riaa Responsible Investment Association Australasia

Responsible Investment Benchmark Report
2020 Australia

SUPPORTING ORGANISATIONS

AXA Investment Managers
BT
PIMCO
TEACHERS MUTUAL BANK LIMITED

RESEARCH PARTNER

KPMG

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Contents

Thank you

OUR SPONSORS

Investment Managers

AXA INVESTMENT MANAGERS

AXA Investment Managers is an active, long-term investor. From equities, fixed income and real assets to alternatives and multi-asset, we marry innovation and risk management in a bid to deliver long-term value for clients. We are responsible investors; we believe that responsible investment not only delivers sustainable, long-term value for clients, it also makes a positive impact on society. This is why we incorporate environmental, social and governance considerations into our investment decisions. We are committed to making investing easier – we want to help investors cut through the noise and empower them to make the right investment choices. We are bringing to bear the power of big data and technology not only to improve our investment offering but to enhance the ways in which we engage with our clients. We manage A$1.3 trillion on behalf of our clients, with 2,360 employees operating out of 28 offices and 20 countries as at end of June 2020.

BT

BT is a leading provider of wealth services in Australia with a proud track record in sustainability. We have been a signatory to the Principles for Responsible Investment since 2007.

BT provides wealth management services to Australians including investment, superannuation and retirement income products and investment platforms. We focus on how we can help our customers and, in doing so, make a sustainable difference through our industry to achieve better environmental, social and economic outcomes.

BT believes that sustainable investment is intrinsic to the provision of long-term value for our customers and are pleased to continue our sponsorship of RIAA's annual benchmark report.

PIMCO

PIMCO

As one of the world's premier fixed income managers, PIMCO's mission is to deliver superior investment returns, solutions and service to our clients. For nearly 50 years, we have worked relentlessly to help millions of investors pursue their objectives – regardless of shifting market conditions.

Leadership in ESG investing is essential to deliver on our clients' financial objectives and to support long-term, sustainable economic growth globally.

As at June 30, 2020 we managed US$1.92 trillion on behalf of our clients. Our professionals work in 17 offices across the globe, united by a single purpose: creating opportunities for investors in every environment.

TEACHERS MUTUAL BANK LIMITED

TEACHERS MUTUAL BANK LIMITED

Teachers Mutual Bank Limited is a values-based bank where profit has a purpose. We are one of the largest customer-owned banks in Australia, with over 210,000 members and $8 billion in assets. Our Bank has four divisions – Firefighters Mutual Bank, Health Professionals Bank, Teachers Mutual Bank and UniBank – that serve workers and their families in key community sectors: education, emergency services and healthcare.

All our retail deposits, mortgages and wholesale products are certified as responsible or ethical by RIAA; these are 97% of all products the Bank sells.

SURVEY RESPONDENTS

We are extremely grateful to the 54 Australian and international investment managers that responded to the survey. They are listed in Appendix 4.

DATA SUPPORT

MORNINGSTAR

Morningstar Australasia is a subsidiary of Morningstar, Inc., a global leading provider of independent investment research. We offer an extensive line of products and services for individual investors, financial advisers, asset managers, retirement plan providers and sponsors, and institutional investors in the private capital markets.

Morningstar provides data and research insights on a wide range of investment offerings, including managed investment products, publicly listed companies, private capital markets and real-time global market data.

In July 2020, Morningstar Inc. acquired Sustainalytics, a globally recognised leader in environmental, social and governance (ESG) ratings and research. In December 2019, Morningstar Australasia Pty Limited acquired AdviserLogic, a cloud-based, financial planning software platform for financial advisers in Australia.

About this report

This is the 19th annual *Responsible Investment Benchmark Report* prepared by the Responsible Investment Association Australasia (RIAA). The report details industry data on the size, growth, depth and performance of the Australian responsible investment market over 12 months to 31 December 2019 and compares these results with the broader Australian financial market.

It comes at a time when there appears to be an inverse relationship between responsible investment commitments made by the investment industry on one hand (higher than ever before and growing), and the continuing decline in the real-world global condition on the other. This raises the question: is the activity we promote and celebrate as 'responsible investment' relevant in today's environmental and social context?

To respond to this observation, in 2020, RIAA has broadened its definition of leading practice standards across responsible investment approaches, detailed on page 14.

RIAA commissioned KPMG to undertake the data collection and analysis for this 2020 report. KPMG provided a platform for a survey to be distributed to 165 investment managers known to be applying responsible investing approaches (the Responsible Investment Research Universe), compiled the data derived from this primary research (survey data) and undertook secondary research on publicly available data.

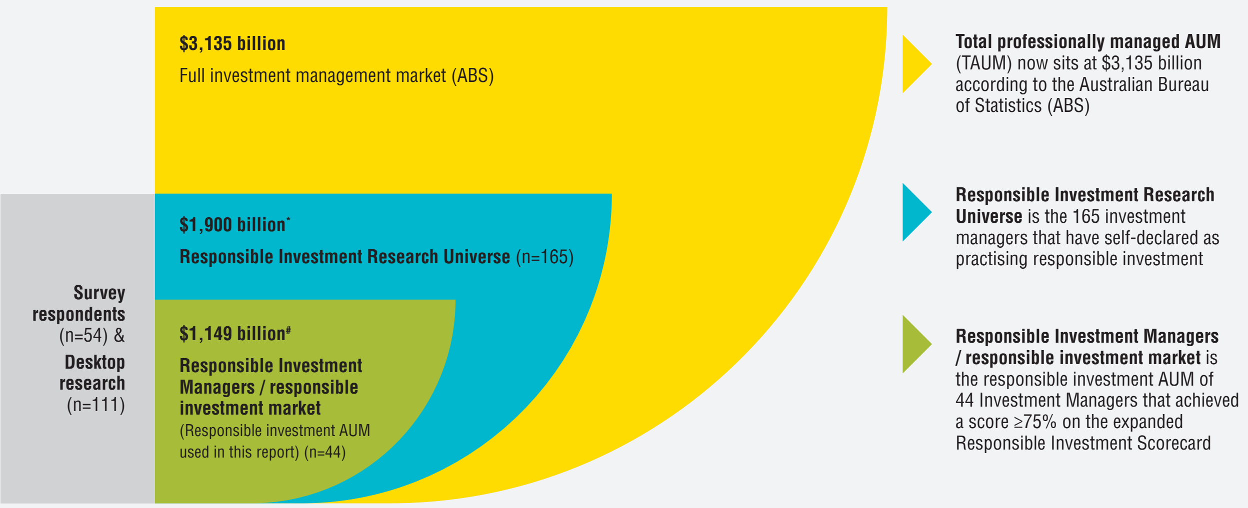
Of the 165 investment managers in the Responsible Investment Research Universe, 54 provided survey responses (survey respondents). Survey respondents were split between asset owners (15%) and investment managers (85%). Asset owners were only included to the extent that they directly manage investments. For the balance of investment managers in the Responsible Investment Research Universe (111), KPMG conducted desktop research over their publicly available information.

Throughout this report, a distinction is made between the full investment management market (all investment managers with operations in Australia, total assets under management (TAUM) as defined by ABS), the Responsible Investment Research Universe (the 165 investment managers that have self-declared as practising responsible investment) and the Responsible Investment Managers (the 44 assessed by RIAA as applying a leading approach to their responsible investment processes and disclosures). Responsible investment AUM reported herein is for the assets managed by leading Responsible Investment Managers to at least one responsible investment approach.

Of the investment managers that responded to the survey, 66% appeared in both the 2018 and 2019 surveys, meaning that 34% are new to the 2019 Responsible Investment Research Universe. This represents significant growth in the Responsible Investment Research Universe from 2018 to 2019. Seventy-four percent of investment managers in the research universe did not meet the score of ≥75% and are therefore excluded from the Responsible Investment Managers listing.

The project was led by Nicolette Boele, Mark Spicer, Samantha Bayes, Stephan Gabadou and Elyse Vaughan. The report production was managed by Katie Braid, with editing by Melanie Scaife and design by Loupe Studio.

FIGURE 1 Research universe and Australia's responsible investment market



* Data for 21 of the 165 (mainly boutique and smaller) investment managers was not publicly available to use in the research universe.

\# Data for three investment managers (Aberdeen Standard Investments, Aviva and Russell Investments) was not received in the survey period and hence 'responsible investment AUM' does not include their AUM.

About the Responsible Investment Association Australasia

RIAA champions responsible investing and a sustainable financial system in Australia and New Zealand and is dedicated to ensuring capital is aligned with achieving a healthy society, environment and economy.

With over 300 members managing more than $9 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across Australia and New Zealand. Our membership includes super funds, fund managers, banks, consultants, researchers, brokers, impact investors, property managers, trusts, foundations, faith-based groups, financial advisers and individuals.

RIAA achieves its mission through:

- providing a strong voice for responsible investors in the region, including influencing policy and regulation to support long-term responsible investment and sustainable capital markets;
- delivering tools for investors and consumers to better understand and navigate towards responsible investment products and advice, including running the world's first and longest-running fund Certification Program, and the online consumer tool Responsible Returns;
- supporting continuous improvement in responsible investment practice among members and the broader industry through education, benchmarking and promotion of best practice and innovation;
- acting as a hub for our members, the broader industry and stakeholders to build capacity, knowledge and collective impact; and
- being a trusted source of information about responsible investment.

ABOUT KPMG

KPMG has one of the largest dedicated sustainability teams in Australia that works with investment managers, asset owners and private equity to develop environmental, social and governance (ESG) strategy, performance and reporting.

KPMG understands that a clear focus on ESG issues is required to support organisations in identifying risks and opportunities that may have significant implications to value creation and portfolio performance. There is a growing opportunity for financial organisations to manage these risks and opportunities and transparently communicate their impacts and performance to members, investors, customers and regulators. KPMG works with organisations to help them manage these emerging risks and opportunities in an integrated way to enhance all aspects of their risk management, reporting and communication.

Executive summary

BACKGROUND

RIAA's 19th annual Responsible Investment Benchmark Report details the size, growth, depth and performance of the Australian responsible investment market over 12 months to 31 December 2019 and compares these results with the broader Australian financial market.

To do this, RIAA reviewed the practices of 165 investment managers known to be applying responsible investment to some or all of their investment practices. These managers control approximately $1,900 billion in assets under management (AUM), which is 60% of total professionally managed AUM (TAUM). Fifty-four of those responses were assessed directly via survey, and supplementary desktop analysis was undertaken for the remaining 111 investment managers.

For a second year, RIAA canvassed superannuation funds to the extent that they directly manage investments, acknowledging the growing trend for superannuation funds to bring investment management in-house.

RESPONSIBLE INVESTMENT IN 2019

In 2019 and for a 19th consecutive year, funds managed under responsible investment approaches grew as a proportion of total professionally managed investments in Australia.

Ever more investment managers are applying a range of responsible investing approaches – from ESG integration and negative screening to sustainability-themed and impact investing.

New data points in 2019 indicate that there is still a gap between those that claim to be practising responsible investing and those that have embedded these practices through formal policies and accountability commitments including disclosing full portfolio holdings.

Investment manager practices are also maturing with a quarter of managers earning the accolade of practising a leading approach to responsible investing against this year's expanded Responsible Investment Scorecard.

Australian responsible investment managers still favour ESG integration and corporate engagement and voting above negative and norms-based screening as their primary responsible investment approaches for constructing portfolios, but managers are increasingly driving capital towards sustainability-themed and impact investing allocations with allocations to Green, Social and Sustainability Bonds more than doubling since last year. Whilst industry practitioners seek to understand and map climate change risk throughout their portfolios, socially themed sustainability funds dominate this responsible investment approach.

This year's findings suggest that investment managers are catching up with consumer interest, with a large leap in AUM being screened for exposures to fossil fuel producers.

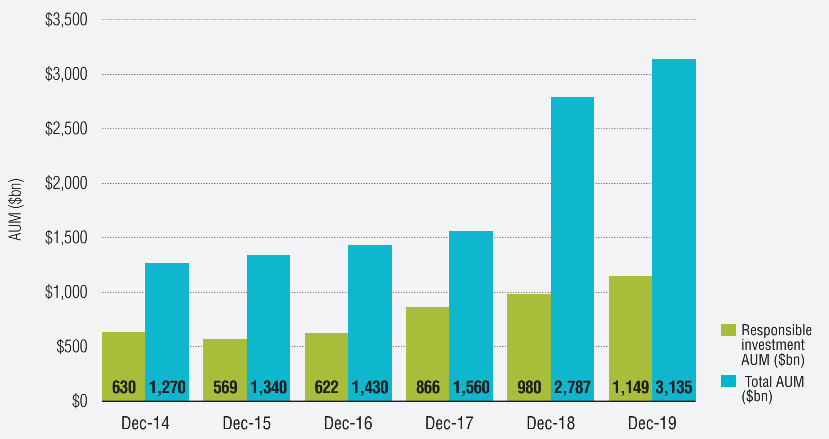
As we enter this new decade, industry analysts and commentators are broadening their view on responsible investing, as it moves into the mainstream for professionally managed investing in Australia. The focus for the decade becomes the extent to which these efforts result not just in better risk-adjusted returns for clients, but also for a more stable and sustainable economy based on assets and enterprises that benefit stakeholders and contribute to societal and environmental solutions.

KEY FINDINGS

1 **The responsible investment market continues to grow,** with associated assets under management (AUM) up 17% over the course of 2019 to $1,149 billion. This represents 37% of total professionally managed assets under management (TAUM), which now sits at $3,135 billion according to the Australian Bureau of Statistics (ABS).[1]*

* The 2019 Benchmark Report has re-stated the 2018 TAUM. The 2018 TAUM was reported as $2,242 billion and has been re-stated to $2,787 billion (as reported by the ABS). Cross-invested assets between managed funds institutions were subtracted from the consolidated assets total, however, this subtraction calculation was already embedded in the total and hence the TAUM was under-stated for 2018. Figure 2 has been adjusted to reflect the correct figure for 2018.

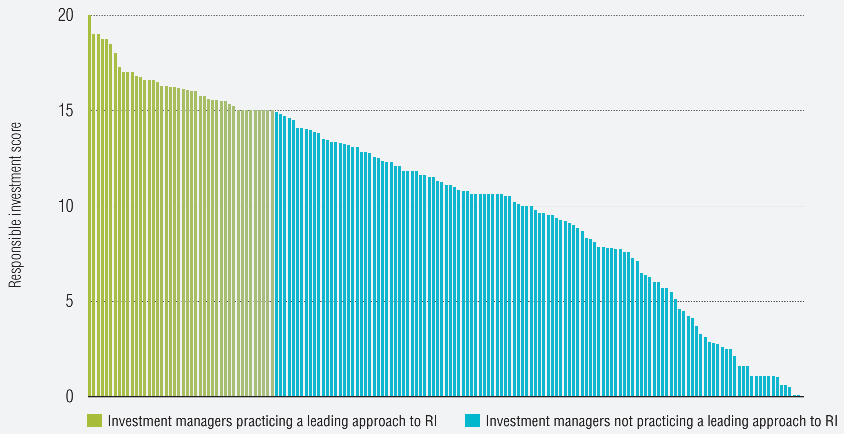
FIGURE 2 **Yearly market value growth of responsible investment AUM and TAUM in Australia ($billion)**



2 **Ever more investment managers apply responsible investing approaches, of which a quarter can demonstrate practising leading responsible investing.** Of the 165 investment managers in the Responsible Investment Research Universe, 44 (27%) are applying a leading approach to responsible investment (score ≥75% on the expanded Responsible Investment Scorecard, which now also rewards commitment to accountability, transparency and allocation of capital towards real economy outcomes).

Further, only those that scored 15/20 (75%) or higher have been included in this report as responsible investment AUM as stated in key finding 1. Therefore, the responsible investment AUM is the sum of all 44 leading Responsible Investment Managers' AUM.

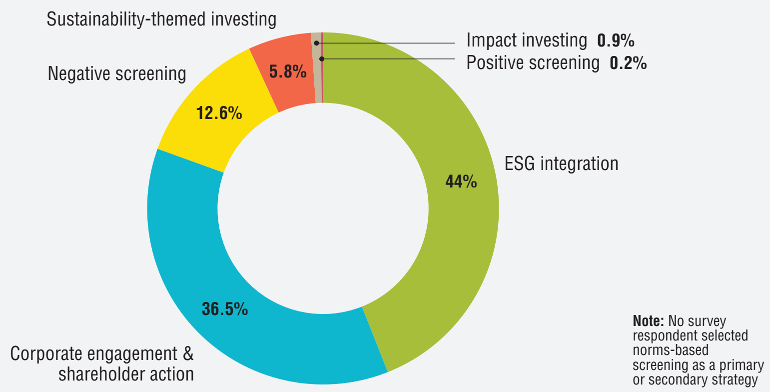
FIGURE 3 Responsible investment scores of the 165 investment managers in the Responsible Investment Research Universe



3 **The responsible investment approaches that most influence the final construction of responsible investor portfolios is environmental, social and governance (ESG) integration, and corporate engagement and shareholder action,** representing 44% and 37% of responsible investment AUM under a primary and secondary investment strategy, respectively. The findings show a small shift in focus by investors on last year's preferences towards corporate engagement and shareholder action.

No survey respondent selected norms-based screening as a primary or secondary strategy.

