Stewardship

Responsible Investment manager survey

OCTOBER 2024

Importance of stewardship

Welcome to one of four themed reports of our 2024 Responsible Investment survey of investment managers. In this edition we focus on stewardship. It is widely accepted that good stewardship practices are vital for improving financial performance for investors. Laying the foundation for strong returns in five or ten years and beyond starts with good stewardship today.

In our 2024 survey, we've focused on the evolving role of stewardship in the asset management industry, particularly in light of recent economic, technological and regulatory shifts. **The asset management industry is experiencing significant transformation driven by a mixture of economic, technological and regulatory factors. These changes are redefining how managers approach investment stewardship and corporate governance**.

- **Technological advancements:** Artificial intelligence and machine learning are enhancing asset management by improving data analysis, real-time Environmental, Social and Governance (ESG) monitoring, and streamlined reporting.
- **Regulatory landscape:** Increased regulatory scrutiny demands more detailed and transparent ESG disclosures across the investment chain, including biodiversity and human rights evaluations.
- **Political conditions:** ESG is increasingly more central to the investment strategies used by European investors, driven by investor demand for transparency, climate action and alignment with social values. However, there is growing backlash, with some investors questioning its impact on financial returns. This pushback challenges asset managers to defend and refine their ESG approaches amidst increasing scrutiny.

These combined factors necessitate the development of robust stewardship strategies that leverage technological advancements, comply with regulatory expectations, and address ESG risks and opportunities. By doing so, we believe asset managers can create sustainable and long-term value for investors, meeting both financial and (where relevant) ethical objectives in an evolving market landscape.

What is stewardship?

In the UK Stewardship Code 2020, the Financial Reporting Council (FRC) defines stewardship as the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.

In our survey, we cover various aspects of stewardship, focusing on how asset managers engage with companies, exercise their voting rights and collaborate with other investors.

We believe that **true stewardship requires more than just discussion; it demands setting clear timebound objectives, monitoring progress, and taking decisive actions when needed**.

To reflect the critical importance of stewardship, we have developed a set of stewardship expectations – criteria that we expect any manager to work towards meeting, across all asset classes.

Investment manager approaches to stewardship

Our survey results show active participation on responsible stewardship and active engagement among managers particularly in respect of climate change. This shift reflects an increasing recognition of the importance of long-term value creation and sustainable practices in investment strategies. The rise in the number of managers adopting formal escalation policies and exercising independent voting decisions underscores a commitment to holding companies accountable and driving positive change. However, there are still areas that we believe require further attention:

- **Engagement on emerging risks** like artificial intelligence, social factors and non-climate environmental factors remains surprisingly low, despite their potential to significantly impact future business operations and societal outcomes.
- **Voting practices** show variability, with some managers relying heavily on third-party recommendations and others more willing to challenge management.
- While collaboration among managers appears strong, with a majority participating in collective efforts, the **decline in those leading high-profile collaborations suggests a need for more active leadership** in these initiatives. Collaborative efforts can amplify the impact of stewardship activities, presenting a unified front to drive more substantial changes.
- Our survey found that managers generally adopt a balanced approach in their engagement with investee companies, preferring to neither fully conform to management's direction nor aggressively push for changes. This moderate approach suggests a prevalent strategy of cautious optimism and targeted engagement. Instead, **we believe managers should shift towards more proactive and constructive involvement**.

What should asset owners focus on when challenging managers on stewardship?

We believe asset owners should focus on several key areas to ensure effective oversight and alignment with long-term value creation:

Compare performance: Compare managers' stewardship performance against peers and best practices to identify areas for improvement.

Promote constructive engagement: Encourage managers to adopt a proactive and constructive approach that is both supportive and strategically critical, promoting collaboration and necessary changes within companies.

Support collaborative initiatives: Question managers about their participation (or lack of) in collective actions such as Climate Action 100+.

Management votes: Ask how often they vote against management. If they vote in line with management, question what actions they have taken separately to ensure management are making improvements where appropriate.

