ESG foundations

Responsible Investment manager survey

OCTOBER 2024

Foundations of Environmental, Social and Governance (“ESG”)

Welcome to one of four themed reports of our 2024 Responsible Investment survey of investment managers. In this report, we bring together the important foundations that an investment manager needs in order to support its responsible investment activities.

In our survey, we have focused on key foundations for managers to have a good overall approach to ESG factors. These are:

- **motivation** for their approach to ESG integration
- **investment in people** with expertise
- investment in **training to build knowledge among decision makers** that are not necessarily experts
- appropriate **oversight from senior experienced individuals**
- **analytical rigour** when using third party ESG data

These areas may not be front of mind when considering a manager’s overall responsible investment approach in a particular fund, but they underpin managers’ other responsible investment activities. It is important to pay attention to these basic foundations as part of understanding a manager’s overall responsible investment approach.

What have we found from our 2024 survey?

- **Managers are continuing to grow specialist ESG or stewardship resource**, which is a positive step in improving managers’ capabilities in the fast-moving world of responsible investment.
- Around **half of the managers give less than five hours of training on responsible investment issues to their investment professionals per year**. For an increasingly complex area that is often poorly understood by non-specialists, this is disappointingly low.
- Although there has been some improvement in the level of board oversight since our 2022 survey, we question its quality– **only 25% of managers have mandatory responsible investment training for board members** (compared to **74%** for mandatory staff training).

What should asset owners focus on when challenging managers?

- **Responsibility:** Question managers on how ESG and stewardship are implemented in their investment processes
- **Resources:** Encourage managers to increase the number of investment professionals with specialist ESG or stewardship expertise and the level of training received by non-specialists
- **Control of third party data quality:** Ask what third party ESG data managers are using, how they use third party data to assess ESG criteria, if the data is fit for purpose, and what steps they take to ensure the quality of ESG data

All statistics in this report relate to the managers that responded to our surveys. See page 8 for survey details.

Motivation for ESG integration

The vast majority of managers – broadly unchanged since 2022 at about **92%** – are carrying out ESG integration with the aim of improving long-term outcomes for clients.