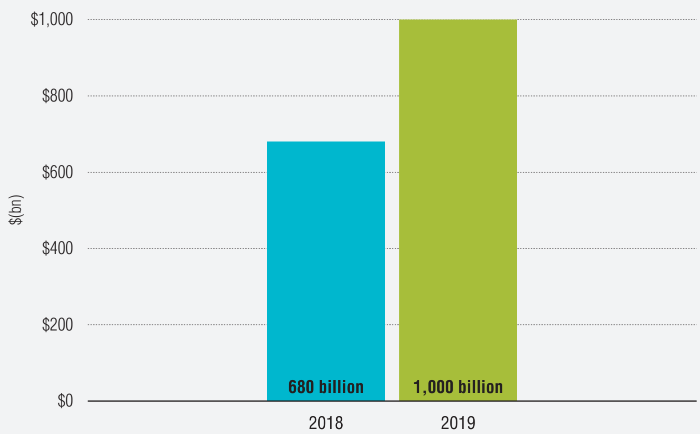
FIGURE 4 Proportion of survey respondent AUM managed using primary and secondary responsible investment approaches



4 **ESG integration is now considered business as usual by survey respondents, with 87% of responsible investment AUM ($1 trillion) managed using ESG integration as a primary approach.**

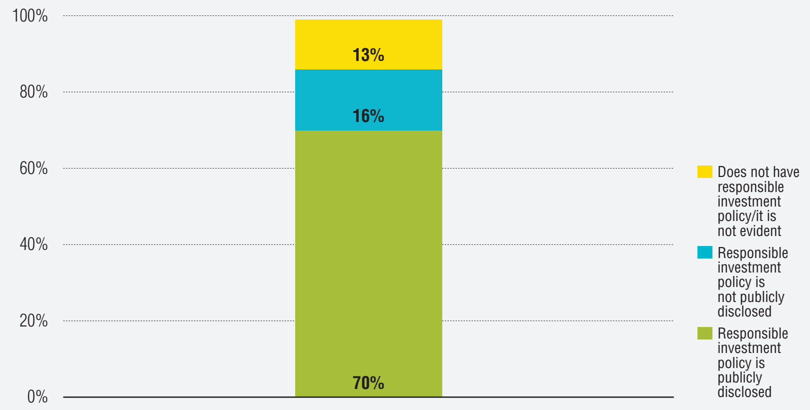
The marked jump for ESG integration (47%) from $680 billion in 2018 to $1 trillion indicates that survey respondents are increasingly recognising that ESG factors provide better and more informed investment decisions, such as valuation and asset allocation.

FIGURE 5 Responsible investment AUM employed in ESG integration as a primary approach ($billion)



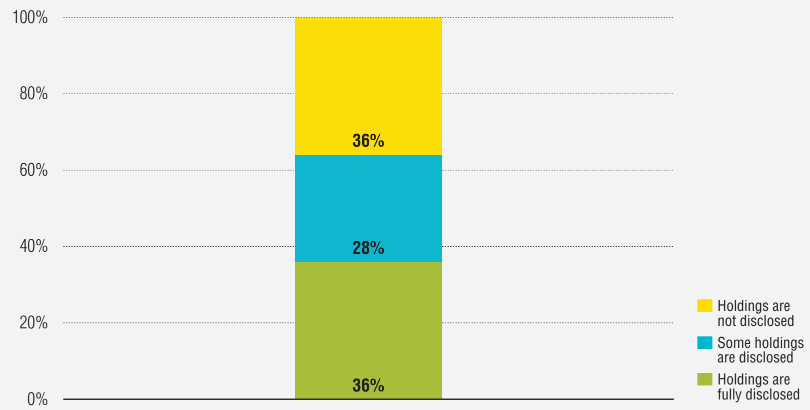
5 **Investment managers are demonstrating a commitment to systematically implementing responsible investing through the development and disclosure of responsible investment policies**. Of the 165 managers in the Responsible Investment Research Universe, 86% have a responsible investment policy and 70% make them publicly available.

FIGURE 6 **Existence and disclosure of responsible investment policy**



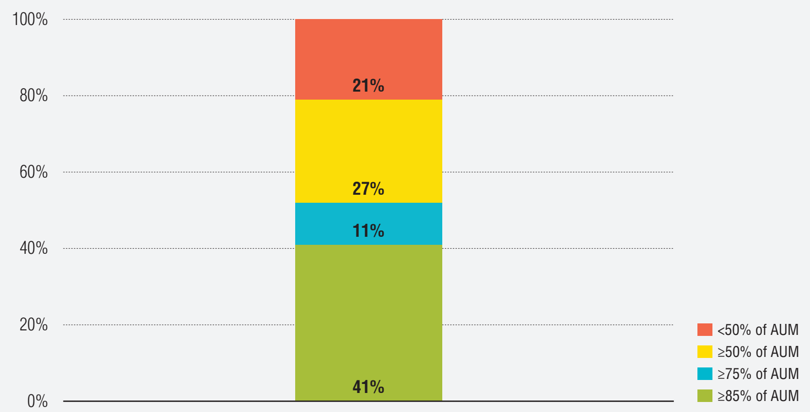
6 Investment managers in the Responsible Investment Research Universe are demonstrating a commitment to transparency through their disclosure of fund holdings. Of the **165 investment managers in the Responsible Investment Research Universe, 36% disclose their full fund holdings and 28% disclose some holdings.**

FIGURE 7 **Level of disclosure of investment managers' holdings**



7 **Seventy-nine percent of investment managers in the Responsible Investment Research Universe have at least one asset class (or 50% AUM) covered by an explicit and systematic approach to ESG integration**, while only 41% have more than three asset classes (or 85% of their AUM) covered.

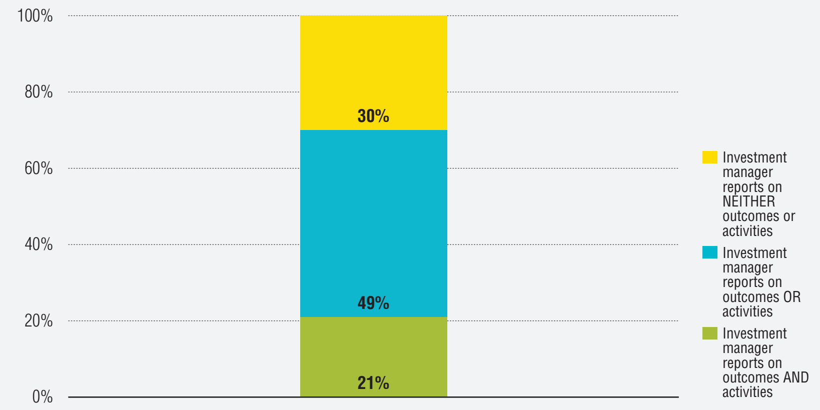
FIGURE 8 **Proportion of AUM covered by an explicit and systematic approach to ESG integration**



8 **Investment managers in the Responsible Investment Research Universe are demonstrating transparency through their stewardship activities,** with 49% reporting on activities or outcomes and 21% demonstrating leading practice by reporting on both activities and outcomes.

This shows that during 2019, active ownership practices continued to mature, with more active, considered and targeted use of voting and corporate engagement.

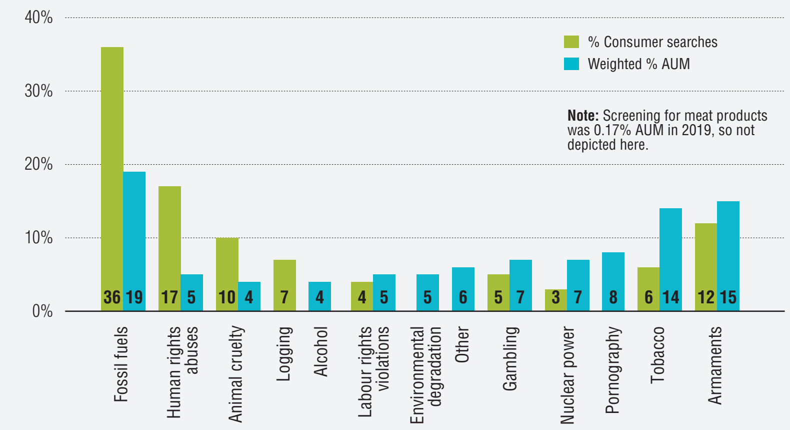
FIGURE 9 **Reporting on corporate engagement activities and outcomes**



9 **Negative screening of fossil fuels is beginning to catch up to consumer interest.** Fossil fuels are clearly front of mind for consumers and survey respondents. In 2018, only 5% of responsible investment AUM for survey respondents who conduct negative screening was screened for fossil fuels. In 2019, 19% of responsible investment AUM has been screened for fossil fuels, growing 14 percentage points from the year before.

For consumers using RIAA's Responsible Returns online tool,[2] the most important exclusionary screens are fossil fuels (36%), human rights abuses (17%) and armaments (12%).

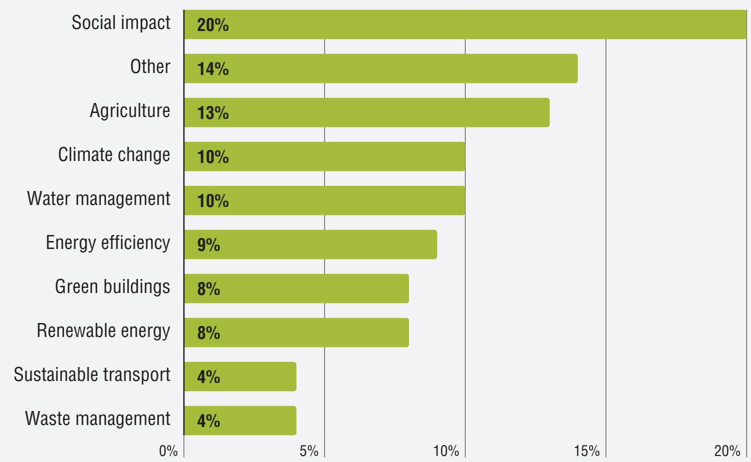
FIGURE 10 **Negative screening – % of consumer searches on Responsible Returns vs survey respondent exclusions (weighted by % AUM)**



10 **Sustainability-themed investing has grown as a responsible investment approach.** Responsible investment AUM using sustainability-themed investing grew from 4% in 2018 to 6% in 2019. The most popular themed investments by AUM are social impact (20%), agriculture (13%) and climate change (10%).

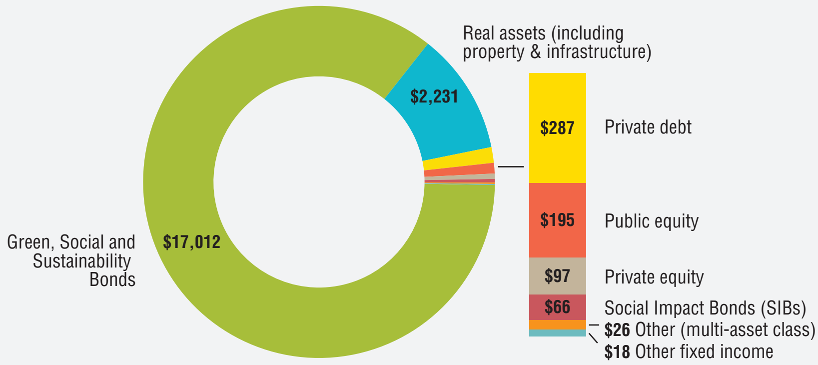
'Other' includes arts, culture and sport; healthcare and medical products; and sustainable fashion and textiles/fashion technology.

FIGURE 11 **Sustainability-themed investments by theme (% AUM)**



11 **Impact investment growth has accelerated** over the course of 2019, driven by the significant increase in market use of Green, Social and Sustainability (GSS) Bonds (248%).

FIGURE 12 **Value of impact investment products by asset class ($million)**



12 **Australian and multi-sector responsible investment funds outperformed mainstream funds over every time horizon.**

International responsible investment share funds outperformed the Morningstar average mainstream international share fund over every time horizon except one year (based on a weighted average performance over 10 years, net of fees).

These findings are consistent with last year, whereby overall it was found that responsible investment funds outperform mainstream funds over most time frames and asset classes.

FIGURE 13 **Performance of responsible investment against mainstream funds (weighted average performance net of fees over 10 years)**

Australian share funds	1 Year	3 Years	5 Years	10 Years
Average responsible investment fund (between 17 and 48 funds sampled depending on time period)	24.7%	11.3%	10.1%	9.0%
Morningstar: Australia Fund Equity Large Blend*	22.3%	9.0%	7.8%	6.8%
S&P/ASX 300 Total Return	23.8%	10.3%	9.1%	7.8%

International share funds	1 Year	3 Years	5 Years	10 Years
Average responsible investment fund (between 13 and 50 funds sampled depending on time period)	22.5%	13.7%	11.0%	11.9%
Morningstar: Equity World Large Blend*	25.2%	12.6%	10.8%	10.9%

Multi-sector growth funds	1 Year	3 Years	5 Years	10 Years
Responsible investment fund average (between 13 and 39 funds sampled depending on time period)	19.48%	11.26%	8.73%	8.24%
Morningstar category: Australia Fund Multisector Growth*	16.22%	7.56%	6.52%	6.88%

*Source: **Morningstar Direct™**

Outperformed by the average RI fund Underperformed by the average RI fund

Introduction

ABOUT RESPONSIBLE INVESTMENT

Responsible investing, also known as ethical or sustainable investing, is a holistic approach to investing, where social, environmental, corporate governance (ESG) and ethical themes are considered alongside financial performance when making an investment. It considers a broad range of risks and value drivers as part of the investment decision-making process in addition to reported financial risk.

Responsible investment includes systematically considering ESG factors throughout the process of researching, analysing, selecting and monitoring investments, acknowledging that these factors can be critical in understanding the full value of an investment.

Responsible investing is also about earnestly executing stewardship duties and working to improve the performance of companies comprising the economy and the stability and sustainability of the financial system more broadly.

In 2020, responsible investing is also about the intentionality of the capital invested – meaning where money is targeted – to avoid harm, benefit stakeholders and contribute to societal and planetary solutions.

INTERNATIONAL RESPONSIBLE INVESTMENT CONTEXT

According to UN Environment Programme's *Sustainable Finance Progress Report*[3] produced for the G20 Sustainable Finance Study Group, 'there is growing evidence that demonstrates the sustainable finance policy over the last year has been characterized by strong growth, increased scope, and greater maturity'. Globally, there are now 730 hard and soft law provisions in financial regulations that embed such sustainability considerations across some 500 policy instruments, with 97% of these laws having been enacted since 2000.[4]

Despite momentum to green up finance, environmental and civil society groups, including UN agencies, consistently report an ever-diminishing quality of natural and human resources globally. The latest *Global Risks Report* by the World Economic Forum points to 'an unsettled world' where climate threats and accelerated biodiversity loss are among the top global risks in terms of likelihood and impact.[5] The last five years are on track to be the warmest on record, natural disasters are becoming more intense and more frequent, and last year witnessed unprecedented extreme weather throughout the world. The current rate of extinction is tens to hundreds of times higher than the average over the past 10 million years – and it is accelerating.

Financial markets are responding to social, environmental and climate change issues, and this response is gaining speed. Countries including China, Canada, the United Kingdom (UK), Hong Kong and New Zealand, as well as the European Union (EU), are taking measures to ensure that their economies and financial markets are resilient, stable and prosperous into this century.

In March 2018, the European Commission presented its 10-point action plan to enable sustainable growth. March 2020 saw the publication of the Technical Expert Group on Sustainable Finance's final report and subsequently in June 2020, European politicians provided final legal confirmation for a taxonomy for sustainable finance activities.[6] This report defines which activities can be legitimately marketed as green or sustainable to incentivise green and climate-friendly investments. In economic terms, the taxonomy for sustainable activities is expected to improve investor confidence and reduce uncertainty and risk, subsequently lowering the cost of capital and more efficiently allocating resources.

It is anticipated that a similar taxonomy will come to Australia through the Australian Sustainable Finance Initiative (ASFI) and hasten the flow of capital into cleaner solutions.[7]

Momentum is growing to embed sustainability and climate risks into financial sector regulation and policies. The Taskforce on Climate-Related Financial Disclosures (TCFD) – created in 2017 to help financial sector entities including banks, insurers, investment entities and asset managers identify exposures to climate risk in their portfolios – is supported by more than 480 investors representing US$42 trillion in assets. From 2020, reporting in line with the TCFD recommendations is required for all Principles for Responsible Investment (PRI) signatories.[8]

In June 2020, the Central Banks and Supervisors' Network for Greening the Financial System (NGFS), of which the Reserve Bank of Australia is a member, released its guide for climate scenarios.[9] The NGFS Climate Scenarios were developed to provide a common starting point for analysing climate risks to the economy and financial system. While developed primarily for use by central banks and supervisors, they may also be useful to the broader financial, academic and corporate communities.

The Global Sustainable Investment Alliance (GSIA) released its biennial *Global Sustainable Investment Review 2018*, showing that global responsible investment assets reached US$30.7 trillion at the start of 2018, a 34% increase from 2016.[10]

AUSTRALIAN RESPONSIBLE INVESTMENT CONTEXT

RIAA's *From Values to Riches 2020* report[11] documents a resounding message from Australian consumers: most expect super funds, banks, financial advisers and other financial institutions to invest their money responsibly and ethically. Investment managers' increased appetite for pursuing responsible investment approaches – or at least for communicating to consumers that they are practising responsible investment – is evidenced by the fact that this report's population of self-declared responsible investors has grown from 120 in 2018 to 165 in 2019.

