The State of ESG in Asia

July 31, 2019

Over the last ten years, environmental, social and governance (ESG) factors have played an increasingly larger role in the investment analysis and decision-making processes for companies and private equity (PE) funds alike. Yet adoption of ESG investing in Asia has been slow, trailing far behind its Western counterparts. As shown in Exhibit 1, ESG investments as a percentage of total managed assets in 2016 was a mere 0.8% in Asia (ex-Japan) compared to 21.6% in the US and 52.6% in Europe[1]. Australia/New Zealand while situated in the Asia Pacific region, was on par with Europe at 50.6%.

Exhibit 1: ESG Investing as percent of total managed assets by region, 2012-2016

<table>
<tr><th>Region</th><th>2012</th><th>2014</th><th>2016</th></tr>
<tr><td>Europe</td><td>49.0%</td><td>58.8%</td><td>52.6%</td></tr>
<tr><td>United States</td><td>11.2%</td><td>17.9%</td><td>21.6%</td></tr>
<tr><td>Canada</td><td>20.2%</td><td>31.3%</td><td>37.8%</td></tr>
<tr><td>Australia/NZ</td><td>12.5%</td><td>16.6%</td><td>50.6%</td></tr>
<tr><td>Asia (ex-Japan)</td><td rowspan="2">0.6%</td><td rowspan="2">0.8%</td><td>0.8%</td></tr>
<tr><td>Japan</td><td>3.4%</td></tr>
<tr><td>Global</td><td>21.5%</td><td>30.2%</td><td>26.4%</td></tr>
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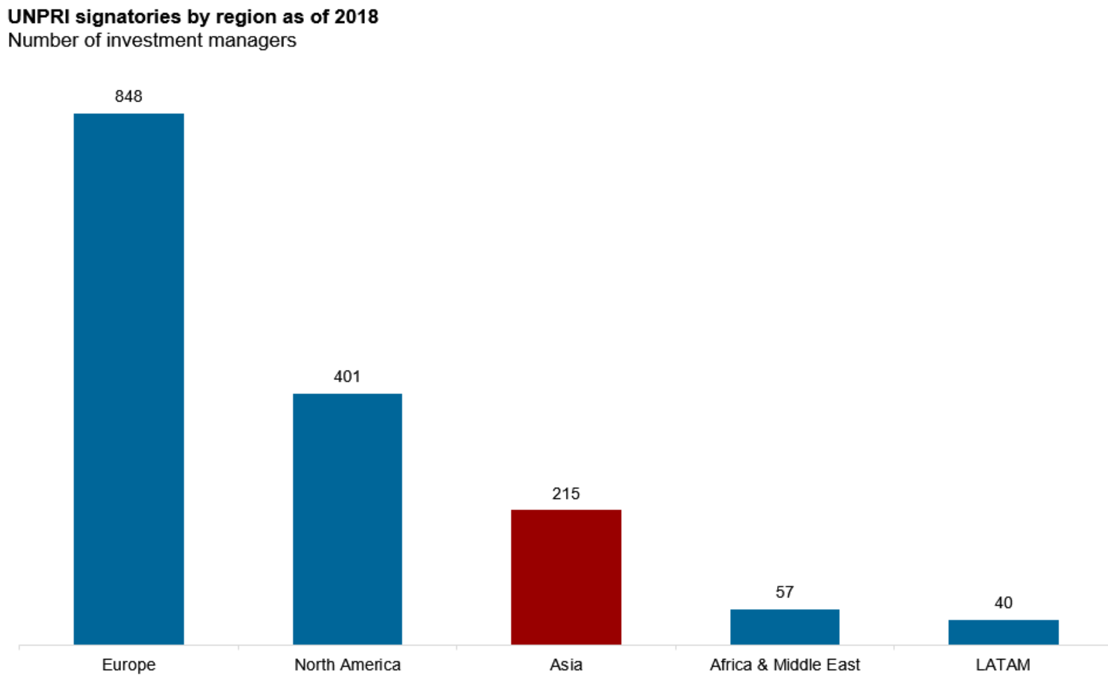
Source: Global Sustainable Investment Alliance

Japan, with 3.4%, has emerged as a frontrunner for ESG in Asia given the launch of the Japanese Stewardship Code in 2014. The Code encourages sustainable investing practices and put the spotlight on ESG for some of the larger Japanese institutional investors. Many credited this reform for pushing Japan's Government Pension Investment Fund (GPIF) to become a signatory of the United Nations-supported Principles for Responsible Investment (UNPRI), paving the way for other institutions in the region to follow suit.

While the number of fund managers who were signatories of the UNPRI grew from 1,200 in 2014 to over 2,000 in 2018[2], Asia still only makes up about 13% of the overall group. As evidenced by Exhibit 2 below, the number of investment managers who are UNPRI signatories in Asia as of 2018 is just over half of North America's and only a quarter of Europe's.