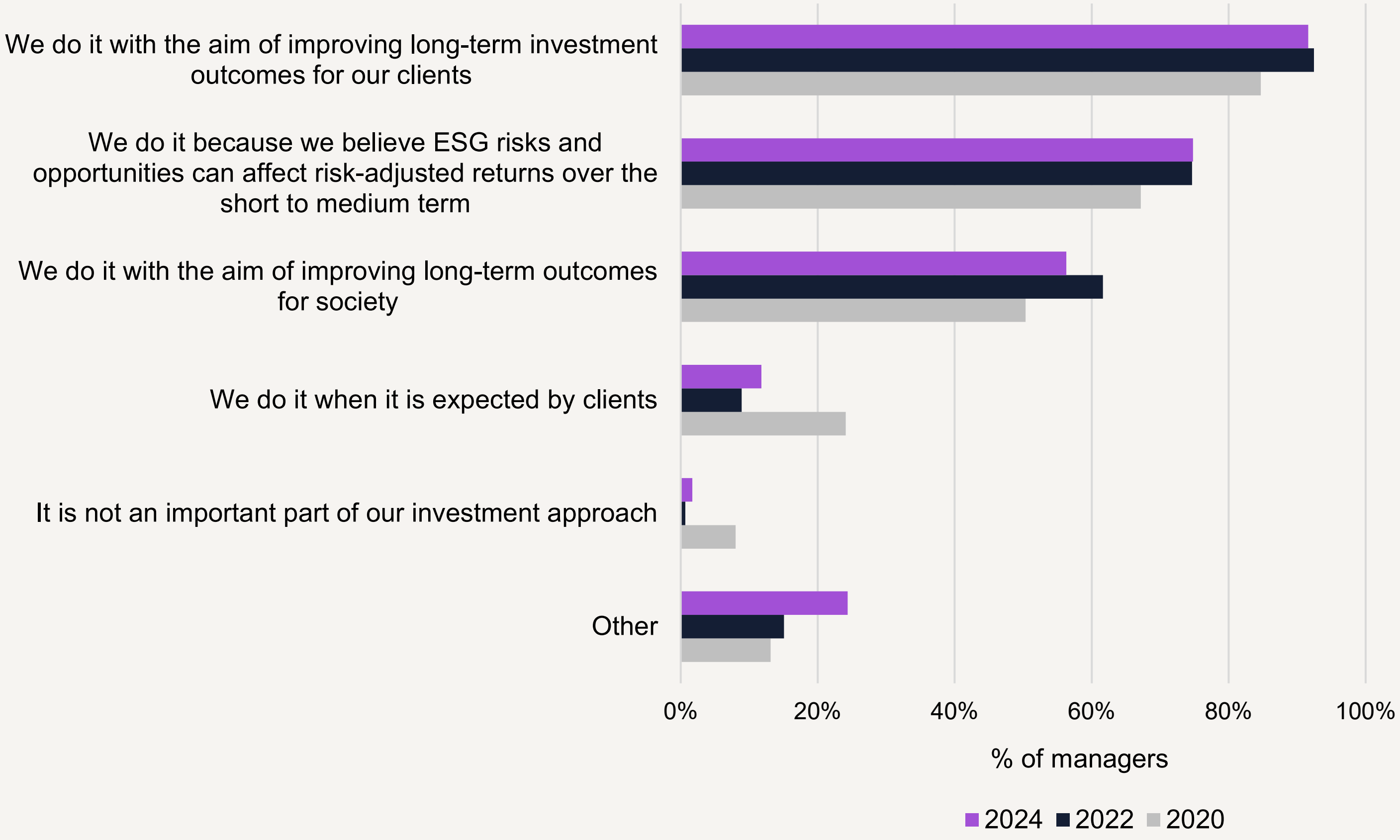
A majority of managers – unchanged at **75%** – also believe that ESG risks and opportunities can affect short to medium-term risk-adjusted returns.

Only a small proportion of managers (**12%**) integrate ESG (only) when it is expected by clients, which has halved since 2020. Encouragingly, there is only a small number of managers that don't consider ESG integration an important part of their process.

The largest shift has been a reduction in the proportion of managers that carry out ESG integration with the aim of improving long-term outcomes for society (**56%** in 2024 vs. **62%** in 2022, **50%** in 2020) (see figure 1).

This may reflect a greater focus from managers on fiduciary duty to their clients. However, are managers also considering that a bad outcome for society will likely lead to a bad long-term outcome for clients? In other words, are they thinking about how the societal impacts of their investments will have repercussions for the economy and hence future investment returns for their clients?

Figure 1: Which of the following statements describe your approach to ESG integration?



