

Initiating the Environmental, Social and Governance (ESG) conversation

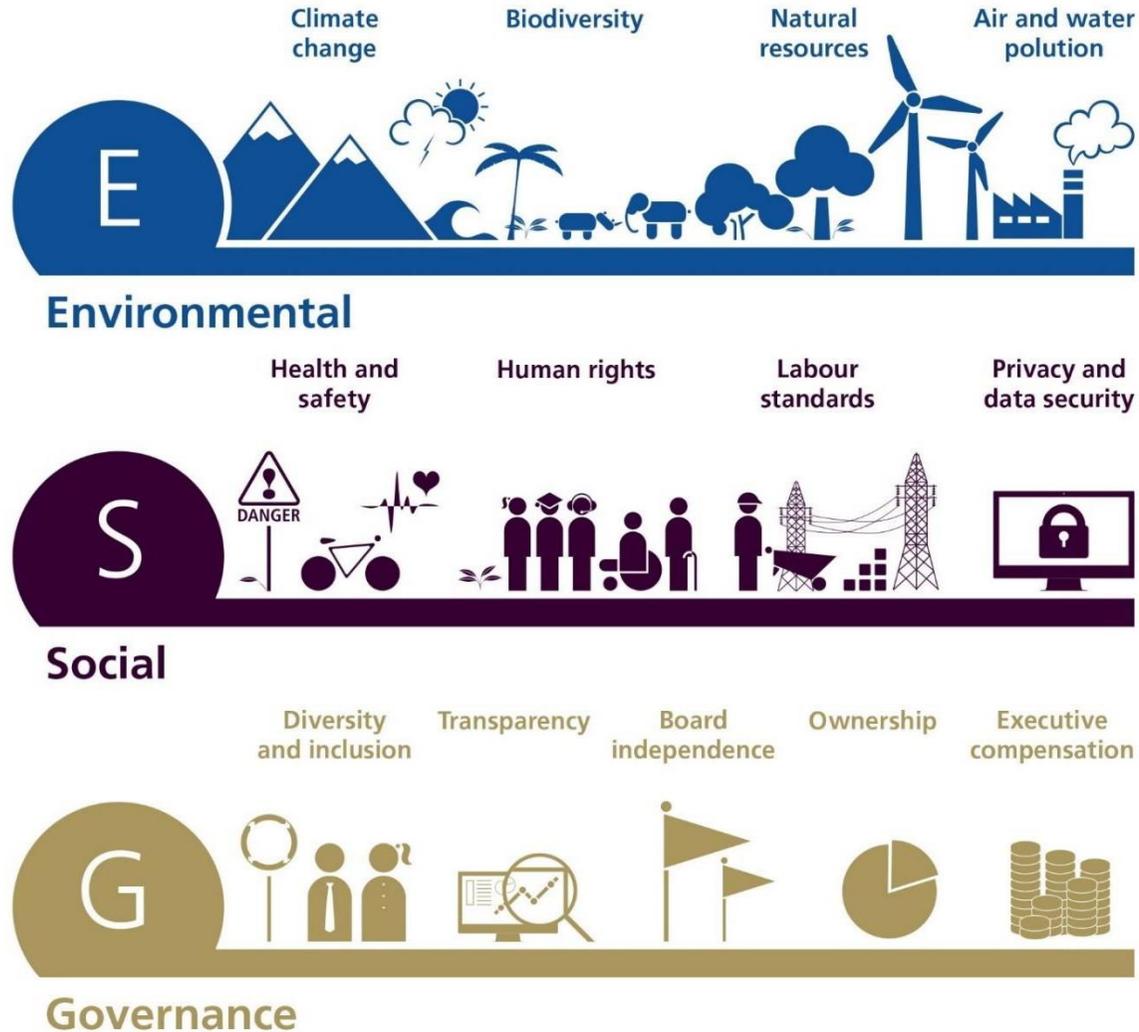
Wednesday 31st March 2021

Robert Hardy – International Technical Director

LGT – VALUES WORTH SHARING



What is ESG?



Source: LGT Vestra

What are my responsibilities – can I ignore it?

- 170 regulatory measures
- European community
- MiFID II amended
- FCA / COBS

What are my responsibilities – can I ignore it?

- DWP
- Sustainable Finance Disclosure Regulation (SDFR)
- Investment Association (IA)
- IA – Sustainable Finance Regulatory Requirement overview
- Too much going on to ignore it

What should we do?

