For professional intermediaries only

The value of ESG:

how mainstream is ESG investing within today's adviser world?

Commissioned by

Rathbones
Look forward

Research by

CORE DATA research

Index

The value of investments and the income from them may go down as well as up and you may not get back your original investment.

Introduction

The speed of societal change driven by ESG (Environmental, Social and Governance) seems inexorable, accelerated by the global pandemic, which is fuelling a reframing of behaviours by all echelons of society. The climate emergency, growing scrutiny of companies' practices, and fast-changing consumer ethics and behaviours typified by the 'Thunberg effect' are together exerting upward pressures on the corporate sector. And in turn asset managers, investment managers, advisers and investors, as each responds to opportunity and need.

By 2025, Millennials will make up an influential 75% of the workforce*, with the pension, investment and wider spending power that accompanies this position. With this generation at the forefront of the demand for societal, business and ethical change, anybody still thinking ESG is a short-term fad has now had their final wake-up call.

Today, £17.4 trillion of assets globally are already classed as adopting responsible investment strategies, a 25% increase since the previous review in 2014. Sustainable funds attracted £31 billion in net inflows in the first half of 2019 alone**.

Lack of industry data

But what of the adviser sector? How mainstream has the adoption of ESG into adviser investment practices become in 2020? And in what ways is the growth of ESG impacting businesses and client relationships?

Most importantly, what value is adoption bringing to advisers? Although understanding this is commercially critical for our industry, there is surprisingly little empirical data available to direct and inform thinking.

To understand what level of value has been created to date for advisers by ESG adoption, Rathbones recently commissioned a new study through specialist financial services research house, CoreData.

Within it, the outcomes for two groups, of 50 advisers each, were compared. One populated by advisers with 20% or less in ESG investments ('non-ESG adopters'), the other with a significantly higher 60% or more allocation ('ESG advisers'), providing robust findings on the value adoption has brought adviser businesses to date.

* https://www.ftadviser.com/investments/2020/05/15/esg-trends-translate-from-us-to-uk-assets/
** Source: CoreData: Advisers and ESG (Environmental, Social and Governance) Investing, The influence of ESG on advice businesses (P4)

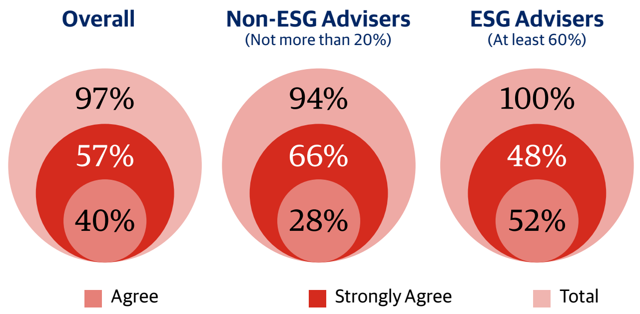
To what extent has the 'ESG world' already changed for advisers?

We began by asking both the 'ESG adviser' and the 'non-ESG adviser' where they stood in relation to ESG.

There was universal consensus that the tipping point for ESG is already behind us. 94% of non-ESG advisers 'agreed' or 'agreed strongly' that "Business and society are changing, so ESG factors will become increasingly important to investment performance", with 100% of ESG advisers agreeing 'very strongly'.

Figure 1: Please state whether you agree or disagree with the following statement about the relationship between ESG investing and performance.

Business and society are changing, so ESG factors will become increasingly important to investment performance.



We then further sought to consider the extent of ESG's normalisation within the adviser world, by understanding what percentage of advisers currently discuss ESG investing with their clients. As well as probing how recently their ESG client conversations started taking place.

Data reveals that the mainstreaming of ESG client conversations appears to have already taken place. Just 3% of the combined total (and 6% of the non-ESG group) still don't talk to their clients about ESG investing. The greatest proportion appears to have begun discussions in the past one to five years, with a high 60% of non-ESG advisers starting then - and a further 14% of non-ESG starting conversations in the past year.

