pi STEWARDSHIP roundtable

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Jen Bishop | Claudia Chapman
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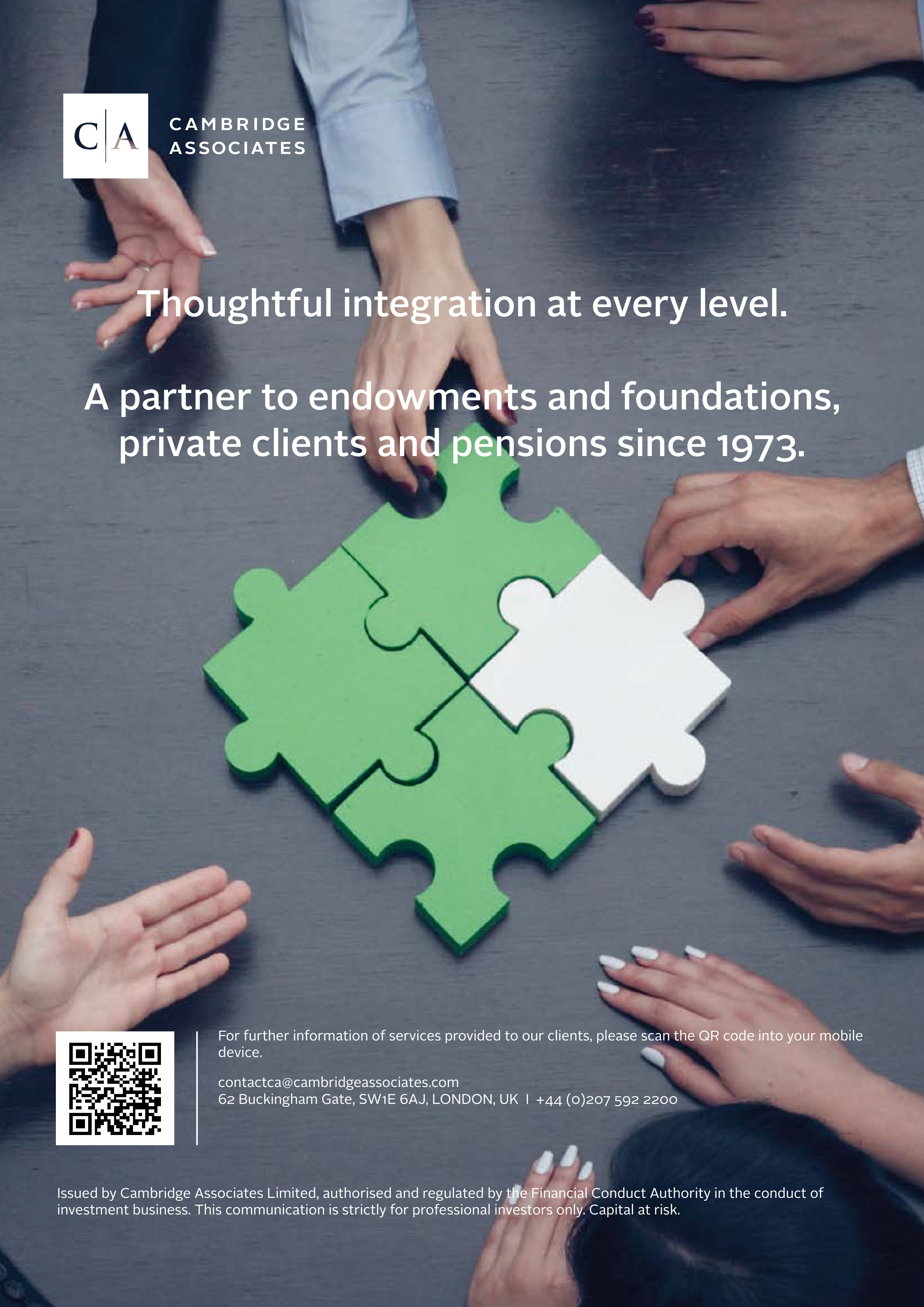
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DISCUSSION: STEWARDSHIP

There was a time when an institutional investor owning equity in a company simply sat down with its directors to make sure they were managing their financial risks and to ask how much money they will make this year.
Things have changed. Savers and other stakeholders now want companies to be greener and more socially responsible and so are pushing those managing their retirement funds to create more sustainable portfolios.
Therefore, attitudes towards stewardship of the assets have changed, but how does this work in practice? *portfolio institutional* sat down with a panel of experts to find out.

How has the definition of stewardship changed since the first UK Stewardship Code was published in 2010?

Claudia Chapman: The code was initially a set of principles around how institutional investors should be the stewards of predominantly UK-listed equity. It was about making UK corporate governance more effective and thinking about the long-term sustainability of companies.

In 2019, we repurposed stewardship to serve the needs of pensioners and savers. For example, if being invested in a company is no longer in the best interests of your members, then you should divest despite the fact that it might mean the company fails.

We extended the definition beyond listed equity. Effective stewardship should be demonstrated irrespective of how your capital is invested. That might be corporate fixed income, sovereign debt, real assets, you name it.

We also saw that investment by UK asset owners in UK plc was declining, so it now covers wherever in the world you are investing.

It also considers decisions before you allocate to an asset, right through to holding and divestment, if that is necessary. Effective stewardship should have positive effects on the economy, the environment and society.

If the UK Stewardship Code has been rewritten for members, what does it mean to asset owners?