Australian regulators and industry bodies support ESG integration and reporting. In a speech delivered in March 2019, Guy Debelle, Deputy Governor of the Reserve Bank of Australia, indicated the first-order economic effects of climate change. The Australian Securities and Investments Commission (ASIC) and the Australian Prudential Regulation Authority (APRA) have also publicly acknowledged the distinctly financial threat of climate change and the need for financial institutions to take action to mitigate these risks.

No recent natural disaster has captured more global attention than the devastating 2019 Black Summer bushfires in Australia. Dozens of people and an estimated one billion mammals, birds and reptiles died in the horrific fires.[12] Australia is no stranger to fires in the dry season, but the intensity and magnitude of the 2019 fires were more severe than experienced in living memory. Australian investors have seen the importance of natural capital to continue providing ecosystem services and have prioritised investments to maintain and increase the natural-capital base. The most popular impact theme employed by impact investors in the Responsible Investment Research Universe is environment, conservation and agriculture.

In March 2019, ASFI was launched with a goal to realign the financial services system to better support economic, social and environmental outcomes. The ASFI process will develop and provide a set of recommendations aimed at enabling the financial services sector to contribute more systematically to the transition to a more resilient and sustainable economy, consistent with the United Nations-backed Sustainable Development Goals (SDGs) and the Paris Agreement on Climate Change. An interim report was published in December 2019.[13] ASFI identified six critical challenges that an Australian financial services sector response must address:

1. Leadership, culture and institutional structures;
2. Decision-making and valuation;
3. Policy, regulation and supervision;
4. Frameworks, tools and standards;
5. Unlocking sustainable finance and allocating capital to where it is needed; and
6. Community and consumer interests and expectations.

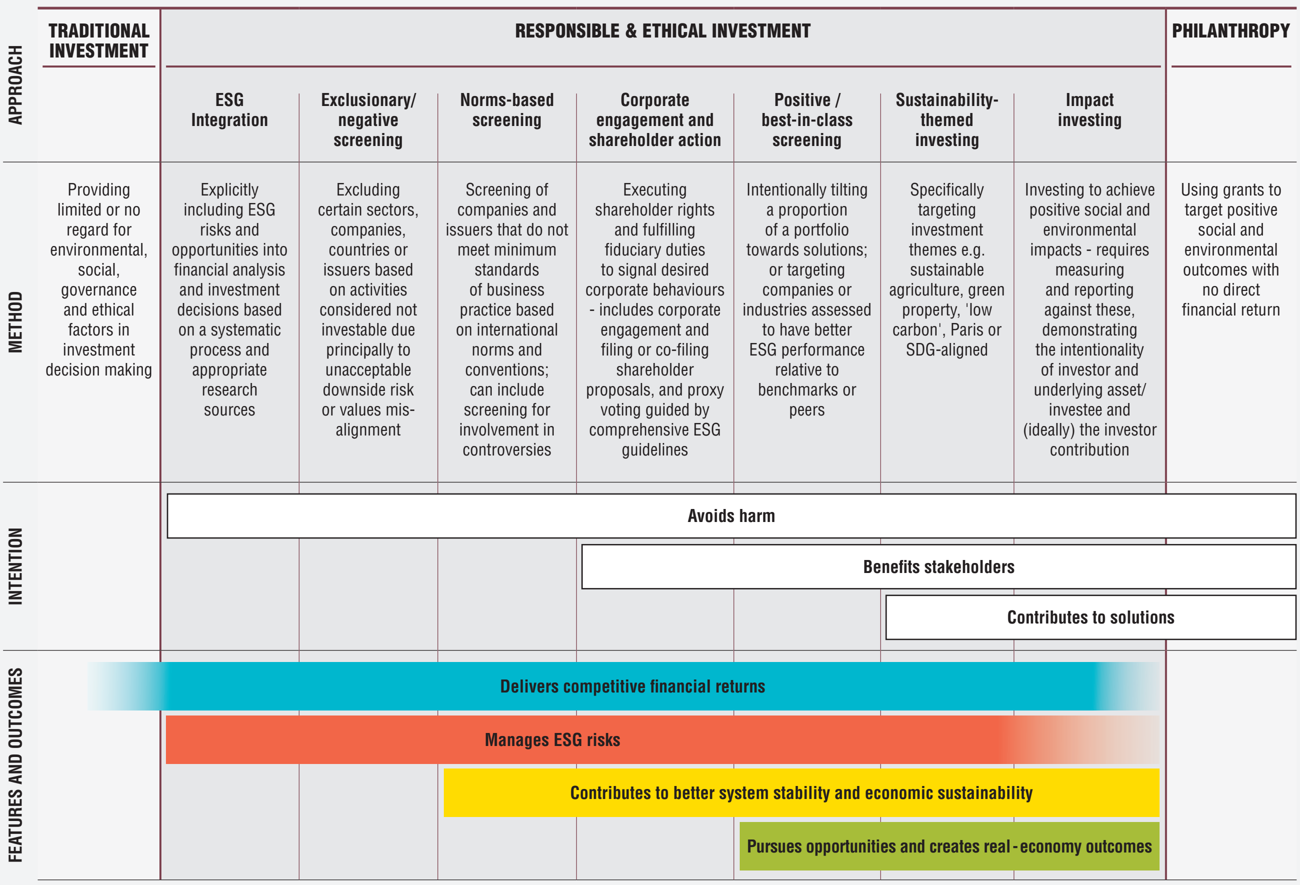
One of the key challenges – unlocking sustainable finance and allocating capital to where it is needed – responds to an urgent need to shift new and existing capital into investments that create and better support sustainable and equitable outcomes for Australian people, the economy, the environment, and investment and trade in the region.

RESPONSIBLE INVESTMENT KEY DRIVERS AND APPROACHES

To enable comparison of Australia's responsible investment market with those of other regions, this report has been prepared in line with the seven approaches for responsible investment (Figure 14) as detailed by the GSIA and applied in the *Global Sustainable Investment Review 2018,* which maps the growth and size of the global responsible investment market.[14]

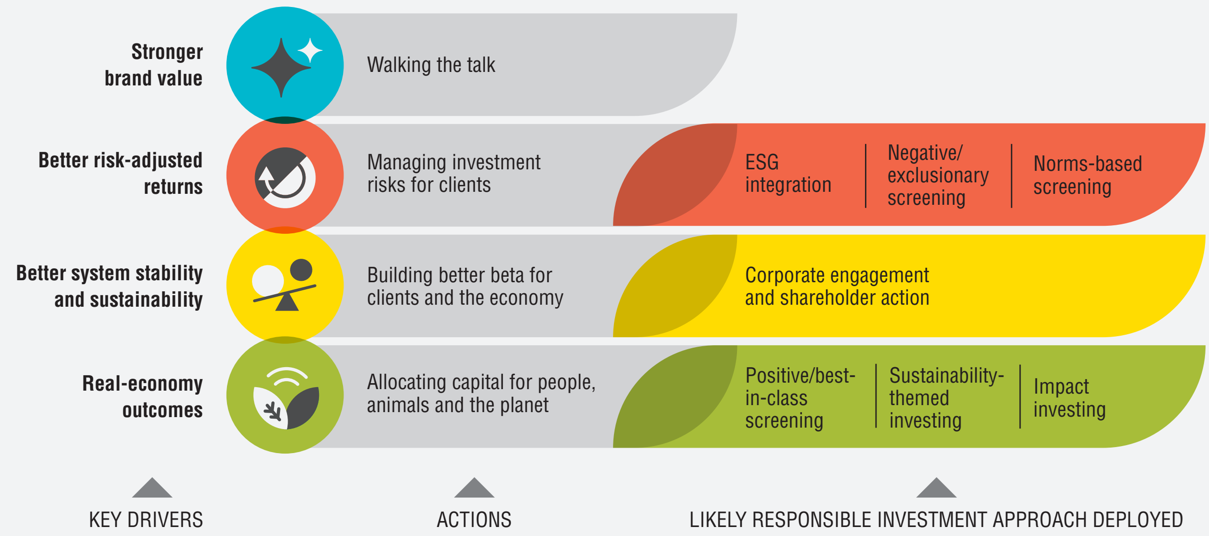
Having arrived in 2020, we bear witness to an ever-increasing expansion of responsible investing strategies being employed across even the most established areas of finance – this includes the world's largest asset manager, BlackRock, announcing its divestment from directly held investments in thermal coal companies.[15]

FIGURE 14 RIAA's responsible investment spectrum



* This spectrum has been adapted from frameworks developed by Bridges Fund Management, Sonen Capital and the Impact Management Project

FIGURE 15 **How the four key drivers for responsible investment align with the seven responsible investment approaches**



The drivers underpinning the strong investor uptake as well as the surge in consumer interest are based on several factors. For investment managers, the key drivers are to:

1. protect or strengthen brand and reputation, meaning favourable treatment with stakeholders such as clients, regulators and employees;
2. deliver better risk-adjusted returns for clients and outperform the benchmark and/or peers;
3. fulfil fiduciary obligations and contribute to better overall system stability and performance; and
4. drive real-economy outcomes and use finance to make a difference in the world.

These four drivers form the basis of the expanded Responsible Investment Scorecard, noting that these – as well as an individual investor's investment beliefs and theses, perspective on risks and opportunities, and dominant client groups – will shape the extent to which each of the seven responsible investment approaches is applied.

For the purposes of this year's report, RIAA has overlaid these four key drivers to undertake responsible investment with the GSIA's seven approaches to responsible investment (see Figure 15). Although not perfectly aligned (i.e. norms-based screening can also be applied to deliver real-economy outcomes), RIAA aims to embed the responsible investment activities of our region's investment managers into a story of intent. When assessed in the context of their intent, we can better make sense of leading practice and whether this results in addressing one or more of the objectives pursued by investment managers in their adoption of responsible investing practices.

DEFINING LEADING RESPONSIBLE INVESTMENT IN THIS DECADE

For the purposes of defining the size of the responsible investment market in Australia, RIAA only includes *assets* managed by investment managers that demonstrate a *leading approach to responsible investment* (leading responsible investment market), rather than all assets managed by organisations that have self-declared as implementing responsible investment (the Responsible Investment Research Universe). (See Figure 1 for the use of terms.)

From 2014 to 2018, RIAA assessed funds against a scorecard of leading practice ESG. In 2019, RIAA has expanded its scoring methodology to more fully account for the evolution in responsible investment practices across the spectrum, from negative screening and ESG integration to corporate engagement and impact investing.

Why an expanded scorecard on leading practice in responsible investment?

Over the last decade, the number and coverage of AUM by signatories to the United Nations-backed Principles for Responsible Investment (PRI) have grown from 700 to 2,760 and from US$30 trillion to over US$115 trillion, respectively.

Yet, Earth's natural systems and its resident species face significant and global challenges, from habitat and diversity loss, climate change and acidification of oceans to desertification of farmlands, decreasing river health and food insecurity, as well as peace and security issues facing a global human population of 7.8 billion living in an increasingly uncertain world.

This inverse relationship between responsible investment commitments made by the investment industry on the one hand – higher than ever before and growing – and the continuing decline in the real-world condition on the other, puts into question whether what we have promoted and celebrated as 'responsible investment' remains relevant in today's context.

This dichotomy underpins RIAA's efforts to drive leading practice standards forward across all responsible investment approaches, as detailed in this section of the report. Leading practice now includes activity in all seven responsible investment approaches and for each of the four drivers underpinning investor commitment to responsible investing (see Figure 15).

RIAA has changed its assessment method in response to several developments:

- Increasingly, investment managers publicise a commitment to responsible investment but fall short of showing how their responsible investment approach is implemented with effect, if at all – hence the expansion of the Responsible Investment Scorecard's parameters making it more challenging to achieve a high score in 2019. Readers will note that between 2018 and 2019, the number of investment managers practising responsible investing increased from 120 to 165 – a jump of 37.5% – with RIAA identifying only a quarter of these implementing responsible investment to a 'leading' standard.
- The new 'business as usual' practices of leading Responsible Investment Managers include the execution of a wide range of responsible investment approaches and a transition from two (returns and risk) to three axes of investing to include consideration of impact.
- Findings from consumer research in Australia demonstrate that consumers expect their responsible investments to avoid harm and ideally help to solve our planet's challenges.[16]
- The inverse relationship between an increasing responsible investment commitment on behalf of investment managers and the continuing decline in the global environmental and social condition confirms that activities to date have been insufficient to create significant change in outcomes (see the break-out box *Why an expanded scorecard on leading practice in responsible investment?*).
- We face urgent and pressing societal and environmental issues that need to be addressed to continue to support the ongoing function of the entire economic system.
- RIAA updated its Constitution and revised its mission at the end of 2018.[17] This has informed the organisation's focus on assessing how the growth of responsible investment in Australia and New Zealand demonstrably contributes to future resilience, prosperity and wellbeing for Australians and New Zealanders and to better align with international measurement approaches.

The expanded scorecard continues to reward strong behaviours to integrate ESG factors, but now increasingly considers those committed to building a more sustainable financial services sector and allocating capital towards solutions for our society and environment. See Appendix 3 for more information on the expanded Responsible Investment Scorecard used to analyse whether responsible investing is being practised by investment managers.

Responsible investment leaders and market share

RESPONSIBLE INVESTMENT LEADERS

In order to ascertain investment managers that are practising a leading approach to responsible investment, data was compiled through a combination of desktop research and supplied directly by investment managers and asset owners through the online survey. RIAA undertook a desktop review of the following:

- all Australian investment managers that are signatories to the PRI (117 in total, up from 93 investment managers the previous year);
- other investment managers on RIAA's database known to practise responsible investment (31 in total); and
- a selection of international investment managers with strong local presence and responsible investment credentials (17 in total).

This Responsible Investment Research Universe of 165 self-declared responsible investors was rated against the four drivers for undertaking responsible investing: 'walking-the-talk', 'managing risk', 'building better beta' and 'allocating capital towards solutions' (see Figure 15). Similar to the approach taken in last year's report, only those demonstrating leading practice were included in determining the size of the Australian responsible investment market.

AT A GLANCE:

- Of the 165 investment managers assessed, 44 (27%) are practising a leading approach to responsible investment (score ≥75% on the expanded Responsible Investment Scorecard, which now also rewards allocation of capital towards real-economy outcomes).
- The 44 investment managers in this group mainly consist of those with a responsible investment AUM of under $50 billion for Australian clients.

Accordingly, the findings in this report are considered to be conservative in nature.

The cut-off score for leading practice has shifted from 80% to 75% this year in acknowledgment of the fact that it has become more difficult to achieve a high score on RIAA's expanded Responsible Investment Scorecard. This is an important step change that enables RIAA to start rewarding new and deeper responsible investment behaviours, such as corporate engagement outcomes and impact reporting, and provides RIAA with broader scope in assessing the growing competition in responsible investment leadership practices for the coming decade.

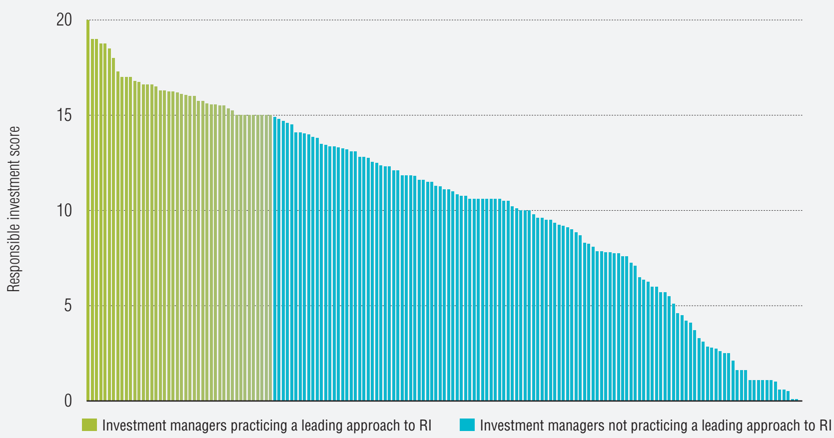
The results of RIAA's desktop research as well as from those who completed the survey are summarised in Figure 16, showing that of the 165 investment managers included in the Responsible Investment Research Universe, 44 (27%) are practising a leading approach to responsible investment. These leaders are comprised of:

- 29 Australian investment managers; and
- 15 international investment managers with a significant presence in Australia.

Leading practice investment managers demonstrate responsible investing in their investment process via:

- the availability and detail included in their ESG investment policies;
- integration of ESG factors in valuation and asset allocation;
- clearly defined approaches to stewardship;
- active ownership (including corporate engagement and voting);
- applied screens to reduce downside risk and tilt towards solutions; and
- meaningful disclosures about these aspects of their investment approach.

