INVESTMENTS
& WEALTH MONITOR

A reprinted article from January/February 2019

U.S. Sustainable, Responsible, and Impact Investing Trends

By Meg Voorhes

INVESTMENTS & WEALTH INSTITUTE®
formerly IMCA

U.S. Sustainable, Responsible, and Impact Investing Trends

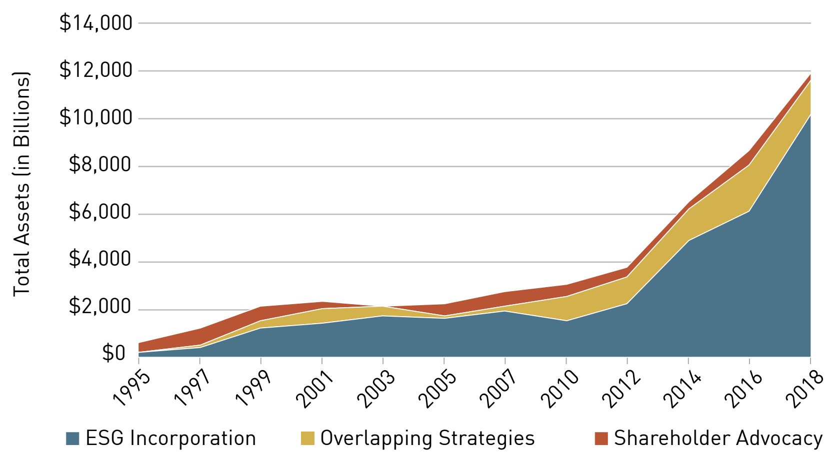
By Meg Voorhes

Sustainable, responsible, and impact (SRI) investing in the United States continues to expand at a healthy pace, as revealed by the latest biennial edition of the US SIF *Report on US Sustainable, Responsible and Impact Investing Trends*. The 2018 edition, released October 31, shows that the total U.S.-domiciled assets under management using SRI strategies grew from $8.7 trillion at the start of 2016 to $12.0 trillion at the start of 2018, an increase of 38 percent. This represents 26 percent—or 1 in 4 dollars—of the $46.6 trillion in total U.S. assets under professional management.

The report further shows that U.S. sustainable investing is taking place across a wide array of investment vehicles and asset classes, and that its practitioners are employing a number of investment techniques and considering multiple environmental, social, and governance (ESG) issues.

Figure 1

SUSTAINABLE AND RESPONSIBLE INVESTING IN THE UNITED STATES, 1995–2018



Source: US SIF Foundation

OVERVIEW

Since 1995, when the US SIF Foundation first measured the size of the U.S. sustainable and responsible investment universe at $639 billion, these assets have increased more than 18-fold, a compound annual growth rate of 13.6 percent (see figure 1).

Through surveying and research undertaken in 2018, the US SIF Foundation identified the following, as shown in figure 2:

- $11.6 trillion in U.S.-domiciled assets at the beginning of 2018 with managers that apply various ESG criteria in their investment analysis and portfolio selection; and
- $1.8 trillion in U.S.-domiciled assets at the beginning of 2018 held by institutional investors or money managers that filed or co-filed shareholder resolutions on ESG issues at publicly traded companies from 2016 through 2018.

After eliminating double counting for assets involved in both strategies, the net total SRI assets at the beginning of 2018 was $12.0 trillion.

