ISSUE BRIEF

INSTITUTIONAL ASSET OWNERS:

STRATEGIES FOR ENGAGING WITH ASSET MANAGERS FOR IMPACT

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GIIN
GLOBAL IMPACT INVESTING NETWORK

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About the Global Impact Investing Network (GIIN)

The Global Impact Investing Network (GIIN) is the global champion of impact investing, dedicated to increasing the scale and effectiveness of impact investing around the world. The GIIN builds critical infrastructure and supports activities, education, and research that help accelerate the development of a coherent impact investing industry. For more information, see www.thegiin.org.

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LETTER FROM THE CEO

Dear reader,

For many, the release of this newest issue brief comes at a time of renewed global anxiety related to the coronavirus pandemic. As we begin another year under the specter of continued disruption, we also face the reality that many of the world's other pressing challenges – like the climate emergency and unacceptable levels of inequality – are still deepening. More and more people see a fraying system beneath this moment of "global poly-crisis."[1]

These foundational cracks in the global order affect everyone, and institutional asset owners are exposed in unique ways to the risks posed by these fundamental changes. On one level, such asset owners are encountering new policies and emerging regulations that shape how they incorporate social and environmental impact considerations into their investment decisions, alongside risk and return. But on a deeper level, many institutional asset owners recognize that seismic jolts to world order also intersect with their fiduciary duty: Problems like the climate crisis and deep social inequities threaten the long-term value of their assets, in addition to the well-being of their beneficiaries.

"When institutional investors incorporate impact efficiently and effectively, they can mitigate the very issues that threaten the long-term value of their assets and leverage their capital to help address the world's most intractable challenges."

Amidst this tumult, investment products that incorporate some consideration of impact – in other words, some consideration of the real-world outcomes – are experiencing substantial inflows of capital. In large part, that momentum has been driven by institutional investors, who hold significant pools of capital and thus wield immense power, especially in private markets.

Nonetheless, that immense power could be wielded in even more efficient, more effective ways by many institutional asset owners. This series of issue briefs, specifically tailored to institutional audiences, is meant to help by exploring approaches that better realize such investors' tremendous potential for positive impact. When institutional investors incorporate impact efficiently and effectively, they can mitigate the very issues that threaten the long-term value of their assets and leverage their capital to help address the world's most intractable challenges.

But in order to successfully translate impact intentions into real world results requires effective engagement with asset managers. Managers are, of course, essential to institutional investors' ability to successfully invest with an impact lens. And yet, we know that challenges persist for asset owners who are trying to achieve impact results through asset manager engagement. This brief explores strategies for better aligning impact expectations and outcomes in these vital relationships.

Owners of institutional assets hold real power to spawn positive change. But time is of the essence – for a sustainable planet, for a stable society, and for a resilient economy. We hope this series of briefs will help guide institutional investors' journeys toward greater impact. After all, the long-term value of their assets – and the well-being of their beneficiaries – are at stake.

Best regards,

Amit Bouri
Co-Founder and CEO of the Global Impact Investing Network
@theGIIN

1 To learn more about the global poly-crisis, see here.

Introduction

This research issue brief offers actionable insights for institutional asset owners seeking to align with asset managers when managing impact performance.

Institutional asset owners are beginning to engage with their asset managers to incorporate impact considerations into investment processes – from setting impact objectives and targets to establishing measurement and management systems. However, both pension funds and insurance companies have cited challenges in aligning with existing asset managers on impact incentives and selecting asset managers. Nearly 40% of asset owner respondents to this research indicated that they 'lack of knowledge on existing asset managers focused on impact' and highlighted this as a challenge in setting or expanding their impact theme priorities. Further over three-quarters of asset owners in the sample (78%) have clearly indicated that understanding how to collect impact data from external asset managers is a challenge when tracking impact progress. Asset managers, too, are evolving as they increasingly shift processes to incorporate sustainability and impact in their direct investments in response to asset owner desires, regulatory shifts, and a quickly changing financial market landscape.