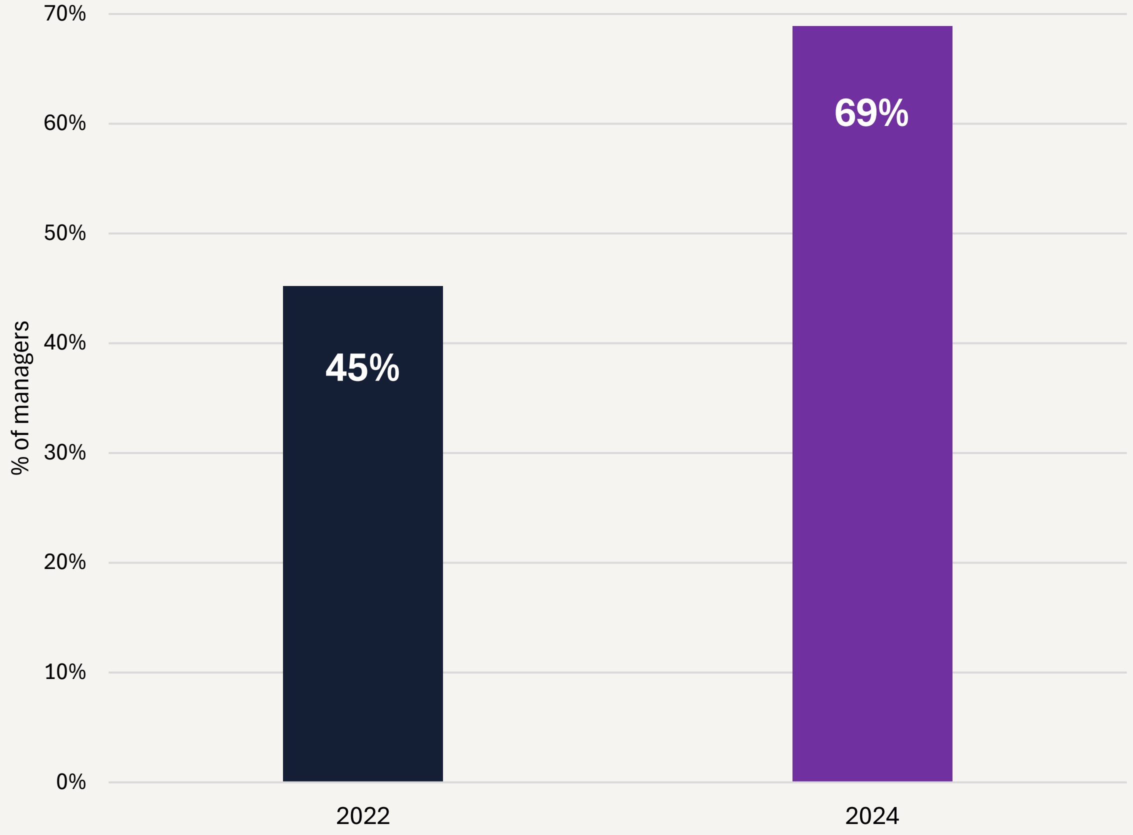
UK Stewardship Code 2020

We see being a signatory to a stewardship code as an indicator of good stewardship practices.

In our 2022 survey, published shortly after the initial wave of signatories to the UK Stewardship Code 2020 was announced, we reported that only **45%** of the managers we surveyed were signatories.

There has been some noticeable progress as **69%** of the managers we surveyed were confirmed by the FRC to be signatories in July 2024. This represents a significant increase and shows that **more managers have demonstrated that they have good stewardship approaches than two years ago** (see figure 1).

Figure 1: Proportion of managers who are UK Stewardship Code 2020 signatories



All statistics in this report relate to the managers that responded to our surveys. See page 11 for survey details.

Climate change and governance are topics managers engage regularly on

We surveyed managers about their engagement topics. Overall, we found good evidence of engagement with companies, or other non-sovereign issuers, across a range of areas.