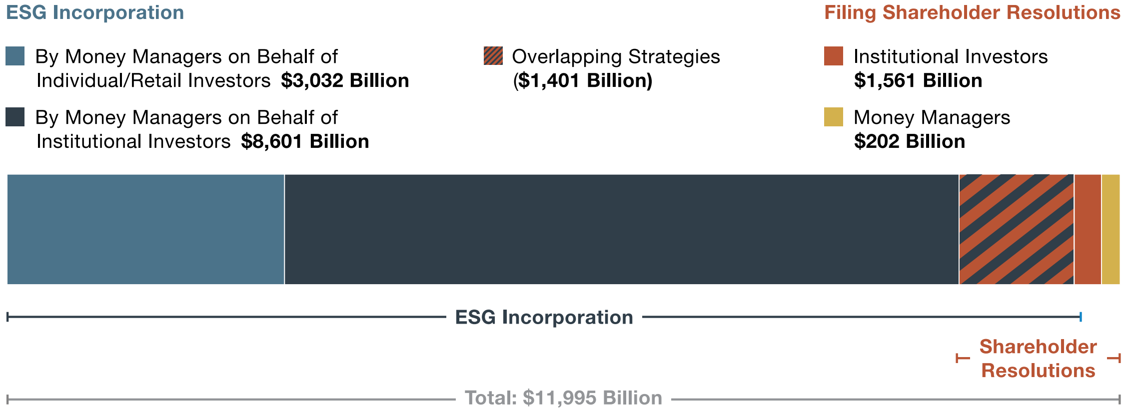
ESG INCORPORATION BY MONEY MANAGERS

The US SIF Foundation identified 365 money managers and 1,145 community investing institutions in 2018 incorporating ESG criteria into their investment analysis and decision-making processes. Of this 2018 total:

- $8.6 trillion was managed on behalf of institutional investors and $3.0 trillion was managed on behalf of individual investors (see figure 2);
- $2.6 trillion—or 22 percent—was managed through registered investment companies such as mutual funds, exchange-traded funds (ETFs), variable annuities, and closed-end funds;
- $588 billion—or 5 percent—was managed through alternative investment vehicles, such as private equity and venture capital funds, hedge funds, and property funds;
- $753 billion was managed through other commingled funds;
- $185 billion was managed by community investing institutions; and
- the balance—$7.5 trillion, or 64 percent— was managed through undisclosed investment vehicles,

Figure 2

SUSTAINABLE AND RESPONSIBLE INVESTING ASSETS, 2018



Source: US SIF Foundation

highlighting the limited nature of voluntary disclosures by money managers incorporating ESG criteria. (We discuss these "uncategorized money manager assets" further, below.)

TOP ESG CRITERIA

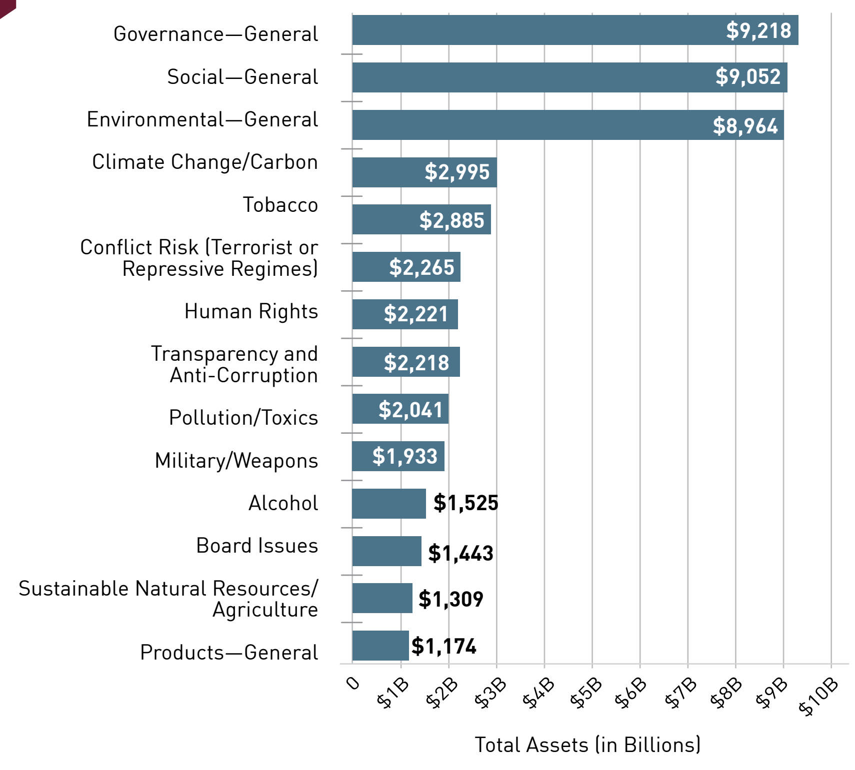
As in 2016, many money managers continue to report that they apply "ESG incorporation" or "ESG integration" across all or a majority of their assets, without further specification, as shown by the top three bars of figure 3.

