

# Share of mind wins share of wallet

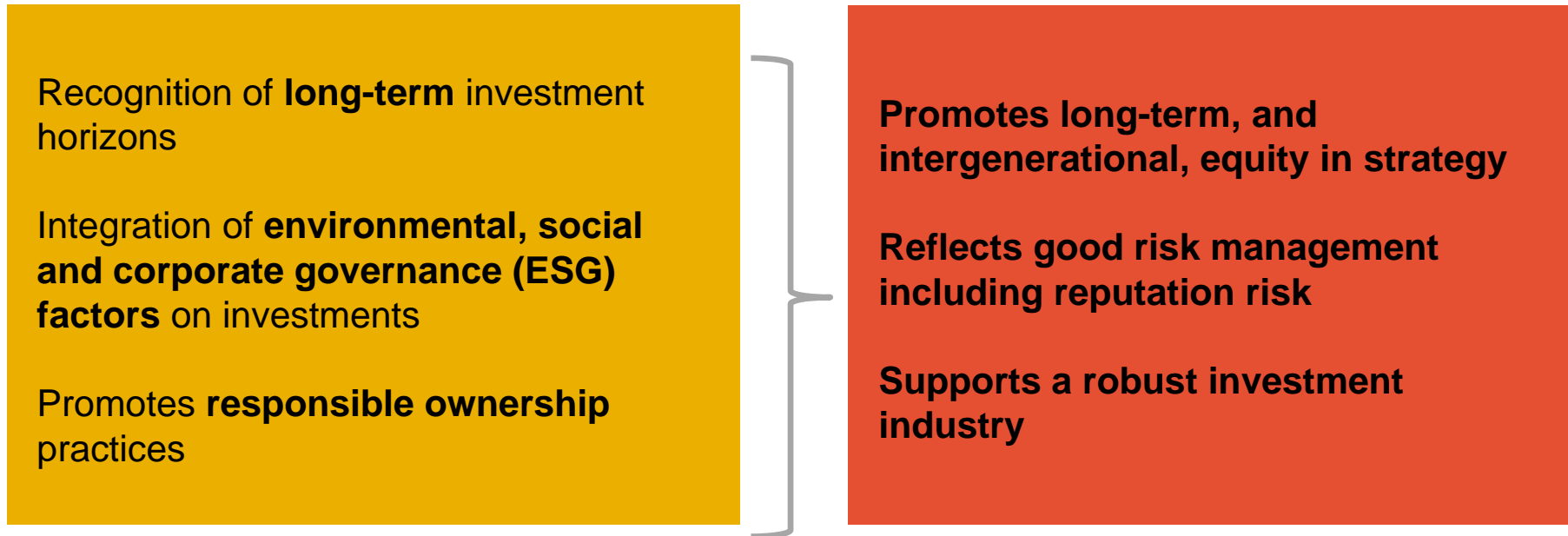
## Allocations to sustainable investment

A presentation to the UN PRI Academic Conference Copenhagen  
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## What is sustainable investing?

- We interpret it to encompass long-term, pure finance-driven investment strategies that incorporate environmental, social and/or corporate governance (ESG) factors in the investment arrangements