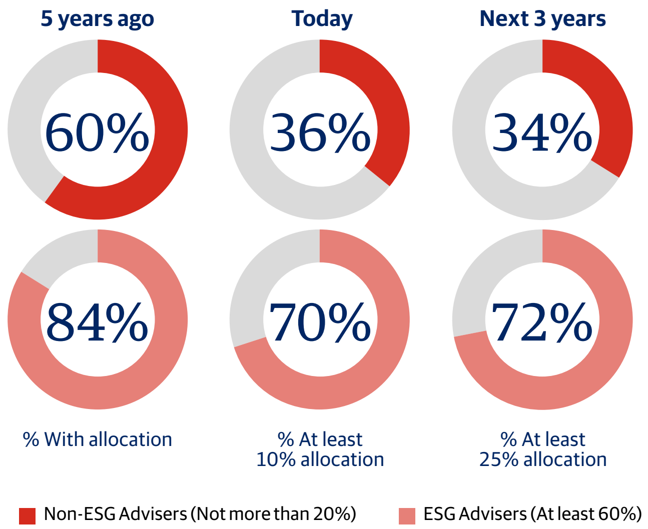
Both groups also confirmed that client adoption of ESG investment had grown significantly in the past five years. While 40% of the non-ESG group's clients had no ESG investments five years ago, this was true for just 8% of their clients today.

Looking forward, 82% of non-ESG advisers expect client adoption of ESG investments to rise further between 10-75% penetration in the next three years. For the ESG group, 70% of their number confirmed that a significant number of their clients have already adopted ESG investments (up from 32% five years ago), and predict this to rise to 98% in the next three years.

"It is very rare to find someone who says 'No, I am not interested in ethical investing.'

Non-ESG Adviser £30-50m

Figure 2: How has the proportion of your clients adopting an ESG/sustainable investment approach changed over the last five years and what are your expectations for the change in the next three years?



How do advisers believe ESG will affect their business in the next five years?

Both the ESG and non-ESG groups recognise the increasing importance of the role ESG will play within their business over the next five years. While this is to be expected from the ESG group (58% predict it being significantly more important), a sizeable 38% of non-ESG advisers predict the same reality, with a further 62% of this group seeing it as 'somewhat more important'.

Allocations predicted to rise significantly

Irrespective of each group's distinct adoption levels today, both sets of advisers believe their ESG investment allocation will rise significantly in the next few years. Yet it is the scale of the increase that is most interesting here. While (as you might expect) 90% of the ESG group predict a rise, 94% of the non-ESG adviser group also believe their allocation will grow, 4% more than ESG advisers, albeit from different current base levels.

94%

of non-ESG advisers believe their ESG allocation will grow in the next 3 years

Figure 3: How do you think your investment allocation in ESG/ethical/sustainable/green funds or strategies will change three years from now?

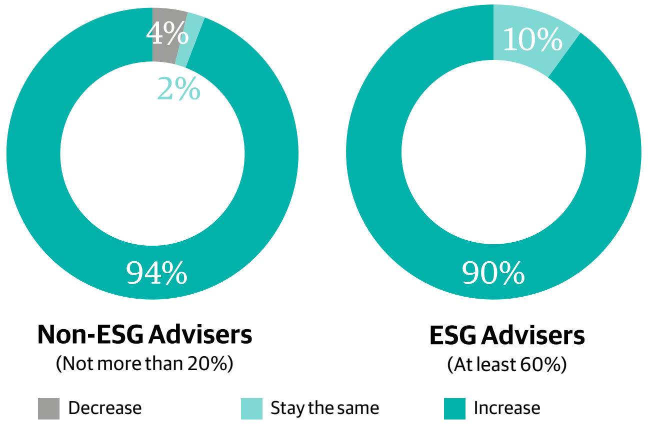
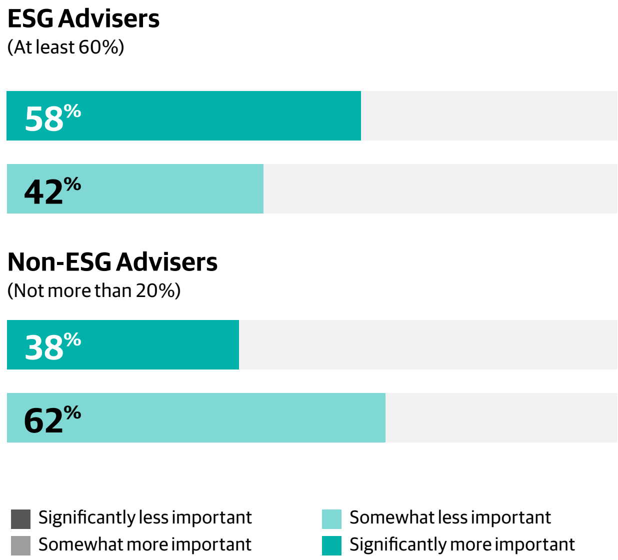


Figure 4: How do you expect the role of ESG considerations within your business to change in the next five years?