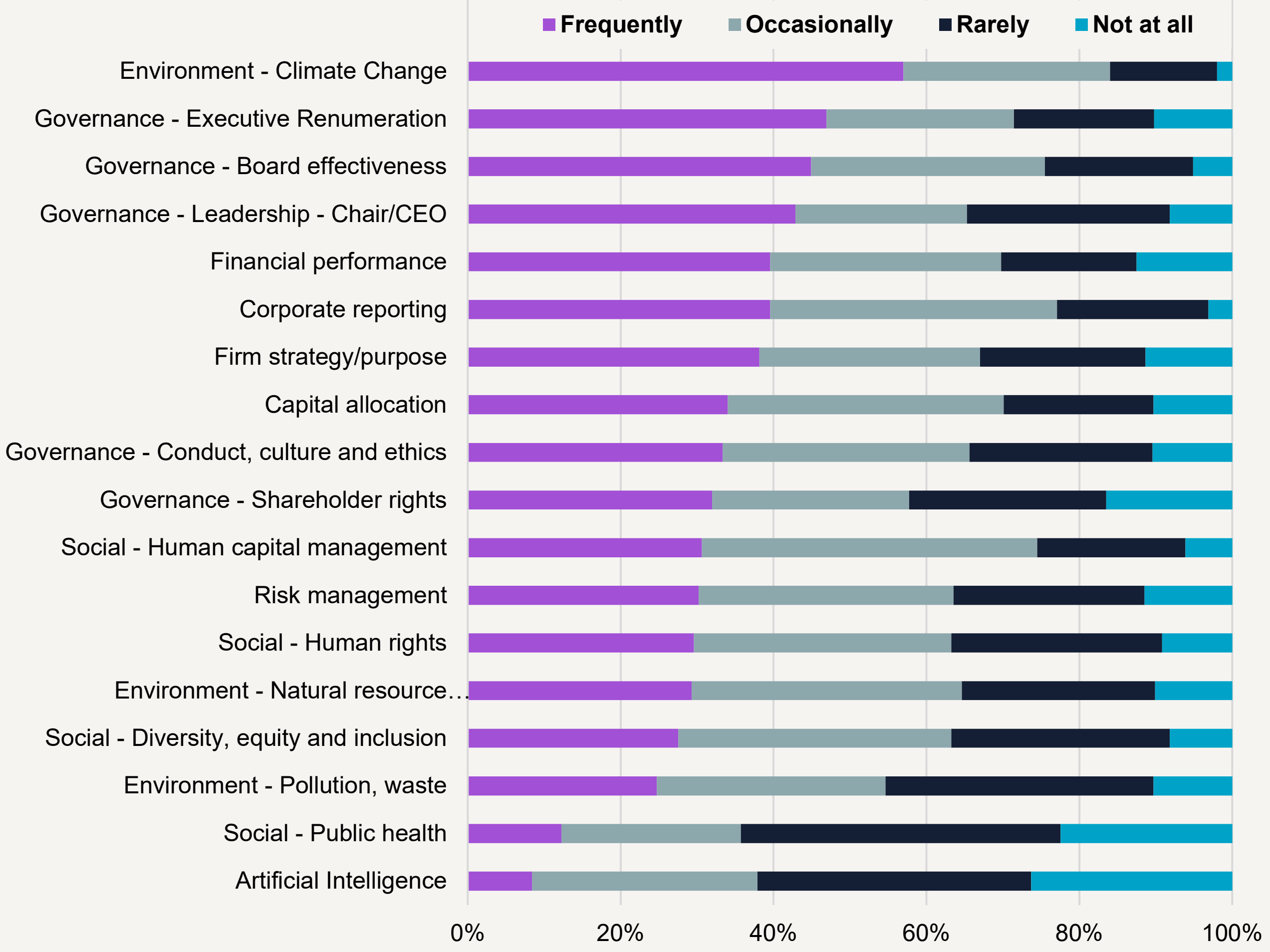
Investment managers commonly use engagement as a tool for managing climate change risk, so it is perhaps not surprising that **climate change is the topic managers engage the most on** (**57%** of managers (see figure 2) said they frequently engaged on this topic)[1].