Incorporating impact into a portfolio requires internal buy-in and organizational motivation. Yet, even once internal motivation has been established, gaps remain in effectively aligning incentives with existing asset managers, allocating capital toward impact, and using that impact capital effectively and efficiently. This research issue brief seeks to fill that gap by offering insight into existing practice and strategies to align with asset managers when managing impact performance. While selecting the right asset managers is an important component, this issue brief focuses on strategies that asset owners can employ to incorporate an impact lens with existing asset managers.

KEY STRATEGIES TO ENGAGE WITH EXTERNAL ASSET MANAGERS

1. **Articulate specific impact objectives or priorities**
2. **Codify impact in formal investment and legal documents**
3. **Identify and use standardized impact reporting systems**
4. **Establish expectations for rigorous impact reporting to enhance alignment**

Methodology

Inclusion criteria and sampling approach

This research includes institutional asset owners – primarily pension funds and insurance companies – that are beginning to consider positive, measurable social and environmental outcomes alongside financial return in their investments. Additionally, the Research Team reached out to asset managers and third-party intermediaries to capture a diverse set of perspectives on the topic of asset owners' engagement with asset managers. This included both those managers and intermediaries that focus on impact and those that do not. This research primarily seeks to address how asset owners are engaging with managers in their existing portfolios to incorporate an intentional, measurable impact in their portfolios, with an emphasis on impact-agnostic, or non-specialized, asset managers.[2] As such, this sample focuses on those institutional asset owners that engage with at least one external asset manager or, in most cases, with multiple external asset managers. The research primarily focused on private markets, with investments made through private debt, private equity, and real assets. The full list of participants is included in Appendix 1.

2 Impact-agnostic (or non-specialized) asset managers are those who do not invest with an intention to generate and actively measure social and/or environmental impacts.

The research process was conducted alongside the GIIN's 2021 Asset Owner Roundtable program.[3] Engagement with the Asset Owner Roundtable program has enabled the Research team to test findings and resonance with a small group of institutional asset owners who are actively working to incorporate impact into their investment portfolios.

Through a targeted outreach approach, the Research Team invited pension funds and insurance companies – that sit at varying stages of the journey to integrate impact into their portfolios – to participate in the research. A quantitative survey was sent directly to 64 institutional asset owners globally. Additionally, interview invitations were sent to 14 asset owners and 17 asset managers and intermediaries to capture perspectives in one-on-one research interviews. These organizations were identified based on their approach to using impact strategies, engagement with external stakeholders, and geographic diversity.

Data collection

Findings in this issue brief rely on quantitative and qualitative data from institutional asset owners along with qualitative data from asset managers and intermediaries. In total, 28 organizations responded and participated in this research. Specifically, findings are derived from:

- A quantitative survey completed by 18 institutional asset owners on approaches to investing capital with an aim to generate positive social and/or environmental outcomes and challenges faced in pursuing impact strategies;
- Qualitative interviews with 18 participants, including institutional asset owners, asset managers, and third-party intermediaries (8 of whom also participated in the quantitative survey), based primarily in the U.S., Canada, Europe, and Australia;
- Desk research on the institutional asset owner landscape, regulatory environment, and resources on engaging with asset managers to incorporate impact into a portfolio.

Nature of engagement with asset managers

While nearly every asset owner included in this sample considers social and/or environmental factors when making investments, often through ESG investing, most have not yet identified a systematic approach to invest with the intention to generate measurable positive outcomes across their portfolios.[4] Many asset owners represented in this research aim to deliver intentional, positive impact within a portion of their portfolios, often as a carved-out mandate or sometimes within a designated asset class. And most are beginning to consider how to incorporate impact as a lens across their portfolios. Across these various approaches to engaging with impact, asset owners in this sample engage with a diversity of asset managers. A few asset owners work specifically with impact-focused asset managers, however a majority engage primarily with impact-agnostic, or non-specialized, asset managers.