To what extent has ESG adoption impacted advisers' business growth?

To understand the commercial value ESG adoption has brought adviser businesses to date, we then asked both groups (in pure terms rather than just in relation to ESG) "How would you rate your business growth over the past five years?" And while both groups had increased in size, the ESG sample had grown considerably faster.

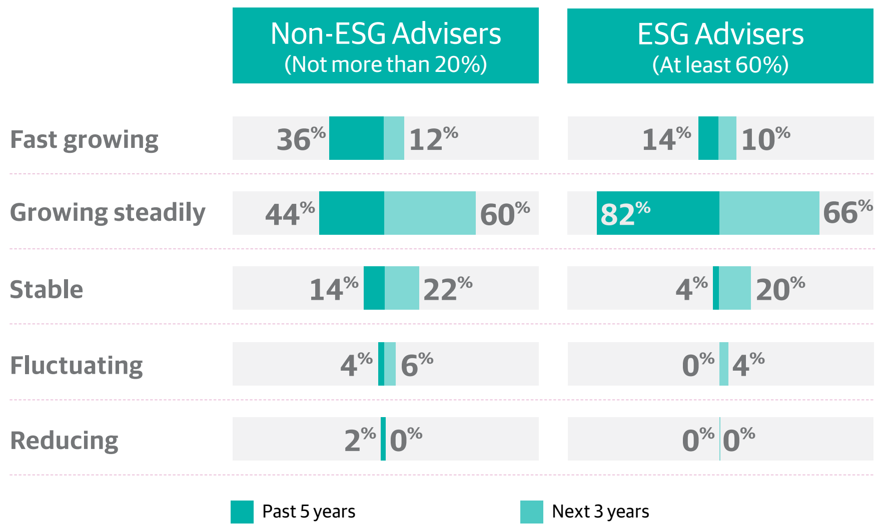
96% of ESG-focused advisers said they had experienced 'fast or steady growth' in the past five years. This contrasted with 80% for non-ESG businesses, with no wider data variables (bar adoption) separating the two groups. Again, while 20% of the non-ESG group defined recent growth as 'stable, fluctuating or reducing', just 4% of the ESG group had experienced growth this low.

Separately, we then asked the two groups how they saw business growth (again in pure terms, not in relation to ESG) over the next three years. Here the figures were more comparable, with 76% of ESG advisers expecting 'fast or steady growth', compared with 72% for those not fully integrated.

96%

of ESG advisers have experienced fast or steady business growth in the last five years

Figure 5: How would you rate your business growth over the past five years and your expectations for the next three years?



The correlation between ESG investing and client relationships

Client engagement and tenure being critical to business stability and growth, we next asked advisers to draw on the role and importance ESG investing played within their client relationships.

We first sought to understand whether ESG investing, per se, contributes to clients being 'more engaged with the investment process'. Both groups believe this is definitely the case, with almost two in three (64%) of the non-ESG group - and 76% of the ESG group - attesting to this.

We then progressed to understanding the correlation between ESG investing and the business dimension of client retention. Here, 64% of the non-ESG group believed it 'facilitated client retention', perhaps surprising given their business is currently invested at only 20%. A higher 80% of the ESG group expressed they felt the same way, providing a combined 72% for the two groups.

Furthermore, analysis of the two groups demonstrates that ESG advisers enjoyed far higher retention than their non-ESG colleagues. 82% of the ESG group had enjoyed average client tenure in excess of ten years, compared to an average 52% for non-ESG. This gap widened further for client tenure of 15 years and more (56% versus 20%).

Figure 6: Please state whether you agree or disagree with the following statements about the role of ESG investing in client relationships.