What about other environmental issues?

Managers gave other environmental issues, such as pollution, waste and natural resource use, **much lower priority**. This reflects the fact that – with the exception of climate change – **governance and corporate strategy topics are at the forefront of managers' engagement**.

Surprisingly, AI is at the bottom of the topics that managers engage on with companies, given the potential impact of AI in all sectors of the economy, both as an opportunity and a risk. Perhaps managers are still in the phase of gathering knowledge on this area – it will be interesting to see how this changes over time.

Figure 2: The extent of manager engagement with companies or other non-sovereign issuers



[1]We provided managers with the following category guidance:
- "Rarely" means a few interactions per year
- "Occasionally" means a few interactions per month
- "Frequently" means several interactions most weeks

Engagement process

We surveyed managers about their engagement practices, and how they interact with the relevant parties to preserve and enhance the long-term value of assets on behalf of clients and beneficiaries.

Effective engagement requires a clear framework - setting clear objectives, maintaining regular dialogue, defining milestones to achieve and having a clear timeframe are key.

Figure 3: Management of engagement by the central team

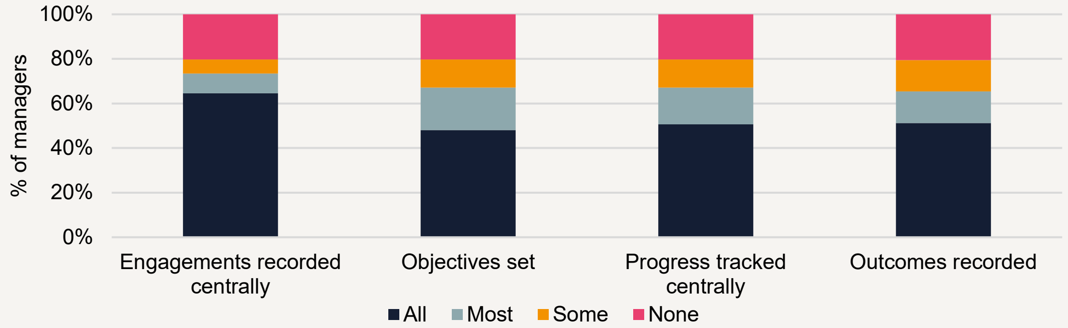
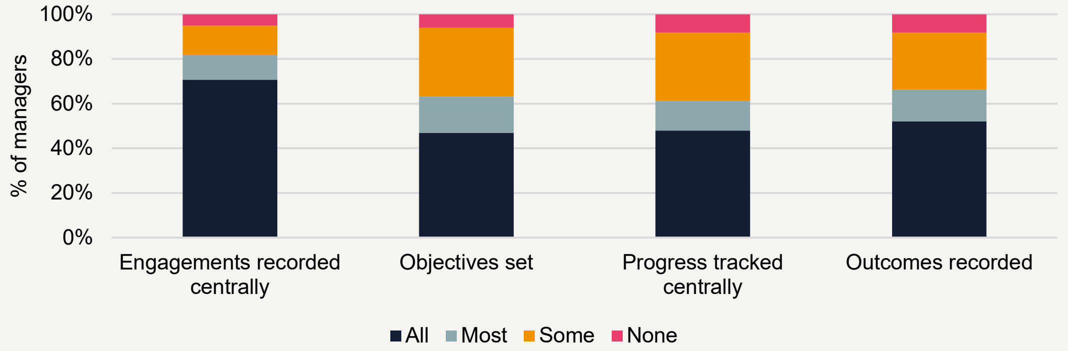


Figure 4: Management of engagement by investment teams



The majority of engagements by managers are being recorded centrally (**65%** do this for all engagements carried out by a central stewardship team, figure 3). However, fewer managers tracked progress and recorded outcomes for all engagements (both **51%**). Most worryingly, **the initial step of setting objectives was the step carried out routinely by fewest managers (48%)**[1].