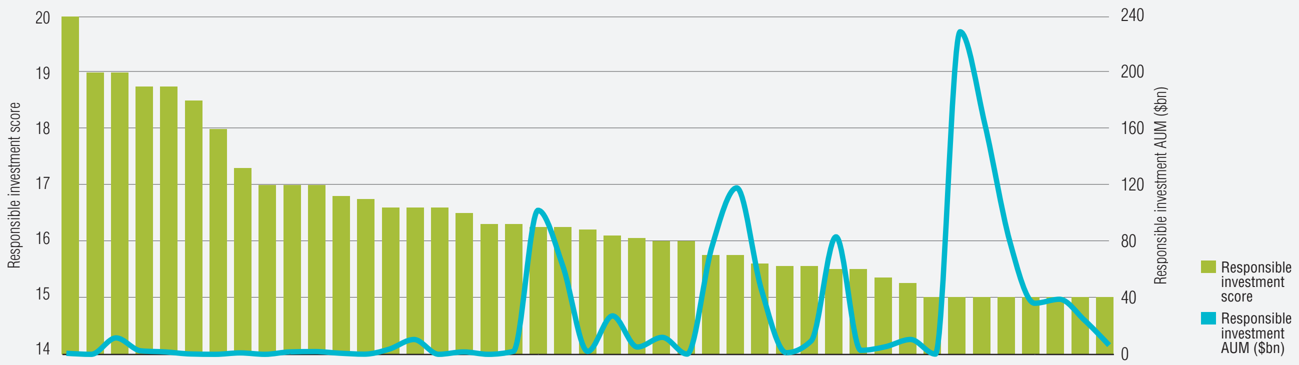
FIGURE 16 **Responsible investment scores of the 165 investment managers assessed**



Leading practice within banking

Although the Responsible Investment Scorecard is designed to assess investment managers' practice, it also captures strong leading responsible investment practice from banks in the form of debt issuances. Examples include green and sustainability bonds from the likes of ANZ, NAB and Bank Australia. Teachers Mutual Bank Limited (TMBL) has its wholesale products certified by RIAA. These debt issuances apply strict ethical criteria for the use of proceeds for its upstream investors and covers TMBL's $1 billion Debt Investment Programme and all Short Term Deposits.

FIGURE 17 **Leading investment managers and their responsible investment scores and associated responsible investment AUM**



Australian investment managers

Aberdeen Standard Investments*
Alphinity Investment Management
AMP Capital Investors Limited
Ausbil Investment Management
Australian Ethical
AustralianSuper
Christian Super
Dexus
Ellerston Capital
Federation Asset Management
First Sentier Investors
First State Super
Future Super
IFM Investors
Impact Investment Group
Local Government Super
Magellan Asset Management Limited
Maple-Brown Abbott
Melior Investment Management
Mercer Australia
Nanuk Asset Management
New Forests
Pendal
Perennial Value Management
Queensland Investment Corporation
Russell Investments*
Stewart Investors
U Ethical
Uniting Financial Services

International investment managers

Affirmative Investment Management
AllianceBernstein
Amundi Asset Management
Aviva*
AXA Investment Managers
BNP Paribas Asset Management
Dimensional Fund Advisors
Franklin Templeton Investments
Generation Investment Management
Janus Henderson Investors
Northern Trust Asset Management
Nuveen
PIMCO
Robeco
UBS Asset Management

*Investment managers for whom data was not received within the survey period; their respective responsible investment AUM has not been included in the total responsible investment AUM of $1,149 billion.

The 44 investment managers in this group consist mainly of those with a responsible investment AUM of under $50 billion for Australian clients, with most of them having a responsible investment AUM under $5 billion for Australian clients. Figure 17 lists these leading investment managers and outlines the responsible investment scores achieved together with the AUM represented.

RESPONSIBLE INVESTMENT MARKET SHARE

Australia has $1,149 billion of leading responsibly managed AUM, which represents a 17% growth on the $980 billion recorded at 31 December 2018 (see Figure 18). Figure 19 shows that leading Responsible Investment Managers in the survey are accountable for 37% of the total assets under management (TAUM) in the Australian investment market as reported by the ABS.

The Responsible Investment Research Universe of self-declared responsible investors has grown from 120 investment managers in 2018 to 165 in 2019. It is estimated that the Responsible Investment Research Universe manages approximately $1,900 billion AUM.

Evidencing real-economy outcomes

Responsible investors have taken moves to better evidence their responsible investment practices by allocating capital towards solutions for our society and the environment. One way of demonstrating this is the adoption of alignment reporting, whereby investment managers report on the outcomes of their investments as well as activities for engagement.

In June 2020, the PRI published guidance on how investors can ‘shape the real-economy outcomes’ of their investments by using the Sustainable Development Goals (SDGs), as it prepares to introduce mandatory outcomes-based reporting for the first time from 2021. The PRI has seen a ‘spike’ in the number of its signatories that have mentioned the SDGs in their reporting to PRI. Thirty-one percent of signatories (650) now mention the SDGs in 2020, up from 24% last year and 16% in 2018. The PRI says accounting for the 2030 goals is a critical part of investors’ fiduciary duty.[18]

Increasingly, investment managers are starting to undertake alignment reporting. For example, Affirmative Investment Management produces a stand-alone report that outlines how its Global Climate Bond has achieved real-economy outcomes such as greenhouse gas emissions avoided and megawatt hours of clean energy generated.[19]

Much of what can be learned about outcomes reporting is borrowed from the impact investing space, especially the Impact Management Project; a forum for organisations that is building consensus around how to measure, compare and report environmental and social impacts.

In August 2019, RIAA launched the Impact Management and Measurement Community of Practice (IMMCOP) to facilitate the sharing of leading practice knowledge and resources for impact management and measurement. IMMCOP helps build RIAA members’ understanding and capabilities in this evolving area of responsible investment, as well as connect with local and global developments.[20]

The 17% growth of responsible investment AUM is partially accounted for by the increased quantity of leading managers (from 34 to 44 this year) being included in the responsible investment market – exhibited by the growth in leading practice investment managers year-on-year.

As in previous years, we asked survey respondents to indicate the strategies that most influence construction of their portfolios – their primary and secondary responsible investment approaches. Primary and secondary approaches are referred to throughout the report to demonstrate the importance that survey respondents place on certain responsible investment approaches. However they do not indicate the only approaches that are used as part of the survey respondents' tools.

The dominant primary responsible investment approach employed in Australia is ESG integration, an approach typically accompanied by corporate engagement and shareholder action as a secondary approach. Eighty-seven percent of responsible investment AUM is managed with ESG integration as a primary approach, representing $1 trillion.

Figure 20 presents a snapshot of primary and secondary approaches used by survey respondents over all of AUM managed to responsible investment approaches. When considering both primary and secondary approaches, sustainability-themed investing AUM has grown in 2020 by 2% to 5.8%. We expect to see this approach to be employed more frequently in the future, both in Australia and internationally, with the development of the EU taxonomy for sustainable activities; this defines which activities can be legitimately identified as 'green' or 'sustainable'.

FIGURE 18 Yearly market value growth of responsible investment AUM and TAUM in Australia ($billion)

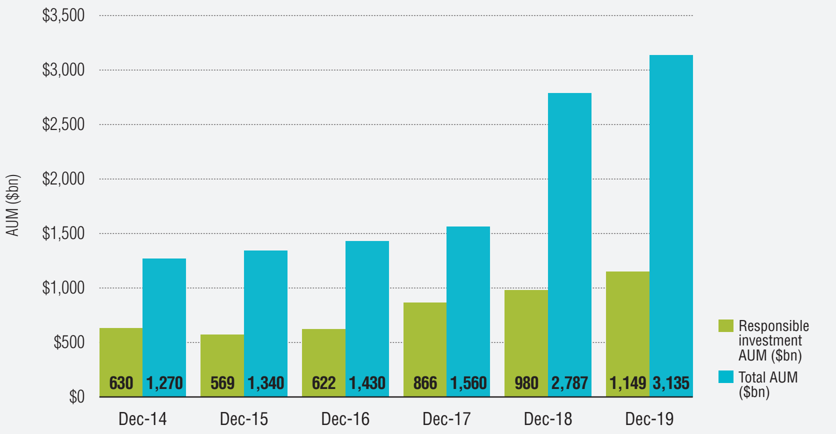


FIGURE 19 Proportion of the full investment management market managed with one or more responsible investment approach

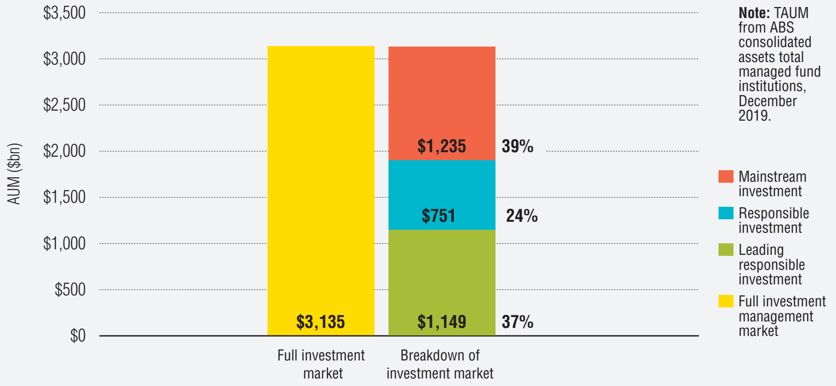
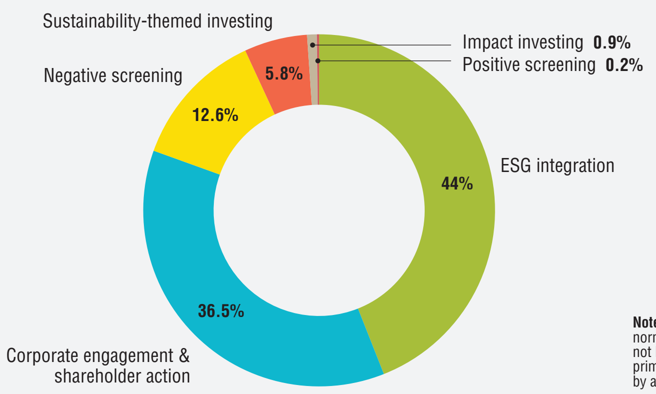


FIGURE 20 Proportion of survey respondent AUM managed using primary and secondary responsible investment approaches



Note: The seventh approach - norms-based screening - has not been nominated as a primary or secondary approach by any investment manager.

Responsible investment approaches and practices

RESPONSIBLE INVESTMENT POLICY

Investment managers are demonstrating a commitment to systematically implementing responsible investment through the development and disclosure of responsible investment policies. Seventy percent of investment managers in the Responsible Investment Research Universe make their responsible investment policy publicly available, while 16% state they have a responsible investment policy but choose not to disclose this document publicly – leaving 14% of self-declared responsible investment managers without a responsible investment policy (see Figure 21).

The purpose of this policy is to articulate the investment manager's beliefs with respect to:

- managing extra-financial factors in the valuation of assets and allocation of capital;
- exercising its fiduciary duty as stewards of capital (including voting over all relevant holdings and disclosing these publicly);
- its role in working with other members of the investment community in delivering a more stable financial and economic system; and
- avoiding harm, benefiting stakeholders and contributing to solutions through its engagement with investee management and allocation of capital towards sustainable assets and enterprises.

A policy is also likely to include a range of commitments for better accountability and transparency such as through disclosures related to underlying holdings, outcomes from corporate engagement and shareholder activism activities, and real-economy outcomes resulting from sustainability-themed and impact investing activities.

KEY DRIVER: Stronger brand value

RESPONSIBLE INVESTMENT PRACTICES:

- 165 investment managers are known to be practising responsible investing.
- 126 (or 77%) of these display their responsible investment commitments publicly, usually on their corporate websites.
- RIAA estimates* that these 126 managers account for approximately $1.9 trillion (or 60%) of the total $3.135 trillion comprising the investment management market.
- This was a similar finding to RIAA's *Responsible Investment Super Study 2019*,[21] which found that 81% of the largest regulated superfunds have some form of responsible investment commitment in place.

* RIAA has a low level of confidence regarding the $1.9 trillion figure, as actual AUM data was available for only around 70% of the 126 investment managers.

FIGURE 21 Existence and disclosure of responsible investment policy in the Responsible Investment Research Universe

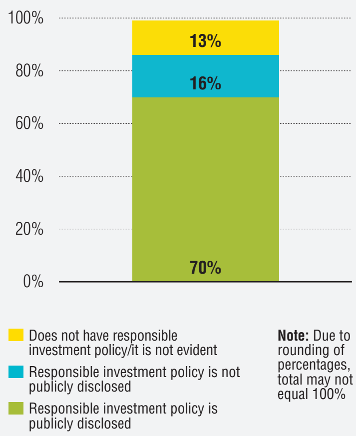
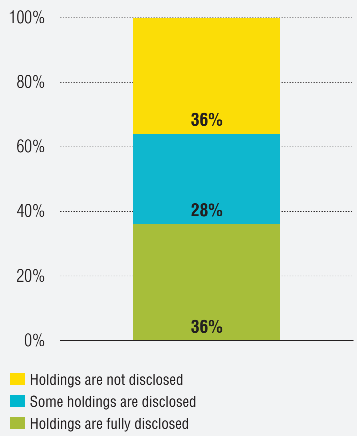


FIGURE 22 The level of disclosure of investment holdings by the Responsible Investment Research Universe



HOLDINGS TRANSPARENCY

Holdings transparency is a new data point for 2020. RIAA considers transparency a cornerstone of accountability and essential for an efficient and effective market-based system. Information related to product holdings helps institutional and retail investors make better informed investment decisions.

Investment managers in the Responsible Investment Research Universe are demonstrating a commitment to transparency through their disclosure of fund holdings. Figure 22 shows that 36% of the 165 investment managers included in the Responsible Investment Research Universe disclose their full fund holdings and 28% disclose some holdings. However, 36% of investment managers in the Responsible Investment Research Universe do not make any public disclosure of holdings, although some of these may disclose holdings directly to their clients only.

According to Morningstar, Australia falls behind the rest of the world in terms of portfolio holdings disclosures as 'sixty percent of the countries require portfolio holdings to be disclosed semi-annually, and nearly all of the others require quarterly disclosure.[22] Australia remains the only country in this survey [of 25 countries] that does not have any [regulatory] requirement to disclose portfolio holdings.'[23] For Australia to stay in step with its OECD peers, complete portfolio holdings should be published regularly.

As key suppliers in asset-owner value chains, investment managers will need to start disclosing full holdings as of December 2020 to comply with ASIC's Class Order [CO 14/443],[24] which requires portfolio holdings disclosure (PHD) for most superannuation trustees. The PHD rules are set out in section 1017BB of the *Corporations Act 2001* (Cwlth) (Corporations Act) and provide that trustees of most superannuation entities must make certain information about their fund's portfolio holdings publicly available and update this at six-monthly intervals.

ESG INTEGRATION

KEY DRIVER: Better risk-adjusted returns

DEFINITION:

Environmental, social and governance (ESG) integration involves the explicit inclusion by investment managers of ESG risks and opportunities into financial analysis and investment decisions based on a systematic process and appropriate research sources. This approach rests on the belief that these factors are a core driver of investment value and risk.

AT A GLANCE:

- ESG integration is the most popular responsible investment approach employed by survey respondents (accounting for primary and secondary approaches).
- In Australia, this approach represents 44% of responsible investment AUM when taking both primary and secondary approaches into account. ESG integration is predominantly used as a primary approach and is often paired with corporate engagement and shareholder action as a secondary approach.
- 87% of the Responsible Investment Research Universe is managed with ESG integration as a primary approach, representing $1 trillion.
- 82% of the Responsible Investment Research Universe deploys ESG integration through factors such as selection of assets, construction of portfolios, risk assessment and selection of managers.
- 79% of the Responsible Investment Research Universe has at least one asset class (or ≥50% AUM) covered by an explicit and systematic approach to ESG integration.
- 28% of the Responsible Investment Research Universe demonstrates the explicit and systematic inclusion of ESG factors in investment analysis and decisions (i.e. fundamental analysis, adjusting financial forecasts and monitoring portfolio weighting and portfolio constituents for changes in ESG exposure).

ESG integration continues to dominate as a responsible investment approach in Australia as well as in the United States, Canada and New Zealand in asset-weighted terms.[25] ESG integration is the second-largest responsible investment approach globally (US$17.5 trillion AUM) after negative/exclusionary screening (US$19.8 trillion AUM) and has experienced the greatest growth in dollar terms over the past two years.[26]

Eighty-seven percent of responsible investment AUM is managed using ESG integration as a primary approach, or $1 trillion AUM. As shown in Figure 23, this represents a marked jump (47%) from 2018, when $680 billion AUM was managed using ESG integration as a primary approach.

ESG integration that is well-defined and systematically embedded in investment and valuation practices can be an effective investment approach. Eighty-two percent of investment managers in the Responsible Investment Research Universe have ESG considerations integrated into their investment approach, including but not limited to:

- selection, retention and realisation of assets;
- construction of portfolios;
- risk assessment and management; and
- selection, assessment and management of managers (if external managers are used).

Seventy-nine percent of investment managers in the Responsible Investment Research Universe have at least one asset class (or >50% AUM) covered by an explicit and systematic approach to ESG integration, while 41% have more than three asset classes (or 85% of their AUM) covered by an explicit and systematic approach to ESG integration (see Figure 24).

Seventy-nine percent of investment managers within the Responsible Investment Research Universe can demonstrate the explicit and systematic inclusion of at least one of the following four ESG practices in their investment analysis and decisions:

- ESG analysis is integrated into fundamental analysis;
- ESG analysis is used to adjust forecasted financials and future cash-flow estimates;
- ESG analysis is integrated in portfolio weighting decisions;
- companies, sectors, countries and currency are monitored for changes in ESG exposure and for breaches in risk limits.

Only 28% of the Responsible Investment Research Universe can demonstrate that all four key ESG factors are incorporated.