Investing in people

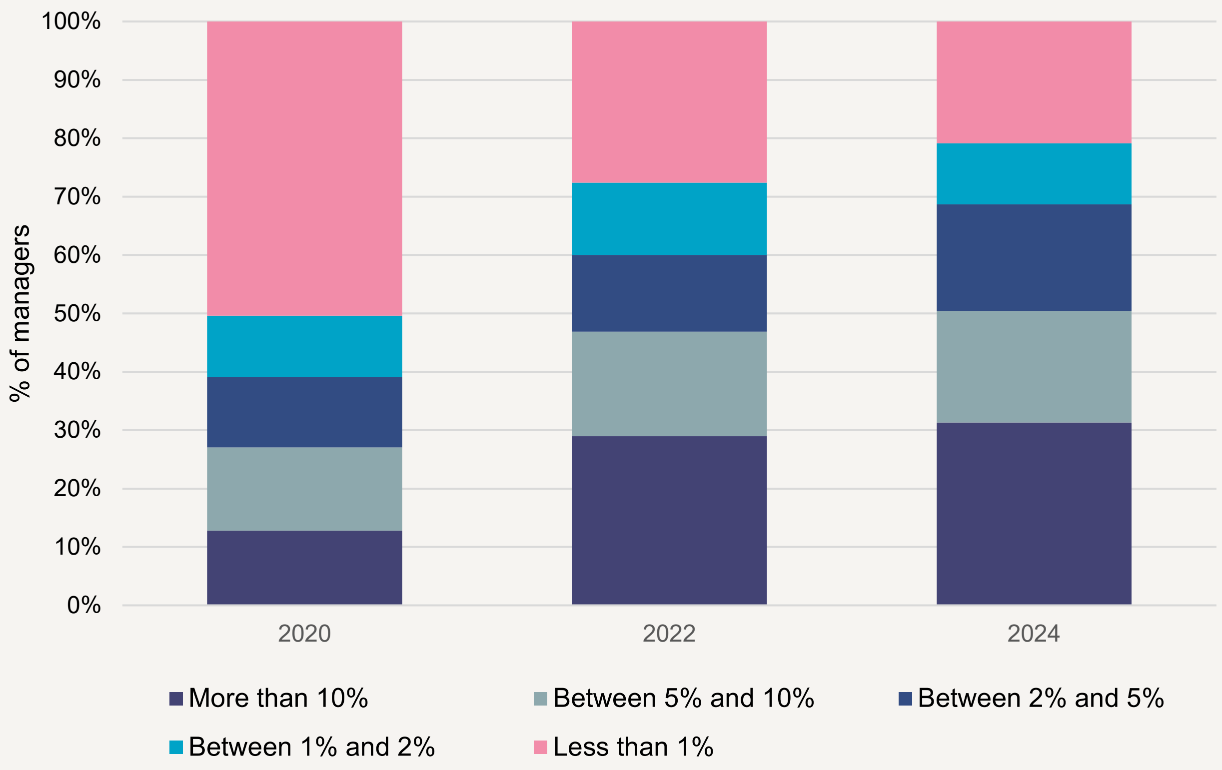
Since our last survey report in 2022, managers have significantly increased the level of resources dedicated to ESG and stewardship.

We expect managers to have a reasonable proportion of investment professionals who are ESG or stewardship specialists.

We found that around **78%** of managers have more than **1%** of their investment professionals as ESG or stewardship specialists, compared to **72%** in 2022 and **50%** in 2020 (see figure 2).

This positive trend reflects a growing recognition amongst investment managers that the fast-moving world of responsible investment requires individuals who can understand, interpret and help their colleagues to apply new understanding about these areas.

Figure 2: Roughly what proportion of your investment professionals are ESG or stewardship specialists?

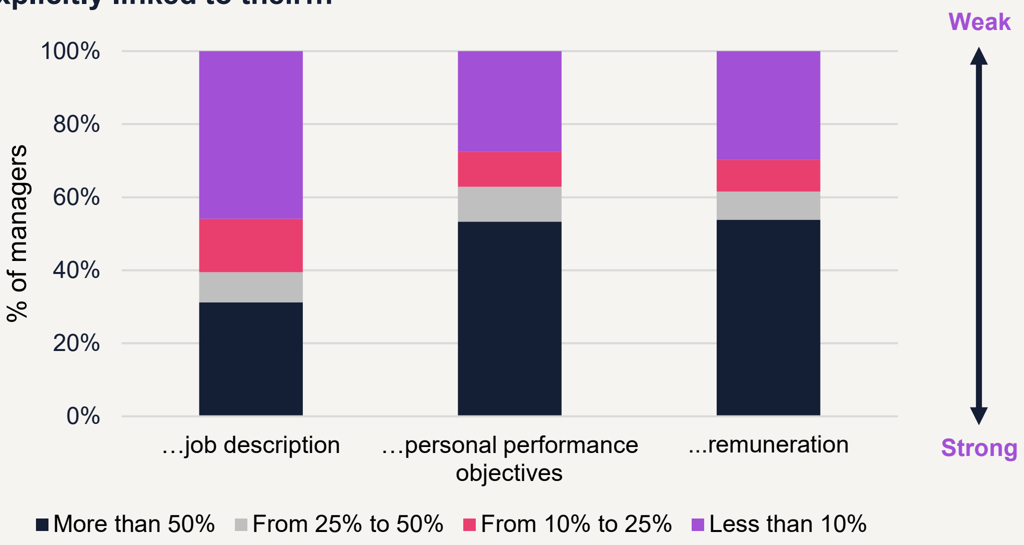


Training and oversight

Despite the important role of responsible investment specialists, we believe integrating responsible investment ("RI") considerations should be part of the day job for all investment professionals' roles.