This indicates that some managers may be mistakenly labelling their interactions with companies as engagement – in our view, it cannot be true engagement without an objective.

What do managers do when engagement is not working?

Engagement can be a powerful driver of real-world change, especially if it is combined with allocation of capital to promote more responsible business practices (for example a lower carbon business model). But **when engagement is not working effectively, escalation may be required.**

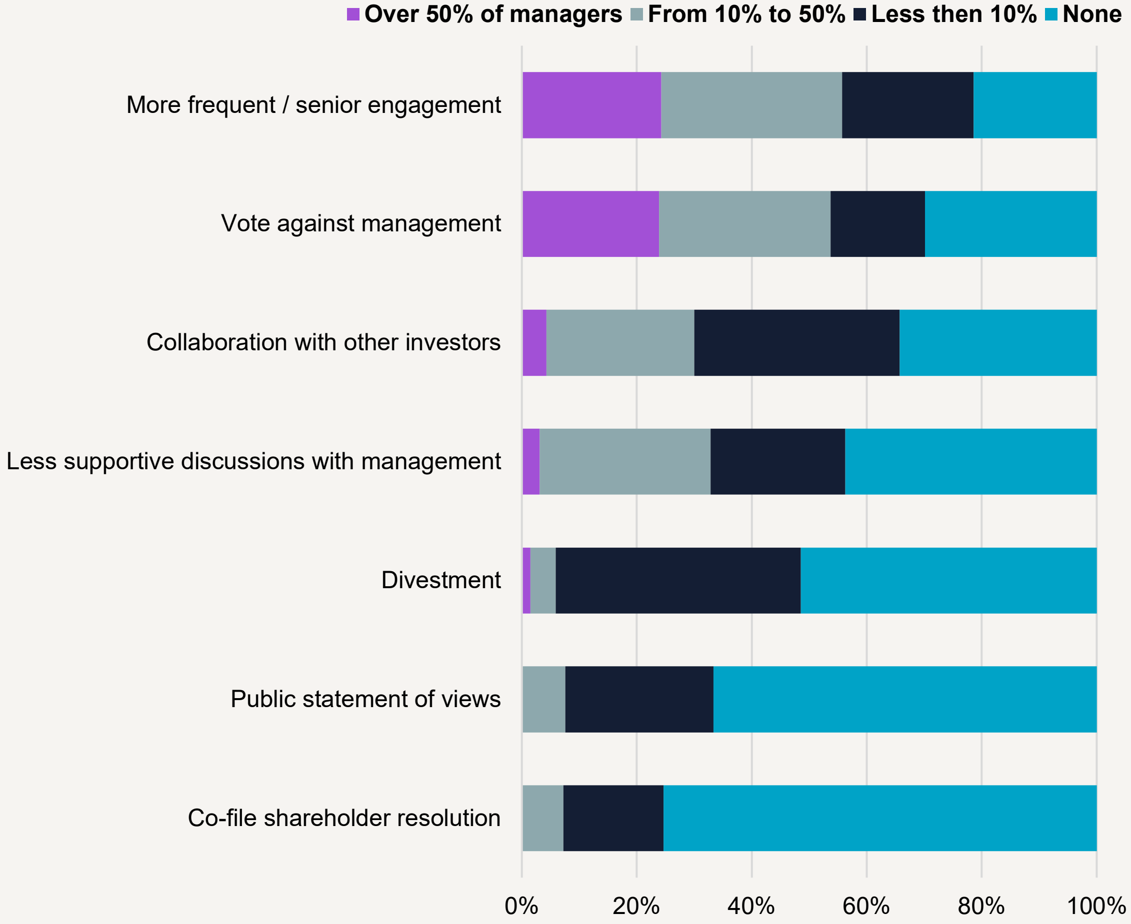
Escalation policies can provide an important framework for managers to drive change where they have hit a roadblock in progress. The proportion of **managers that have a formal escalation policy** to help them achieve their engagement objectives has increased from **58%** in our 2022 survey to **65%** in 2024. Of the managers that do have a formal escalation policy, **97%** outline steps taken in cases of unsuccessful engagements, and **82%** integrate escalations into wider stewardship reporting.

