

ADOPTERS' EVIDENCE 2023

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The **IMPACT INVESTING** PRINCIPLES *for* PENSIONS

How are our Adopters embedding impact into governance & advice?



Investment consulting and fiduciary management organisations have joined us as Adopters of The Impact Investing Principles for Pensions since 2021. These organisations are crucial in guiding the flow of pension fund investments. In adopting The Impact Investing Principles for Pensions, investment consulting and fiduciary management firms agree to provide evidence on a regular basis, on the way in which The Principles are applied within their companies.

This paper highlights the main themes emerging from

their evidence statements, which demonstrate the integration of ESG into investment processes but often reveal gaps in embedding impact within governance, operations and service offerings.

As highlighted in the box, 'Questions asset owners need to ask of their advisers & managers to understand how impact is integrated', Adopters often frame impact in terms of climate or net-zero targets, overlooking broader social impacts. They must make clear the corporate-level impact goals their advisers support and how these translate into manager research and client advice.


Questions asset owners need to ask of their advisers & managers to understand how impact is integrated

Adopters often refer to impact as climate or net-zero targets, overlooking other impacts such as social. It is important for clients to understand the corporate-level impact goals the organisation is supporting and how these filter through to manager research and client advice. Predominantly the evidence demonstrates ESG is integrated into investment processes; however, it remains unclear how impact is embedded within an organisation's governance, operations and service offerings.

- 1** What distinguishes ESG criteria from impact investing and how does this shape your investment approach?
- 2** How does the integration of impact into your firm's philosophies and operations affect governance practices?
- 3** How can you deliver quantitative and qualitative strategic advice to clients regarding impact investing?
- 4** What metrics and benchmarks do you utilise to assess and measure the effectiveness of your impact integration strategies?
- 5** How can you improve managers' impact investing through engagement rather than opting for divestment?
- 6** How do education and training improve your impact integration, understanding of ESG practices and sustainability culture?



Embedding impact & ESG – insights into Adopters' practices & priorities

 **P**ositively, Adopters reported the implementation of a methodology that typically commences with client education through training, leading to the formulation of ESG beliefs, policies and targets, which are subsequently integrated into specific investment objectives. Adopters often leverage specialised committees or teams tasked with exploring impact opportunities across all asset classes.

Defining impact beyond ESG

We covered ESG and impact integration in this report and assessment. Establishing a shared understanding of impact investing throughout the process is essential. Impact investing transcends financial goals and ESG risk mitigation; it encompasses the generation of positive outcomes for stakeholders and actively contributes to solutions. This distinction must be clearly communicated for the benefit of clients, and to assist them in shaping their beliefs and objectives. There are occasions where ESG and impact are treated as homogenous when they are, in fact, distinct but mutually reinforcing approaches. Additionally, investment consultant and fiduciary manager Adopters should offer comprehensive insights to clients regarding their approach to assessing the impact performance of allocations, ensuring transparency and fostering accountability.

Embedding impact into the firm's philosophy beyond investment advice

Firms demonstrated a strong commitment to embedding impact into their philosophies and operations, with particular attention to net-zero targets, and education and training initiatives. They prioritise sustainability throughout their entire operation, with most of them setting ambitious net-zero and decarbonisation targets, while actively advising clients on sustainability matters.

ESG considerations are integrated into client advice

and used to empower clients through strategic guidance and training. There is also a focus on ESG risks and stewardship priorities, with firms advocating for impact investing and supporting ESG integration through training and public engagements. Some Adopters emphasised risk management and sustainability integration across all levels of operations, with structured governance and a focus on diversity, equity and inclusion.

Pensions for Purpose's perspective

Adopters often mention sustainability aspects are embedded across their entire investment decision-making process.

It typically starts by considering ESG risks, the current oversight by managers and alignment with trustees' objectives. A workplan is then developed, which can include the potential for enhanced monitoring and engagement from managers, updates to guidelines and improved articulation within policies. The role of consultants was highlighted as essential.

At one Adopter, consultants are incentivised through their remuneration to provide high-quality tailored advice to clients and conduct themselves in a manner that is in keeping with the firm's values, which includes ESG matters. All consultants are expected to understand ESG issues and advise their clients appropriately. An annual performance development process informs each consultants' end of year rating, including their bonus, which is linked to performance against each of the firm's values.

Another Adopter applies minimum exclusion criteria (where they manage assets directly, they exclude companies with exposure to controversial weapons and material revenues from thermal coal). Given the widespread adoption of net-zero goals and adherence to climate commitments among several Adopters, there is a clear opportunity to broaden the focus to include other thematic areas in the years ahead. Additionally, we are keen to understand how these organisations integrate social and governance factors into their portfolio construction processes.

