Investment Insights

Asset managers' sustainability disclosures - words vs. actions

This report sets out the key findings of our recent review of BW rated asset managers' sustainability disclosures, including Environmental, Social and Governance (ESG) data. This includes key areas of strength and weakness, and importantly whether managers' 'actions' (such as their integration of sustainability factors) are reflective of their 'words' (such as the commitments they have signed up to).

This report is written with the backdrop of investors struggling with a lack of consistent and reliable information - making it hard for them to make appropriate and informed sustainability decisions. A recent survey highlighted that:

- 40% of investors said a lack of robust ESG data was holding back their integration of ESG; and
- more than a quarter ranked 'difficulties accessing the information as I need' as the leading challenge they faced in implementing ESG.

Although the industry has experienced significant improvements in sustainability disclosures over the past few years, our findings demonstrates that there's still a long way to go.

Key learnings

1

Comparing apples with pears:

Due to characteristics specific to each asset class, comparing carbon data across different asset classes is not advised. In addition, caution should be taken when comparing year-on-year data for the same asset class, as methodologies and / or data coverage may have changed, meaning apparent trends can be misleading.

2

Voting tug of war:

Climate and environmental management and stakeholder resolutions are increasingly divisive. We have observed a large divergence in voting practices of asset managers with support for environmental and climate resolutions at Annual General Meetings of companies averaging at c.50%.

3

Words are not yet actions:

Whilst we have seen a significant uptick in the number of managers signing up to net-zero initiatives (e.g. Net Zero Asset Managers Initiative), this is generally not yet resulting in managers integrating net-zero commitments within their funds and providing better quality climate data.

4

Alignment of Stewardship considerations:

It is encouraging to see that asset managers are generally aligned with what investors are most concerned with when setting their stewardship priorities.

Click to scroll through charts

Comparing apples with pears

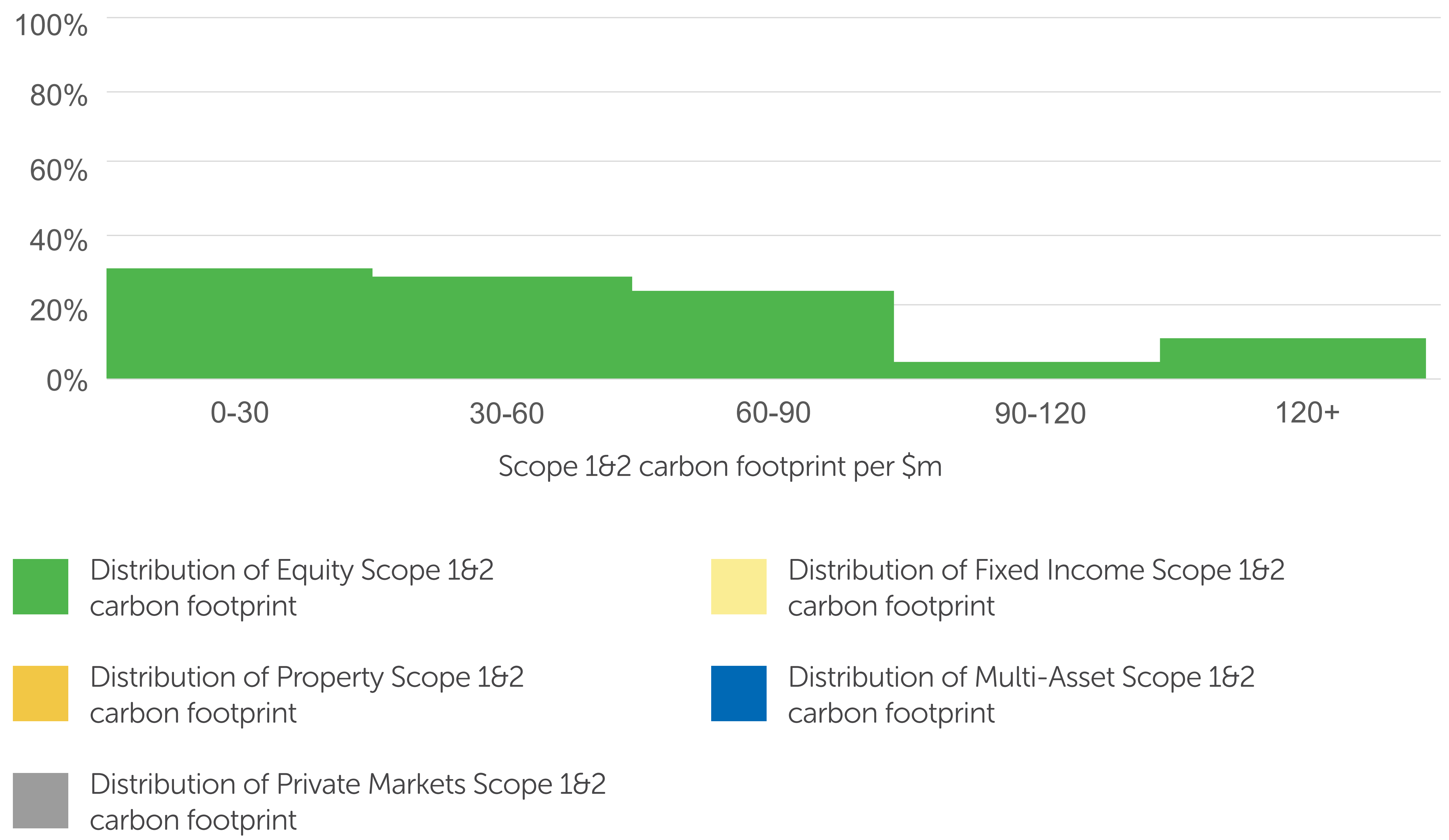
There have been significant improvements in the reporting and provision of carbon footprint data in recent years. However, investors must be cautious with how they interpret the data, particularly when comparing across asset classes.