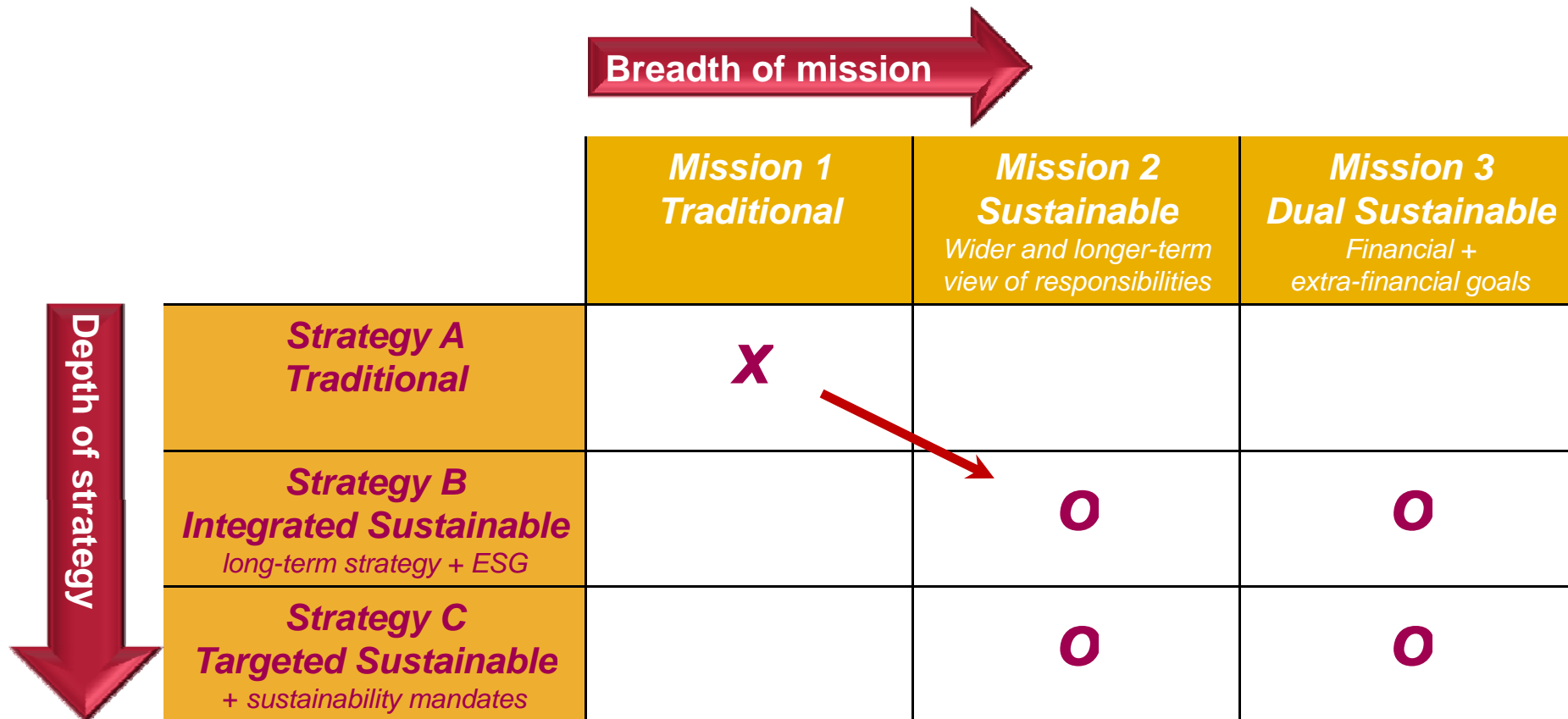


*Long-term investing that is intergenerationally efficient and fair*

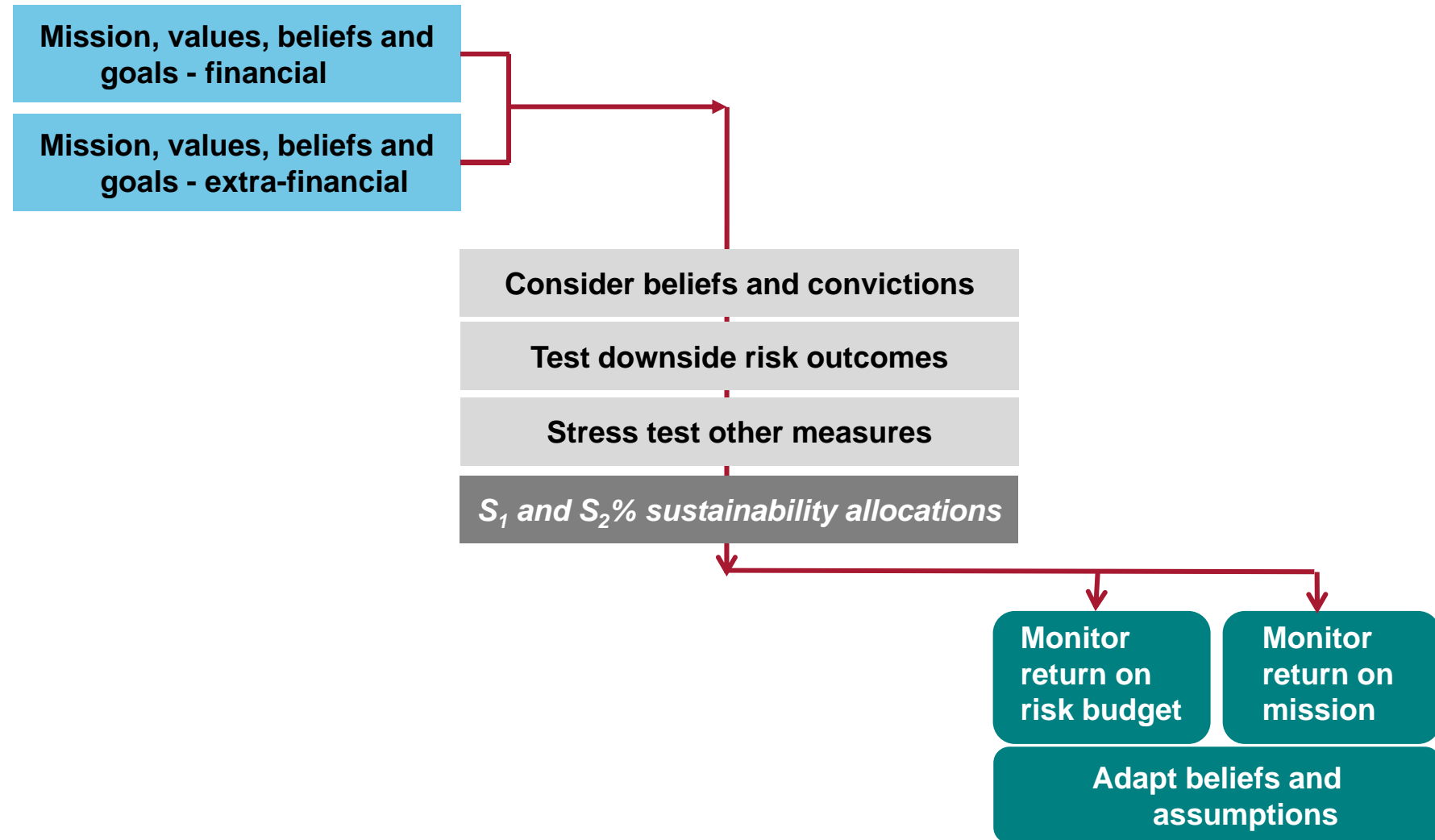
## Two sustainable investment strategies

	Sustainable strategy types	Characteristics
<u>Integrated</u> ESG and active ownership mandates	<p>Mandates that adopt an integrated* approach to ESG risks and opportunities and pursue influence in relation to their investment through active ownership methods like voting and engagement (integrated= takes account of these extra-financial ESG factors alongside the mainstream financial factors)</p> <p>Widely applied to equity, real estate and infrastructure mandates; also applied to bonds and private equity mandates</p>	<p>Easier to implement</p> <p>Lower impact on risk and return</p> <p>Current uptake moderate and growing</p>
<u>Targeted</u> sustainable investment mandates	<p>Mandates targeting assets which will be beneficiaries of ESG and sustainability trends such as the transition to low-carbon economy, increased environmental regulation, natural resource efficiency, human capital factors Includes: environmental opportunities, clean tech, clean energy, clean water, clean air, waste, human/ labour rights</p> <p>Widely applied to equity, private equity, infrastructure mandates; also bonds, commodities including carbon</p>	<p>Harder to implement</p> <p>Larger impact on risk and return</p> <p>Current uptake very low but growing</p>

# Sustainable investing requires clarity of mission and strategy



## Allocation process for sustainability



## Allocation to Sustainable Mandates

### Four principles

- Allocations require the articulation of investment beliefs that present the performance case after risks and costs are taken into account
- Quantification of return estimates is too uncertain for direct use in the allocation process, but quantification of risk estimates can be used
- Allocation should be scaled by reference to conviction reflecting beliefs, governance and mission considerations
- The target limit to the allocation should reflect the sustainability of the allocation through a stress test of expected performance cycles.

