Sustainable investment – a call to action

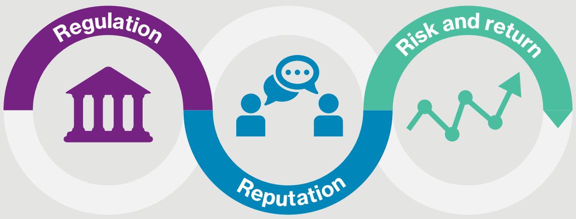
By Adam Gillett

As investors and regulators now recognize the importance of sustainable investment, the key issue becomes translating thinking into action.

In recent years, many drivers have powered sustainable investment's momentum, and the cumulative effect has elevated its importance on many asset owners' agendas. Pressure has come from the end savers (such as pension fund beneficiaries) for institutions to consider sustainability topics that are important to them – think of the fossil-free campaigns at universities across the U.S. and U.K., for example. Regulators and industry bodies have also introduced new standards and guidance to improve investment practices (such as IORP 2 in Europe) and transparency.

It is not unusual to see mainstream media headlines highlight sustainable investment issues – corporate scandals such as Wells Fargo and Uber, as well as industry-wide topics such as executive compensation, board diversity and supply chain management. Indeed, many sustainability-related issues are very much in the general public consciousness, perhaps none more so than climate change, which was recently described as "the single biggest urgency" for investors by Adrian Orr, CEO of the New Zealand Superannuation Fund, widely recognized as one of the leading global asset owners.

Figure 1. **Drivers of sustainable investment**



Investors often ask what evidence there is to support the financial value of sustainable investment, and we believe the increasing body of evidence for the risk/return benefits of this area is compelling. Asset owners across the world are taking note and making significant portfolio responses. The Government Pension Investment Fund – the world's largest pension fund – has been a very vocal proponent over recent years, and is heavily contributing to the wave of stewardship and environmental, social and governance (ESG) activity in Japan and across Asia. NZ Super announced its climate change policy last year and, alongside many other institutions (primarily in Northern Europe), is making major portfolio changes especially around low-carbon investing.

The evidence
See our publication "Show me the evidence"[1] – where we present a range of academic studies and meta-studies that demonstrate the positive financial impact of ESG factors and stewardship on risk and return outcomes.

While individual asset owner actions will likely have significant positive impact, we believe there is also great power in collective action raising standards across the industry and improving outcomes.

Figure 2. **Integrate sustainable investment into the investment process**

With all this activity, other asset owners are looking to explore what sustainable investment can mean in practical terms for their portfolios. At Willis Towers Watson, we have long believed in the importance of sustainable investment in successful long-term outcomes. We also believe that integrating sustainable investment into the entire investment process from mission and objectives, through asset allocation and portfolio construction, to monitoring and reporting, is the best way to realize the full value available here.

Willis Towers Watson's beliefs
We believe that sustainability issues have a material impact on risk and outcomes, both financial and nonfinancial. Our full philosophy and approach to the subject is outlined in "Sustainable investment and stewardship – our position."[2]

We recognize that the interpretation and application of sustainable investment principles will vary according to the context of each organization. This context includes governance budgets, objectives and operating models, among others. Sustainable investment is sometimes dismissed as a topic only large asset owners can accommodate, but we believe there are minimum standards that all asset owners should adopt, which we outline below:

1. Undertake training and education to build your understanding of sustainable investment, including the regulatory and legal context
2. Determine your fund's position on sustainable investment and articulate it in key documents (such as the Statement of Investment Principles or equivalent)
3. Incorporate material sustainability-related themes into asset and liability assumptions, and your strategic asset allocation process
4. Factor sustainable investment and stewardship criteria into your manager selection, monitoring and reporting processes
5. Communicate your position and activities to relevant stakeholders (e.g., regulatory bodies, plan participants, sponsors, service providers and the market)

While individual asset owner actions will likely have significant positive impact, we believe there is also great power in collective action raising standards across the industry and improving outcomes. Many investors take a similar view, and multiple collaborative initiatives exist that drive important change and offer asset owners the opportunity to extend their sustainable investment actions and impact alongside like-minded investors. Among those initiatives which investors may want to join are the Principles for Responsible Investment (PRI), relevant local or global stewardship codes, or regional organizations such as EuroSIF in Europe and ACSI in Australia.

Collaborative initiatives
We believe in the importance and impact of collaborative initiatives to give the investment industry a stronger voice and drive change for the benefit of all participants.[3]

The breadth of the sustainable investment topic also means there are multiple other areas for asset owners to explore. Impact investing and megatrends are just two such examples that have received particular attention recently. Often though, embedding sustainable investment principles into an organization is a gradual process, and investors can therefore aim for the minimum standards above as a base line, with plans to do more further down the track as their organization progresses and the industry evolves.

Megatrends
Megatrends are large-scale, transformative developments that will impact our economies, businesses and communities. We have recently investigated the trends that are most important to global investors and the associated risks and opportunities in collaboration with the PRI.[4]
Also, see later article in this publication on page 20.

Impact investing
Impact investing refers to investments made with the specific intent to generate measurable, beneficial environmental and/or social impact alongside a financial return. Investors often align the topic with the UN Sustainable Development Goals (SDGs) framework.

The momentum behind sustainable investment is, in our view, both welcome and merited. However, it is vital to be able to harness this and translate it into affirmative investment actions that capture the potential of the subject. We believe all investors have a part to play here, and that inaction comes with significant risks. While it is often tempting to focus on best practice and what leading asset owners are doing, we believe it is equally, if not more important to highlight what all asset owners can and should be doing. The minimum standards outlined above represent a starting point and a call to action that we hope will drive real change.

[1] "Sustainable Investment, show me the evidence," Willis Towers Watson, 2017. Available here: www.willistowerswatson.com/en/insights/2018/02/sustainable-investment-show-me-the-evidence

[2] "Sustainable investment and stewardship – our position," Willis Towers Watson, 2017. Available here: www.towerswatson.com/en-GB/Insights/IC-Types/Ad-hoc-Point-of-View/2014/02/Sustainable-investment-and-stewardship

[3] Some recent highlights of our activity in this area can be found at www.towerswatson.com/en-GB/Services/Services/sustainable-investing

[4] www.willistowerswatson.com/en/insights/2017/12/2017-investment-institutions-trend-index

[redacted]