In collaboration with

Vidrio Views

ESG Survey: Clarity Lacking in True ESG Integration

The asset management world has something in common with global politicians these days in that the path forward to implementing meaningful ESG considerations is still fraught with fragmentation.

Vidrio in partnering with boutique advisory firm Close Group Consulting, was able to pinpoint some of the discrepancies in the alternatives and private markets industry.

This survey of investors and managers was conducted across two weeks in mid-October and pre-empted the 2021 United Nations Climate Change Conference, also known as COP26, which kicked off October 31 and is scheduled to run to November 12, 2021.

One of the main findings of our "Vidrio Views" survey this month, and somewhat surprising in nature, was that many large global allocators that have been leading the charge on integrating ESG into their investment processes have not tied those same factors to the compensation they pay portfolio managers and researchers responsible for implementing these strategies.

Tamara Close, Guest Commentator

CFA, Founder and Managing Director of Close Group Consulting

Tamara has over 20 years of combined experience in capital markets and ESG strategy. She is based in Montreal and works with investment management firms and asset owners across asset classes to advance their ESG integration practices within their investment and risk management processes, Tamara was also previously Managing Director and Head of ESG Integration for KKS Advisors, a global ESG advisory firm, and she recently launched an industry-leading ESG integration maturity assessment tool providing standardized industry best practices in a scalable technology-driven solution.

About Vidrio Views

Vidrio Views is a series of monthly market surveys and corresponding reports that analyze the sentiment of leading institutional allocators and LPs in relation to the industry's most pressing topics of the day.

On the specific question of "Do you consider ESG performance/metrics as part of your compensation plans?" none of the survey participants considered this a formal metric at this point. While this finding was somewhat surprising in nature given the large amount of information we hear from both allocators and managers on the importance of ESG, the survey also identified a divergent set of opinions and approaches that reflect the somewhat complex nature of implementing an ESG strategy generally.

Do you consider ESG performance/metrics as part of your compensation plans?

Yes

0%

No

100%

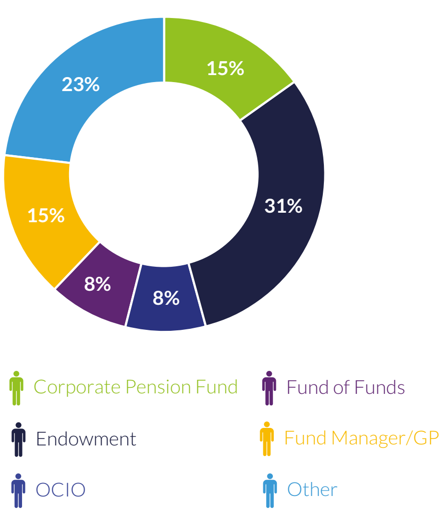
Not currently, but planning to

0%

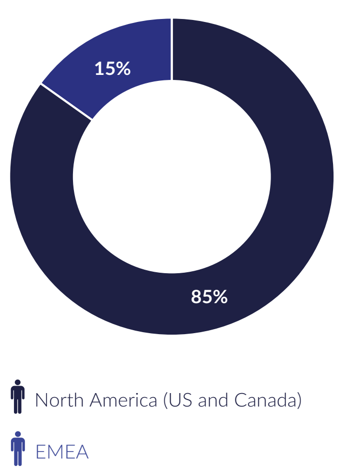
Following on from our September "Vidrio Views" survey that looked at the uptake in crypto investing and some of the main drivers for global allocators, we wanted to take a further deep dive into what allocators and managers are thinking as it relates to making meaningful steps to integrate ESG strategies into their overall investment process and some of the challenges of data and structural issues arising from that undertaking. Not all questions in the survey were limited to one answer and some questions were written to allow multiple responses.

For this month's "Vidrio Views" we surveyed a wide swath of institutional investors -- including OCIOs (8%), (15%) corporate pension funds, (31%) that identified as endowments, (8%) were fund of funds, (15%) fund manager/GPs and (23%) identified as others. Geographically (85%) of the survey respondents were in the US and (15%) in EMEA.

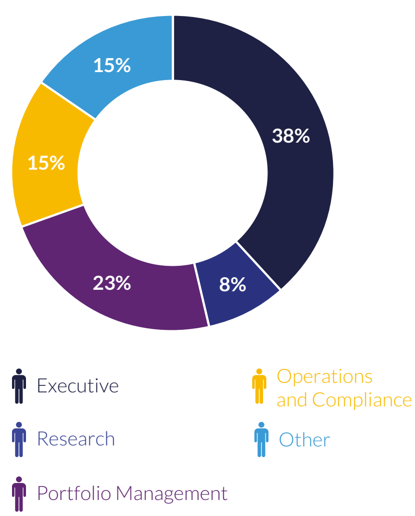
Which of the following best describes your organization?



What is your geographic location?



What is your current role?



We discovered a mix of ESG approaches. We asked, "What do you see as the primary roadblock (if any) to your organization's ability to successfully integrate ESG investment practices?" Responses were mixed though equally distributed. This was led by 42% of respondents that said comparability and reliability of data was a notable roadblock on integrating ESG data. Roughly one-quarter of respondents attributed confusion as to what constitutes best practices, while 16%attributed this roadblock to effectively calculating ESG-specific performance.

What do you see as the primary roadblock (if any) to your organization's ability to successfully integrate ESG investment practices?