Prior problems with the allocation process have resulted in very low allocations so far across the industry, but this is likely to change

## Allocations to integrated and targeted ESG

Fund characteristics	'Conviction points' to ESG	Allocations to integrated ESG	Allocations to targeted ESG
Corporate pension fund with mid-level governance	0	Nil	Nil
Corporate pension fund with strong governance and beliefs in ESG	1-2	Up to 50% of assets	Up to 4%
Public pension fund with dual mission	2-3	Up to 75% of assets	Up to 6%
Sovereign fund	0-4	Up to 75% of assets	Up to 8%
DC fund choice based on member self-select with environmental identity	2-4	Up to 50% of assets	Up to 8%
<p><b>Note:</b> approximate guidance to targets only; funds will tend to reach their targets slowly Conviction points are based on assessment of mission, sustainability beliefs and governance</p>			

## Adherence to PRI

- There is evidence of worldwide traction of PRI
- The benefits of one dominant framing of RI/ SI is a unifying force
- The allocation framework provides demonstration of PRI adherence

PRI adherence framework		
	Asset owners	Asset managers
<b>Principles</b>	Consider mission and beliefs Adopt statements on missions and beliefs	Consider mission and investment philosophy
<b>Decision-making</b>	Adopt an SI allocation framework Decide on <b>S<sub>1</sub></b> and <b>S<sub>2</sub></b>	Adopt integrated investment approach
<b>Monitoring</b>	<b>Background checks</b> – oversight of managers positions / disclosures on PRI <b>Decision checks</b> – check consistency with beliefs <b>Performance attribution covering ESG</b> <b>Extra-financial performance</b> – KPI's in carbon, water, environment, labour	<b>Produce reporting</b> aligned to asset owners requirements opposite  <b>Demonstrate adherence to PRI</b> through combined quantitative and qualitative process