The size of the footprint is primarily driven by the asset class

The charts on the right show the range of carbon footprints for different funds across asset classes. There are noticeable trends in the distribution of carbon footprints between assets classes. The next page highlights key trends that we have identified.

Keywords +

1. Distribution of Equity Scope 1&2 carbon footprint



Furthermore, even when comparing footprints of funds within the same asset class, it is important to understand what is driving the differences and whether it is a function of data quality, an intentional, active decision, or merely an outcome of the funds' underlying holdings. For example, if a fund switched from holding a company that did report its emissions to one that did not, the total emissions would appear to fall when in fact, it would just be the coverage that was falling.

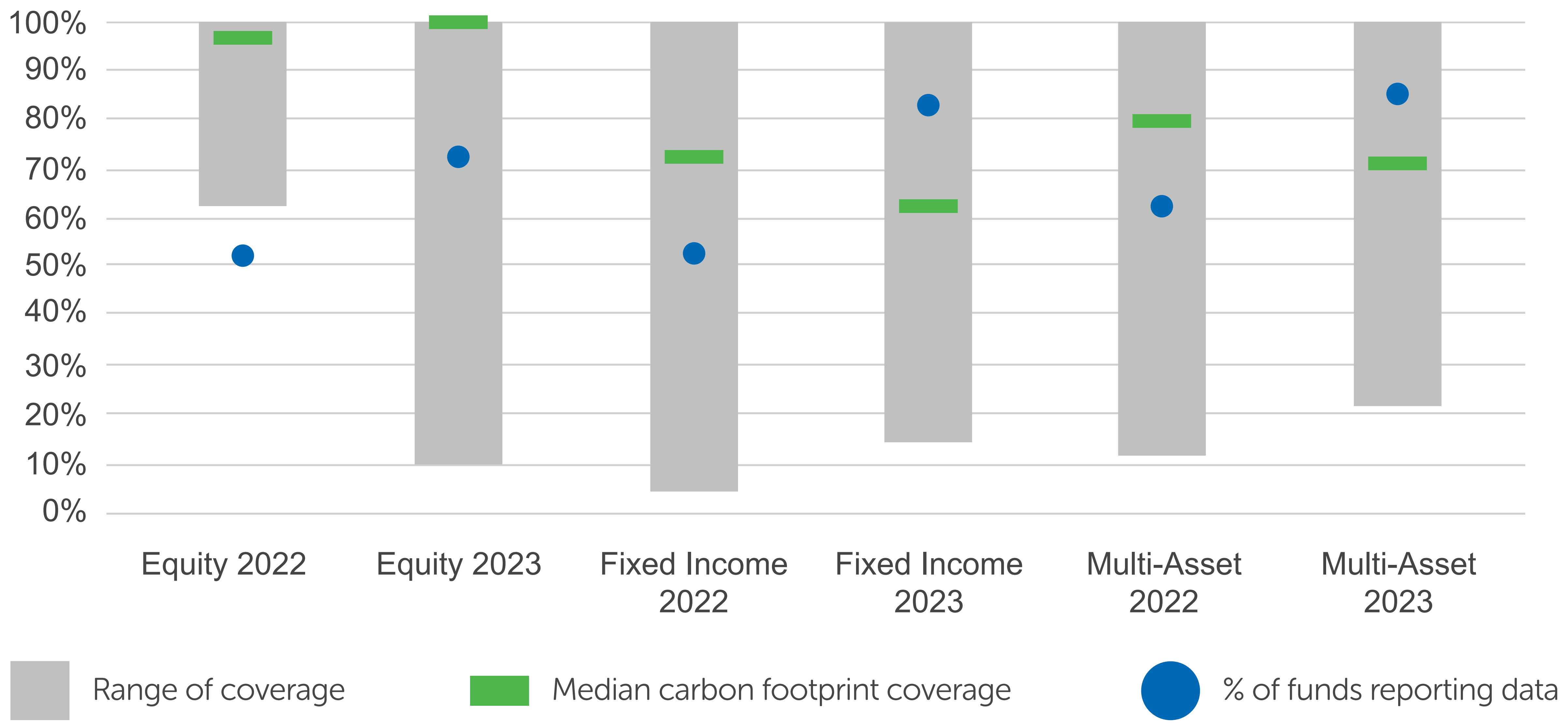
What the numbers tell you	What the numbers miss
Most equity and fixed income investments have a carbon footprint below 90 CO_2e tonnes per \$m.	The carbon footprint of emerging market equities tends to be higher than that of developed markets. As such, where footprints are higher (e.g. >60), this is likely a function of asset allocation (e.g. Emerging Market exposures, which has been primarily driven by Developed Markets offshoring emissions, as well as lower efficiency in these regions). Similarly, riskier credit assets (such as emerging market or high yield, the latter tending to have a higher allocation to the energy sector) typically have a higher carbon footprint. As such, where footprints are higher (e.g. >60), this is likely a function of asset allocation. However, where footprints are lower (e.g. <30), this may be driven by managers / indices actively managing climate risks and or due to the make-up of the asset allocation.
Most multi-asset funds also have a carbon footprint below 90 CO_2e tonnes per \$m.	The distribution of emissions in multi-asset funds is similar to equity and fixed income because those funds tend to have relatively high exposures to these asset classes. Reductions in footprints in this asset class may be driven by the active management of climate risk, but they could simply be due to the make-up of the asset allocation (whilst the latter could also explain higher carbon footprints, such as exposure to infrastructure assets).
Property investments have a low carbon footprint in comparison to other asset classes.	The carbon footprint of property investments as measured on the previous page (i.e. by considering scope 1&2 data) only include data relating to, for example, the combustion of fossil fuels for heating and the use of electricity within properties held. As such, carbon footprints tend to be fairly low. However, including scope 3 data (e.g. what tenants might be responsible for) could paint a very different picture.
Private market investments have a wide range of footprints, as you might expect given the breadth of that market.	Low numbers tend to be funds with higher private debt exposure, whilst higher numbers tend to be funds with higher infrastructure exposure.

It is important to understand what is driving differences in your various asset holdings' carbon footprints. This will allow appropriate comparison and lead to more informed decision making when considering portfolio allocations.