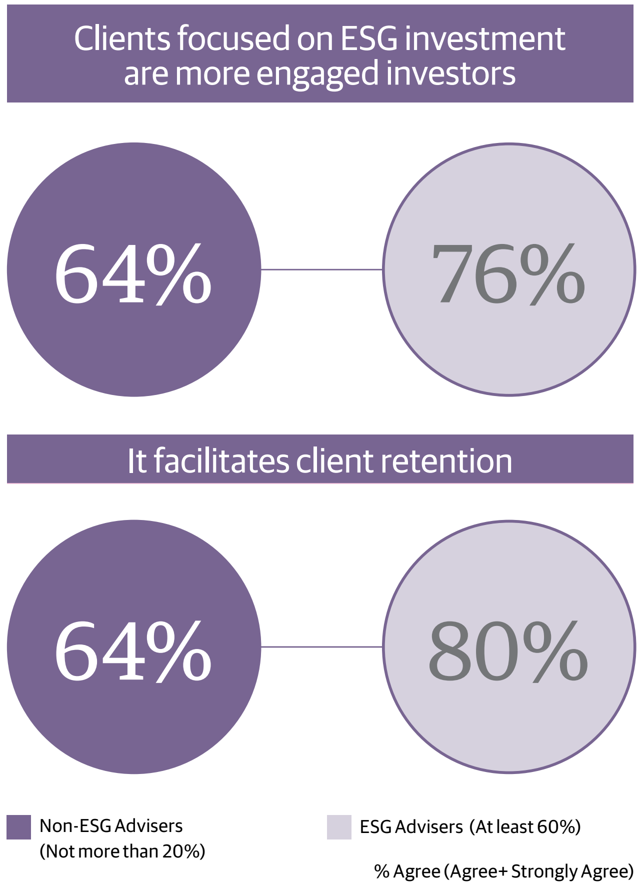
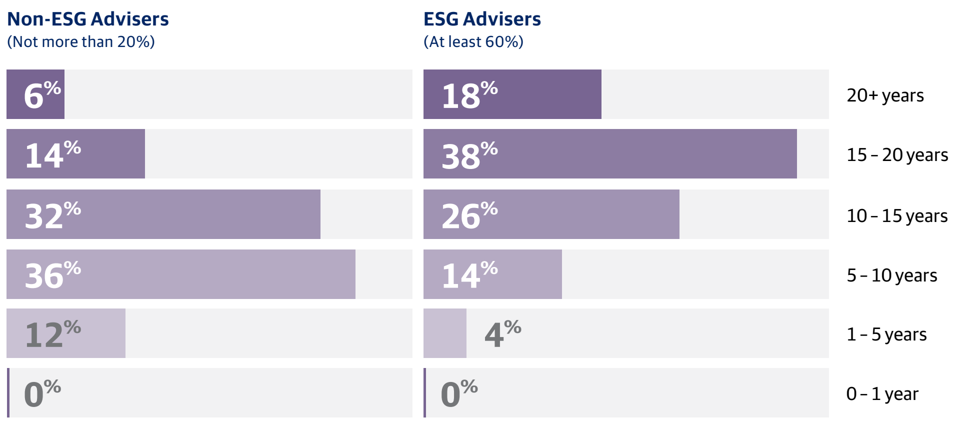


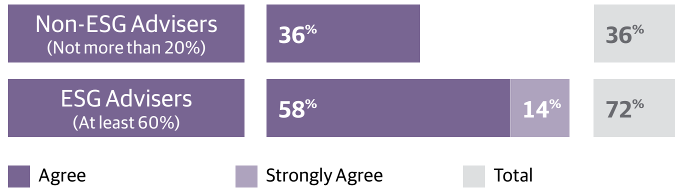
Figure 7: What is the average tenure of your clients?



The role of ESG in influencing client referrals

Both groups were then asked if, in their experience, ESG investing led to increased levels of new business referrals from clients. A high 72% of ESG advisers either 'agreed or strongly agreed' with this reality, compared with just half that (36%) of the non-ESG group.

Figure 8: Please state whether you agree or disagree with the following statement "It leads to increasing referrals among advisers".

