TITLE:
On short-termism, impact, doing no harm, making a difference

CONTENT:
I recently wrote a piece as a call for financial advice firms to raise their Sustainable Finance market participation. Whilst not a pre-requisite, before continuing with this article you may wish to have a read as I continue heavily with the theme! (read it here https://esgaccord.co.uk/some-thoughts/)

We designed the ESG / Sustainable Finance Triage and Values Questionnaires compliance frameworks with the aim to reduce (compliance risk-loaded) assumptions, to educate neutrally, raise Distributor/Manufacturer relationships, reduce broad risks, increase best-practice-suitable-outcomes for clients… Yes, to increase Trust, Transparency and Tools (https://www.fca.org.uk/firms/climate-change-sustainable-finance) in this fast evolving new space!

Emphasis so far in the UK has been on disclosures. The new HM Treasury document 'A new chapter for financial services' explains the Sustainability Disclosures Requirements 'SDR' which will be an economy wide regime. And it says the FCA will introduce a new sustainable investment label based on this;

"Enable consumers to quickly and easily see the environmental impact of their investments. The government will work with the FCA to introduce a sustainable investment label. This will cover retail investments using information provided through the SDR"

Additionally the proposed TCFD scope will cover 98% of AuM in both the UK asset management market and held by UK asset owners, representing £12.1 trillion in assets managed in the UK. This made me want to know what is the scale and reach of the adviser market here:

A conservative estimate of AUM for the Financial Advice sector stands at approximately £272Bn (end 2019 https://www.pimfa.co.uk/about-us/industry-statistics/) and there were 27,557 financial advisers in the UK in 2019 (https://www.nextwealth.co.uk/financial-advice-market-trends-uk/).

So here we go again. Our gap. Policy makers are giving us the taxonomy and disclosure regulations. Following this (and let me stress here please that PROD now does in fact mean matching target outcomes to clients so this means advisers should now be including ESG/SF preferences surely!) the interests of clients and the infusing of ESG & Sustainable Finance values will come from conduct principles

So we can see the scale and scope of TCFD. Accounting frameworks - TBL, ESG metrics are like a web running right through the whole financial system. Almost half of global assets under management are now linked to emissions pledges so the entire investment industry has reached a 'tipping point 'with $43tn in funds committed to net zero. (https://on.ft.com/3qPm5Dr). The corporate implications and advice implications are huge.

Onto short-termism: Sort-termism alarm bells rang for me when I read the NextWealth ESG Tracker Study https://www.nextwealth.co.uk/esg-tracking-study-2021-update/nextwealth-esg-report-april-2021/ - it stated;

"56% - More than half of advisers believe they should offer ESG badged funds in addition to a general Centralised Investment Proposition (CIP)".

This can be read a number of ways. It appears great, yes OK the adviser market has reached its own tipping point - more advisers believe in adding ESG badged funds to their advice proposition. On the other hand, it screams out a lack of broad market understanding regarding the whole scale and scope of change on the horizon - TCFD scope will cover 98% of AuM UK! ESG & Sustainability generally needs to be viewed as whole business /market and long term, not a bolt on fund option to add to your service proposition. Any advisers worth their salt, especially those interested and targeting Wealth Transfer, Family, long-term investing or indeed exit planning, need to grasp this quickly. There is huge opportunity for those who do grasp this quickly, before the funds shift to the next generation.

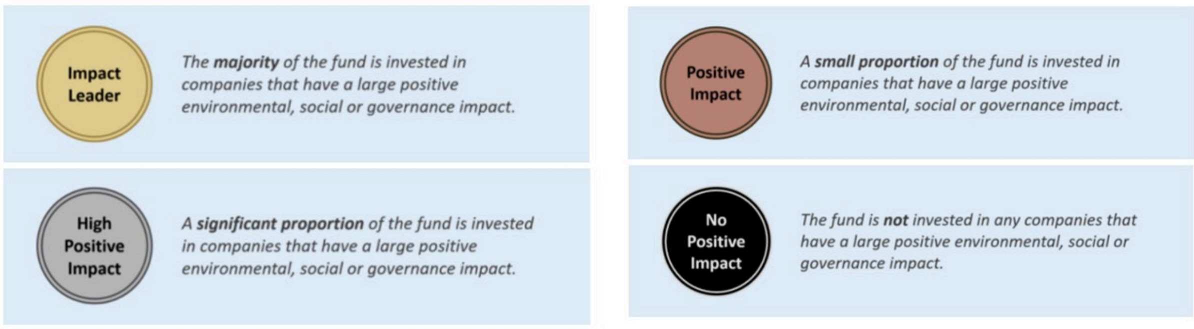
In this piece I've already referenced the FCA Trust, Transparency and Tools - which I whole-heartedly agree with. What I'd like to bring up next is the Adviser gap. So far and rightly, due to scale, we have Asset Managers and Consumer driven information for Sustainability.

In the FCA Insight article last week - 'Sustainable investing: objective gradings, greenwashing and consumer choice', the survey conducted is "comparing features' of funds and the response from consumers. No explanation or education of terms - basics as end-consumer facing. Basically the results show that ESG images, descriptions and strategies have no statistical effect on consumer choice, but randomly assigned ESG medal badging (presented as objective information) does have significant effect on choice.

Also just in is guidance via FCA Authorised fund managers 'assessments of their funds' value https://www.fca.org.uk/publications/multi-firm-reviews/authorised-fund-managers-assessments-their-funds-value. I'm pulling at strings of relevance to the categorisation of funds into Article 8&9 funds, the release of the publication shows the FCA preparing for uptick in reporting needed to accommodate all the new ESG/SF funds and TCFD requirements. The FCA expects; "all AFMs to consider these findings and use them to assess their AoV processes".

OK, now tie-in all this with mandatory TCFD and the SDR and we are good to go right? Well, yes and no. The adviser/client 'sustainability preferences and outcomes' compliance gap is still not addressed (hello ESG Accord!). And here is another thing which I think falls under Transparency:

The terminology used in the sample medal badging. Sample medal gradings are presented as objective info, great. But the descriptive terms used are as follows



(Source: https://www.fca.org.uk/insight/sustainable-investing-objective-gradings-greenwashing-and-consumer-choice)

The use of the term 'impact'. Does this imply the 'Impact Leader' badge is an Impact fund with dual capacity to generate positive and measurable impact alongside a quantifiable financial return? I don't think or believe the FCA means to imply this. At ESG Accord we have discussed and are often struck by the potential confusion of using the term 'Impact' for the board category of clients who 'wish to do no harm / make a difference'.

Unfortunately, without additional warnings attached, will the 'non-advised' end-consumers know this difference? This can increase the risk of entering into a product they don't understand, which is potentially a higher risk than their profile? Financial Advisers can clearly help by raising market participation through their compliance systems and increase knowledge of the nuances and differences across the Sustainable Finance values spectrum.

I'd like to leave you with this; 96% advisers say they have clients invested in ESG, sustainable, ethical or impact funds or solutions. And, 83% of advisers include a question about ESG investing in the Know Your Customer (KYC) or fact find process (NextWealth ESG Tracker Study).

The investable universe has already changed with almost half of global assets under management are now linked to emissions pledges. The FCA Consultation Paper 21/17 "Our proposals aim to increase transparency and enable clients and consumers to make better informed decisions".

We have PROD, we have MiFID II now. Is a single, simplistic question sufficient to raise market participation? We don't think so.

REFERENCES

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