Last year's data is old news

The graph on the right considers the change in coverage for scope 1 and 2 emissions from 2022 to 2023 within funds that invest in public markets. The **blue** dots represent the percentage of funds that reported data within each asset class. Each coloured bar then shows the range of coverage (for those managers that were able to report) in that asset class for that year – so we can see that in 2022 equity funds reported on between 62% and 100% of the underlying holdings' carbon footprints.

As with the emissions data shown on the previous page, the fact that we can create these charts shows that there have been big steps forward in the production of data and the consistency of the data produced. However, the data provided is still changing quickly and comparing data between years can lead to incorrect deductions being made. Please use the pop-ups to see the stories behind on the year-on-year changes in each of the asset classes.



Equity +

Fixed Income +

Multi-Asset +

Keywords +

Investors - particularly those reporting under TCFD - should be mindful that the availability and coverage of emissions data can vary significantly across asset classes and managers and should share with their managers their expectations of being able to increase data quality over time.

2. Voting tug of war

Environmental and climate appears divisive.

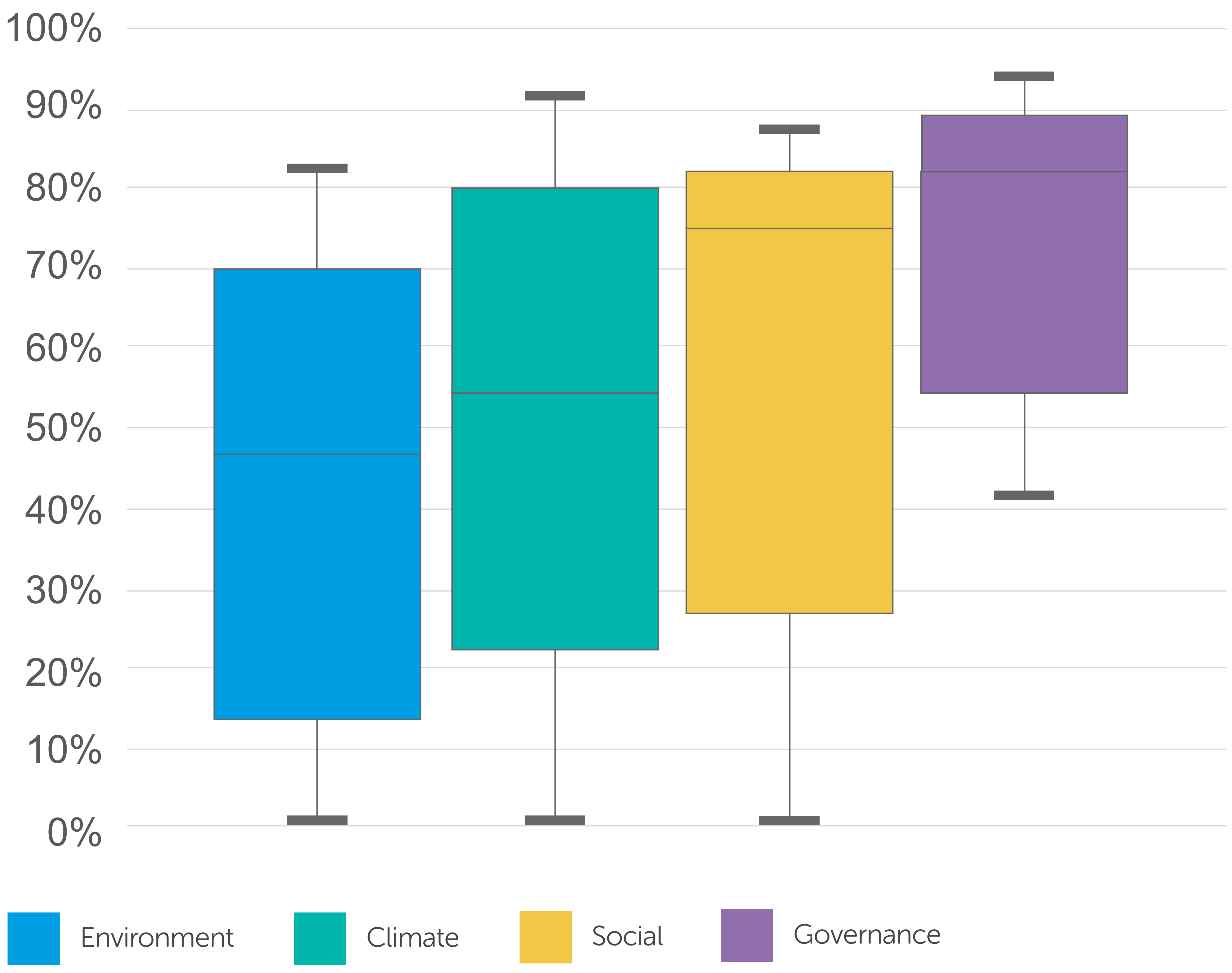
The graph to the right shows the % of votes that each surveyed manager voted in favour of climate and ESG resolutions as a % of all votes cast. The range shows the spread of support for resolutions in each category - where the coloured boxes represent the middle 50% of managers.