Figure 3 highlights include the following:

- Climate change was the most important specific ESG issue considered by money managers in asset-weighted terms; the assets to which this criterion applies more than doubled from 2016 to 2018 to $3.0 trillion.
- Tobacco-related restrictions apply to $2.9 trillion in assets, a more than fivefold increase from 2016.
- Conflict risk, which includes policies that restrict investing in companies doing business with terrorist or repressive regimes, was the leading specific social criterion for money managers, affecting $2.3 trillion in assets under management.
- Assets managed with human rights criteria were next at $2.2 trillion.
- Transparency and anti-corruption, affecting $2.2 trillion in money manager assets, was the top specific governance criterion, with growth of more than 200 percent from 2016.
- Concern among money managers and their clients about civilian firearms was reflected in the fact that $1.9 trillion in assets were subject to restrictions on investments in weapons, a nearly five-fold increase from 2016.

Figure 3

LEADING ESG CRITERIA, BY ASSETS, FOR MONEY MANAGERS 2018



Note: Data are aggregated across all investment vehicle types, including separate account vehicles and uncategorized money manager assets.

Source: US SIF Foundation

UNCATEGORIZED MONEY MANAGER ASSETS

Some of the growth cited above in assets subject to specific ESG criteria is a result of trends among the uncategorized money manager assets. These undifferentiated assets, reported by 159 money managers, fell into the following three overlapping categories:

- Money managers who responded to the US SIF survey but selected the "other" miscellaneous category rather than a specific investment vehicle category (e.g., mutual fund, private equity fund, separately managed account). Here, managers may have lumped groups of assets together by ESG criteria rather than listing every single product; however, they did disclose specific ESG criteria associated with these unspecified pools of assets.
- Money managers who applied general ESG incorporation across all of their assets and did not provide an itemization of the funds to which these assets applied.
- Money managers who did not respond to the US SIF survey but who did file Transparency Reports for the global Principles for Responsible Investment program. Although these reports ask respondents to provide total assets and to describe their ESG investment policies, they do not require assets to be disaggregated by vehicle type.

Despite these difficulties, considerably more detail emerged through the 2018 research on the ESG criteria considered across these uncategorized money manager assets than the research team had been able to obtain in 2016. Although 73 to 76 percent of these assets in 2018 were subject to unspecific general ESG criteria, this is less than the comparable 83 to 86 percent reported by the managers of these assets in 2016.

Notably, five of the leading specific ESG criteria cited by these managers at the start of 2018 were absent from their top-10 list in 2016: tobacco, human rights, military and weapons, labor, and conflict risk. Tobacco, moreover, affects $2.15 trillion in assets, making it the top specific criterion considered by the managers of these assets.

In addition, the remaining five specific criteria on this top-10 list are now reported to apply to significantly more assets than in 2016. The leading environmental issue, climate change, is now considered across $1.98 trillion of uncategorized money manager assets, a 62-percent increase over the $1.22 trillion of these assets subject to this criterion in 2016. Transparency and anti-corruption, the top specific governance issue, is applied to $1.90 trillion in assets, a more than threefold increase from the $579 billion reported in 2016. Pollution and toxics considerations now affect $1.60 trillion, a 161-percent increase over 2016, and considerations of sustainable natural resources and agriculture affect $1.00 trillion, up 65 percent over the affected assets in 2016. A similar percentage increase was seen in the assets affected by board issues.

MOTIVATIONS FOR SUSTAINABLE INVESTING

US SIF gathered data from 365 money management firms; a subset of 141 with combined ESG assets of $4.2 trillion voluntarily responded to a question on their motivations for incorporating ESG criteria into their investment process. Perhaps not surprisingly, the leading motivation, based on the number of money managers citing it and the assets they represent, is client demand, as shown in table 1. But more than half the respondents also cited such reasons as to fulfill missions or values, to pursue social or environmental benefits, to improve returns over time, to minimize risks, and to fulfill fiduciary duty. For the first time in 2018, US SIF asked whether implementing one or more of the UN Sustainable Development Goals was a motivation. Although only 40 percent of the responding managers cited this as a factor, they collectively represented more than $2 trillion in ESG assets.