While some institutional asset owners work with a sole fiduciary manager that manages their entire investment portfolio, a majority of asset owners in this sample engage with multiple external asset managers. The external asset manager either manages a segregated mandate for the asset owners, or manages a fund in which the asset owner is one of the Limited Partners (LP). Perhaps unsurprisingly, those interviewees with segregated mandates described that they had significant influence over their asset managers. Meanwhile, those asset owners that represent one LP of many within a fund found it challenging to exert influence and encourage their asset managers to incorporate impact within their investments. Asset owner size and type of mandate play a critical role in influencing external manager engagement approaches.

On average, asset owners in the sample reported engaging with about 30 asset managers in their existing portfolios. However, this figure varied widely based on the size of the owners' assets under management, asset class focus, business model, and geography. Several interviewees also shared various structures through which they invest. For example, one interviewee indicated that all listed assets are managed through an investment management company, or pool, alongside other LPs. Several others indicated that they work with a third-party consultant or intermediary to manage their fund investments, however most in this sample work directly with their external managers.

3 The GIIN's Asset Owner Roundtable program convenes a leadership group of senior executives from institutional asset owners to facilitate exchange of impact investing practices and learnings, deepen asset owners' understanding of impact investing opportunities, and equip the group with the information and tools to refine their own internal practices.

4 The Principles for Responsible Investment (PRI) offers a series of technical guides on the selection and management process for how to engage with asset managers. This guidance offers insight for asset owners seeking to integrate ESG requirements in strategic asset allocation, develop mandate requirements and RFPs, and select, appoint, and monitor asset managers. Learn more here.

Challenges in pursuing impact alongside asset managers

Both asset owner and manager interviewees described similar barriers in partnering to incorporate impact in their investment strategies, in particular when articulating and aligning on impact priorities and implementing an impact reporting process. When asked about challenges in setting or expanding impact priorities, 39% of asset owner respondents indicated that they lacked knowledge of existing asset managers that are focused on impact. Further, when asked about challenges in tracking impact progress, 78% of respondents cited an inability to understand how to collect impact data from third-party asset managers or investments as the top challenge, along with determining which impact indicators to select to gauge progress.

i. Institutional asset owners often set broad impact objectives: Asset owner interviewees described articulating broad impact priorities or objectives, most commonly across three to five impact categories, namely climate, housing, and energy. Several respondents indicated interest in expanding their impact priorities from primarily environmental to also social. Notably, less than half of respondents included in the sample reported setting quantitative impact targets at either the portfolio or asset class level. Most institutional asset owners have yet to set impact targets outside of the climate context. Several asset manager interviewees reflected on the lack of specificity and clarity when asset owners shared an interest in pursuing an impact goal in alignment with their fiduciary duty. One asset manager remarked that they do not experience pressure from their asset owners on impact, but instead receive requests from pension funds to generate positive outcomes, without any direction or guidance on the type of positive outcome or expectations on impact metrics that are most relevant to track. Another asset manager interviewee shared that its asset owner clients consistently ask for "alignment to the Sustainable Development Goals (SDGs)" without specifying impact objectives outside of the climate context.

ii. Established fund structures limit asset owner influence: External asset managers sometimes manage a segregated mandate for the asset owners, which makes it easier for their asset owners to influence the investment process. For example, one insurance company with a segregated mandate shared that since their asset managers work for and rely on their capital, the managers are flexible and responsive in aligning with the insurance company's impact priorities and reporting requests, which included annual impact reporting across a set of relevant impact metrics. However, most institutional asset owners in this sample represent one LP of many within their external managers' funds. Several pension funds described that, as one LP of many, they have experienced challenges in exerting influence and encouraging their asset managers to incorporate impact considerations into their investments. Additionally, as one of many LPs, given the legal requirements for anonymity in this fund structure, there is minimal scope for collective action and to work alongside other asset owners in the fund.

iii. Lock-in effect is prevalent once investment and legal terms have been established: Once the negotiation between an asset owner and external manager is complete, it is exceptionally challenging to introduce a new clause or amend the agreed upon strategy. Investors will rarely revise existing legal and investment documents once terms have been established given concerns around interfering with the effectiveness of a strategy, cost implications for external managers, and the requirement to bring all other LPs on board. Some asset owners have shared that there is scope to revisit investment and legal documentation in subsequent funding rounds, presenting opportunity to incorporate impact formally in later funding stages.