Central themes from Adopters' evidence submissions

1

Governance:
the integration of impact into firms' philosophies and operations, particularly focusing on net-zero targets, education and training initiatives, sustainability prioritisation, and diversity, equity and inclusion efforts.

2

Strategy:
firms integrate The Impact Investing Principles for Pensions into strategic advice, including collaboration with clients, consideration of ESG risks and opportunities, utilisation of metrics, and commitment to internal peer review and training.

3

Delivering advice:
providing quantitative and qualitative strategic advice to clients through training, impact assessment, leadership papers, stewardship priorities and ESG reporting packages.

4

Engagement:
Adopters are actively engaging with investment managers to enhance their ESG practices, setting minimum requirements, providing detailed explanations for deficiencies, and encouraging improvements rather than opting for divestment.



Adopters of
Impact Investing
Principles for Pensions

Thanks for the leadership provided by our Adopters.





WEBLINK
Find out more about the Principles

1 Firms' mission, governance & reporting



How Adopters routinely include impact investing as a topic for consideration with new and existing pension fund clients

Governance

Respondents committed to embedding The Impact Investing Principles into their governance, focusing on engagement and education, ESG integration, responsible investing, sustainability and net-zero goals.

Adopters typically show dedication to long-term impact and sustainable investment by:

- **Promoting client education** through regular ESG training and developing bespoke ESG beliefs and policies, while actively seeking new impact opportunities across asset classes. Some have developed a market map of available sustainable and impact strategies for all clients.
- **Embedding ESG and stewardship** across their investment approach, incentivising consultants to give high-quality advice aligned with their values.
- **Considering ESG risks and stewardship priorities** to achieve impactful outcomes in public markets.
- **Integrating sustainable throughout their investment process**, applying minimum exclusion criteria and targeting net zero by 2050.
- **Focusing on sustainable investment training** to ensure consultant competence, maintain data integrity, conduct peer reviews and commit to the *Net Zero Investment Consultants Initiative*.

Considerations for asset owners

There was little detail on what motivates consultants to consider and integrate impact into their research or advisory roles, as well as how impact allocations have changed over the years. Greater disclosure is needed on how clients are increasing their impact allocations and whether there have been any changes in the advice they receive or the available investment opportunities. For example, one Adopter, saw an increase from 19 to 23 clients invested in sustainable funds over a year, but the reasons for this rise were unclear. These are important questions for asset owners to consider when appointing advisers.

Strategy

Adopters comprehensively integrated the Impact Investing Principles for Pensions into their strategic advice to clients, by collaborating with them on sustainable and impact investing, emphasising the importance of ESG risks and opportunities within the portfolio. Their approach includes:

- Applying an ESG beliefs questionnaire to understand client preferences and providing tools like ESG ratings reports and carbon dashboards for enhanced transparency.
- Using *TCFD* reporting and climate risk strategy in alignment with clients' existing policies.
- Routinely including ESG and climate risks in strategic advice, using metrics like Implied Temperature Rise and SustainEx.
- Equipping consultants with the resources and training to ensure proficiency in sustainable investment practices, with a commitment to internal peer review and participation in initiatives like the *Net Zero Investment Consultants Initiative*.

Delivering strategic advice

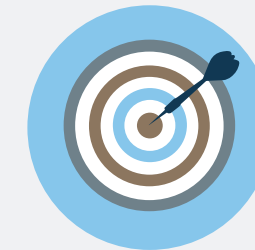
Firms give qualitative and quantitative strategic advice focusing on:

- **Regular impact training:** on climate change, nature breakdown, social factors and carbon markets.
- **Impact assessment:** ESG beliefs are linked to a manager evaluation framework, helping clients to improve ESG credentials over time.
- **Knowledge sharing:** issuing leadership papers on ESG topics, like carbon-reduction and biodiversity.
- **Stewardship:** core clients have set at least three impactful stewardship priorities, viewed as a primary way to create impact in public markets.
- **ESG reporting:** quarterly ESG and climate summary page, and interactive-climate dashboard; annual fiduciary management ESG report, implementation statement, and *TCFD* reports provided to all clients.
- **Support:** a dedicated team of asset transfer specialists to help clients move assets.

Considerations for asset owners

While Adopters often help clients identify their position on the spectrum of impact investing, there is a lack of clarity on how they assist clients in transitioning from traditional towards sustainable and impact investing. How do they enhance their advisory services by offering concrete strategies and actionable steps for clients to progress along the spectrum? This is an important question for investment consultants and fiduciary managers.