Table 1

MOTIVATIONS FOR SUSTAINABLE INVESTING

Reason	Number of Money Managers	% of Managers Responding	ESG Assets (in billions)
Client Demand	115	82%	$4,160
Mission	114	81%	$2,509
Social Benefit	112	79%	$2,494
Returns	107	76%	$3,696
Risk	106	75%	$4,026
Fiduciary Duty	82	58%	$3,986
UN Sustainable Development Goals	57	40%	$2,151
Regulatory Compliance	31	22%	$1,864
Total Responding	**141**		**$4,180**

Note: Managers of community development loan funds who responded to these questions also are included. Respondents could choose multiple reasons, so counts and percentages do not sum.
Source: US SIF Foundation

ESG INCORPORATION TECHNIQUES, STYLES, AND ASSET CLASSES

A slightly different subset, 131 money management firms representing $3.2 trillion in assets, voluntarily responded to a question about the ESG incorporation techniques they use. The leading technique is ESG integration—the systematic and explicit consideration of ESG risks and opportunities in financial analysis—although exclusionary screens also are widely used, as shown in table 2.

Sustainable, responsible, and impact investing is not confined to a single asset class. A subset of 132 managers with more than $3 trillion in combined ESG assets provided a breakdown by asset class. Nearly half (49 percent) of their combined ESG assets were

Table 2

ESG INCORPORATION STRATEGIES BY MONEY MANAGERS, 2016

Strategy	Number of Money Managers	% of Managers Reporting	Assets Affected (in billions)
ESG integration: the systematic and explicit inclusion by investment managers of ESG risks and opportunities into traditional financial analysis	98	75%	$2,578
Negative/exclusionary: the exclusion from a fund or plan of certain sectors or companies based on specific ESG criteria	87	66%	$2,149
Positive/best-in-class: investment in sectors, companies, or projects selected for positive ESG performance relative to industry peers	81	62%	$299
Impact investing: targeted investments, typically made in private markets, aimed at solving social or environmental problems	80	61%	$80
Sustainability-themed investing: the selection of assets, specifically related to sustainability in single- or multi-themed funds	71	54%	$212
Total Responding	**131**		**$3,156**

Source: US SIF Foundation

invested in public equities; 42 percent were in publicly traded bonds or fixed income and 9 percent were in other classes such as cash and private assets.

Fund and product offerings in the ESG space are dominated by active management. Of the 135 money management firms that responded to a survey question on this topic, active management accounted for 92 percent of the $4.0 trillion in ESG assets they collectively represented. Because 2018 marked the first time that US SIF posed this question to survey respondents, there is no comparable data from previous years to suggest whether the active versus passive breakdown is changing. However, one clue that passive investing approaches may be gaining ground is offered by the strong growth in ETFs that consider ESG factors, from just 25 ETFs with $3.5 billion in assets in 2016 to 69 with $7.4 billion in 2018.

ESG INCORPORATION BY INSTITUTIONAL INVESTORS

In addition to money managers, US SIF also conducted research on 496 institutional investors with $5.6 trillion in ESG assets. The data received from these institutional asset owners shows how and why they incorporate ESG criteria into their investment analysis and portfolio selection. The group included institutional asset owners and plan sponsors such as public funds, insurance companies, educational institutions, philanthropic foundations, labor funds, hospitals and healthcare plans, faith-based institutions, other nonprofits, and family offices.

Of this $5.6 trillion in institutional ESG assets:

- Public funds represented the largest share (more than $3.0 trillion).
- Investment policies related to conflict risk affected $3.0 trillion, making it the single most prominent ESG criterion, in asset-weighted terms.
- Similar to trends among money managers, tobacco faced some of the largest growth as a single ESG factor, at more than 120 percent.
- Continuing a trend that began in 2012, criteria related to climate change and carbon emissions remained the most important environmental issue for these institutions, affecting $2.2 trillion.
- The most prominent social issue after conflict risk was equal employment opportunity and diversity, addressed in $1.6 trillion of institutional assets, a 128-percent increase from 2016.
- Investment restrictions related to weapons now affect just more than $1.5 trillion in assets, a 78-percent increase since 2016.

INVESTOR ADVOCACY

From 2016 through the first half of 2018, 165 institutional investors and 54 investment managers collectively controlling nearly $1.8 trillion in assets at the start of 2018 filed or co-filed shareholder resolutions on ESG issues (see figure 2). Religious institutions and money managers constituted the majority of these shareholder proponents, but public funds represented the largest share of assets involved.