iv. Strong desire to adhere to existing role structures and values: Several asset owner interviewees indicated that they selected their external manager given the manager's strong ability to generate financial returns within their established investment strategy. Asset owner interviewees indicated that they did not want to influence that existing strategy. In many cases, external asset managers do not have an intrinsic motivation to incorporate impact measurement and management into their investment process. Some asset owner interviewees thus also highlighted the importance of selecting external asset managers whose values align with their own, which may present opportunity to engage on impact even after investment terms have been negotiated.

v. Difficult for asset owners to gauge impact associated with their portfolio: Impact reporting was the most commonly cited challenge among both asset owner and manager interviewees. Several asset owner interviewees shared that they were unclear on how to align impact reporting standards across their large portfolio of asset managers and capture meaningful impact data on the real-world outcomes associated with their investments. This makes it especially difficult for asset owners to understand the impact of their investments through external managers, in particular non-specialized ones. Two pension funds indicated that understanding outcomes is critical when communicating impact to their board of trustees and beneficiaries. Additionally, nearly all asset manager interviewees identified challenges in the impact data collection and reporting process, as most non-specialized asset managers do not have impact measurement and management processes in place. In fact, two asset managers shared that they do not have an impact measurement expertise, and often rely on others in the industry, including research houses, academics, or non-governmental organizations, to help guide their impact measurement and reporting. Several asset managers anecdotally indicated that reporting on outcomes can be costly, and it is not always evident that asset owners are willing, or able, to pay additional fees and cover those costs.

Strategies to align impact incentives with asset managers

Institutional asset owners and managers described their current approaches and considerations when articulating impact objectives, codifying impact in formal documentation, and implementing impact reporting processes. Several strategies have emerged to enable stronger impact alignment between asset owners and their existing external managers.

Articulate specific impact objectives or priorities

Asset managers often look for narrowly defined impact outcomes to inform their investment approach and ensure they are meeting their asset owners' expectations. In some cases, asset managers have also expressed interest in having their asset owners provide specific impact targets instead of broad impact themes. However, asset owners are often hesitant to express a clear, targeted focus for their external managers beyond achieving strong financial performance and complying with regulatory requirements. In many cases, pension funds and insurance companies do not have explicit, narrow targets and instead identify broad impact categories, such as climate action or affordable housing. In other cases, asset owners are focused on the process through which their asset manager is looking to achieve impact, instead of articulating outcomes. For example, one pension fund indicated that it "rarely expects impact outcomes from its managers" and instead, focuses on its asset managers' impact-specific approach to incorporating impact into its own due diligence and selection using impact scoring criteria. This hesitation to articulate specific impact objectives may stem from a fear around diluting returns by potentially constraining an asset manager's scope to achieve financial performance, as indicated by several interviewees, both asset managers and owners alike.

For those asset owners invested in external funds, opportunities to invest into high performing managers with a strong track record are limited. As a result, some asset owner interviewees investing in external funds as an LP shared some hesitancy around imposing constraints on their managers. Meanwhile, asset owner interviewees with segregated mandates demonstrated a greater willingness to formulate requirements for asset managers based on their impact objectives and set quantifiable targets more often, still in alignment with their fiduciary mandate. For instance, one European insurance company with segregated mandates has established clear impact targets and works closely with their external managers to ensure each investment made is contributing to their social and environmental targets at the portfolio level.

Opportunity

There exists a clear opportunity for asset owners to set impact targets that are quantitative, well-defined, time-bound, and driven by evidence. For climate goals, institutional asset owners can rely on science-based targets (SBT), which offer data-driven targets in line with the Paris Agreement as laid out in the Intergovernmental Panel on Climate Change (IPCC). This approach can be applied across a range of impact themes to address a diversity of social and environmental challenges using global development targets. Others have begun to articulate social targets at the portfolio-level, using a top-down approach across their investments seeking to generate positive social impact.[5] With narrowly defined impact targets, asset owners may be better equipped to articulate specific impact targets to asset managers and focus on outcomes associated with their investments, not just the process.