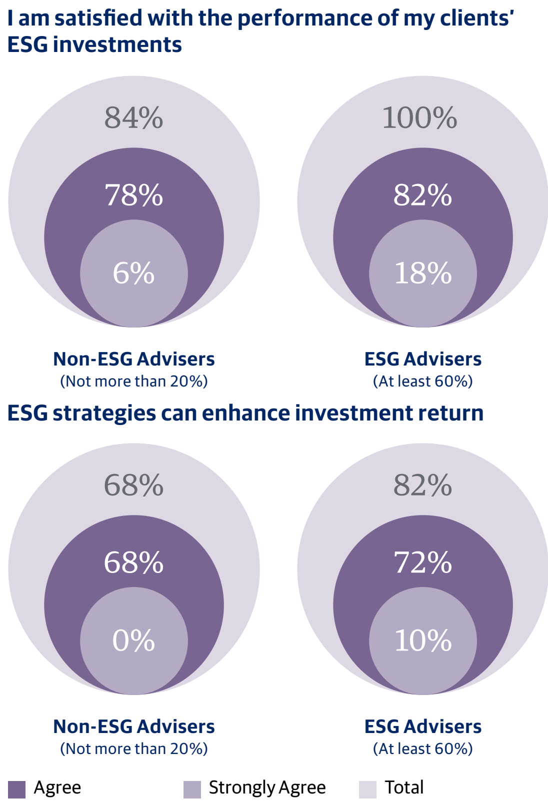


Changes in adviser perceptions of ESG investment performance

Performance has always been a fundamental proof point for the success of advisers' investment strategies for clients, and in turn a key part of their value.

Therefore, in constructing this research study, understanding advisers' perceptions of ESG investments' overall performance was essential. Especially in the light of historically-held views based on the smaller, less-sophisticated ESG investment choices of yesteryear.

Figure 9: Please state whether you agree or disagree with the following statements about the relationship between ESG investing and performance.



Perceptions appear to have been replaced by a new reality in 2020. Over two thirds (68%) of the non-ESG group now confirm their belief in ESG investments' ability to 'enhance investment returns', rising to 82% for ESG advisers.

Moving from belief to personal experiences of clients' ESG performance, 84% of the non-ESG group 'agree or strongly agree' that they are satisfied with the performance of their clients' ESG investments. A 92% positive sentiment for the two groups combined.

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84% **of 'non-ESG investors' are satisfied with their clients' ESG performance**

"People are more engaged by ESG than they are with general investing. It encourages a two-way dialogue. They want to know and understand. You talk through the companies that they're investing in and how the funds have performed. So yes, it's a lot more engaging."

ESG Adviser 50-£100m

How prepared are advisers for ESG becoming business as usual?

While this study provides a groundswell of evidence that advisers believe root-and-branch ESG integration is the imminent future, it also shows many advisers do not appear to be ready for this, whether MiFID II's direction becomes mandatory or not.

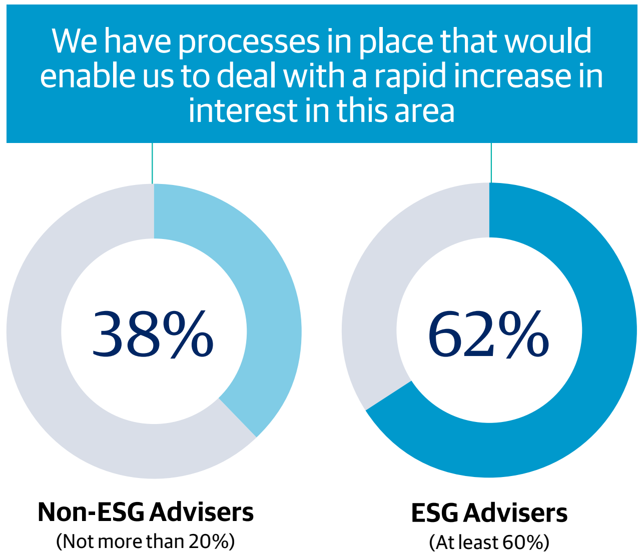
As you'd expect, ESG advisers are better prepared. 34% of them cite ESG is already fully integrated into their business, compared with just 2% of non-ESG advisers.

2%

of non-ESG advisers say ESG is fully integrated into their business

Further probing the two groups' readiness, only just over one in three (38%) of non-ESG advisers currently has processes in place that would enable them to deal with a rapid increase in client interest, contrasting sharply with almost two in three (62%) from the ESG adviser group.

Figure 10: To what extent do you agree with the following statement?



Significant gaps in knowledge

The research reveals significant gaps in non-ESG advisers' understanding, with fewer than one in three (30%) of this group saying they have a strong understanding of ESG/ethical/sustainable/green investing. Less than half that of the ESG group of advisers (68%).