However, only **60%** of managers' escalation policies include timelines or triggers for escalation. As a result, for a large proportion of managers, it remains unclear when escalation will come into play. Given that this should be a key component of the policy, this is disappointing.

2 The results in this paragraph are based on engagements carried out by a central stewardship team. It was a similar picture for engagement carried out by investment teams (figure 4) except that the proportion responding "none" rather than "some" was higher for all four steps.

How do managers escalate engagement?

Figure 5: Which escalatory actions have managers taken with issuers?



Where escalation is being carried out, the most common methods are more frequent or more senior engagement (**79%**) and voting against management (**70%**). Divestment was used to some extent by **49%** of managers.

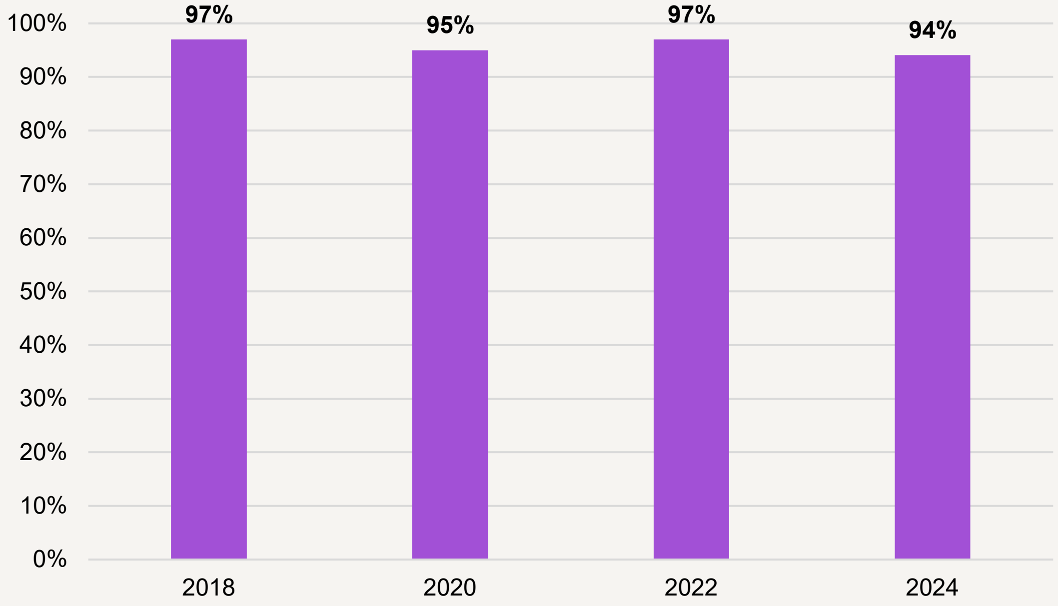
It is encouraging to see that collaboration with other investors, an important element of stewardship, is used by the majority of managers (**66%**) (see figure 5).

Investors can co-file or lead the filing of resolutions. Filing a resolution at a company allows investors to escalate engagement on a particular issue. It provides a clear ask of the company, demonstrating what investors expect from them. Of the managers we surveyed, **24%** said they co-filed or led the filing of at least one resolution over the year. As this is quite a significant step in the escalation process, it isn't surprising that this is relatively low.

Voting

Voting rights are an important way in which shareholders can hold company management to account. Investors should expect managers to vote on their behalf whenever practical.