Confusion as to what constitutes best practice

25%

Challenges of ESG data (comparability, reliability, etc.)

41.67%

Calculating ESG-specific performance

16.67%

Internal adoption

0%

N/A

16.67%

Other (please specify)

0%

A lot of these findings, while surprising in their nature, were not unusual given the lack of consistency on universal views of ESG integration and agreements on data and metrics we have seen at both CGC and Vidrio through our relative experiences. True ESG integration is an issue that investors and allocators alike have been wrestling with for many years and not something we feel is going to be simply resolved over time.

This was also evident through the survey responses and specifically on the matter as to whether ESG factors are considered a key investment factor for allocators and managers in their investment processes. Investors were relatively split: 23% said that they considered ESG a key investment factor in line with financial factors, while 23% said that they considered ESG factors a key part of the investment process though at a lower weight than financial factors. The same number of respondents agreed to this factor but caveated their responses dependent on the specific strategy or underlying investment at hand. However, 30% of respondents did not consider ESG as a key investment factor for their investment processes.

Is ESG considered a key investment factor for your investment process?

Yes, in line with financial factors

23.08%

Yes, but at a lower weight than financial factors

23.08%

Yes, but depends on the strategy/underlying investment

23.08%

No

30.77%

Investors are still divided on applying ESG factors in risk and opportunity assessments. Fewer than half 38% said they were relying on ESG factors, while over half 54% said they were either planning on it or not doing this at all, while only 8% said they were waiting for more concrete regulatory standards before formally incorporating an ESG framework into their investment decision-making processes.

Are you actively applying ESG factors as part of your risk and opportunity assessments?

Yes

38.46%

No

30.77%

No, but planning to

23.08%

We are awaiting for more concrete regulatory standards before formally incorporating an ESG framework into our investment decision-making process.

7.69%

This lack of formal factors and approaches also showed up in the area of ESG data management. On the question of using third-party ESG data providers, fewer than one-quarter 23% actually do, while 15% said they use external providers, but also create internal ratings.

How are you using third-party ESG data providers in your investment process?

Do not use third-party providers

38.46%

Use a single third-party provider

23.08%

Use multiple third-party providers

23.08%

Use external providers but also create internal ratings

15.38%

Looking at the main drivers for ESG integration more broadly among allocators, overwhelming most 73% identified board and stakeholder demand, while 18% identified the integration of ESG standards to create alpha or manage portfolio risks. An equal amount of 18% identified this driver to ensure alignment with market best practices.

If you are an allocator/LP, what is the main driver for ESG integration? Choose all that apply.

Board / stakeholder demand

72.73%

To create alpha

18.18%

To manage risk

18.18%

To align with peers

9.09%

To ensure alignment with market best practices

18.18%

N/A

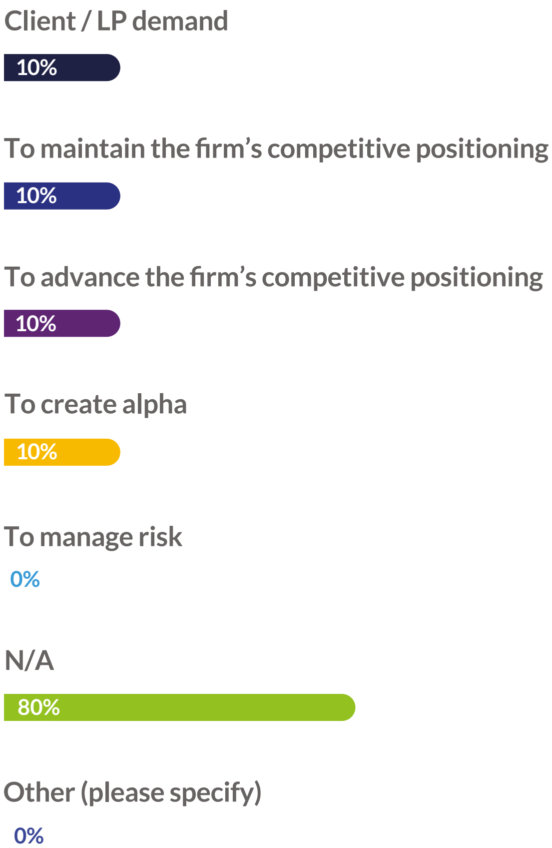
18.18%

Other (please specify)

0%

Divergence over the applicability of ESG investment processes also showed up on the GP side. While most 80% said the question did not apply to them, other drivers of GPs behavior include meeting client/LP demands (10%). Another 10% said integration helped its firm to remain competitive, while another 10% said it advanced their firm's competitive positioning. More importantly, 10% said it allowed them to create alpha.

If you are a fund manager/GP, what is the main driver for ESG integration? Choose all that apply.



All these results will be discussed this month at a live webinar that will take place on Friday, November 19, 11am-12pm EST as part of the current Talking Hedge Santa Monica Virtual series. The webinar will include a panel of allocators and fund managers that will review the results of this survey and discuss actionable takeaways for your own ESG integration processes, including application of best practices and how best to leverage data and technology to support your operations.

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About Vidrio Financial

Vidrio Financial is the first Technology Enabled Service for allocators — providing software and data services to institutional investors globally. Vidrio's data aggregation, analytics and applications help solve complex fund management problems, improve operational efficiency and reduce risk for multi-asset-class portfolio investors. Our clients are the world's premier allocators to external managers.

Contact info@vidrio.com to learn more.