Yet gaps in knowledge are evident in both groups. One in four (26%) of non-ESG advisers said they understood the difference between ethical, sustainable, ESG and impact investing, but did not know how to apply them. This dropped to 14% within the more thematically experienced ESG group. A worrying 13% of the combined groups wrongly felt that the terms were interchangeable.

And a combination of CPD and adviser support is undeniably required, with just three in ten (30%) of the non-ESG group claiming they have a strong understanding of ESG/ethical/sustainable/green investing. 40% of this same group then expressed that they need more support on introducing ESG investing to their clients, be that from providers, industry CPD or other channels.

1 in 5

advisers is unable to apply ethical/SRI/ESG or Impact investments to their portfolio

For both groups, working with specialist partners provided a potential solution for specific ESG roles. Over half (58%) of non-ESG advisers said they would consider partnering for centralised propositions, 44% for DFM and 42% for fund investment. This rose to 72%, 62% and 44% for the ESG group.

While the tipping point for ESG investing is long past, advisers and providers need to do considerably more to inform and prepare themselves.

Less than

1 in 3

of non-ESG advisers has a strong understanding of ESG investing

Figure 11: To what extent do you agree with the following statement?

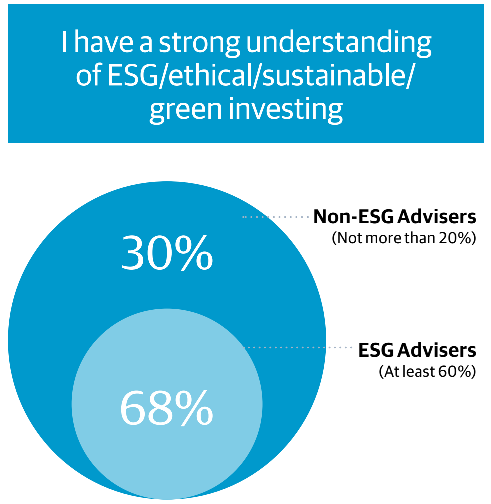
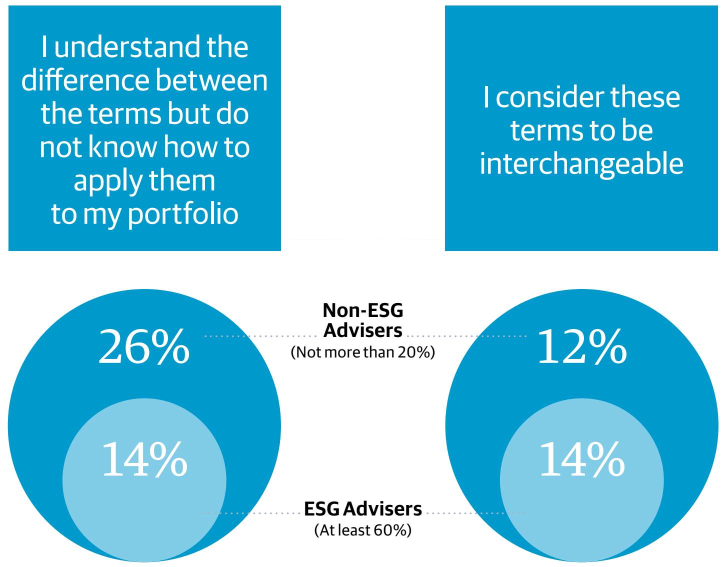


Figure 12: Which of the following holds true for you?



Conclusion

We commissioned 'The value of ESG' to build insight into the effect adviser adoption of ESG is having on their businesses over time. Dividing advisers into two differing levels of historic adoption, allowed us to objectively define the business value that the research shows has been created.

The findings of the study make many things glaringly obvious. While some advisers were historically naysayers about ESG as a fad, or sceptical about its investment performance, there has been a sea change in thinking, with adopters and low adopters alike now recognising ESG strategies' ability to deliver for their clients.

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Client conversations about ESG investing appear to have become business as usual and normalised, with just 3% of advisers saying they don't talk to their clients about ESG.

And while we set out to explore ESG adoption's business value for advisers, the report demonstrates this reality time and time again. In ways as diverse as the speed of business growth, extended client tenure and client engagement.

Advisers of all allocation levels recognise that the tipping point is past. 94% of 'non-ESG' advisers recognise "business and society are changing, ensuring ESG factors become increasingly important to investment performance". With or without a MiFID II mandate.

