

LAPFF report reveals failings in passive fund governance

Professional Pensions, 28th May

A significant proportion of equity holdings managed within passive funds are not subject to high levels of environmental, social and governance risk management, an audit reveals.

The Local Authority Pension Fund Forum - which represents 49 local authority pension funds with combined assets of over £75bn - commissioned ESG specialists RImetrics to assess the ESG competencies of the biggest global passive asset managers.

It evaluated Legal & General Asset Management, State Street Global Advisors and UBS Asset Management - collectively responsible for £700bn of passive equity funds. Barclays Global Investors declined to participate.

RImetrics provided LAPFF with in-depth evaluations of individual fund manager ESG strengths and weaknesses.

Fund managers were evaluated and rated across five key responsible investment themes of strategic orientation, engagement, research, proxy voting and transparency.

The key findings were:

- Managers vote proxies but do not do so consistently across the world. An estimated £130bn of assets are not regularly voted.
- Managers engage with companies to some degree but again this is not consistent across the world. It is estimated £350bn of assets are rarely, if ever, engaged.
- Resources are limited. A total of 11 individuals were identified who are responsible for the implementation of ESG policies for these £700bn of assets, held in upwards of 3000 companies across the world. Additional resources are provided in some cases by mainstream active management teams and managers make use of voting service providers. Nonetheless, asset managers must inevitably be selective in their approach, particularly to engagement. RImetrics estimates investment totalling less than 4/100th of 1 basis point in Responsible Investment, RI overall.
- Managers consistently voted proxies in the UK and US although elsewhere the pattern is more mixed.
- Managers tend to be most active in engagement terms either where their RI staff are based or where they hold the bulk of their assets.
- Small cap stocks are rarely engaged. Managers tend to focus their engagement activities on their largest holdings.

- Holdings in emerging markets are typically never engaged. There was no evidence £15 billion of assets, held in upwards of 1000 companies, are engaged on behalf of clients, despite probable higher levels of ESG risk.