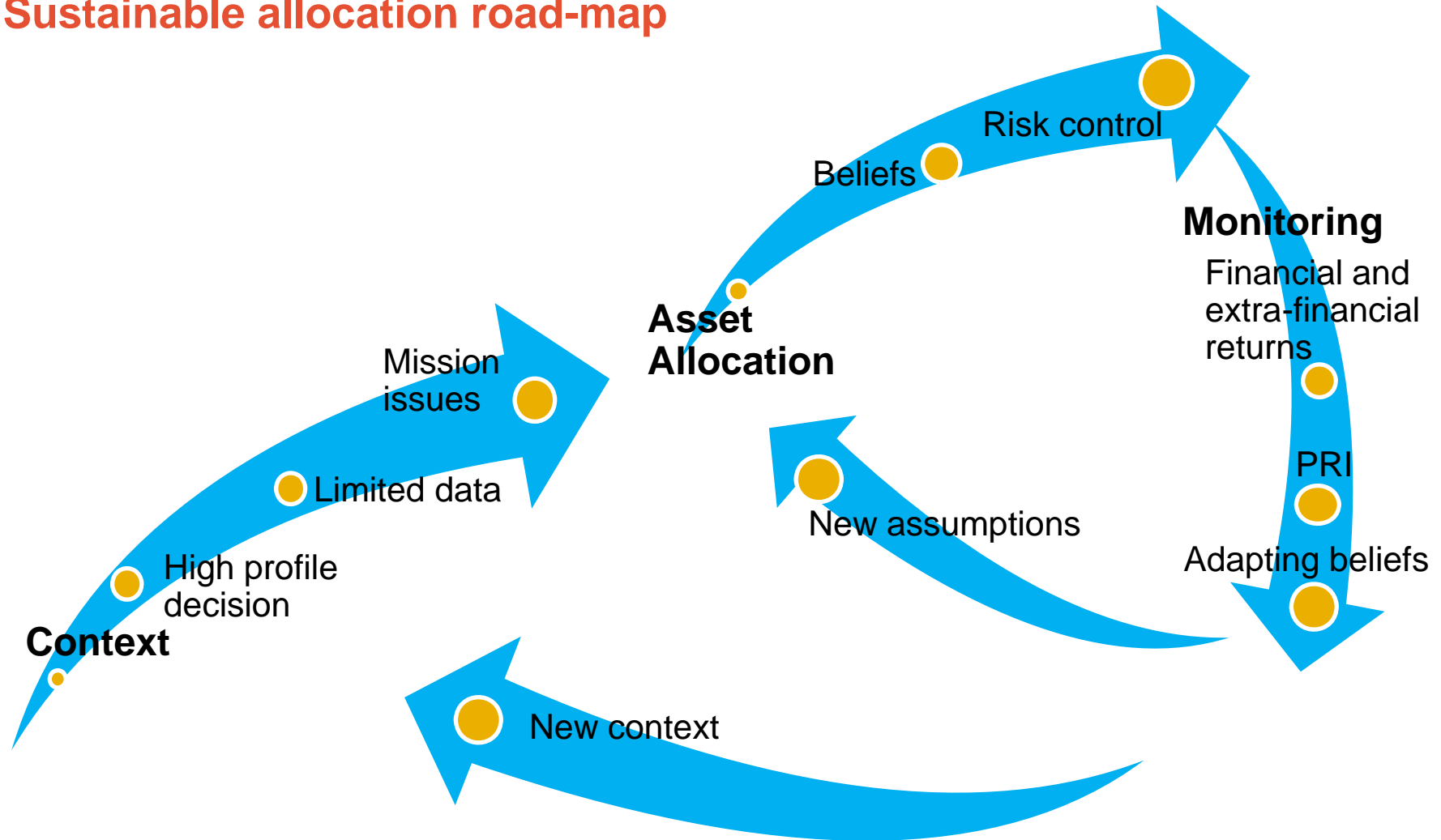
## Typical approaches from managers

ESG type	Manager type	Typical examples
Integrated ESG	Traditional fund managers with separate 'integration-branded' products	Examples include Schroder and Goldman Sachs Typically overlay sustainability analysis onto existing process, often with emphasis on research from external providers
	Holistic integration of sustainability factors across products and asset classes	Examples include Generation and Robeco Typically incorporate macro sustainability factors into asset allocation, sector and company research
Targeted ESG	Mainstream managers invested in quoted equity sustainability mandates	Examples include Sarasin and Henderson Typically use screening and sustainability assessment to focus investment attention and apply ESG themes
	Boutique managers with sustainability targeted mandates in quoted and unquoted sector	Examples include Impax and Climate Change Capital Typically overlay financial analysis over sustainability themed investment ideas

## Example strategies from funds

Fund	ESG Integration and active ownership	Sustainable mandates
PGGM (Netherlands)	Integrates ESG into research on most asset classes Voting and engagement done directly and through outsourced approach	Responsible equity, microfinance, forestry, renewable energy, infrastructure, clean-tech PE Allocation target of around 3%
Pension Fund – Global (Norway)	Integrates ESG considerations into listed equity and real estate portfolios Voting and engagement	Environmental investment programme launched 2009, yet to be invested. Allocation target of around 1%
CalPERS (US)	Voting and engagement Activism program	Activist funds (corporate governance) Clean-tech Allocation target of around 2%

# Sustainable allocation road-map



## Summary

- There are road-blocks to sustainable investing – the ways around have to involve strong thinking and process
- Integrated ESG - easier but less impact on return and risk  
Targeted ESG - harder and more impact on return and risk
- The suggested framework for deciding sustainability allocations combines the inputs of strong beliefs and strong risk control
- Monitoring sustainability requires accounting for extra-financial returns alongside the financial returns
- Monitoring should also consider changing beliefs and context as well
- This monitoring framework can also produce a stronger PRI model

## Where is this going?

- Disciplined thinking matters – sustainable strategies will be held to higher levels of account
- There are a number of practical issues about how sustainable investing will develop
  - The leadership of world class funds will be influential
  - PRI as a positive collaborative force
  - Supply and demand arguments critical, present capacity limited
  - The measurement and benchmarking support needs to develop
  - Fiduciary boards have limited knowledge and experience at present
  - Governments influential in regulation in markets and over institutional funds
- Sustainable investing will take an increasing profile in the institutional funds area – for reasons of opportunities and risks it is worth investing time in it

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