FIGURE 23 Responsible investment AUM employed in ESG integration as a primary approach ($billion)

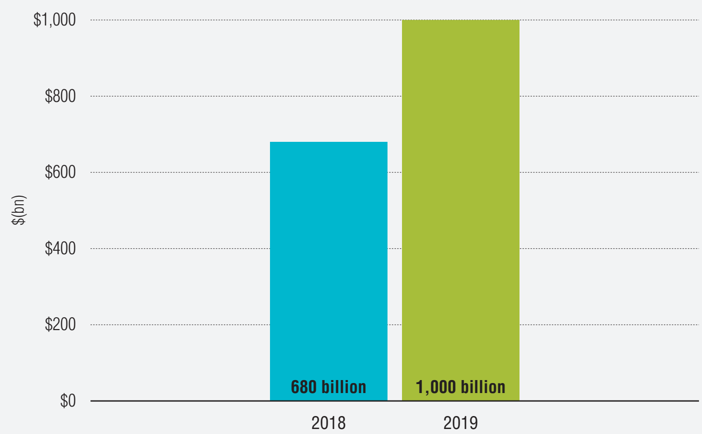
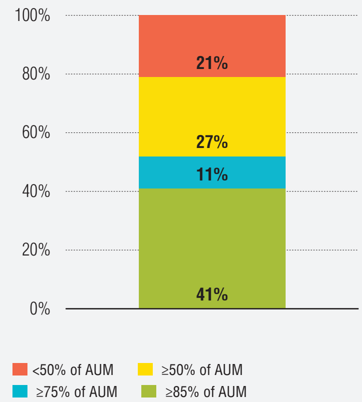


FIGURE 24 Proportion of AUM covered by an explicit and systematic approach to ESG integration



NEGATIVE/EXCLUSIONARY SCREENING

Negative or exclusionary screening is the omission from a portfolio of certain companies or issuers, product categories or practices on the basis of reported controversies, mis-alignment with international norms, industry or economic activity classification, or 'unacceptable' revenue exposure by the excluded company or issuer.

Leading practice for investment managers using an exclusionary approach involves having a transparent and systematic process of applying the screen. Where revenue thresholds are included, it is leading practice to disclose them. Within the Responsible Investment Research Universe for this report:

- 58% of investment managers have a transparent and systematic process of applying exclusionary screening; and
- 27% of investment managers disclose revenue and activity thresholds applied to screens.

Figure 25 shows the most frequently negative screened themes by issue across all survey respondents. Given negative screening approaches do not typically cover an entire portfolio of products, these results represent a fraction of their entire portfolio of AUM.

Weapons, tobacco, gambling and pornography continue to be the most frequently screened categories. During 2019, large investment managers such as BlackRock, AMP Capital and Pendal introduced investment options that exclude issues like thermal coal, tobacco, gambling and pornography. BlackRock, for example, has committed to stop investing in directly held companies that generate more than 25% of their revenue from thermal coal. The policy will force it to divest about $80 million worth of holdings in Whitehaven Coal and New Hope Coal but controversially it allows the company to continue investing in big diversified thermal coal producers like Glencore and BHP.[27]

Figure 25 shows an increasing awareness of more contemporary or topical issues including environmental degradation and high sugar content and/or predatory marketing. Frequency of screening of environmental degradation has increased by 14 percentage points from 2018, while high sugar content and/or predatory marketing has increased by six percentage points.

RIAA has expanded the survey questions in 2019 to enable a more detailed view of the kinds of exclusions being applied by survey respondents. This has included the

KEY DRIVER: **Better risk-adjusted returns**

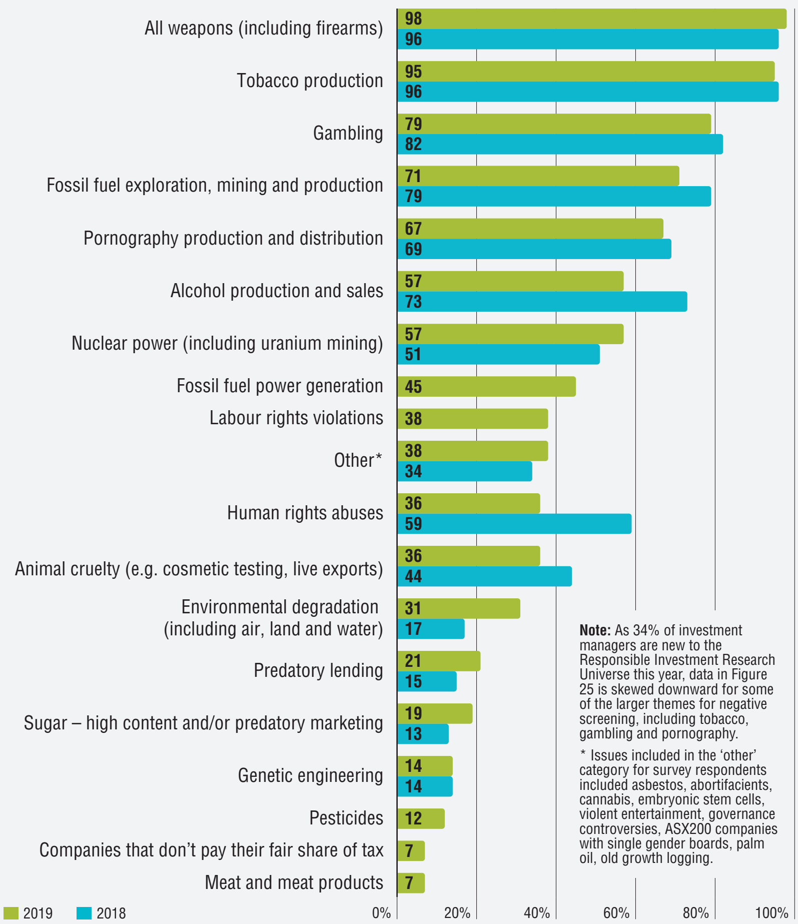
DEFINITION:

Negative/exclusionary screening of investments is the systematic exclusion from a fund or portfolio of certain sectors, companies, countries, or issuers based on activities that do not meet certain criteria. Exclusion criteria (based on norms and values) can refer, for example, to product categories (e.g. weapons, tobacco), company practices (e.g. animal testing, violation of human rights, corruption) or controversies.

AT A GLANCE:

- Considering only primary and secondary approaches, negative screening accounts for 12.6% of responsible investment AUM of survey participants, making it the third-most popular responsible investment approach in Australia.
- 58% of the Responsible Investment Research Universe has a transparent and systematic process of applying exclusionary screens.
- 27% of the Responsible Investment Research Universe discloses revenue and activity thresholds relevant to exclusionary screens.
- Tobacco is the issue most frequently screened (95% of those applying negative screening). This is followed by gambling (79% of those applying exclusionary screens).
- Screening for issues such as sugar content and/or predatory marketing and environmental degradation has grown significantly in 2019. High sugar content screening frequency has increased from 13% in 2018 to 19% in 2019, while environmental degradation has increased from 17% in 2018 to 31% in 2019.
- In 2019, 19% of negatively screened responsible investment AUM is screened at some level for exposure to companies involved in fossil fuels, growing 14 percentage points from only 5% in 2018.
- Survey respondents are paying more attention to consumer values and concerns.

FIGURE 25 Frequency of issues being screened (by number of survey respondents who negatively screen)



introduction of sub-categories for fossil fuels and weapons (see Figure 26 and Figure 27) and addressing the following issues in the survey for the first time:

- companies that don't pay their fair share of tax;
- meat and meat products;
- pesticides and;
- labour rights violations.

This year, fossil fuels have been split into three sub-categories:

1. exploration, mining and production of fossil fuels ≤10% of revenue exposure;
2. exploration, mining and production of fossil fuels >10% of revenue exposure; and
3. fossil fuel power generation.

Seventy-one percent of survey respondents screen for fossil fuel exploration, mining and production, the most common among fossil fuel screens. This is followed by screening for companies that generate power using fossil fuels (45%).

Among exclusions for fossil fuel exploration, mining and production, 33% of investment managers screen for both revenue thresholds across their portfolio of investment products. This is because exclusions often differ across investment products, for example one product may screen out companies that derive equal to or less than 10% of revenue from fossil fuel exploration, mining and production, while simultaneously screening out more than 10% of revenue in another product.

For survey respondents using one of the revenue screens for fossil fuels, it is most common to screen out investees that derive more than 10% of their revenue from the exploration, mining and production of fossil fuels.

The most important exclusionary screens according to consumers are fossil fuels (36%), human rights abuses (17%) and armaments (12%). This is based on data from RIAA's Responsible Returns online tool, which shows the key issues customers search for when choosing a responsible and ethical superannuation, banking or investment product that best match their interests.[28] In 2019, the tool attracted approximately 3,000 users per month. Figure 28, highlights the variation between exclusions survey respondents apply and the consumer interest, with the largest variation shown to be pornography, yielding no consumer searches.

Increasing consumer dialogue around fossil fuels in particular seems to have increased the prevalence of screening during 2019.

During 2018, 32% of consumers searched for funds screening out fossil fuel companies. However, only 5% of the AUM of Responsible Investment Managers who responded to the survey was covered by these exclusions. Since then, this has increased to cover 19% of AUM in 2019 (see Figure 28).

FIGURE 26 Frequency of screening for fossil fuel exploration, mining and production

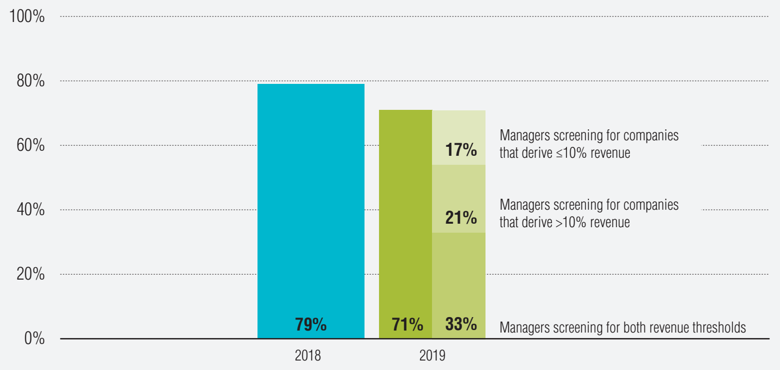


FIGURE 27 Frequency of screening for weapons vs controversial weapons

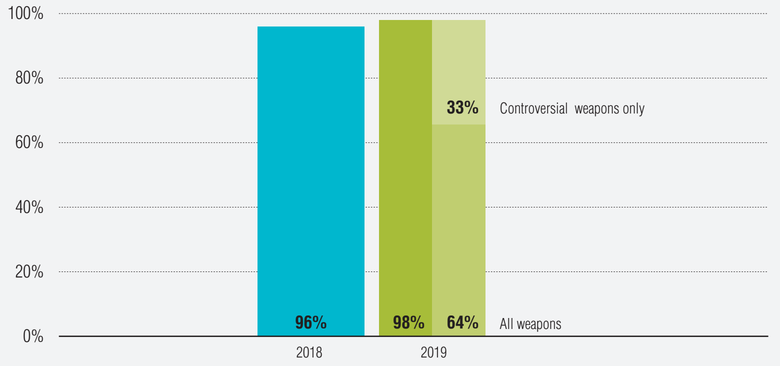
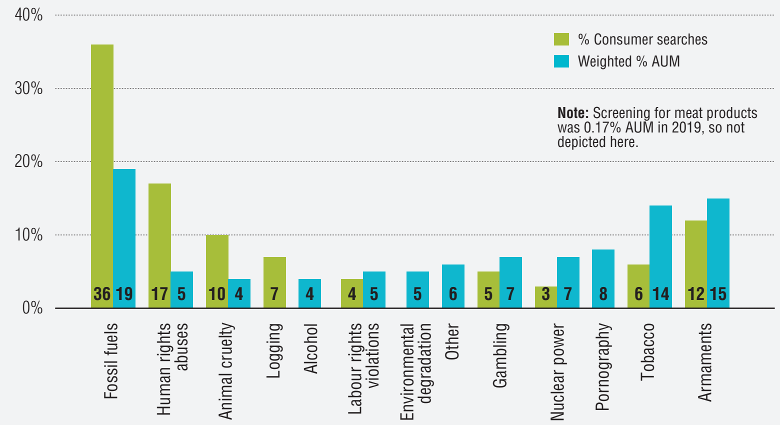


FIGURE 28 Negative screening – % of consumer searches on Responsible Returns vs survey respondent exclusions (weighted by % AUM)[29]



NORMS-BASED SCREENING

Norms-based screening is not a primary feature of the Australian responsible investment landscape. Twenty-three percent of survey respondents use norms-based screening, however, it does not form part of either their primary or secondary approach.

Figure 29 illustrates that the most popular norms screened by survey respondents are the UN Global Compact, PRI, UN Framework Convention on Climate Change and the Sustainable Development Goals (SDGs).

In November 2019, Sweden's central bank, Riksbank, sold Western Australia and Queensland bonds as the bank will no longer invest in assets from issuers with a large climate footprint, even if the yields are high.[31] Riksbank believes it has a role to play to ensure it is not exacerbating global warming and that its activities should be aligned with international treaties such as the Paris Agreement.[32]

As societies' expectations around transparency of impact grow, so too will investors' consideration of norms. It is estimated that to meet the SDGs by 2030, $5-7 trillion in investment is required from the private sector per year.[33] According to the PRI, this investment cannot only come from new capital, but needs to involve investors redirecting existing capital from entities that they invest in. As investors face increasing pressure to be good stewards and improve real-economy outcomes, frameworks such as the SDGs become an important enabler for investment decision-making and improved transparency.

The PRI's *Investing with SDG Outcomes,* released in June 2020, sets out a five-pillar framework for investors to understand real-world outcomes of their investments and align them with the SDGs.[34] Part of this process involves norms-based screening through mapping existing investments to the SDGs and determining the scale of investments in SDG-aligned activities. In addition, investors should take intentional steps towards setting policies and targets to achieve specific SDGs, for example food security or action on climate change. On a practical level, these considerations will cause investors to increase their practice of norms-based screening when considering a new investment, by actively looking for companies and screening in companies that are transparent about their SDG contribution, in addition to screening out those that have negative SDG outcomes.

In an integration between norms-based screening and sustainability-themed investing, products such as Pengana

KEY DRIVER: **Better risk-adjusted returns**

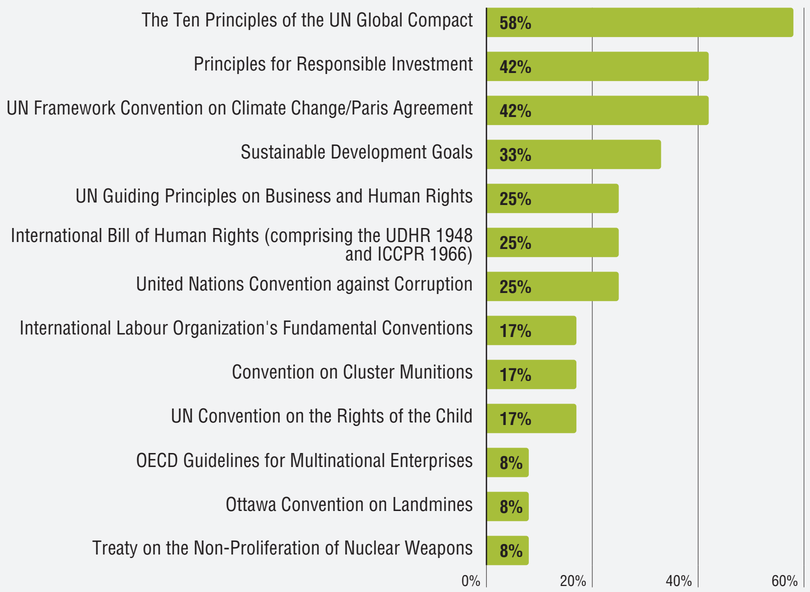
DEFINITION:

Norms-based screening involves the screening of investments that do not meet minimum standards of business practice. Standards applied are based on international norms and conventions such as those defined by the United Nations. In practice, norms-based screening may involve the exclusion of companies that contravene the UN Convention on Cluster Munitions, as well as positive screening based on ESG criteria developed through international bodies such as the United Nations Global Compact, International Labour Organization, United Nations Children's Fund, and the UN Human Rights Council.

AT A GLANCE:

- 23% of investment managers within the Responsible Investment Research Universe use norms-based screening as part of their responsible investment approach.
- Norms-based screening is not nominated by any respondent as a primary or secondary approach.
- The lack of penetration of norms-based screening in Australia contrasts with its popularity in Europe, where it is used by 77% of investors, according to the *Global Sustainable Investment Review.*[30]

FIGURE 29 **Frequency of norms-based screening (by number of survey respondents) in Australia**



Capital's Pengana WHEB Sustainable Impact Fund and Colonial First State's Affirmative Global Bond Fund demonstrate that managers are pushing efforts to make their assets under management more sustainable. Both these products have most of their revenue in business activities that advance one or more SDGs and seek investments that have a quantifiable impact.[35]

The EU's taxonomy sets sustainability criteria for use in financial products based on minimum safeguards (e.g. OECD Guidelines on Multinational Enterprises and the UN Guiding Principles on Business and Human Rights).[36] This tool will help investors, companies, issuers and project promoters navigate the transition to a low-carbon, resilient and resource-efficient economy.

As the world prepares for economic recovery following the COVID-19 crisis, tools for assessing the environmental impact of an investment and public spending are needed more urgently than anticipated during the naissance of the EU taxonomy. It is anticipated that the findings of the Australian Sustainable Finance Initiative will lead to the development of something similar for Australian investors to use.