Figure 6: Proportion of eligible votes exercised by listed equity managers from our surveys



Listed equity managers continue to exercise a high proportion of votes when they are eligible to do so, at an average of **94%** of votes over the year to 31 December 2023 (see figure 6). This high proportion is relatively consistent when looking at differences between the regions that managers are headquartered.

How do listed equity managers vote?

A high proportion of listed equity managers are willing to vote against management or abstain where appropriate – on average, they did this for at least one vote at **37%** of Annual General Meetings (AGMs) during the same period, compared to **35%** and **33%** in our 2022 and 2020 surveys respectively. However, there continues to be a wide variation, with the managers' individual answers ranging from **less than 1% to 94%** of AGMs.

We expect managers to vote against management or abstain some of the time – they should be willing to express contrary views after consideration, rather than just voting with management.

How much do listed equity managers rely on recommendations from proxy advisers when voting?

A related topic is the extent to which listed equity managers rely on recommendations from proxy voting advisers when voting.

We believe managers should apply their own views when voting, drawing upon their own knowledge of the companies they invest in, even when using a proxy advisor.

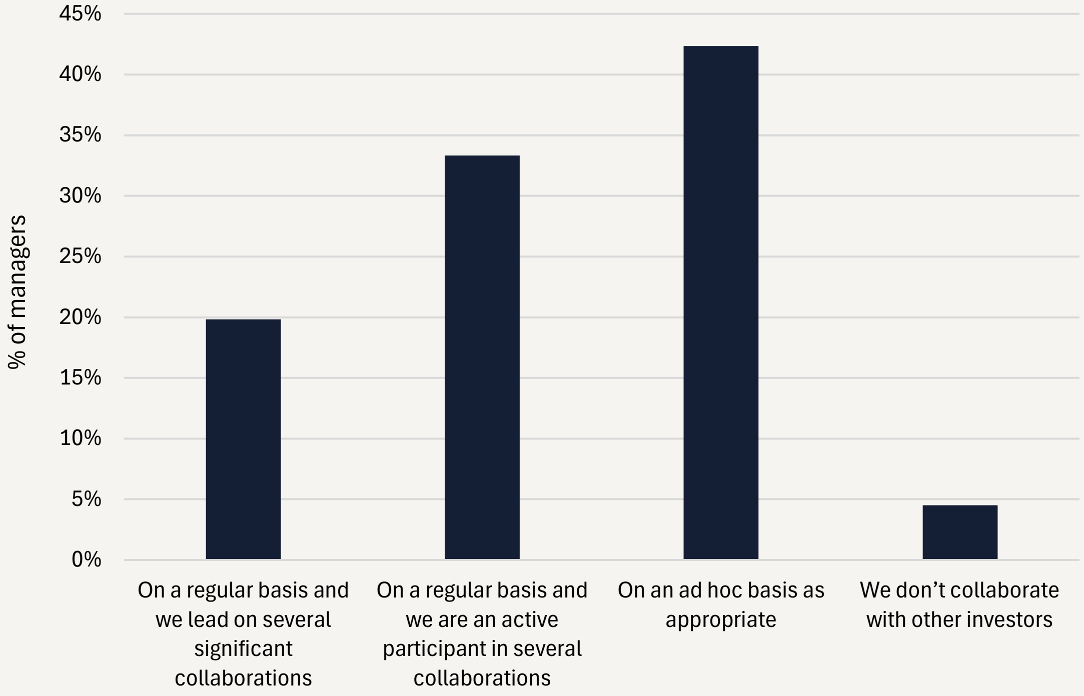
It is therefore positive to note that, in our 2024 survey, **only 9% rely completely or a lot on proxy voting on advisors' recommendations.** This is a significant and welcome improvement compared to our 2022 and 2020 surveys when **16%** and **14%** respectively did so.

Collaboration

Collaboration can be an efficient and effective way for managers to increase their influence to achieve collective aims. It also benefits the recipient by receiving one clear message from a group rather than multiple messages which can sometimes be conflicting.