Our 2024 survey found that only **31%** of managers incorporate RI in the job description for most of their investment professionals, a figure that is broadly consistent with our 2022 findings. However, **53%** of asset managers explicitly link ESG and/or stewardship considerations to the performance objectives of most investment professionals (see figure 3), up from **46%** in 2022. As in 2022, it was a similar picture for remuneration (**54%**).

Figure 3: Proportion of managers' investment professionals that have ESG and/or stewardship explicitly linked to their…



Understanding the issues

In order for investment professionals to be comfortable taking RI into account, they need good understanding of the topic. We asked managers about the extent of formal RI training provided to investment professionals and found that **51% of managers give less than five hours a year of formal training** to investment professionals on RI.

For an often complex and varied area that is changing rapidly, we believe five hours should be the bare minimum, so this is disappointing.

What is the quality of board oversight?

Our surveys show some progress in board oversight. We found that **81% of managers had someone at board level with responsibility for oversight of ESG and/or stewardship**, compared to 67% in our 2022 survey.

It is concerning that for the vast majority of managers it is not mandatory for board members to receive RI training. Responsible investment training is mandatory for board members for only **25%** of managers (compared to **23%** in our 2022 survey). We think this is poor and indicates that board oversight of managers' RI may not be as strong as other aspects of the business.

This compares with **74%** of managers that reported that training is mandatory for all relevant staff (up from **69%** in our 2022 survey).

Quality control of third party data

Are managers applying adequate quality controls to third party ESG data?

ESG data is important for managers to take account of ESG factors in their investment decisions. Most of them source at least some of this data from third parties, particularly when investing in public markets. However, there are many different ESG data providers, using varying methods and sources. It will rarely be appropriate to take third party data at face value with no scrutiny from managers themselves.

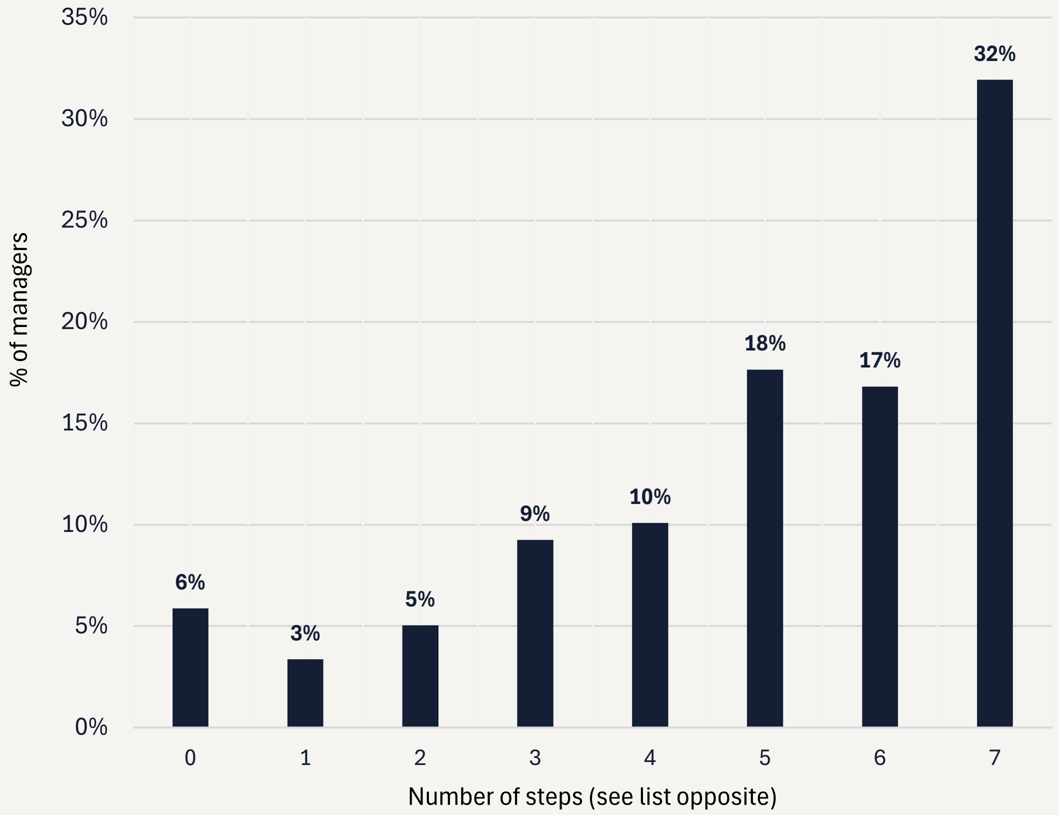
In our experience, ESG data from third parties requires review and, in some cases, adjustment, to take into account the manager's own knowledge, to achieve internal consistency and to ensure that the data is appropriate for the manager's purpose.