CORPORATE ENGAGEMENT AND SHAREHOLDER ACTION

KEY DRIVER: **Better system stability and sustainability**

DEFINITION:

Corporate engagement and shareholder action refers to the employment of shareholder power to influence corporate behaviour. This may be conducted through direct corporate engagement such as communications with senior management or boards, filing or co-filing shareholder proposals, and proxy voting in alignment with comprehensive ESG guidelines.

AT A GLANCE:

- No investment manager stated that corporate engagement and shareholder action is their primary responsible investment approach. However, it continues to be the most popular secondary approach, applied to 73% of AUM.
- When taking both primary and secondary approaches into account, corporate engagement and shareholder action continues to represent the second-most popular responsible investment approach (37% of AUM).
- 45% of the Responsible Investment Research Universe uses voting across all holdings.
- 49% of the Responsible Investment Research Universe demonstrates transparency by reporting on either voting or corporate and shareholder action activities; this is up from 39% in 2018.
- 58% of investment managers within the Responsible Investment Research Universe are members of more than one collaborative initiative, for example the Investor Group on Climate Change (IGCC), PRI or Climate Action 100+.

During 2019, AUM of investment managers using corporate engagement and voting as a secondary approach increased to $840 billion from $628 billion in 2018. Active ownership practices continue to mature, with more active, considered and targeted use of voting and corporate engagement by responsible investors in our region and across the globe. Within the Responsible Investment Research Universe, investment managers are demonstrating active ownership and stewardship with:

- 45% engaged in voting across all possible holdings (e.g. directly held equities, or in mandates for fund manager and other third parties to action); and
- 23% engaged in voting across funds to which they are materially exposed.

However, 33% of the Universe did not vote across any of their holdings.

With a surging number of resolutions focused on ESG issues being put to company AGMs, this has resulted in much engagement activity across issues including climate (Paris-aligned transition planning and climate-related targets and disclosures), lobbying activities, fair payment of taxation, labour rights, human-rights risks and Indigenous rights.

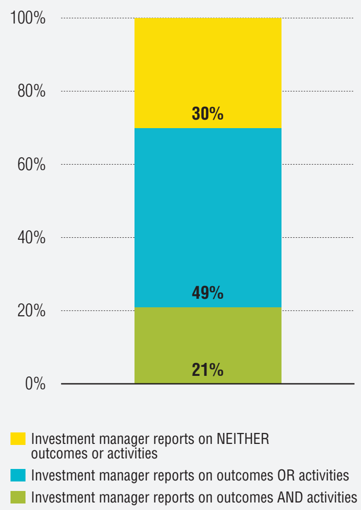
Globally, voting against boards has increased in support of stronger action on climate change. Investors have been more willing to co-file resolutions and withdraw support from industry bodies that are lobbying against Paris alignment. This has required companies to set emissions targets on scope 1, 2 and 3 emissions, and new standards on mining tailings dams that improve safety, and even work to limit the sales of assault weapons from retail stores.

A major focus of engagement activities has been ensuring companies are positioned to transition in alignment with Paris Agreement. The Australian Centre for Corporate Responsibility has found widespread support for numerous shareholder proposals relating to climate risk disclosure and climate lobbying in Australia.

Engagement activities have focused on supporting the implementation of the *Modern Slavery Act* (2018) in Australia.[37] For example, at Coles' AGM in November 2019, three investment managers co-filed the first modern slavery resolution in Australian corporate history.[38] The resolution urged Coles to align its ethical sourcing policies and supplier requirements across its domestic fresh food supply chains to meet industry best practice.

In terms of stewardship accountability, it is leading practice for investment managers to have a clear voting policy and periodically

FIGURE 30 Reporting on corporate engagement activities and outcomes



Active stewardship and why it matters

Active ownership occurs when investors use their formal rights (proxy voting and filing shareholder resolutions) and their position as an investor to influence the activity or behaviour of an organisation. The use of this approach gives a clear indication of investors' willingness to engage with the companies they invest in and positively contribute to the sustainability of their business model as well as the stability of the economy (and financial markets) more broadly.

Voting and corporate engagement are critical components of good stewardship and are fundamental to most investment managers' processes. At high level, these activities can be regarded as 'business as usual' given active investment managers of sufficient size generally meet with company management teams to discuss results and meet with board members to examine resolutions. Likewise, voting at AGMs is standard procedure for most professional investors. What counts is how investors are voting to support (or not) key resolutions to improve transparency, environmental or social performance of investee companies; this is increasingly the focus of civil society groups and other stakeholders looking to leverage the muscle of investors to affect company behaviours and hold investors to account for the behaviours and performance of investee companies.

While this approach requires significant time and therefore has implications of fees for actively managed funds, there are some benefits in terms of performance. For example, Australian Ethical, AustralianSuper and UniSuper offer actively managed super products applying responsible investing approaches and are among the five super products to deliver positive 12-month returns (net of fees) during the COVID-19 crisis.[39]

report on their stewardship and voting activities. Increasingly, leading investment managers are publishing their voting activities throughout a financial year as well as the outputs of this exercise. For example, Ausbil produces a stand-alone advocacy and engagement report, which outlines that it engaged 114 of Australia's largest companies in 117 engagements focused on achieving better ESG and investment outcomes, tackling issues such as modern slavery, climate change and plastic pollution.[41]

Figure 30 (previous page) demonstrates that of the managers in the Responsible Investment Research Universe that are involved in stewardship activities:

- 49% demonstrate reporting on either activities **or** outcomes; and
- 21% demonstrate leading practice, reporting on activities **and** outcomes.

The growth in transparency of activities may be due in part to greater adoption of ESG disclosure standards and guidance, including the Financial Services Council's Principles of Internal Governance and Asset Stewardship, which sets out obligations for fund managers' disclosures on their voting policies and the influence placed on companies they invest in.[42] This includes rules for how investment managers disclose their corporate voting policies and how they attempt to engage and influence the companies they invest in on ESG issues.[43]

Fifty-eight percent of investment managers within the Responsible Investment Research Universe are members of more than one collaborative initiative (for example RIAA, IGCC, PRI or Climate Action 100+). Collaborative initiatives across all parts of financial services, as well as academia, civil society and government, are vital to garner a diversity of opinion as well as provide skills and experience to realign the financial services sector to support greater social, environmental and economic outcomes for the country.

POSITIVE/BEST-IN-CLASS SCREENING

Positive screening is employed as a targeted primary or secondary approach by a relatively small proportion of the survey respondents (less than 1% of AUM). However, positive screening is used more widely as part of the responsible investment approach, with 57% of survey respondents using positive screening as part of their investment approach.

Figure 31 shows the most frequently screened issues by survey respondents are renewable energy and energy efficiency (63%), green property (60%) and more sustainable companies (57%). However, with the recent Australian bushfires, it is possible that issues focusing on building

KEY DRIVER: **Real-economy outcomes**

DEFINITION:

Positive screening of investments is the inclusion of certain sectors, companies or projects selected for positive ESG or sustainability performance criteria such as the goods and services a company produces, or how well a company or country is responding to emergent opportunities such as the rollout of low- and zero-carbon energy assets. The GSIA includes **best-in-class screening**, the involvement in investment in sectors, companies or projects selected from a defined universe for positive ESG performance relative to industry peers. However, RIAA and its members are increasingly integrating best-in-class as a supplementary lens to ESG integration.

AT A GLANCE:

- 57% of survey respondents indicate the use of positive screening as part of their investment approach, despite positive screening accounting for less than 1% of AUM across both primary and secondary approaches.
- This regional proportion is below the ~3% reported globally according to the *Global Sustainable Investment Review.*[40]
- In funds that use positive screening, the most screened category is renewable energy and energy efficiency, closely followed by green property, sustainable companies and healthcare.
- Renewable energy and climate change solutions is the most searched inclusion selected by consumers according to RIAA's Responsible Returns online tool, accounting for 36% of searches.

FIGURE 31 **Positive screening – frequency of issues screened by survey respondents**

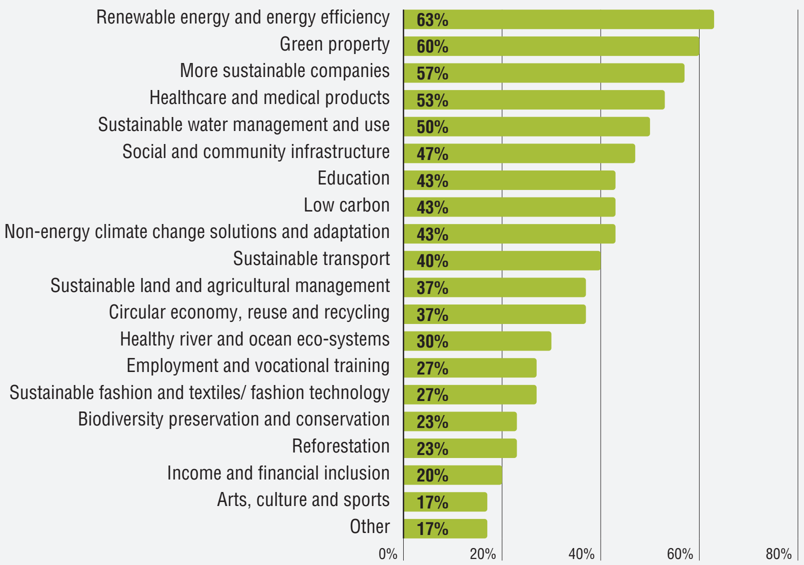
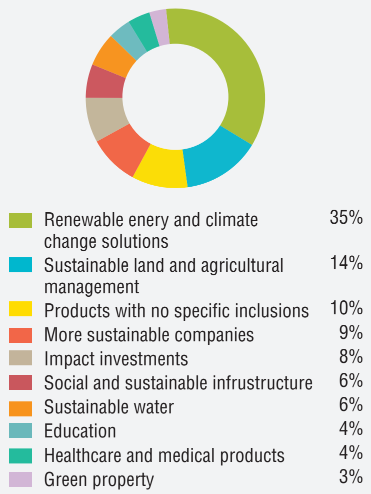


FIGURE 32 **Positive screening – consumer searches using the Responsible Returns online tool (% of consumer searches)**



Note: Due to rounding of percentages, consumer search figures do not total 100%.

resilience of natural systems will become more prevalent. These include sustainable land management (screened by 50% of respondents), biodiversity (23%) and healthy aquatic ecosystems (30%).

One of the funds using positive screening as a primary approach is Federation Asset Management. Its product, Federation Alternative Investments, has a clear approach targeting investments in renewable energy, adaptive technologies and social infrastructure, including disability housing and healthcare.[44]

The most screened issues by survey respondents, i.e. renewable energy and energy efficiency, are consistent with consumer searches on RIAA's Responsible Returns online tool for renewable energy and climate change solutions, as illustrated in Figure 31 and Figure 32. This is followed by green property, sustainable companies and healthcare. The second-most searched for issue by consumers using the Responsible Returns online tool, sustainable land management, is only screened by 37% of funds. In addition, customers are searching for investments that positively screen more sustainable companies. Based on this, it appears survey respondents' screening is beginning to match consumer concerns.

SUSTAINABILITY-THEMED INVESTING

Funds listing sustainability-themed investments as their primary or secondary approach have nearly doubled since last year. Most of this growth has occurred in secondary approaches, which has grown from $4.1 billion in 2018, to $127.5 billion in 2019, while as a primary approach it has shrunk from $70.1 billion in 2018 to $5.5 billion in 2019. This may be due to the growing use of ESG integration as a primary approach across leaders in responsible investment. In addition to this, definitional differences between 'positive screening', 'sustainability-themed' and 'impact investing' may have shifted the results.

Four of the survey respondents – BNP Paribas, Nanuk Asset Management, New Forests and Stewart Investors – use sustainability-themed investing as their primary approach. These investors primarily invest in international equities and/or forestry and farmland. Survey respondents employing sustainability-themed investing as their primary approach are predominantly associated with sustainable land management and agricultural management, followed by renewable energy and energy efficiency.

More broadly, for survey respondents who use sustainability-themed investing as part of their investment approach, the most popular themes by weighted assets under management are social impact (20%), climate change (10%) and agriculture (13%) (see Figure 33).

Within the social impact category, social and community infrastructure (for example, affordable housing) and employment and vocational training are the most popular. These impacts are sought by 8% of weighted AUM each.

KEY DRIVER: **Real-economy outcomes**

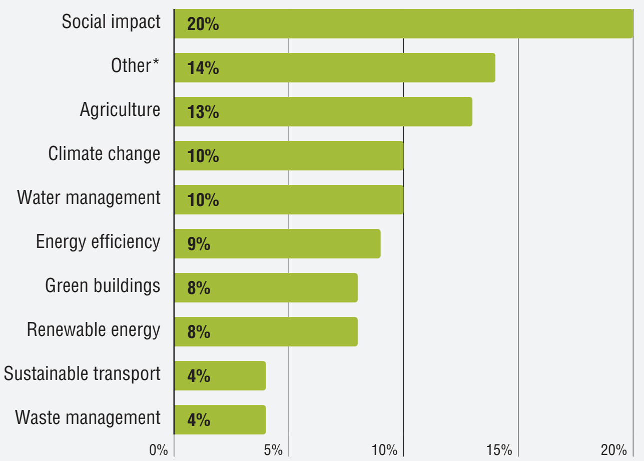
DEFINITION:

Sustainability-themed investing relates to investment in themes or assets specifically related to improving social or environmental sustainability. This commonly involves funds that invest in clean energy, green technology, sustainable agriculture and forestry, green property or water technology.

AT A GLANCE:

- Sustainability-themed investing has grown as a responsible investment approach. As a secondary approach, it represents $127.5 billion of AUM. Taking into account both primary and secondary approaches, sustainability-themed investing has grown from 4% of AUM in 2018 to 6% of AUM in 2019.
- The most popular themed investments by AUM are social impact (20%), climate change (10%) and agriculture (13%).

FIGURE 33 Sustainability-themed investments by theme (% AUM)



* 'Other' includes arts, culture and sport; healthcare and medical products; and sustainable fashion and textiles/fashion technology.

IMPACT INVESTING

Impact investing grew by 44% from $13.8 billion in 2018 to $19.9 billion, representing almost 1% of Australia's $1,149 billion responsibly managed market in 2019. The uptake and growth of impact investing is a response within the finance sector to increasing investor demand and the enduring societal and environmental challenges that we face globally and locally.

Impact investment opportunities span all asset classes. In absolute terms, green, social and sustainability (GSS) bonds dominate the impact investment category, with 85% of impact investment bonds and $17 billion in AUM. These principally include bonds issued primarily from overseas issuers, however, they also include some issuances of green bonds by Australian organisations,

KEY DRIVER: **Real-economy outcomes**

DEFINITION:

Impact investing refers to investments made with the explicit **intention** of generating positive social and/or environmental impact alongside a financial return, and **measurement** of this impact. Ideally, an impact investment will also provide **additionality,** meaning delivery of benefits beyond what would have occurred in the absence of the investment.

AT A GLANCE:

- The total disclosed impact investment pool equates to $19.9 billion AUM in 2019. Therefore, impact investing represents just under 1% of responsible investment AUM.
- AUM using this responsible investment approach grew by 44% from $13.8 billion in 2018 to $19.9 billion in 2019 for assets managed by survey respondents.
- The most popular impact theme targeted by survey respondents is environment, conservation and agriculture (54% of product universe).
- Green, Social and Sustainability (GSS) Bonds account for 85% of products using this approach.
- The weighted average annualised returns (net of fees) for impact investments widely offered to survey respondents ranged between 3.5% for private debt and 11.3% for public equity. GSS Bonds averaged 5.1% p.a., while real assets returned 7.4% p.a. and Social Impact Bonds (SIBs) returned 3.9% p.a..

Benchmarking Impact

In 2020, RIAA published *Benchmarking Impact: Australian Impact Investor Insights, Activity and Performance Report 2020* in partnership with the Deakin Business School at Deakin University.

Benchmarking Impact brings together two pieces of research: a study of 125 Australian investors – accounting for $1,722 billion of the country's assets under management – and a study of 111 impact investment products widely offered to Australian investors at 31 December 2019.

Part 2 of this report shows how the impact investment market is growing in Australia and sheds light on the diversity of asset classes across products and types of impacts being targeted. It features data for the period 1 January 2018 to 31 December 2019 from 125 investors overseeing 117 retail and wholesale impact investment products in Australia.

The report shows that the market for impact investments has continued to develop significantly, growing by 249% from 2017 to 2019 and increasing in size from $5.7 billion as at 31 December 2017 to $19.9 billion as at 31 December 2019, with 111 impact investment products widely on offer to Australian investors.

Performance data:

- The weighted average annualised returns (net of fees) during the study period (1 January 2018 to 31 December 2019) for impact investments widely offered to Australian investors ranged between 3.5% for private debt and 11.3% for public equity. GSS Bonds averaged 5.1% p.a., while real assets returned 7.4% p.a. and SIBs returned 3.9% p.a.
- Financial returns on impact investments targeting environmental outcomes are higher at 5.5% p.a. on a weighted average basis for 2018–2019 than for impact investments targeting social outcomes (4.4% p.a. in the same period).
- Respondents to the 2020 Australian Impact Investment Survey report that overwhelmingly (92%) their impact investments are meeting or exceeding their financial return expectations.
- Financial return expectations among Australian impact investors are high, with three quarters of investors expecting competitive or above market rates of return on their impact investments.
- 25% of investors are willing to accept below market rates of return and only 1% of investors target capital preservation.

