

## ESG exuberance is at all-time highs. But will investors buy?

As investors increase their focus on mission-based investing, they continue to grapple with ESG and what it means to them.

**By David Shalom, Director of Capital Introductions at Pershing**

Innovation. New investment solutions. That's how managers deliver value and attract new investors.

Only time will tell how much staying power any new strategy or strategy-variations will have. Will interest fade? Or will demand grow over time?

Strategies focusing on Environmental, Social, and Governance (ESG) considerations are all the rage today, dominating the new launch market. These strategies are hotly debated at investment conferences, and ESG stories are covered heavily by the media. Managers want to talk about it, and investors are listening. Enthusiasm is turning into exuberance, but is exuberance turning into explosive growth?

The answer is "Not yet." In the normal course of business, allocators meet with many managers (across strategies) to understand what is available to them and to determine which categories, themes, and missions align with their actual investment activities. Investors rarely broadcast their plans on narrowing their searches, selecting finalists, and making allocations. With that said, every now and then, investors will anonymously share their actual intentions via surveys.

During the first half of 2022, BNY Mellon / Pershing's Capital Introductions team surveyed 70 investors about their true ESG objectives. We set out to better understand their motivations, identify specific areas within the E, the S, and the G that investors actually care about, and determine what commitment to ESG resourcing they actually have. What we unearthed was telling.

Investors revealed that ESG adoption is still very much in its infancy. Unsurprisingly, most respondents did not have specific ESG goals yet. Before ESG strategies can achieve wider adoption, investors shared that developing deeper expertise within each discipline of ESG is still needed. To add to that, investors select investment strategies that make money. As a result, respondents shared that they need to see more wide-spread evidence that ESG

strategies can deliver competitive returns and achieve their mission.

Investors also gave us a peek into on their own implementation of ESG investing. In the normal course of business, most investors put money to work via asset allocation buckets. Of those we surveyed, only 4% were allocating to ESG strategies today via asset allocation buckets. That means 96% were not investing in ESG in a formal way, which is the biggest indicator of where the actual demand for ESG strategies is currently. In addition, 30% of our investors shared that they allocate to ESG strategies opportunistically, which is further evidence of a slower pace of ESG adoption.

Another key indicator is around measurement. The old saying goes, “You can’t manage what you don’t measure.” Our survey found that only 17% of investors were measuring progress towards their ESG goals, while the rest were not measuring ESG progress at all.

Through our poll, we not only discovered why ESG funds may not be experiencing exponential growth yet, but we also uncovered meaningful clues as to the future of ESG adoption. For example, our survey revealed investors’ plans for expanding their ESG resourcing -- a big indicator of growing interest. 16% shared that they already have the necessary ESG expertise today, while 37% of our investors said that they plan to grow their expertise overtime.

On the topic of goals measurement, 27% of our investors were in the process of hashing out which ESG metrics should be used, which is evidence of increasing formality around ESG investing.

Investors also disclosed different missions within ESG. For those with Environmental missions, many investors shared interest in strategies that advance Energy Transition and Climate Change Mitigation. Newer areas of interest include strategies that reduce Air Pollution-and-Wildfires, improve Waste Management, and increase Clean Water Availability.

For those with Social missions, many respondents shared that their main interest continues to be in investment strategies that advance Diversity and Inclusion. Newer areas of interest include investment strategies that advance Talent Development and Retention, Workforce Health and Safety, and Healthcare and Pharmaceutical Access.

Many investors with Governance missions shared their interest in strategies that focus on traditional areas of shareholder activism, including Independent Directors, Board Entrenchment, and Executive Compensation. Newer areas of interest include Cybersecurity and One Share, One Vote.

In conclusion, as investors develop more depth within the fields of ESG, as more ESG funds deliver competitive returns, and as more standardized measurement metrics are adopted, demand for these strategies will continue to grow.