We have observed a large divergence in voting practices across asset managers, with the median support for environmental and climate resolutions at Annual General Meetings of companies being around c.50%.

It is worth noting that the data includes both shareholder and management resolutions where management resolutions garner far higher support than shareholder resolutions. Shareholder resolutions tend to be more far reaching than management proposals, asking for companies to go further in these areas. We note that asset managers will also take differing approaches to voting on management vs shareholder resolutions.

Click on the chart to see our key learnings.

% of votes in favour of resolutions



The large variance between managers means that it is important for investors to make sure the actions of the managers they have selected reflect their expectation and their stewardship priorities - don't assume that your managers are taking similar approaches to voting.

Click to find out more

3. Words are not yet actions

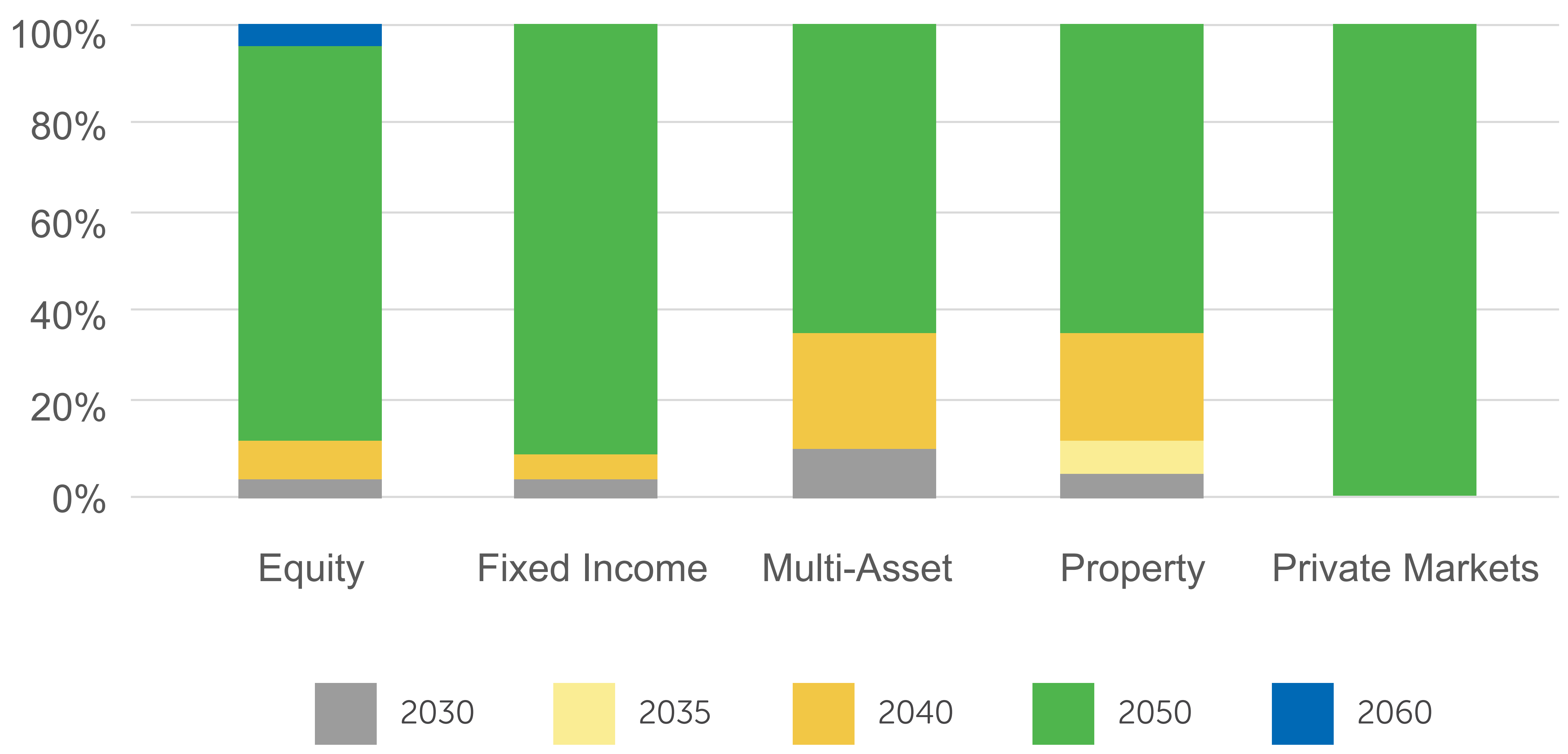
The increased regulatory and investor focus on sustainability in recent years has led managers to sign up to a plethora of initiatives. However, the question remains - has this translated into a change in behaviour?