Example

QSuper articulates clear impact objectives on climate change mitigation to their asset managers by explicitly stating a net zero target across its total investment portfolio by 2050 and is working on establishing interim climate targets and net zero glide paths by asset type. QSuper requires asset managers to present a business case for potential investments to reach net zero by 2050 and detailed decarbonization pathways before proceeding with an investment.

Codify impact in formal investment and legal documents

Before selecting an asset manager, there is opportunity for asset owners to document impact objectives formally in legal documents and investment policy statements. However, when engaging with external asset managers in their existing portfolios, asset owner interviewees shared that formal documentation of impact priorities and objectives becomes more challenging. Several interviewees indicated that documenting impact formally in requests for proposal (RFP), investment policy statements, and legal documents is critical, and has enabled asset owners to hold their managers accountable to achieving their documented impact objectives. Examples of formal documentation in the investment policy statements include: a description of the impact strategy, narrowly defined statements that reflect impact targets, and description of processes that demonstrate how impact is incorporated into various stages of decision-making. Other asset owner interviewees have anecdotally shared how impact considerations form part of the investment process, including due diligence and investment selection, when codified into formal documentation.

5 Learn more about institutional asset owners' approaches to setting both social and environmental goals and targets here.

Many asset owners and managers in the sample have codified environmental impact in both their investment policy statements and relevant legal documents, in particular from a climate risk perspective, acknowledging that mitigating climate risk plays a role in maximizing value. While climate goals have gained broad traction and momentum, especially in light of the Net Zero Asset Owner Alliance and increasing threat that climate risk poses, the same does not yet hold true for other environmental topics and social-focused impact themes. A handful of asset owner interviewees indicated that while incorporating Net Zero reporting requirements into contracts and formal documentation is simpler, integrating other types of impact, especially social impact, is inherently more difficult. One pension fund based in Europe highlighted that it regularly attempts to incorporate impact into the legal contracts for their fund investments without success, as the legal team on the asset manager side often revises the impact clauses making it challenging to formally codify the impact objectives and process expectations. In this case, the pension fund has been successful in integrating the net zero reporting requirements into the contracts, with a focus on required disclosures and transparency on carbon emissions. This perhaps suggests that as regulatory environments shift toward increasing requirements for impact reporting, formal documentation is a more viable route and legal teams may be more open to incorporation.

Generally, for those investors that incorporate impact formally, the legal teams on both the asset owner and asset manager side are involved in contract structuring and negotiation of impact within the legal document. While it is exceptionally rare to revise existing legal and investment documents and negotiate once terms have been established, in some cases asset owners shared that they have engaged in impact-oriented discussions with their managers in preparation for a subsequent funding round in order to set the stage for codifying impact. This can also help asset owners to establish a baseline for expectations when engaging with other asset managers and inform future asset manager selection.

Opportunity:

Moving forward, several asset owner interviewees indicated that they would like to build their internal infrastructure to more formally incorporate impact into decisions – for example, by establishing an impact committee to operate alongside a traditional investment committee to incorporate impact into due diligence. Others indicated that they intend to compare asset managers across a set of standardized impact metrics to inform their selection. Several asset owners and managers also raised the opportunity of fee-based structures for impact to account for the cost of measuring and managing impact, and to incentivize achieving strong impact performance. Two pension funds indicated that manager fees based on impact outcomes to financially incentivize achievement of impact targets could be a viable strategy to increase alignment. One asset manager shared that they have recently embarked on an effort to tie impact to carry as a way of incentivizing achievement of impact goals.