2 Supporting clients to set their strategy



How Adopters support pension clients to review the ESG impact across their investment portfolio and provide recommendations

Defining impact

Adopters of The Principles view impact opportunities as assets or products that generate positive social or environmental outcomes aligned with the *United Nations'* sustainable development goals (SDGs), highlighting intentionality, measurability and additionality. They see impact investing as contributing to measurable positive social or environmental impact alongside financial returns, requiring commitment to solving challenges, setting impact objectives, and robust measurement and reporting.

It is important to distinguish between ESG risks and achieving environmental, social and governance impact. While many Adopters are extremely capable of managing ESG risks, how they focus on achieving tangible impact across environmental, social and governance dimensions varies immensely.

One Adopter, for example, annually reviews the ESG capabilities of their investment managers, including their level of ESG and impact integration. The company employs scorecards tailored to each asset class that encompass impact-focused questions, resulting in a fund-specific score ranging from 'meets additional impact criteria' to 'significantly fails to meet criteria.' Similarly, another Adopter provides clients with a sustainability document, integrating climate change risk analysis and reporting alongside additional impact metrics from market-leading climate change data providers. However, a third Adopter primarily focuses on understanding and integrating ESG impacts, with examples including training on *TCFD* and various thematic workshops.

Considerations for asset owners

While ESG integration is widespread, achieving impact remains a distinct focus area. Some firms are actively incorporating impact considerations into their reporting and advisory processes. ESG risk management is prevalent, but there is still a varied approach to achieving tangible environmental, social and governance impact among Adopters.

ESG recommendations review

Firms demonstrate their commitment to reviewing and providing recommendations to clients through reports and documentation. It includes an annual review of investment managers' ESG capabilities and the level of ESG integration in client funds, resulting in fund-specific scores across pillars such as investment approach and reporting, with a focus on impact criteria. Clients receive quarterly investment performance reports, including ESG scores and comments, fostering active engagement with managers for improvement.

Some respondents issue an annual sustainability or ESG report to clients as part of their fiduciary management service, enhancing climate change risk analysis and reporting through partnerships like *MSCI*. Climate change metrics are often included in the report, helping investors understand their portfolio's impact on climate change.

Impact review and updates

Respondents currently provide annual sustainable investment reports to clients as standard. In some cases, clients receive quarterly ESG updates, with medium-to-large clients typically undergoing an annual impact assessment.

3 Supporting clients with implementation



How Adopters support pension fund clients to set impactful objectives, implement their strategy and monitor their investments

Impact goals

Adopters provided case studies highlighting how they assist their clients in setting, implementing, managing and monitoring impact objectives. The approach to setting these goals is often client-driven and tailored to their specific needs, rather than being offered as standard practice. Examples included:

- **Client belief-setting workshops:** helping clients select specific goals of interest, like climate action, and setting robust targets, such as increasing emissions data coverage.
- **Investment and ESG beliefs questionnaire:** followed by extensive training on ESG and sustainability, leading to a successful manager selection process aligned with the client's sustainability goals.
- **Focus on TCFD implementation and stewardship priorities:** guiding clients to achieve net-zero goals and monitor funding risks.
- **Collaboration with a local authority pension fund:** implementing a social housing mandate to align with risk-return objectives while generating positive social impact, leveraging the SDGs' framework to target outcomes like poverty alleviation and sustainable communities.

Impact measurement tools

Adopters offer various measurement tools to help clients monitor their targets and assess alignment with impact goals. For example, one firm develops client-specific reporting frameworks tailored to ESG or SDG beliefs and objectives, covering a range of metrics such as emissions, gender diversity and climate. They are also building an in-house

ESG reporting tool to provide a broader range of consistent measures. Another organisation uses an annual ESG ratings exercise to collect data from managers and populate a carbon dashboard, including details on carbon emissions, exposure to sustainability risks and implied temperature rise. An external provider was appointed to enhance reporting metrics, including carbon emissions, fossil fuel exposure and biodiversity.

A different Adopter assists clients in reviewing climate impacts through sustainability monitoring reports and supports in completing TCFD reports covering climate governance, risk management, strategy and metrics/targets.

Metrics

The focus on climate metrics within tools remains strong. Some Adopters use total greenhouse gas (GHG) emissions and carbon footprints. Others are developing their own metrics; for example, one firm has a client-specific metric reporting framework which aligns with a client's ESG or SDG beliefs and objectives for ongoing target monitoring. While some clients opt for the monitoring of broad ESG metrics – for example, emissions, the gender diversity of boards, and engagements undertaken on ESG grounds – others focus exclusively on climate-related metrics. Another Adopter collects various information from managers which they use to populate their 'carbon dashboard', offering insights on sustainability aspects where data is available, including carbon emissions (carbon footprint and WACI), SDG risk outcomes (eg percentage of women on boards, exposure to UN Global Compact violators), the level of engagement on ESG issues and implied temperature rise.