Net-zero

Over **2/3rds** of asset managers considered are signatories to the Net Zero Asset Managers (NZAM) initiative.

However, only **21%** of funds considered currently have net-zero targets.

Spread of net-zero target dates by fund type



Keywords +

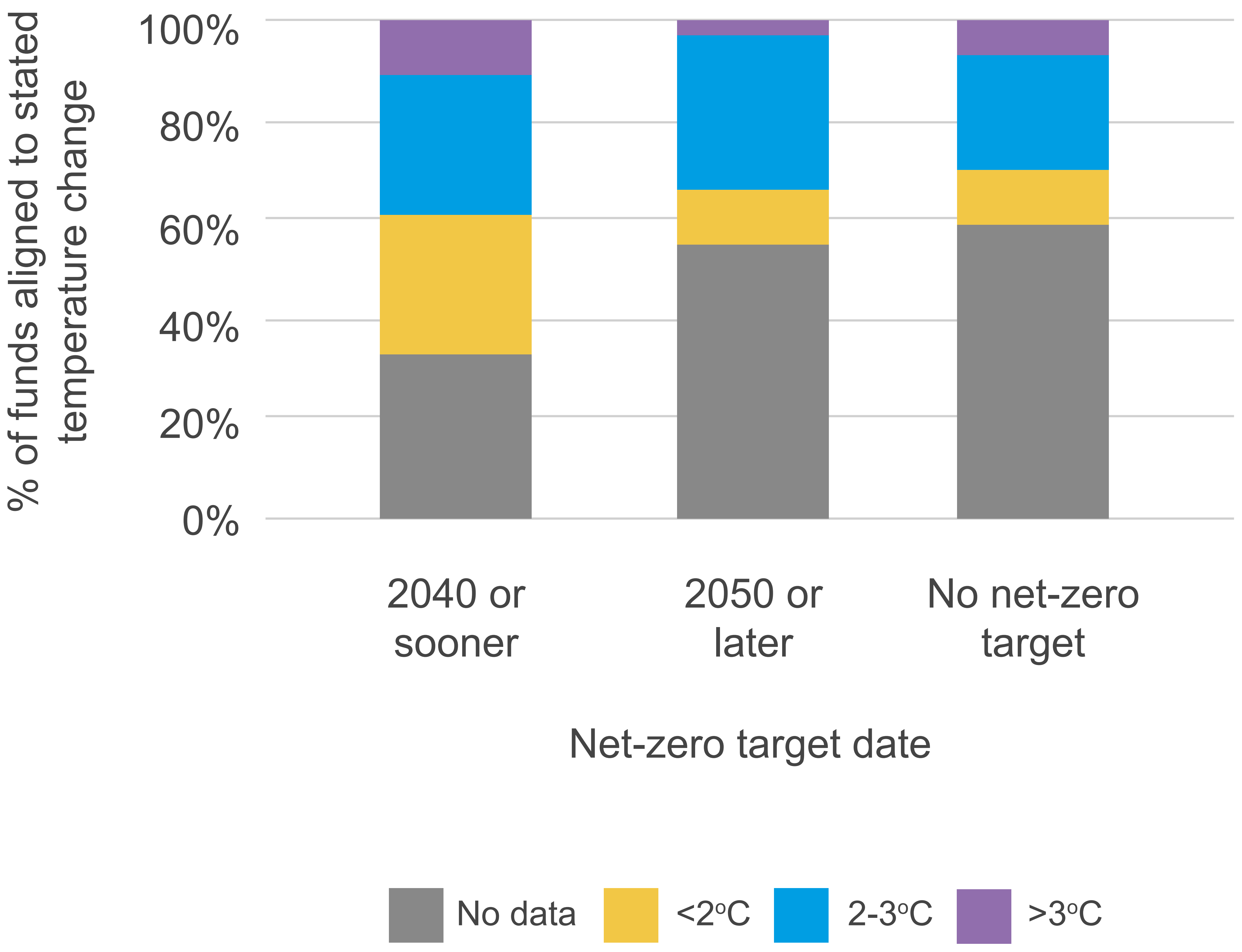
We do not currently see any meaningful correlations between being a signatory to the NZAM initiative and being able to provide more or better quality data, a higher focus on climate engagements with underlying firms, and / or setting net-zero objectives on funds. We will continue to monitor this, as we are conscious that this may change over time, as words / commitments turn into meaningful actions.

Temperature alignment

Temperature alignment metrics for the funds considered range from 1.5°c (associated with a number of net-zero aligned funds), up to 8.8°c (associated with an Emerging Markets Debt Fund). The median alignment was 2.6°c, significantly higher than what is expected to be required to avoid material impacts from the physical risks of climate change.

Data availability in the area is low, with over half of funds (57%) not being able to provide this.

Whilst there is a significant improvement in data availability for funds with a net-zero target of 2040 or sooner, perhaps more interestingly, data is not significantly more forthcoming for funds with a 2050 or later net-zero target compared to funds with no target. Furthermore, funds with a longer-term net-zero target only show a marginal improvement in temperature alignment compared to funds with no target, as shown in the graph to the right. We also note that, proportionally, there is an increase of funds aligned to >3 °C for funds with a net-zero target of 2040 or sooner but we note that data availability will play a part in this.