Example

Trill Impact integrates impact requirements throughout its RFPs and private placement memoranda (PPM) to document impact formally and build alignment with its asset owners. Trill also codifies impact to establish accountability for incorporating impact metrics, including tonnes CO_2 emissions avoided by customer, transition to green jobs, and number of clients reached, into its funder sourcing, investment structure design, and impact reporting. Trill has also tied impact to financing products in partnership with asset owners, including credit structures with rebates for achieving specified SBTs. Trill shares that its LPs have been able to incentivize impact outcomes by collaborating across these innovative models and codifying impact in its investment policy.

Identify and use existing standardized impact reporting systems

Expertise in impact measurement and management often sits with asset managers, as acknowledged by both asset owner and manager interviewees. Some asset managers in the sample use existing standardized tools and frameworks to varying degrees and report different types of information related to impact, including the UN Sustainable Development Goals (SDGs), Impact Management Project (IMP), and the IRIS+ system. Others indicated using data provided by companies that are applying the Global Reporting Initiative (GRI) and the Sustainability Accounting Standards Board (SASB). Still others reported using their own proprietary impact measurement tools. Asset owners have anecdotally shared that they are less familiar with standardized industry tools and frameworks for impact measurement and management, but are looking for standardized outcomes reporting. One pension fund, in particular, noted the use of the IRIS+ system across its external asset managers; however, most others were not yet implementing standardized systems to track impact.

Nearly all institutional asset owners in the sample expressed uncertainty around identifying the relevant impact metrics. Several asset owners shared that within existing systems or frameworks, they feel there are too many impact metrics, which can make it difficult to identify what is most relevant for their portfolio. Asset owner interviewees thus described a desire to converge toward platforms that can help GPs focus on a limited number of impact indicators. A handful of other asset owners shared concerns around impact-washing and marketing traps, wary that asset managers may provide large amounts of granular impact information or share positive impact stories devoid of appropriate contextualization or relation to real-world outcomes. Given the many strategies focused on responsible investing, sustainable investing, and impact, several asset owners also shared concerns around asset managers positioning investments as impact investments, despite a lack of intention or measurable outcomes associated with the investment. With a theory of change, asset owners can identify the outcomes they are most interested in, and engage with their asset managers to assess the relevant impact indicators and report back using a standardized framework

Opportunity:

Asset owners can leverage and integrate existing resources and standards into their requests from asset managers. Asset managers have shared that impact is often reported at different levels – company or portfolio – but this is not always aligned with their asset owners' expectations. For example, one asset manager interviewee emphasized the value in asset owners clarifying whether they are interested in receiving impact data at the company-level or fund-level. This can inform how asset managers structure and communicate impact information. In another example, a pension fund described receiving impact data from an external manager related on carbon emissions, energy usage reductions, and jobs created. However, in order to effectively communicate the real-world impact to its stakeholders, the pension fund was more interested in outcomes-level information at the portfolio level, instead of company-level metrics. In the long-run, interviewees described that standardized impact indicators would be useful for differentiating between asset managers and for informing selection and management approaches.

Example

Across a diverse group of asset managers in its private markets portfolio, Fondaction requires reporting across specific impact metrics, such as contributing to the creation and maintenance of quality jobs, avoiding and reducing GHG emissions, and supporting gender equity across its investees, in order to enhance standardization. To identify relevant impact metrics, Fondaction relies on the IRIS+ system for measuring and managing impact, the IMP Five Dimensions, and the Global Reporting Initiative (GRI). Fondaction offers to engage with asset managers to ensure that mechanisms to collect these impact data are in place. In addition to regular impact reporting, Fondaction also conducts external audits of their asset managers' impact reporting to verify their claimed impact.

Establish expectations for rigorous impact reporting to enhance alignment

Once a set of standardized reporting frameworks and/or systems has been mutually agreed upon, continuously monitoring progress is critical. Most asset owner interviewees engage in discussions on impact objectives and progress each time they engage in discussion with asset managers. Nearly all engage in some form of impact reporting, whether it's through disclosures to the PRI via the outcomes-based reporting framework, impact reporting in their annual reports, or separate reports focused on impact.[6]

However, many asset owners included in the sample highlighted a lack of alignment across their external managers reporting on impact in a standardized, rigorous way. Pension funds in particular shared challenges in identifying how to implement a standardized reporting process across their portfolio of external managers, especially when their managers are also reporting to other LPs. For example, one pension fund described the impact reporting process as "not systematic and varied across its diversified portfolio invested through five managers." In particular, those asset owners that are smaller in size and/or invest in funds alongside other asset owners expressed concerns in adding pressure to their external asset managers with additional reporting requests.

