LGIM Head of Sustainability Solutions, Caroline Ramscar

ESG: Opportunities ahead

LGIM Head of Sustainability Solutions, Caroline Ramscar, discusses with *Pensions Age* how LGIM can help trustees meet their ESG and sustainability investment objectives for 2022 and beyond

What do you expect 2022 to bring in terms of developments within sustainability and ESG?

2021 really was the year of ESG, dominated at the end by COP 26 and the resulting headlines on climate and how the private sector can help play our part. We expect this spotlight to remain in 2022.

We are already seeing schemes adopting more sustainable climate benchmarks, looking at their carbon footprint and where they can make changes. Trustees have clearly been thinking about this in 2021 but it will start to play out in 2022 with increased regulatory and market scrutiny. So whereas in prior years we've seen a growing interest around climate considerations in investments, I expect this to come to the fore in 2022, and that discussions will split off into other areas such as biodiversity loss and deforestation. Trustees are already starting to ask about what these issues could mean for their portfolios and our engagements with companies in these areas.

LGIM recently signed the Eliminating Agricultural Commodity-Driven Deforestation commitment letter and for several years now, we have been embedding thinking around deforestation and biodiversity into our engagement activities, particularly under our longstanding targeted engagement programme, the Climate Impact Pledge.

We fully expect that trustees and end investors will start to question their asset managers more rigorously around these new areas of focus.

Therefore, with the spotlight on climate, increasing regulation, and the societal shifts we see around us, asset managers need to provide robust investment solutions to help clients meet their own decarbonisation and climate goals.

It is also important to note that the regulator is also saying to trustees, 'don't forget about the S and the G'. We're fully expecting a more explicit appreciation of the S and the G in regulation down the line. LGIM have been focusing on these issues for a number of years; healthcare is a core long term theme for our stewardship team, and we are seeing increased interest in this area, particularly where trustees have started to think about their investments following Covid-19 and the pandemic.

Within healthcare, trustees may be familiar with pharmaceutical companies, but consideration also needs to be given to the activities of the food sector, given its impact on nutrition, and which to-date may have received less attention. Antimicrobial resistance is one key area of focus: in particular how this challenge plays out in the food chain and what companies are doing to tackle it.

There is a lot of work being done to reduce the reliance on antibiotics in the food sector, where we have been engaging with companies such as McDonalds* and Tesco*. More broadly, our Climate Impact Pledge engagements with food producers and retailers takes a holistic approach to the interrelated issues mentioned earlier of climate, biodiversity and deforestation.

Another important area of focus is diversity. We know that there has been much work and progress around gender diversity in recent years, but there is much more to be done to improve wider diversity and representation. We've been looking at diversity for a number of years, reflected in our voting and engagement policies and are starting to vote now from an ethnic diversity perspective and will vote against boards where ethnic diversity representation is lacking.

Could you clarify how LGIM are helping their clients achieve their sustainability objectives, such as those you mentioned?

The best way as an asset manager to help clients meet any of their objectives, sustainable or otherwise is to provide robust investment solutions – the investment case has to stack up – and to work in partnership with our clients to help them in meeting their own regulatory obligations or sustainability objectives, for example where they have their own decarbonisation goals in place. It is about providing the capability and mainstream solutions that are aligned with the client's risk-return profile and providing the asset class exposures that they require alongside their sustainability objectives.

Our climate solutions that we have available across our index range of funds are a good example of this capability, where there are decarbonisation targets or goals for alignment with the objectives of the Paris Agreement embedded within the funds. For those clients that want to reflect broader ESG considerations more explicitly, our Future World Index funds are a great option, where clients achieve market cap exposure whilst meeting sustainability objectives such as reduced carbon emissions intensity versus the benchmark. On the active side, we have recently launched an actively managed diversified credit portfolio which is aligned with the UN Sustainable Development Goals. The fund will target higher levels of growth and income than traditional portfolios whilst embedding a new proprietary approach to the incorporating the UN Sustainable Development Goals into the investment process.

We've also been working in partnership with Tumelo, which is a fintech company, as a way of exploring innovative ways of tackling specific themes that investor end members and trustees care about. For example, 2021 pay and climate were highlighted as key issues through the Tumelo platform that end members were particularly passionate about. We can help members understand how their investments align with these principles, which I think is really powerful, particularly for trustees when thinking about member considerations and how they can better engage with their pensions.

What about those managing pension funds. What should they be looking for when selecting managers?

It's really important that investors and trustee boards ask their asset managers what they are doing on their behalf, to ask about their voting policies and look at the voting records: What they have voted for and against, if they haven't voted why not, what drives their voting policies, how asset managers define and measure the impact of their actions and how they embed ESG considerations in their organisation as well as in their investment process.

For example, we publish all of our voting and engagement policies and voting records on our website and we publish the results of our Climate Impact Pledge and our proprietary ESG scoring of underlying companies. This information is all publicly available for our clients as well as the companies themselves to see.

Also, look to the wider group or structure in which they operate; if you have a parent company, are they committed to responsible investing, is this something culturally that is consistent across the organisation.

We also must acknowledge that the pace of change and the new regulatory requirements over the past few years in this area is at times overwhelming for trustees, alongside all of the other things they need to think about. I would therefore ask how easy does your asset manager make thinking about these things for you, do they provide guidance, help, training, and support where you need it?

As the pace of change is so fast, what developments do you see ahead? What should trustees be aware of?

We know that we don't have time to wait in tackling climate change so the regulation, and particularly the government's net-zero strategy has prioritised climate and the 'E' considerations, but we know that the regulator is reminding trustees that they shouldn't forget about the 'S' and the 'G'. This will be important and areas of focus such as executive pay, diversity at board and wider company level and healthcare, as mentioned earlier, will be important.

I think as the year progresses, there will also be a greater focus on greenwashing. There will be much tighter and clearer rules and regulations on this, so that it's much clearer to trustees and end investors what is held within their funds. There's going to be a lot more focus on whether funds are actually doing what they say they're doing. There will be a lot of industry focus on evidencing to clients and to regulators the climate and sustainability credentials of funds.

For new developments, I think there'll be much more focus on investments that meet the portfolio's risk/return profiles whilst also making real world impact. We expect there to be a lot more focus on alternatives, as investors are looking for diversification in their portfolios to capture these attractive yields beyond traditional markets and to make more impactful investments.

The thing that excites me most for 2022 is that we are seeing very engaged and informed trustee boards wanting to discuss these issues and not just focussing on the risks, but also the opportunities that integrating ESG considerations into portfolios presents; there's a lot more information and understanding in the market. This provides a real opportunity in 2022 to make a difference.

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