4 Measuring and managing outcomes



How Adopters support pension fund clients to make changes to their objectives, investments and third-party advisers

Impact goals

Adopters assist pension scheme clients in setting, implementing, managing and monitoring their investments according to their impact objectives, through specific strategies and frameworks.

Case studies

The case study examples on the following pages demonstrate how Adopters of The Impact Investing Principles for Pensions collaborate with clients to align their investment strategies with impact objectives, fostering positive change while meeting their financial goals.

One firm collaborated with a high-profile DC master trust client focused on ESG and climate-related considerations. The client aimed to develop a climate-centric investment strategy aligned with their long-term goals, while addressing both climate risks and opportunities, as well as other sustainability issues related to nature and society.

Another organisation, *XPS Investment* (see *overleaf*) helped a client with strong ambitions for net zero to design and implement a detailed framework for achieving net-zero emissions by 2050, with clear interim targets and alignment to industry frameworks, enabling effective monitoring and ongoing engagement with investment managers:

Additionally, another company, *Barnett Waddingham* (see *over the page*) worked with a global conservation charity to align investment

goals with impact goals, proposing a clear impact policy and investment strategy targeting climate-aligned, biodiversity and agriculture funds.

Improving investment managers' engagement approach

Our Adopters are improving their investment managers' impact investing process through active engagement. The majority of respondents, as part of their annual ESG assessment process, actively engage with their investment managers to drive improvement in ESG integration rather than opting for divestment. In some cases, third-party managers are held to minimal ESG standards for inclusion in portfolios. It is important to note these standards primarily related to ESG factors rather than explicitly impact-related issues.

Adopters typically employ an active engagement approach with investment managers to enhance their ESG practices. They often set minimal risk management and stewardship requirements when they are recommending funds to clients. Investment managers failing to demonstrate these obligations are provided with detailed explanations and are encouraged to make improvements. For example, following their annual ESG monitoring, one Adopter identified a fixed income fund with weak ESG integration and engaged with the manager to explore possible improvements.

Adopter case studies

Developing a climate strategy – XPS Investment

Background

A client with a significant UK profile and links to the UK government had the desire to be market-leading in their commitment to climate change. While the client had strong ambitions to reach net zero, their targets and policies were loosely defined.

Solution

XPS helped design a comprehensive framework for implementing the net-zero strategy, which considers the nuances of the client's mandates and their managers' capabilities, sets clear parameters for achieving the objectives and is aligned to the *Institutional Investors Group on Climate Change Net Zero Investment Framework*. The framework included an overall ambition to reach net zero by 2050, with interim targets to reduce emissions by 50% by 2030 with a 7% year-on-year absolute reduction. The client now has an established net-zero strategy which is soon to be implemented and will allow them to effectively monitor and review progress against their goals as well as initiating effective ongoing engagement with their investment managers. The strategy is successful in aligning the ambition of the client with the sponsor and the UK's national goals.



Global conservation charity – Barnett Waddingham

Background

The conservation charity had set out its impact goals as an organisation. Barnett Waddingham proposed the goals of its investments may be aligned to the impact goals of the organisation, by targeting investments in specific impact areas.

Solution

As an initial step, they proposed the charity should set out a clear, robust and transparent impact policy that considered the organisation's conservation goals, while being aware of the constraints of the investment portfolio, and the availability of investment products today, and into the future. We also suggested an investment strategy which balanced the objectives of the investment portfolio with these impact goals through investments in:

- Climate-aligned investments.
- Biodiversity funds
- Agriculture funds.

Leave us your feedback

? How would you like the Principles to evolve?

Are there any refinements needed to the Principles? If so, what do you suggest?

? How would you like evidence gathering to develop?

Do you like the open-ended approach or would you like us to ask specific questions (for example, list out your memberships of relevant industry organisations).

? How can we improve data gathering?

We believe that the most powerful evidence is, ultimately, the rate of adoption by clients. There seem, however, to be challenges in collating this information. What suggestions do you have for collating this information; how can Pensions for Purpose and the Impact Investing Institute help?

? Would you like your organisation to be explicitly recognised for particular areas of excellence?

Certain aspects of Adopters' responses showed creativity and thought leadership. How would you like to be acknowledged? For example, through awards or through invitations to speak at events?

Pensions for Purpose

Pensions for Purpose already offer access to general information and education through our membership and Community. We also run tailored events for individual pension funds.

Join us

If you would be interested in joining Pensions for Purpose, please contact Stephen Darlington, our Membership Manager (use the 'get in touch' button below).

● Charlotte O'Leary is CEO, and Bruna Bauer is Research Manager, at Pensions for Purpose

Please get in touch
with your ideas
or to join us