Impact reporting occurs annually, as reported by most investors in the sample. However, several indicated that bi-annual or even quarterly impact reporting occurred for several fund investments. Overall, reporting frequency varies based on the impact expectations, asset class, asset manager maturity and capacity, and the strength of the relationship with the asset managers. In fact, one asset manager described how multiple LPs request reporting on revenue-alignment to the Sustainable Development Goals (SDGs) to approximate assets associated with each SDG based on underlying products and/or services. However, several interviewees in the sample highlighted that the SDG revenue-alignment approach is considered insufficient in speaking to the outcomes or impact associated with the investments.

6 Learn more about the PRI's Reporting Framework here.

Opportunity:

Asset owners can establish formal processes for alignment on impact incentives, engage in on-going dialogue (both formally and informally) to gauge progress toward real-world outcomes, and leverage existing industry associations to align processes and expectations across their various external managers.

Example

CDPQ believes in the value of learning from its asset managers' practices and leveraging those strong relationships in the development of its impact strategies. Through engagement in formal and informal, candid dialogue with existing external managers, CDPQ is able to gauge the impact performance of its external managers and assess progress. Beyond regular dialogue that occurs alongside financial performance discussions, CDPQ tracks key performance indicators across several impact themes, including diversity, equity, and inclusion and climate action. CDPQ hopes that ongoing conversations with asset managers and identification of key metrics can lead to market convergence around impact indicators and industry infrastructure that enables differentiation among asset managers.

Regulatory shifts and disclosure requirements

Regulatory shifts across the world, primarily the establishment of sustainability taxonomies and ESG disclosure requirements, are placing increased pressure on asset owners to demonstrate achievement of claimed impact. In Europe, the Sustainable Finance Disclosure Regulation (SFDR) has mandated ESG disclosure for asset managers, and the EU taxonomy for sustainable activities is aiming to provide clarity on environmental sustainability of various economic activities. In the United States, the Securities and Exchange Commission is debating several regulatory measures, including requiring asset managers to explain their criteria for labeling investment products 'green', 'sustainable', or 'low-carbon'.[7]

Asset owners and managers in Europe spoke to the effect that SFDR has had on their methods of tracking and reporting impact. Regulatory shifts that mandate ESG disclosure, environmental stewardship, or other impact obligations may help influence asset owners' interactions with asset managers and provide the needed structure and reporting templates that nearly all asset owners in this sample are seeking.

Looking ahead

Asset owners are keen to achieve more impact and to engage with asset managers as partners in the process. To further motivate deeper engagement on impact, asset owners and asset managers shared several strategies that they would like to adopt moving forward. With clear articulation and documentation of impact goals, asset owners will be well-equipped to interact with asset managers and offer an appropriate level of direction and specificity. Establishing a transparent reporting and disclosures process – relying on existing standardized systems for measuring and managing impact – can not only ensure an appropriate focus on capturing relevant impact information, but also enhance alignment across asset managers within a portfolio. This shift from reporting on dollar-value revenues that align to the SDGs (i.e., SDG-revenue alignment reporting), as used by several asset owners and managers in the sample, to an approach increasingly focused on short- and long-term impact outcomes using standardized metrics can ultimately help asset owners drive toward a deeper integration of impact within investment processes.[8]

These strategies can be pursued individually or collectively, with significant opportunity for collective approaches through industry associations. A collective approach may motivate the development of new products and encourage adoption of existing tools into the investment process that will enable institutional asset owners to more systematically direct capital toward real-world outcomes. Industry initiatives and network organizations, such as the Net Zero Asset Owner Alliance, the PRI, and the GIIN, have helped asset owners identify a strategic roadmap and begin to incorporate impact considerations into their processes and investment approach, strengthening internal capacity. Industry engagement can enable investors to build internal buy-in among relevant stakeholders (including the board of directors/trustees and senior leadership), present evidence to demonstrate the financial viability in an impact strategy, and identify a standardized approach for measuring, managing, and reporting on impact.