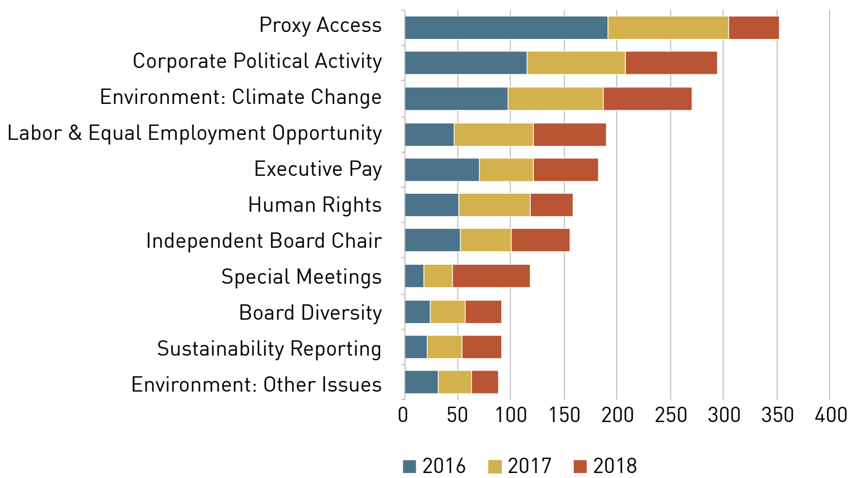
As shown in figure 4, the leading issue raised in shareholder proposals from 2016 through 2018, based on the number of proposals filed, was "proxy access." Investors filed 353 proposals at U.S. companies during this period to facilitate shareholders' ability to nominate directors to corporate boards. As a result of the strong investor support for these proposals, the share of S&P 500 companies with proxy access policies grew from 1 percent in 2013 to 65 percent in 2017.

Disclosure and management of corporate political spending and lobbying were also top concerns. Shareholders filed 295 proposals on this subject from 2016 through 2018. Many of the targets were companies that have supported lobbying organizations that oppose regulations to curb greenhouse gas emissions.

A surge in shareholder proposals on climate change that began in 2014, when investors wrestled with the prospects of "stranded" carbon assets and U.S. and global efforts to curb greenhouse gas emissions, has continued: 271 proposals were filed from 2016 through 2018.

Figure 4

LEADING ESG ISSUES 2016–2018, BY NUMBER OF SHAREHOLDER PROPOSALS FILED



Note: Data for 2018 show numbers of proposals filed for 2018 meetings through July 15, and all vote results known as of July 15.
Source: ISS, Sustainable Investments Institute

The proportion of shareholder proposals on social and environmental issues that receive high levels of support has been trending upward. During the proxy seasons of 2012–2015, only three shareholder proposals on environmental and social issues that were opposed by management received majority support, but 18 such proposals received majority support during 2016–2018.

Investors increasingly are engaging in ways other than filing shareholder resolutions. A subset of survey respondents, including 49 institutional asset owners with more than $1 trillion in total assets and 88 money managers with $9.1 trillion in assets under management, reported that they engaged in dialogue with companies on ESG issues. The extent of engagement reported by money managers has increased notably since 2016, when only 61 managers with $6.9 trillion in assets reported that they engaged companies on ESG issues.

CONCLUSION

In short, sustainable and responsible investing is a dynamic field that is gaining practitioners and popularity. What unites its diverse investment approaches—and ultimately distinguishes them from the broader universe of assets under management in the United States—is the explicit consideration of ESG risks and opportunities in investment decision-making and engagement.

Meg Voorhes is director of research at US SIF: The Forum for Sustainable and Responsible Investment. She earned a BA in economics from Wesleyan University and a Master of International Public Policy from the School of Advanced International Studies at Johns Hopkins University. Contact her at mvoorhes@ussif.org.

REFERENCE

US SIF. 2018. Report on US Sustainable, Responsible and Impact Investing Trends. https://www.ussif.org/trends. Washington DC: US SIF.

INVESTMENTS & WEALTH INSTITUTE®
formerly IMCA

5619 DTC Parkway, Suite 500
Greenwood Village, CO 80111
Phone: +1 303-770-3377
Fax: +1 303-770-1812
www.investmentsandwealth.org