledge or qualified talent while the share of Asian investors with ESG investments or policies — at just 39% — lags behind that in Europe and the US at 91% and 72% respectively. Should the younger generations be able to take advantage of the emergence of the sector, they will stand to gain promotion opportunities.

To build Hong Kong into a green financial centre, we recommend implementing the following measures:

1) Bringing in more open-fund-type companies and attracting a variety of private equity funds to establish and operate in Hong Kong.
2) As the primary market regulator, the SAR Government should advocate reduction in management fees for various mutual funds and Exchange Traded Funds (ETFs). Compared with mature green financial markets in Europe and the US, where the fee is usually below 1%, many of the green funds and ETFs in Hong Kong lack attraction due to their charge of more than 1%.
3) Building an official carbon-market platform, making use of Hong Kong's role as an international financial centre to provide professional ESG and "comply

or explain" standards and audits as well as matchmaking services for international investors and Mainland enterprises.

4) Accelerating the education and nurture of ESG and green financial talent. While there is no lack of companies looking to tap into ESG-related opportunities, there is a shortage of professionals who meet official standards or the market requirements.

If Hong Kong is able to ride on the ESG and green-finance trend, creating more new jobs allowing for high social mobility for our younger generations and consolidating its status as an international financial centre along the way, it will stand to steadily advance towards a sustainable green economy.