Impact data:

- The vast majority of impact investment products target environmental outcomes, however products targeting social outcomes have seen a significant (10 times) increase on the $242 million reported in the 2018 *Benchmarking Impact* study.
- The majority of impact investment products are overwhelmingly directed towards conservation, environment and agriculture ($16.8 billion or 84%), followed by multiple outcomes ($1.8 billion or 9%), and housing and local amenity ($766 million or 4%) and income and financial inclusion ($327 million or 2%).
- In 2019, impact investments delivered a broad range of social and environmental impacts, including:

32,000
Number of homes for people on low to moderate incomes, living with disability, or transitioning out of homelessness

788,000
Healthcare treatments & mental health interventions delivered

200,000
People provided with access to financial services

483,235
Megalitres of water saved, treated or delivered

5 million
tCO2e abated/ avoided and 84,000 GWh renewable energy produced

446
Jobs secured by candidates previously excluded from employment

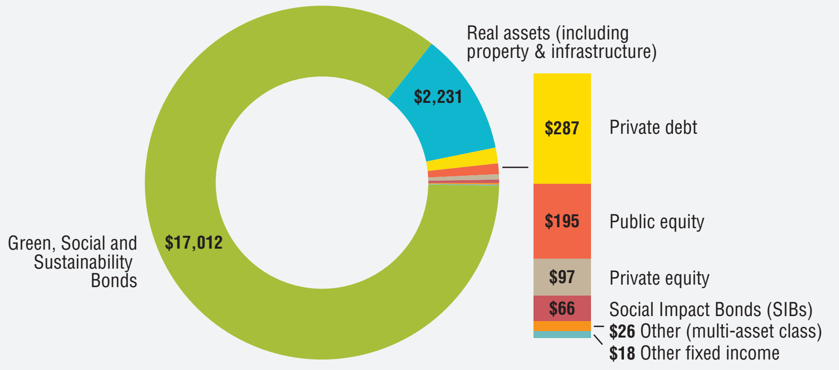
37,856
Homes provided with electricity

including large retail banks. The remaining $2.9 billion in impact investments comprise real assets ($2.2 billion), private debt ($287 million), public equity ($195 million), private equity ($97 million), social impact bonds (SIBs) ($66 million) and others ($44 million) (see Figure 34).

To populate this section of the report, data is used from three sources: primary research (survey data), desktop research and data extracted from RIAA's biennial stand-alone *Benchmarking Impact 2020* report.[45] These three data sources draw on different samples of investment managers with differing intent. This report contains data from investment managers that perform impact investing as one part of their mainstream investment approach and the *Benchmarking Impact 2020* report is based on data from managers that are principally targeting impact investing as core to their investment thesis.

For a more detailed discussion of impact investments in Australia, refer to RIAA's *Benchmarking Impact 2020* report or the breakout box *Benchmarking Impact*.

FIGURE 34 Value of impact investment products by asset class ($million)



Financial performance

RIAA assessed the performance of the survey respondents' responsible investment AUM (classified by asset class and product type), against the performance of mainstream funds over one-, three-, five- and ten-year time horizons, shown in Figure 35.

The average performance in each time horizon has been determined using the asset-weighted returns (net of fees) as reported by each survey respondent. Using a comparable methodology, **Morningstar Direct™** calculated the mainstream performance indices and fund comparison data. Key findings are summarised below:

- The leading practice responsible investment Australian share funds surveyed outperformed mainstream Australian share fund benchmarks for all periods.
- Responsibly invested international share funds outperformed the Morningstar average mainstream international share fund over each time horizon except the one-year time period.
- The leading practice responsible investment Multi-sector funds surveyed outperformed mainstream Australian share fund benchmarks for all periods.

COVID-19 AND THE PERFORMANCE OF RESPONSIBLE INVESTMENTS

In a time of massive market disruption brought on by the global COVID-19 pandemic, RIAA's briefing note *COVID-19 and the performance of responsible investments*[46] explores how responsible investment funds that integrate ESG and other responsible investment approaches have performed compared to the rest of the market.Research undertaken by MSCI,[47] AXA Investment Managers,[48] Fidelity International,[49] Schroders,[50] BlackRock[51] and Morningstar[52] demonstrates that more sustainable companies are performing better and responsible investment funds are largely continuing to outperform the general market.

The thesis that responsible investing supports stronger outcomes for society and the environment, alongside delivering superior financial returns, has been put to one of its toughest market tests with the COVID-19 pandemic. The COVID-19 crisis has highlighted that investment managers executing responsible investment approaches are more resilient to the downside experienced during recent economic volatility.[53]

FIGURE 35 **Performance of responsible investment against mainstream funds (weighted average performance net of fees over 10 years)**

Australian share funds	1 Year	3 Years	5 Years	10 Years
Average responsible investment fund (between 17 and 48 funds sampled depending on time period)	24.7%	11.3%	10.1%	9.0%
Morningstar: Australia Fund Equity Large Blend*	22.3%	9.0%	7.8%	6.8%
S&P/ASX 300 Total Return	23.8%	10.3%	9.1%	7.8%

International share funds	1 Year	3 Years	5 Years	10 Years
Average responsible investment fund (between 13 and 50 funds sampled depending on time period)	22.5%	13.7%	11.0%	11.9%
Morningstar: Equity World Large Blend*	25.2%	12.6%	10.8%	10.9%

Multi-sector growth funds	1 Year	3 Years	5 Years	10 Years
Responsible investment fund average (between 13 and 39 funds sampled depending on time period)	19.48%	11.26%	8.73%	8.24%
Morningstar category: Australia Fund Multisector Growth*	16.22%	7.56%	6.52%	6.88%

*Source: **Morningstar Direct™**

Outperformed by the average RI fund

Underperformed by the average RI fund

Market drivers and future trends

To gain further insight into the increased use of responsible investment approaches, RIAA asked survey respondents to indicate the key drivers pushing them towards adopting responsible investing approaches and the key factors hindering it.

KEY GROWTH FACTORS

Survey respondents were asked to identify the top three drivers for growth in their responsible investment funds; these are shown in Figure 36.

Demand from institutional investors is the most-cited reason for growth by survey respondents. Thirty-eight percent of survey respondents said institutional investor demand is a driver for growth in their responsible investment funds, increasing from 24% in 2018. Within open text answers, survey respondents were able to elaborate on reasons for growth. Interestingly, survey respondents indicated that institutional investor demand is mainly driven by ESG integration on existing products, but not responsible investment funds/products. This confirms ESG integration is becoming a core part of mainstream portfolio decisions.

Growing interest by underlying investors to align investments with mission/values (36%) is the second-largest driver of growth in responsible investment funds, followed by the growing acceptance that ESG factors impact the financial performance of investments (35%). This belief has been tested and confirmed during the COVID-19 crisis, where ESG investments in Australia performed on average 1% better than general balanced or growth fund options in the quarter ended 30 March.[54] Nineteen percent of survey respondents also indicated that the expectation of improved long-term performance or risk mitigation is a driver.

Retail investor demand is a driver for 24% of funds, up from 21% in 2018. Survey respondents cited external events, including the bushfires, climate strikes and increasing public awareness of climate risk, as a driver of growth in retail demand.

International initiatives or commitments for sustainable finance are driving growth in responsible investment funds for 8% of investors, growing from 2% in 2018. Developments include the EU taxonomy for sustainable activities and PRI. Such initiatives enable investors to contribute systematically to the transition to a more resilient and sustainable economy.

GROWTH DETERRENTS

Survey respondents noted that the key factors restricting growth of AUM into responsible investment funds are performance concerns (37%), lack of awareness from members of the public (35%), lack of understanding and capacity within the institution (27%), and mistrust created by green washing (20%) (see Figure 37).

FIGURE 36 Key drivers of market growth by survey respondents

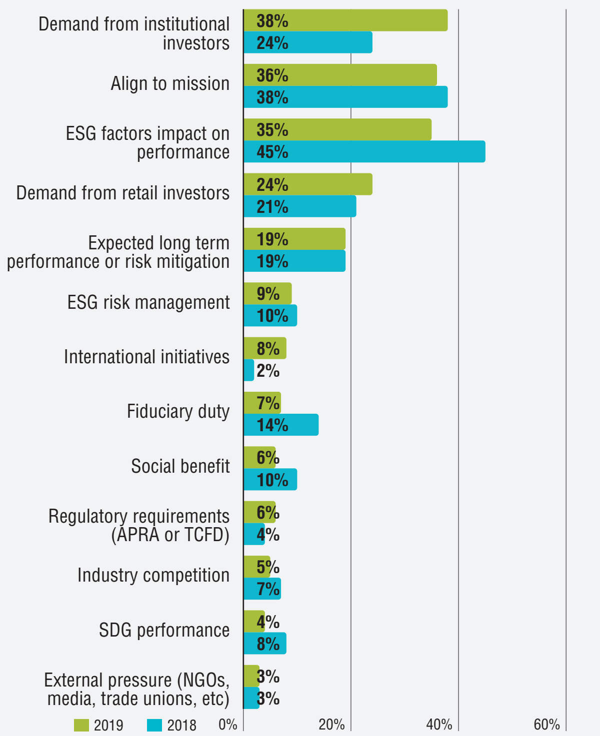
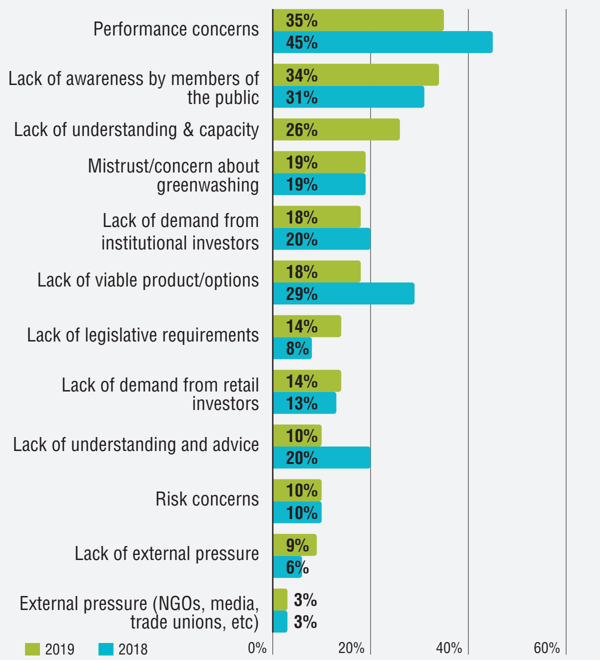


FIGURE 37 Key deterrents to responsible investment market growth by survey respondents

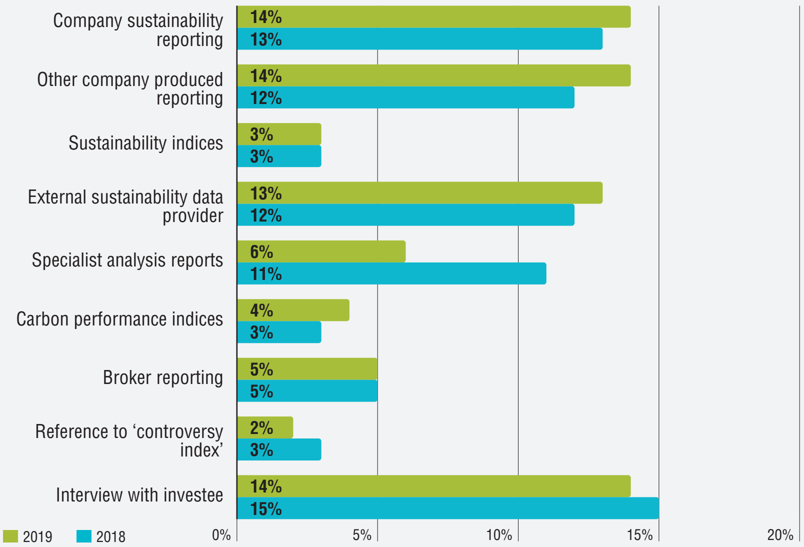


Concern about performance has reduced from 45% of survey respondents in 2018 to 37% in 2019, indicating that investors are more confident with the returns provided by responsible investment funds. Perceptions of responsible investment performance are beginning to align more closely with fact, with responsible investment funds on average outperforming mainstream funds.

Survey respondents were asked about which sources of information they used most when making investment decisions on responsible investment. They nominated the investment target company as their central data source, with 14.4% using interviews with the investee and 14% using investee company sustainability reports (see Figure 38). A further 13.6% use other information produced by the target company such as annual reports, the company website or investor reporting.

External information, such as from ESG research providers, is increasingly being used in the investment decision-making process. For example, 13.1% of investors use external sustainability data providers, while a further 5.9% use specialist analysis reports.

FIGURE 38 Key sources of information used to make responsible investment decisions



Appendices

APPENDIX 1A: ABBREVIATIONS

ABS	Australian Bureau of Statistics
APRA	Australian Prudential Regulation Authority
ASFI	Australian Sustainable Finance Initiative
ASIC	Australian Securities and Investments Commission
AUM	Assets under management
EU	European Union
ESG	Environmental, social and governance
GSIA	Global Sustainable Investment Alliance
GSS Bonds	Green, Social and Sustainability Bonds
IGCC	Investor Group on Climate Change
IMMCOP	Impact Management & Measurement Community of Practice
IMP	Impact Management Project
PRI	UN-backed Principles for Responsible Investment
RI	Responsible investment
RIAA	Responsible Investment Association Australasia
RI AUM	Responsible investment assets under management
SDGs	Sustainable Development Goals
SIBs	Social Impact Bonds
TAUM	Total assets under management
TCFD	Taskforce on Climate-Related Financial Disclosures
UN	United Nations

APPENDIX 1B: DEFINITIONS

Responsible investment assets under management (responsible investment AUM): Only those investment managers that scored 75% or more on the Responsible Investment Scorecard have their AUM included in the responsible investment AUM total. RIAA took this approach so that only those demonstrating leading practice would be included in determining the size of the Australian responsible investment market. This methodology was fairly applied to investment managers across all asset classes and sizes.

Investment managers refers to the financial institutions (asset managers and asset owners to the extent that they directly manage investments in-house) included in the report's analysis that were assessed directly via the online survey or whose data was included via desktop research.

Responsible investment also known as ethical investing or sustainable investing, is a holistic approach to investing, where social, environmental, corporate governance and ethical themes are considered alongside financial performance when making an investment. There are many different ways to engage in responsible investment, and investors often use a combination of strategies such as negative or positive screening; environmental, social and governance (ESG) integration; and impact investing.

Primary approach refers to a responsible investing approach deployed by an investment manager that is used in the first instance when guiding the investment approach of the company's products and services. The **secondary approach** refers to the approach implemented in conjunction with the primary approach when making responsible investing decisions. There are seven main responsible investment approaches: ESG integration; corporate engagement and shareholder action; negative/exclusionary screening; norms-based screening; positive/best-in-class screening; sustainability-themed investing; and impact investing.

Definitions for each of the seven responsible investment approaches: The following guidance was provided to participants to help them classify the responsible investment approaches applied to their investments.

Integration of ESG
GSIA states: the systematic and explicit inclusion by investment managers of environmental, social and governance factors into financial analysis.

RIAA elaborates: the explicit inclusion by investment managers of environmental, social and governance risks and opportunities into financial analysis and investment decisions based on a systematic process and appropriate research sources. This approach rests on the belief that these factors are a core driver of investment value and risk.

Negative or exclusionary screening
GSIA states: the exclusion from a fund or portfolio of certain sectors, companies or practices based on specific ESG criteria.

RIAA elaborates: the exclusion from a fund or portfolio of certain sectors, companies, countries or issuers based on activities considered not investable. Exclusion criteria (based on norms and values) can refer, for example, to product categories (e.g. weapons, tobacco), company practices (e.g. animal testing, violation of human rights, corruption) or controversies.

Norms-based screening
GSIA states: screening of investments against minimum standards of business practice based on international norms and standards such as those issued by the Organisation for Economic Co-operation and Development, International Labour Organization, United Nations (UN) and the UN's Children's Fund (UNICEF).

Corporate engagement and shareholder action
GSIA states: employing shareholder power to influence corporate behaviour, including through direct corporate engagement (i.e. communicating with senior management and/or boards of companies), filing or co-filing shareholder proposals, and proxy voting that is guided by comprehensive ESG guidelines.

RIAA elaborates: executing shareholder rights and fulfilling obligations to influence corporate behaviour, including through direct corporate engagement (i.e. communicating with senior management and/or boards of companies), filing or co-filing shareholder proposals, and proxy voting that is guided by comprehensive ESG guidelines and policies, and accompanied by disclosure of activities and outcomes.

Positive or best-in-class screening
GSIA states: involves screening investment in sectors, companies or projects selected for positive ESG or sustainability performance relative to industry peers.

RIAA elaborates: the inclusion in a fund or portfolio of certain sectors, companies or practices based on specific ESG criteria such as the goods and services a company produces, or how well a company or country is responding to emergent opportunities such as the rollout of a net zero carbon economy. Includes best-in-class screening, which involves investment in companies or projects selected for positive ESG performance relative to industry peers and that achieve a rating above a defined threshold.

Sustainability-themed investing
GSIA states: investment in themes or assets specifically related to sustainability (e.g. clean energy, green technology or sustainable agriculture).

RIAA elaborates: investment in themes or assets specifically contributing to sustainable solutions – environmental and social – where impact is intentional and measured (e.g. sustainable agriculture, green buildings, lower carbon tilted portfolio).