[1] "Driving ESG Investing in Asia", *Oliver Wyman* and AVPN, 2018.
[2] "Asia-Pacific Private Equity Report 2019", *Bain & Company*

Exhibit 2: UNPRI signatories by region



Source: UNPRI

Within the group of Asian investment managers (red bar), only a subset of 25% have an internally-managed private equity mandate. ESG is still considered a relatively new topic for many private equity managers in Asia.

A report from Bain & Company drives home this point:

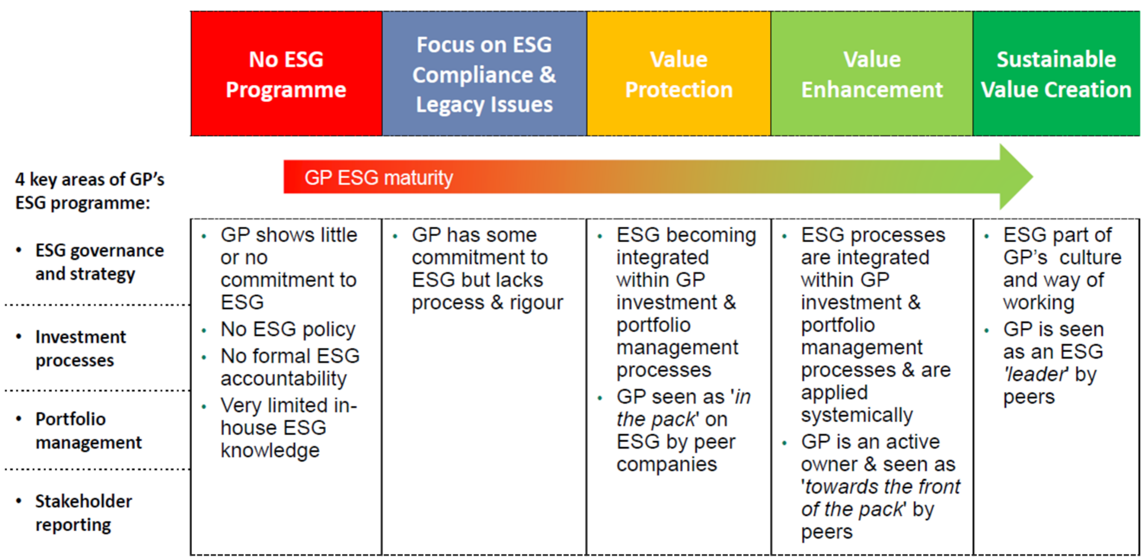
- 55% of Asian LPs still do not have an ESG investing policy for private equity
- 60% of Asian PE funds do not require their portfolio companies to report on ESG issues or responsible investment
- 13% of Asian GPs say they have fully integrated ESG considerations at the investment committee level

Axiom and ESG

As one of Asia's most local and experienced PE fund management firms, we are conscious that our investment management activities and business operations can have a positive impact on businesses, communities and the environment. As such, Axiom formalized our ESG policy on September 2017 and officially became a UNPRI Signatory in December 2017. As a signatory, Axiom commits to promoting the six UNPRI Principles (more information on the Principles can be found here: https://www.unpri.org/pri/what-are-the-principles-for-responsible-investment).

In 2019 we conducted ESG-related due diligence on our GPs in Axiom IV by evaluating their ESG policies and the degree of ESG integration within their investment decisions. GPs were then graded according to the chart in Exhibit 3.

Exhibit 3: ESG Grading Chart for GPs



We observed that 50% of our GPs had Advanced policies in ESG, 19% had Developing policies and 31% had no ESG policies at all (Exhibit 4). Moreover, we observed that our Growth and Buyout GPs tend to have more developed ESG policies compared to our VC GPs (Exhibit 5). VC GPs are generally ESG aware, but face difficulties in developing ESG policies due to the early stage nature of their portfolio companies.

For our GPs with no ESG program, Axiom encourages them to begin thinking about ESG and consider appointing a champion to drive ESG initiatives within their firm. If material ESG risks are identified during the on-going due diligence process, Axiom will require our GPs to commit to implementing appropriate measures to mitigate those risks.

Axiom recognizes that many challenges remain in the adoption of ESG considerations amongst fund managers in Asia. For many, there is still a lack of awareness about ESG and misconceptions surrounding its perceived effect on hindering financial performance. As more and more LP institutions in the region begin to incorporate ESG factors into their investment processes, this will no doubt have a trickle-down effect to the GPs and portfolio companies. Axiom commits to adopting best practices for ESG from our LPs and peers and further commits to helping educate our GPs to do the same.