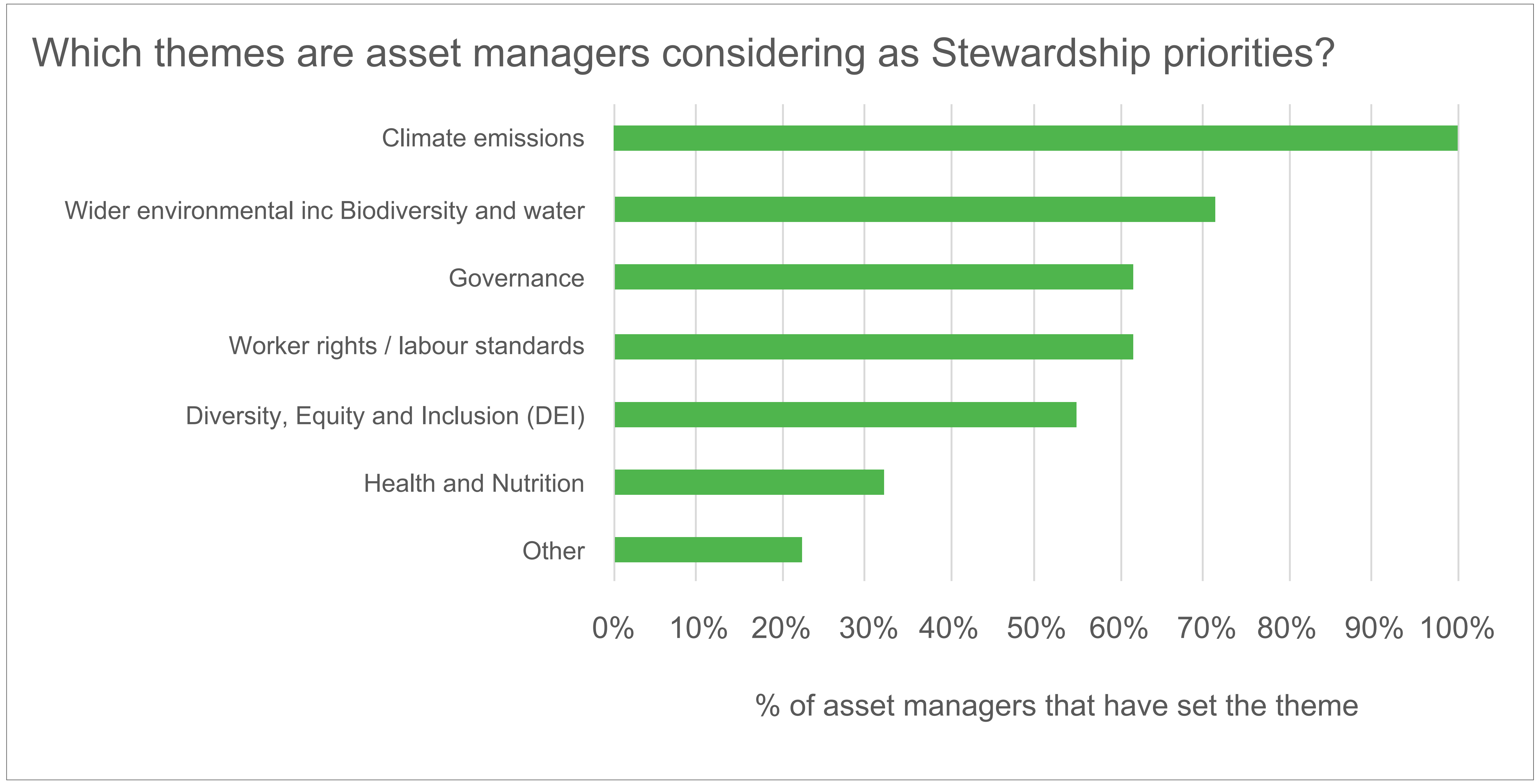
Keywords +

Our research revealed numerous managers signing up to net-zero initiatives (e.g. Net Zero Asset Managers Initiative) but many had not yet integrated net-zero commitments within their funds and were no closer to providing better quality climate data.

4. Alignment of Stewardship considerations

The stewardship priorities of asset managers appear to be largely in line with the topics that are of most concern to investors. Based on our discussions with clients, it appears that asset managers are considering what the asset owners are most concerned with, when setting the priorities.

Click on the chart to see more insight into managers' priorities.



Keywords +

We encourage investors to consider their stewardship priorities and how well this aligns with that of their chosen asset managers.

So, what should you do?

Whilst we have generally seen improvements in data and reporting, it is still too easy for data to be misinterpreted. It is therefore important for investors to look behind the data and remain engaged in discussions with asset managers to drive better practices.

1. Comparing apples with pears +

2. Voting tug of war +

3. Words are not yet actions +

4. Alignment of Stewardship considerations +

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Please contact your Barnett Waddingham consultant if you would like to discuss any of the above topics in more detail. Alternatively get in touch via the following:

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