Yet more needs to be done. The study reveals significant gaps in many advisers' knowledge of ESG strategies and products, and how to properly align them with client investment objectives. Adviser businesses - and providers - need to work closely together to overcome this, and better explain the value of ESG to their end clients.

Rathbones

Rathbones provides individual investment and wealth management services for private clients, charities, trustees and professional partners. We have been trusted for generations to manage and preserve our clients' wealth. Our tradition of investing and acting responsibly has been with us from the beginning and continues to lead us forward. Our ambition is to be recognised as the UK's most responsible wealth manager.

- **In business since 1742**
- **A FTSE 250 listed company**
- **Managing more than £50.4* billion for our clients**
- **15 offices throughout the UK and Jersey**

*31 December 2019

Our purpose

We see it as our responsibility to invest for everyone's tomorrow. That means doing the right thing for our clients and for others too. Keeping the future in mind when we make decisions today. Looking beyond the short term for the most sustainable outcome. This is how we build enduring value for our clients, make a wider contribution to society and create a lasting legacy. Thinking, acting and investing responsibly.

Our principles

Responsible and entrepreneurial in creating value

It's through responsible entrepreneurship that we achieve the best results for our clients. Our people are trusted to pursue value. They know when to change course to preserve it too. Being responsible for today and tomorrow, we are open to the new yet always guided by the long view.

Courageous and resilient in leading change

Responsibility demands courage. We are not afraid to ask difficult questions or make changes that need to be made. We stand up for what's right, accepting that this can be challenging sometimes. We know that investing for tomorrow and leading the way can take time. We have the discipline and resilience to see things through.

Collaborative and empathetic in dealing with people

Managing wealth responsibly takes collaboration: with each client, among colleagues and with professional partners. What matters is not who's best but what's best for our clients. Empathy brings insight. It's important to know what wealth means for our clients as individuals and for their families too. It's our responsibility to understand each generation's changing priorities.

Professional and high performing in all our actions

We take our professional responsibilities seriously. We are accountable for what we do: to our clients, to each other and to the future. Investment in our people and the fabric of our firm renews our culture of high performance. Never compromising on quality because we have a responsibility to be here tomorrow.

SRI Services

We would like to thank SRI Services for their specialist help in consulting on the construction of the questions within this research study.

SRI Services is the UK's only independent company devoted entirely to advancing retail Sustainable and Responsible Investment (SRI) funds - which we define as the full range of regulated ethical, sustainable and responsible investment funds that are designed to meet the needs of individual investors with an interest in environmental, social and/or ethical issues.

Our purpose is to encourage - and help facilitate - the expansion of this area, in order to help effect positive environmental and social change and meet individual investors' personal values-based needs better. We believe in transparency and improving access to investment information. As such, our main area of work, the Fund EcoMarket fund tool is open to everyone - however our core focus is on financial services professionals, particularly financial advisers and other financial services intermediaries.

We are not authorised to offer investment advice and do not deal directly with individual investors. SRI Services and our free-to-use fund tool Fund EcoMarket were created by - and are managed by - Julia Dreblow BA Hons, DipPFS who has specialised in this area since the 1990s.

Areas of business:

Provision of information and tools to facilitate the expansion of retail Sustainable, Responsible and Ethical Investment (SRI). This is primarily via our fund hub Fund EcoMarket, but supported by the sriServices.co.uk (our original adviser support) site. As at Q3 2019, Fund EcoMarket boasts over 1,000 unique users per month (Google Analytics).

Consultancy and collaboration with a diverse range of retail financial services. Julia also serves on the UKSIF board and is a Transparency Task Force advisory board member.

Consultations - we view it as essential to respond to industry consultations that help further the expansion of SRI, sustainable, climate-friendly, ESG and related investments. (See www.fundecomarket.co.uk/help/blog for links.)

Our purpose is simple: to advance retail sustainable and responsible investment.

We fill a gap in the market by helping (mainly) financial advisers and other intermediaries to understand and meet their clients' 'green and ethical' investment goals more easily.

The Fund EcoMarket database tool is a comprehensive, 'whole of market' database. Funds are listed in directory style - and can be 'sifted' with the help of six filter options.

The Fund EcoMarket includes a Fact Find questionnaire, which uses our unique 'SRI Styles' segmentation system to help users identify their preferred SRI Styles via a client microsite.

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