7 Learn more about the U.S. regulatory landscape and labeling requirements here.

8 The Sustainable Development Investments - Asset Owner Platform (SDI-AOP) is an asset owner-led platform that uses artificial intelligence to accelerate the adoption of SDGs among asset owners and enhance engagement between stakeholders. This platform presents an opportunity for field-builders and standard-setters to further integrate standardized reporting on real-world outcomes into asset owners' impact measurement and management practice. Learn more here.

Across the sample, investors noted a greater need for industry tools, resources, and infrastructure to facilitate deeper consideration of impact including:

- The ability to differentiate between asset managers and make informed manager selections based on financial and impact performance, and alignment on values;
- Guidance on approaches to apply an impact lens across a full portfolio in collaboration with existing asset managers, with an emphasis on case studies;
- Audit and verification tools to assess the credibility and robustness of a manager's impact management process and impact results;
- Research on how investments perform from an impact perspective across various asset classes and the relationship between financial and impact performance;
- Standardized impact reporting frameworks to leverage across a portfolio of external managers.

Significant opportunity exists for pension funds and insurance companies to deepen engagement with their external asset managers at each stage of the investment process, ultimately enabling investors to better use their portfolios in a way that integrates real-world outcomes alongside risk and return and serve their beneficiaries to build a world where all can thrive.

Appendix 1: List of participants

We are grateful to the following organizations who participated in the research:

Aegon Asset Management

Australian Ethical Investments

CDPQ

Christian Super

Church Commissioners for England

City of Zurich Pension Fund (PKZH)

Fondaction

Mercer

MN

Nedlloyd Pension Fund

NEST

Nordea Life and Pension

NSW Treasury Corporation

Palestine Investment Fund

PGGM

Prudential Financial, Inc., Impact & Responsible Investments Group

Q Super

South Yorkshire Pensions Authority

Stiftung Abendrot

Temasek

The Church Pension Fund

Trill Impact

UBS Asset Management

Wespath Benefits and Investments

Zurich Insurance Group

Appendix 2: Definitions

Institutional asset owners use a variety of terms, such as real-world outcomes, real economy impacts, and positive outcomes, to describe their impact. Across these examples, investors are seeking and often tracking positive, measurable social and/or environmental impact.

Fiduciary duty: An obligation to act in the best interest of another party. (Investopedia)

External asset managers: Those managing capital on behalf of institutional investors.

Impact: Positive social and/or environmental results; also used interchangeably with 'positive outcomes.'

Impact category: Sectors that align with the industry classes standardized by The International Standard Industrial Classification of All Economic Activities (ISIC) and based on the input received by hundreds of stakeholders involved in the development of IRIS+. (IRIS+ Glossary)

Impact investments: Investments made with the intention to generate positive, measurable social and environmental impact alongside a financial return. They can be across asset classes, in both emerging and developed markets, and target a range of returns from below-market to market-rate, depending on the investors' strategic goals. (GIIN)

Impact theme: The type of strategic objectives or approaches investors or enterprises employ to achieve the primary social and/or environmental effect they intend to delivery. (IRIS+ Glossary)

Investment beliefs: Set the direction for investment policy, investment practice, and organizational culture. They help define how the asset owner will create investment value, in the context of future uncertainty, risk and opportunity. (PRI)

Limited partner: A limited partner is a part-owner of a company whose liability for the firm's debts cannot exceed the amount that an individual invested in the company. (Investopedia)

Target: A quantitative or qualitative goal against which progress is measured.

Contact the GIIN

Please direct any comments or questions about this issue brief to research@thegiin.org. To download industry research by the GIIN and others, please visit https://thegiin.org/research.

Disclosures

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