It is positive that most managers surveyed collaborate on a regular or ad hoc basis, and only a small proportion not at all (**5%** similar to our 2022 survey) (see figure 7).

Figure 7: Frequency of collaboration with other investors



Amongst the managers we surveyed, **39%** were a member of Climate Action 100+, **17%** were a member of Nature 100 and **19%** were a member of PRI Advance.

- **Climate Action 100+:** An investor-led initiative, currently comprising more than 700 investors, with the aim of ensuring the world's highest emitters take actions on climate change.
- **Nature 100**: An investor-led initiative aiming to reverse nature and biodiversity loss by focusing on greater corporate ambition and action.
- **PRI Advance group**: An initiative led by the Principles for Responsible Investment (PRI) which utilises institutional investor stewardship to progress human rights issues, thereby protecting and enhancing risk-adjusted returns.

However, only **20%** of managers stated that they were leading on several high-profile collaborations, compared to **28%** in our 2022 survey.

How can we help?

Bespoke approach

Annual Health Check
Assess your current stewardship approach and receive tailored recommendations for improvements

Manager meetings
Attend manager meetings under your consultant's facilitation with a focus on stewardship or ESG risks and opportunities

Engage and escalate
Engage with your manager, setting clear timebound "asks" for managers, and escalating as required where expectations are not met.

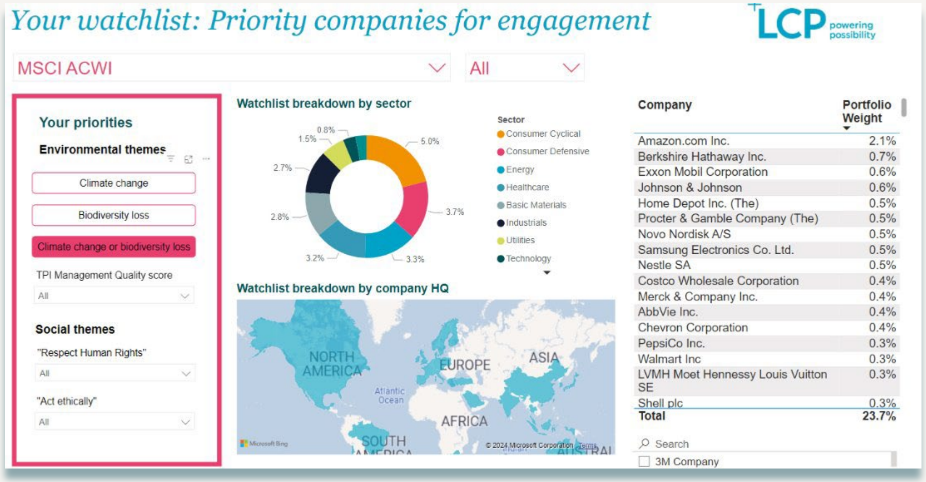
Annual stewardship reporting
Monitor progress on your engagements with managers and consider next steps and recommended actions. Select your most significant votes and/or most significant lending decisions using our stewardship dashboard (see opposite), for inclusion in your implementation statement.

Delegated approach

LCP Influence
New LCP service (coming soon) where we undertake focused engagement with key managers on trustees' behalf.

LCP Influence aims to drive changes in managers' behaviours to protect your members' interests by focusing our engagement efforts, requiring stronger asks of managers and measuring changes. We will provide trustees with decision-useful reporting, clearly identifying room for manager improvements and making clear recommendations to drive impact.

LCP stewardship dashboard



Please get in touch to find out more

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

ESG foundations

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; and
- 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 70 and 119 managers. The percentages quoted are for the managers answering the specific question.

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At LCP, our experts help to power possibility by navigating you through complexity to make decisions that matter to your business and to our wider society. We are powered by our desire to solve important problems to shape a more positive future. We have market leading capabilities across pensions and financial services, insurance, energy, health and analytics.