This is why we asked managers what measures they take to ensure ESG data quality. We asked managers to select which of the following list of steps they were taking:

- Comparison of multiple providers prior to initial appointment
- In-depth due diligence into selected provider(s) prior to appointment
- Review of alternative providers at least every two years
- Comparison of multiple data sources on an ongoing basis
- In-house processes to identify anomalous data points
- Review of key data points by in-house experts
- Query data issues with providers

77% of managers use four or more different steps to ensure the quality of ESG data sources from third parties (see figure 4).

Figure 4: How many steps do you take to ensure the quality of ESG data sources from a third party, if any?



How can we help?

It is important that, when selecting a manager, you check their investment approach and philosophy aligns with your beliefs as an asset owner.

Please get in touch to find out more

Agree your own responsible investment philosophy

Develop your philosophy through a survey of board members' investment beliefs, discussion of the results, and training on relevant topics such as options for addressing climate change risk in portfolios.

Engage with existing managers

Communicate your RI philosophy to your managers and compare with their philosophy to understand areas of alignment and deviation.

Select managers that align with your beliefs

Assess each manager's responsible investment philosophy as part of your selection process and whether it is consistent with your beliefs.

How did we carry out our survey?

This is one of four reports with results from our seventh responsible investment survey of managers. You can find our other three reports on climate, stewardship and systemic stewardship here:

Climate change

Stewardship

Systemic stewardship

We invite a wide selection of investment managers to complete an in-depth survey about responsible investment roughly every two years. It covers:

- their approach to environmental, social and governance issues
- their stewardship practices, such as exercising voting rights, engaging with company management and policy advocacy

This year we have four separate reports summarising the findings. Some of the questions are the same as our previous surveys. We have also asked a number of new questions. In particular our expectations of how managers approach systemic risks have evolved, so this year we have introduced more questions relating to systemic stewardship and made this the subject of one of our four reports.

Our survey covers the managers' firm-wide approach to RI. However, there are usually differences in implementation between different funds and strategies offered by the manager.

In our consulting to clients, our opinion on a particular strategy integrates the survey results with specific research into the RI approach of that strategy. In this way, we incorporate the important firm-wide aspects of a manager's responsible investment approach into our view on particular strategies that they manage. RI is a standard agenda item in our meetings with managers, where we probe what they do in practice.

119 investment managers completed our 2024 survey. Around half of the responses are from UK-based investment managers, including the major institutional UK managers. Managers completed the survey between April and June 2024.

We make comparisons with the survey results from our 2020 report (148 managers responded between August and September 2019) and our 2022 report (146 managers responded between August and September 2021).

Some managers did not answer every question in the survey. Results in this report are based on responses from between 100 and 119 managers. The percentages quoted are for the managers answering the specific question.

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