Impact investing
GSIA states: targeted investments aimed at solving social or environmental problems where capital is specifically directed to traditionally underserved individuals and communities, as well as financing that is provided to businesses with a clear social or environmental purpose.

RIAA elaborates: impact investments satisfy three core principles: intentionality, measurability and contribution:

Intention
- the investor and/or manager intend to benefit stakeholders and/or contribute to solutions through their investments (as evidenced in the 'impact thesis'); and
- the impact performance objectives of each asset being invested in are principally (meaning equal to or greater than 50% with impact intention aligned with B and C; balance of fund at least A) benefiting stakeholders or contributing to solutions.

Measurability
- an investor or manager has an impact thesis; and
- has a demonstrated process for managing impact; and
- at least annually reports impact performance to relevant external stakeholders.

Contribution
- at a minimum, the investor or manager can demonstrate that they signal that impact matters (this means to proactively and systematically consider measurable positive and negative enterprise impacts in their investment decision-making); and
- communicates this consideration to external stakeholders.

The Impact Management Project (IMP) convention classifies the impact performance (or goals) of an enterprise as either:

A. (Act to avoid harm) – the enterprise prevents or reduces significant effects on important negative outcomes for people and planet; or
B. (Benefits stakeholders) – the enterprise not only acts to avoid harm, but also generates various effects on positive outcomes for people and the planet; or
C. (Contributes to solutions) – the enterprise not only acts to avoid harm, but also generates one or more significant effect(s) on positive outcomes for otherwise under-served people and the planet.

APPENDIX 2: METHODOLOGY

REPORTING BOUNDARY

This report covers the 2019 calendar year and, where possible, data disclosed has been recorded as of 31 December 2019. Data from some investment managers was not available on a calendar year basis and in these cases, data was taken from the closest available reporting date. All financial figures are presented in Australian dollars.

The financial sector is a globalised industry. Responsible investment funds may be held in one country, managed in another and sold in a third, meaning that a level of estimation is applied in order to demarcate the boundary of the Australian market. This report is intended to inform readers of the nature and scope of responsible investing in Australia. As such, it includes assets managed within the Australian region, as well as assets managed outside the region where these are managed on behalf of Australian clients. Selected international investment managers have been included in this research based on their known operations in our region, managing assets on behalf of Australian clients, and strong responsible investment commitments, including through membership of RIAA (as at 2019 calendar year). This list grows each year as more international managers are disclosing their responsible investment activities within the Australian context.

For a second year, ABS data was used to calculate the TAUM figure, as it was felt the ABS's underlying definitions are well aligned with the uses and applications of the overall data set moving forward. The TAUM data point used for this report is defined by ABS as 'Consolidated assets total managed funds institutions' rather than the 'Total managed fund industry' data point. The consolidated position of the managed funds institutions refers to assets of those financial intermediaries (e.g. life insurance corporations, superannuation funds and unit trusts) which operate in the managed funds market by acquiring assets and incurring liabilities on their own account. Typically, these institutions arrange for the 'pooling' of funds from a number of investors for the purpose of investing in a particular type or mix of assets, with a view to receiving an ongoing return or capital gain.

The 'Total managed fund industry' data point is not used in this report as this also includes the funds under management of investment managers on behalf of clients other than managed funds institutions. This research is primarily targeted at investment managers, rather than asset owners, with a focus on capturing the underlying managers of the capital being deployed responsibly in this market. Data was captured from asset owners to the extent that they directly manage investments in-house.

DATA COLLECTION

Data used to compile this report was generously provided by and collected from:

- investment managers and asset owners;
- **Morningstar Direct™,** which provided data for the average performance of mainstream managed fund categories; **Morningstar Direct™** also provided a secondary source of AUM data for some of the funds listed;
- RIAA's databases;
- desktop research of publicly available information regarding assets under management, performance data and investment approaches from sources including company websites, annual reports and PRI Responsible Investment Transparency Reports; and
- RIAA's *Benchmarking Impact 2020* report was used to inform the Impact Investing section.

A total of 165 investment managers were targeted as respondents to this survey; 54 financial institutions responded by providing information directly while 111 were assessed through desktop analysis. In total, this research managed to gather a comprehensive summary of the full responsible investment market in Australia. Responses that identify the key drivers and detractors of responsible investment were only taken from survey respondents. No data has been extrapolated from its original source.

DATA SELF-CLASSIFICATION

Those investment managers who completed the online survey were asked to self-classify their assets under management covered by the seven responsible investment approaches. For example, an investment manager would indicate that 40% of their assets are covered by a sustainability-themed investment approach.

Through discussion with the investment managers and an analysis of survey responses, it was ascertained that there is a grey area when classifying sustainability-themed investing and impact investing. The latter term is being used in the market as a colloquial term for any style of themed allocation towards solution-style investments, such as renewable energy.

The research methodology does cursory checks over self-declared data, but the data is not assured. RIAA continues to inform and educate the market about the differences between these styles of investment and how to self-classify.

DATA ANALYSIS AND REPORTING

The RIAA online survey aimed to capture data from funds where the investment decision is made internally/directly at the asset level and where the funds are managed on behalf of Australian beneficial owners.

As many investment managers apply several investment approaches, the data collection survey required respondents to identify a single primary responsible investment approach. The survey also requested that respondents nominate any secondary strategies, identify any overlap of approaches and help in categorising funds. This approach was used to create an accurate depiction of the responsible investment environment in Australia.

Where investment managers have applied multiple responsible investment approaches (e.g. a fund may apply ESG integration as well as approaches such as negative or positive screening), we have categorised the fund according to the primary responsible investment approach being pursued. The primary approach is identified by the organisation in their survey response, however, RIAA performs a review of all survey responses to ensure that approaches are categorised consistently across the cohort of responses and that investor responses are categorised consistently year-on-year.

Fund overlaps between survey respondents have been removed, where identified, from the reported figures. RIAA is continuously working to improve its data collection process to enhance the quality of reported figures and to ensure that all products in the Australian market are identified.

It is important to note that all information in this survey is 'self-reported' by survey respondents and only limited analysis is performed over statements made. There is no assurance of statements.

DATA COMPLETENESS

Many of the products in the Australian responsible investment market are not bound by any public reporting, disclosure requirements or independent review (assurance). This report includes both retail and wholesale investment products and increasingly, superannuation fund mandates, individually managed accounts and separately managed accounts. Some investment custodians are reluctant to supply information for reasons of privacy or commercial confidentiality. Data pertaining to funds held outside of managed responsible investment portfolios was not accessible. For this reason, as well as matters identified in the reporting boundary section above, this report provides a conservative depiction of the responsible investment environment in Australia.

APPENDIX 3: RESPONSIBLE INVESTMENT SCORECARD

The expanded scorecard examines and scores organisations against the four drivers for responsible investing (of equal weighting):

1. Walking-the-talk
   - coverage of total AUM by responsible investment or ESG practices;
   - publicly stated commitments to responsible investment;
   - responsible investment policy; and
   - commitments to the transparency.
2. Managing risk
   - systematic processes for ESG integration as well as evidence demonstrating how this process is applied as part of traditional financial analysis;
   - disclosure of ESG integration; and
   - evidence of systematic and transparent application of screens.
3. Building better Beta
   - evidence of activity in other areas of active ownership and stewardship including voting and engagement; and
   - membership of a collaborative investor initiative.
4. Allocating capital
   - systematic and transparent positive screening and/or sustainability investment criteria; and
   - intentional, systematic and transparent process of contributing to solutions by way of impact investment criteria and measurement.

RIAA assessed Australian and a selection of international investment managers that have an active presence in Australia based on their publicly available information including websites, PRI responsible investment transparency reports and all other available material. All investment managers were scored using the Responsible Investment Scorecard criteria.

This year, investment managers were given the opportunity to score themselves against the Responsible Investment Scorecard via an online survey. These results were then cross-referenced against the responsible investment score awarded. Some allowances were given for funds taking credit in areas where it was possibly not clear enough and/or for measuring other factors, and scores were harmonised if required.

Only those investment managers that scored more than 75% have their AUM included in the responsible investment AUM total. RIAA took this approach so that only those demonstrating leading practice would be included in determining the size of the Australian responsible investment market. This methodology was fairly applied to investment managers across all asset classes and sizes.

See table for detailed scoring methodology for this year's report:

Core pillars and weighting	Question description	Scoring methodology
1. **Walking-the-talk = 5 points**		
1.1 **Coverage of total AUM by responsible investment**	What proportion of all AUM is being managed with a responsible investment strategy?	1.0 = 100% 0.75 = 75% – 99% 0.5 = 50% – 74% 0.1 = 10%-49%
1.2 **Responsible investment policy**	Does your organisation have a responsible investment policy? Is your responsible investment policy disclosed publicly? The policy needs to outline your organisation's principles, commitments and approach to responsible investment.	2.0 = yes and publicly disclosed 1.0 = yes, not public 0 = no
1.3 **Commitment to transparency**		
1.3.1 **Disclosure of responsible investment commitment**	Does your organisation report its approach to responsible investing and its implementation clearly on its website?	1.0 = responsible investment approach is disclosed in greater detail, such as including link to PRI Report and/or responsible investment approach 0.5 = self-declared as doing responsible investment but no detail 0 = no disclosure
1.3.2 **Disclosure of fund holdings**	Does your organisation disclose a FULL list of its investments?	1.0 = disclosure of FULL fund holdings 0.5 = some holdings are disclosed 0 = no
2. **Managing risk = 5 points**		
2.1 **Systematic process for ESG: Is there evidence of integrating ESG into traditional financial analysis described?**		
2.1.1 **ESG embedded into strategy**	How embedded is ESG integration into strategy? Does responsible investment approach account for the explicit inclusion of ESG factors? Select all that are relevant to your approach to ESG integration. ESG factors are systematically considered in the: A. selection, retention and realisation of assets B. construction of portfolios C. risk assessment and management D. selection, assessment and management of managers (if you use external managers).	0.5 = at least one aspect considered or all four 0 = no aspects considered
2.1.2 **Extent of relevant asset class that ESG covers**	What is the extent of relevant asset classes covered by your explicit and systematic approach to ESG integration?	0.5 = equities, fixed income corporate, fixed income sovereign OR at least 85% of AUM 0.3 = at least two main asset classes OR 75% of AUM 0.1 = at least one main asset class OR 50% of AUM 0 = no option selected
2.1.3 **ESG factors in investment analysis**	Consider how your organisation demonstrates the explicit and systematic inclusion of ESG factors in investment analysis and investment decisions. Select all that are relevant. A. ESG analysis is integrated into fundamental analysis B. ESG analysis is used to adjust forecasted financials and future cash flow estimates C. ESG analysis is integrated in portfolio weighting decisions D. Companies, sectors, countries and currency are monitored for changes in ESG exposure and for breaches in risk limits	1.0 = all 4 0.75 = at least 3 0.5 = at least 2 0.2 = at least 1 0 = no option selected
2.1.4 **Disclosure of ESG integration**	Does your organisation disclose its approach to ESG integration? (such as through PRI reporting, website etc.)	1.0 = yes 0 = no
2.2 **Evidence of systematic and transparent application of screens**		
2.2.1 **Applying screens to investments**	Does your *organisation* have a transparent and systematic process of applying screens (such as norms-based, controversies and negative screens)?	1.0 = yes 0 = no
2.2.2 **Revenue and activity thresholds applied to screens**	Does your *organisation* disclose revenue and activity thresholds applied to screens?	1.0 = yes 0 = no

3. **Building better Beta = 5 points**		
3.1 **Evidence of activity in other areas of active ownership & stewardship: voting**	To what extent does the organisation demonstrate stewardship and active ownership commitments, such as through voting and proxy voting?	2.0 = voting across all possible holdings (e.g. directly held equities, or in mandates for fund manager and other third parties to action) OR 1.0 = voting across those holdings for which the fund is materially exposed 0 = no voting
3.2 **Evidence of activity in other areas of active ownership & stewardship: corporate engagement**	How does your organisation demonstrate stewardship commitments, such as corporate engagements?	1.0 = company engagement reporting on activities AND 1.0 = company engagement reporting on outcomes 0 = no engagement
3.3 **Member of collaborative initiative**	Is the organisation a member of a collaborative initiative? E.g. Investor Group on Climate Change, Principles for Responsible Investment, Climate Action 100+, other groups?	1.0 = member of more than one group OR 0.5 = member of one group 0 = no groups
4. **Allocating capital = 5 points**		
4.1 **Evidence of systematic and transparent positive screening and/or sustainability investment criteria**	What evidence exists of a systematic and transparent process of benefiting stakeholders (positive screening and/or sustainability themed investing)? Select all that apply.	1.0 = explanation of positive social or sustainability-themed screen, including disclosure of thresholds and materiality for investment (e.g. GRESB, Green Star rating etc.) 1.0 = extra-financial targets set (e.g. at least 30% lower carbon intensity than index) 1.0 = company engagement case studies or other evidence demonstrating benefit to stakeholders
4.2 **Evidence of intentional, systematic and transparent process of contributing to solutions by way of impact investment criteria and measurement**	Is there evidence of an intentional, systematic and transparent process of contributing to solutions (impact investing and measurement of impact)?	1.0 = investment criteria including intentionality as evidenced by publicly disclosed impact thesis and/or setting of impact targets, for example AND 1.0 = measurement and reporting on real-economy outcomes from investment

APPENDIX 4: SURVEY RESPONDENTS

Aberdeen Standard Investments	First Sentier Investors	Perennial Value Smaller Companies Trust
Acadian Asset Management	First State Super	Perpetual Limited
Affirmative Investment Management	Future Super	PIMCO
Alphinity Investment Management	Generation Investment Management	Queensland Investment Corporation
Altius Asset Management	Hyperion Asset Management	Resolution Capital
AMP Capital Investors Limited	IFM Investors	Rest
Australian Ethical	Impact Investment Group	Russell Investments
AustralianSuper	JANA Investment Advisers	Solaris Investment Management
AXA Investment Managers Asia (Singapore) Limited	Local Government Super	State Street Global Advisors
Balanced Equity Management	Maple-Brown Abbott	Stewart Investors
BlackRock	Martin Currie	Technical Investing
BNP Paribas Asset Management Australia Limited	Melior Investment Management	Teachers Mutual Bank Limited
Christian Super	Mercer Australia	U Ethical
Cooper Investors	Nanuk Asset Management	Uniting Financial Services
Daintree Capital	New Forests	Vanguard Investments
Ellerston Capital	Northern Trust Asset Management	Warakirri Asset Management
Ethical Investment Advisers	Nuveen	WaveStone Capital
Federation Asset Management	Pendal	

APPENDIX 5: OTHER ORGANISATIONS USED IN DATA (DESKTOP RESEARCH)

AAG Investment Management Pty Ltd	Brandon Capital Partners Pty Ltd	Fortius Funds Management
AGNITIO Real Estate Investments	Brightlight Group Pty Ltd	Franklin Templeton Investments
Allan Gray Australia	BT Financial Group	Future Fund
Allegro Funds Pty Ltd	Campbell Group	GPT Group
AllianceBernstein	Cbus	Greencape Capital
Amundi Asset Management	Celeste Funds Management	Growth Farms Australia
Antipodes Partners Limited	Charter Hall Group	Gunn Agri Partners
Aoris Investment Management	Continuity Capital Partners	HESTA
Ardea Investment Management	Dalton Nicol Reid (DNR) Capital	Infradebt
Argo Infrastructure Partners LP	Dexus	Infrastructure Capital Group
Artesian Capital Management Pty Ltd	Dimensional Fund Advisors	Intrinsic Investment Management
Ausbil Investment Management	ECP Asset Management	Investa Property Group
Auscap Asset Management	EG Funds Management	Investors Mutual Limited
Australian Catholic Superannuation	Eiger Capital	ISPT Super Property
Avenir Capital Pty Ltd	Eight Investment Partners	Janus Henderson Investors
Aviva	ESSSuper	Karara Capital
Bell Asset Management Limited	Ethical Partners Funds Management	Kilter Rural
Bentham Asset Management	Fairlight Asset Management	Kinetic Investment Partners
Blue Oceans Capital	Foresight Group LLP	Kirwood Capital

L1 Capital
Laguna Bay
Legg Mason
Lendlease
Lennox Capital Partners
Lighthouse Infrastructure
Liverpool Partners
Longwave Capital Partners Pty Ltd
Macquarie Asset Management
Magellan Asset Management Limited
MaxCap Group
Merlon Capital Partners
Metrics Credit Partners
Mirvac Group
Munro Partners
NAOS Asset Management Ltd
NGS Super
Nikko AM Australian Equities
Northcape Capital
NovaPort Capital
Pacific Equity Partners
Pacific Road Capital
Palisade Investment Partners Limited
Paradice Investment Management
Pengana Capital
Perennial Value Management
Phoenix Portfolios
Plato Investment Management
Platypus Asset Management
PM Capital
Providence Asset Group
QBE Insurance
Qualitas
RARE Infrastructure Limited
Redpoint Investment Management
Renaissance Asset Management
Revolution Asset Management
Rivera Farming P/L
Robeco
Sage Capital
Spheria Asset Management
Stafford Capital Partners
State Super
Sustainable Insight Capital Management
Talaria Capital
Taurus Funds Management
Ubique Asset Management Pty Ltd
UBS Asset Management
UniSuper
VanEck Australia
Vantage Infrastructure
Whitehelm Capital
Wilson Asset Management
Wisdom Funds
Yarra Capital Management

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