- Check Providers
- Fact finding
- Defensive Step



The future is here?

- EU Sustainable Finance Disclosure Regulation (SFDR) and UK domestic legislation
- The Lang Cat "Crossing the Event Horizon": An adviser guide
- Central Investment Propositions (CIPs)/Central Retirement Propositions (CRPs)/Suitability

Some Perspectives: Sustainable Finance Disclosure Regulation (SFDR)

- Came into force in March 2021

Asset Managers

- Funds will be divided broadly into three categories:
 - Integrate a sustainability factor assessment into their investment process
 - Have sustainability characteristics but work on an "exclusion" basis as opposed to specific "sustainability" agenda
 - Have a sustainability agenda

Some perspectives: Sustainable Finance Disclosure Regulation (SFDR)

- **Advisers**
 - Amendments to MiFID II
 - Will see advisers be required to directly ask clients about their sustainability preferences

"And take them into account when assessing the range of financial instruments and insurance products to be recommended"*

*Source: Richard Bacon FCA Director of Strategy, Building trust in sustainable investments, October 2020

What about the FCA?

...As the audience will be aware, the EU is pursuing several ambitious regulatory initiatives under the Sustainable Finance Action Plan.....

*We welcome the UK Government's commitment in the Green Finance Strategy to 'matching the ambition of objectives' of the EU's Plan. We are therefore working closely with the Government and other regulators on **how to implement the EU's proposals in the UK.***

Immediate areas of focus are the Sustainable Finance Disclosure Regulation and the EU's Taxonomy for sustainable activities.

*The FCA recognises the **benefits of internationally-aligned approaches.** We therefore fully support the Government's commitment to promoting globally consistent standards and to strengthen the UK's status as a global hub for sustainable finance.*

FCA: Guiding Principles

- Consistency in messaging and approach. Does what it says on the tin and matches consumers' expectations.
- A product's ESG focus should be clearly and fairly reflected in its objectives.
- A product's documented investment strategy: should set out clearly how its sustainability objectives will be met.
- The firm should report on an ongoing basis its performance against its sustainability objectives.
 - This is about giving consumers the information they need to understand whether the stated objectives have been achieved in a quantifiable and measurable way.
- The firm should assure ESG data quality, understand their source and derivation.

The Lang Cat: "Crossing the Event Horizon"

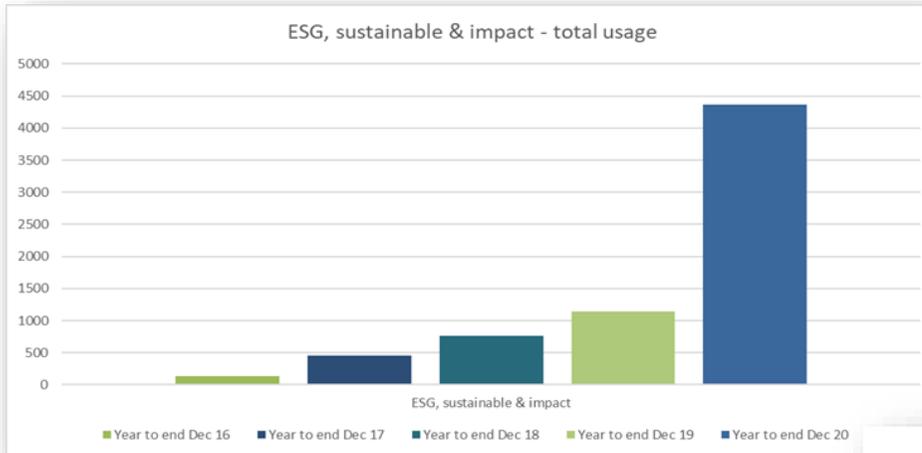
Identified five themes:

- **Clarity:** Sector noise, language effects of "greenwashing"
- **Demand:** The public gets what the public wants or the public wants what the public gets
- **Conflict:** Will regulation bring back more "product-centric" recommendations
- **Gravity:** Some degree of impact on adviser suitability is inevitable
- **Influence:** Between the investment and advice sectors

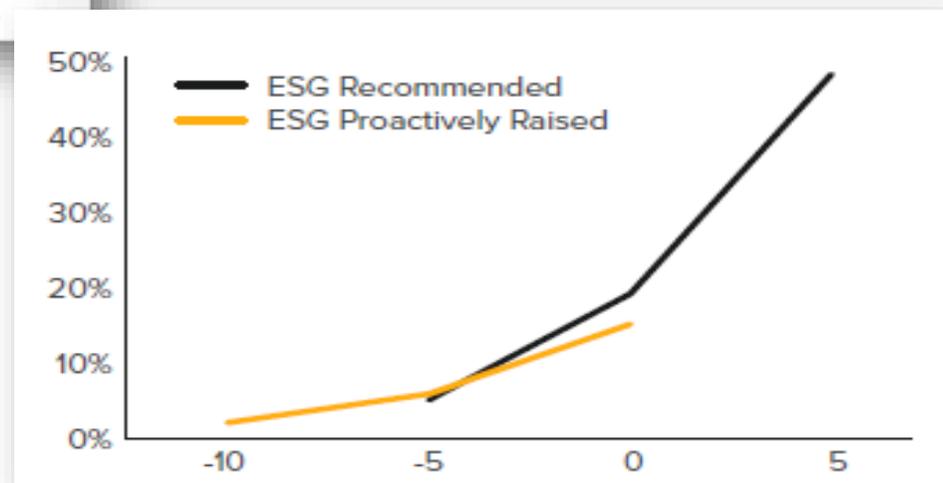


Source: The Lang Cat "Crossing The Event Horizon"- An Adviser Guide 2021

The Lang Cat: Demand



Relates to total touch points on this page of the ThreeSixty website:
<https://www.threesixtyservices.co.uk/client/analyse/threesixty-research/ethical-investing/>



Source: The Lang Cat "Crossing The Event Horizon" - An Adviser Guide 2021

The Lang Cat: Conflict

- Framing the ESG conversation with a client
 - How to identify their values and interests?
 - How are these integrated and expressed within a CIP/CRP and suitability?
 - Care about "not leading the client"
 - Impact on CIP construction
 - DFM: Model Portfolios
 - Multi-Asset funds or broader fund range
 - The emergence of "primary" and "secondary" CIPS?
 - Blending?

Understanding the client

Discussing differing styles of ESG investment to establish broad areas of interest

What is ESG investing?

ESG investing involves considering **environmental**, **social** and **governance** factors alongside financial considerations when assessing investment opportunities.

When fund managers (acting on behalf of the investors investing in their funds) are deciding which companies to invest in they may search out and include companies based on their ESG characteristics.

Environmental factors refer to how companies are performing in their stewardship of the environment, for example:

- Carbon footprint
- Energy consumption
- Greenhouse gas emissions

Social factors consider how companies are manage relationships with employees, suppliers, customers, and the areas where they operate, for example:

- Human rights and social justice
- Working conditions and employee relations
- Health and safety standards

Governance factors focus on company leadership. For example:

- Board diversity, structure and pay
- Avoidance of bribery and corruption
- Management & culture

ESG investing offers the potential to invest in ways that reflect the values that are important to you through using investment solutions that aim to take related ESG characteristics into account.

ESG investing may be referred to by other terms such as socially responsible investing, sustainable investing, impact investing, or values based investing.



Sustainable investing questionnaire

Understanding your values

Before providing you with comprehensive financial advice, your Financial Adviser will assess your capacity for loss, attitude to risk and financial objectives. Increasingly, financial advisers are looking to capture a client's desire to achieve more than financial return with their investment portfolios. This questionnaire is designed to guide the conversation in relation to your sustainability goals.



Source: LGT Vestra

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Some ideas for content



Source

<https://www.theia.org/sites/default/files/2019-11/20191118-iaresponsibleinvestmentframework.pdf>



Source

<https://www.thepfs.org/media/9223844/good-practice-guide-social-impact-investing.pdf>

Checklist

- ✓ Choosing an investment manager that has a clearly thought out and demonstrable sustainable investment process
 - What is the commitment and mission behind the allocation of capital
 - What is the ESG integration process, how is it measured and assessed
 - What is the impact generated, and how is it being measured

- ✓ Being able to document the sustainable approach the DFM is taking, along with evidence of alignment of capital to sustainable investing themes (SFDR disclosure: a common way to inform investors of sustainable risk & investment types)
 - Important due diligence for you as a financial advice firm
 - For your client it is a transparent expression of where capital is invested

- ✓ Selecting a Fund Manager that is integrating sustainable principles within their own business 'walk the walk'

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