Jen Bishop: We see it as a risk management tool. It is a way to ensure that we are looking after all risks over all horizons.

Sometimes that can be conversations around why people are not thinking long term. Our members are focused on financial outcomes. They want to understand how an investment might affect wider stakeholders, but they also want to know how it will affect them, given that they rely on their pension income.

It is increasingly easier to tie environmental, social and governance risks to financial outcomes. Being able to prove that is helpful during conversations around fiduciary duty.

Michael Marks: Stewardship is about protecting our clients' assets. We bring a universal owner perspective to engaging with governments, international organisations or individual companies to raise market standards across the board.

To bring that to life, we engage with governments because they set frameworks. For example, when auto manufacturers were told that beyond a certain date they could no longer sell internal combustion engine cars, they replied that it was impossible to meet that deadline. The moment frameworks were put in place, however, it was amazing how quickly those companies changed their business models to address what was achievable.

Our clients expect us to think about the levers we have, which could be using our

vote or engaging with companies or governments on regulation and policy.

What role does Cambridge Associates play when it comes to stewardship?

Deborah Christie: On the manager research side, our role is to understand what people like Michael are doing in terms of engagement. How is it integrated into the fundamental analysis? Are they writing resolutions? Who are they collaborating with to raise the bar? This helps us to understand where many of the boutique managers we cover could collaborate with like-minded investors to effect change.

Our other role, as stewards of our clients' capital, is to help them understand where engagement fits into their investment policy. We then help select managers who are active in engagement. We work with clients to craft policies or letter writing campaigns or figure out who to collaborate with.

We come at it from both sides. Everything we do is customised to a client's interests and can range from social justice issues to climate to a just transition.

Deborah Gilshan: One of my favourite quotes on stewardship is in *Security Analysis* by Benjamin Graham and David Dodd: "The choice of a common stock is a single act; its ownership is a continuing process. Certainly, there is just as much reason to exercise care and judgement in being as becoming a shareholder."

We have to be careful not to make this something that is relatively new, because it is fundamental to good investing. The idea of a continuous process of ownership is an important way of thinking about this.

How receptive are companies to making big changes?

Gilshan: Stewardship has its limits. Companies do not automatically do what you ask of them and we can't keep engaging on an issue if they don't respond.

Remuneration is a good example. It is fascinating that we have a system where, when shareholders vote down an advisory vote, the answer is more engagement. Why would I engage further on a pay plan I voted against because it is not in the interest of my clients? That is a systemic issue in the stewardship chain that we need to think about.

Marks: Are companies willing to engage? Some are, some aren't.

We approach stewardship by looking at how we can engage with companies to help raise the bar across their sector and the country in which they operate.

We have had some successes, which are not solely down to us because stewardship is rarely an individual activity. In China, the government has set a 2060 net-zero policy. But through conversations in the country, we have companies targeting net zero by 2050.

This is an example of shareholder stewardship leading to an outcome that a company would not necessarily have planned for on their own. But some companies are reticent to engage, so we are not always successful.

Simon Rawson: My challenge is not getting BP and Tesco to the table. It is getting investors prepared to use their tools to deploy that stewardship, such as a voice at the AGM and a public voice, because the majority don't use them.

In our research on the world's 80 largest asset managers, 80% said they have private dialogues and send letters to companies, but the number who spoke at an AGMs falls to 25%. Those who have filed a shareholder proposal drop to 20%.

Shipra Gupta: There is no one-size-fits-all here. There are state-owned companies where there is most often a dismissal of engagement with investors, while there is dual class share ownership, so bringing about change in those companies comes with its own issues.

But equally, we have challenged companies on not having, for example, sustainability KPIs related to executive compensation, and they have shown great intent, asking us to share best practice with them. Another example is of a company where the board member responsible for diversity, equity and inclusion has proactively engaged with us. So there are nuggets of great examples of investor-corporate engagements.

The other challenge for investors is how do we use our limited resources to make the greatest impact. Is it by our largest shareholding? Or should we put our energies behind the companies which are the next size down from the mega caps, where arguably we possibly can expect to have greater influence?

Chapman: Because there are such high expectations of investors to tackle these issues, there is an assumption that you can be everything to everyone. But there is an opportunity to control that narrative.

We spoke to a small investment manager who has limited resources and is going to tackle mental health as "everybody's doing climate". They have identified mental health as a systemic risk and the UK Stewardship Code, by identifying systemic risk as a stewardship priority, has given them the mandate to have that narrative.

Perhaps the best use of your resources is to engage with regulators and policymakers to change the system, rather than having a one-to-one engagement with a company that is not going to respond.

Marks: Our role is not to tell a company what to do. We are not meant to steer the ship. But if the ship is struggling over something, such as remuneration, we want to be the tug that comes alongside and helps it to the shore.

We should engage on all of our selected topics. Asset owners may have different perspectives and prioritise less financially material issues, but as an asset manager, for each theme we focus on, I ask the team to answer: why does this matter to our clients as investors? If we don't answer that question, are we doing our job as investment stewards?

Bishop: There has been a setback on stewardship. It feels like some of the conservative voices in America have been so loud that some managers have significantly decreased what they are willing to do. We would have graded them A, B or C on stewardship a year ago, but now in some cases it is much lower.

The pushback on anything that can affect short-term profit is strong. Some managers are finding it hard to balance long-term goals with implication for short-term profits because the US has spoken loudly to them on this.

Where we were once trying to get managers to improve on stewardship, it is now a question of: are they doing at least the minimum?

Gupta: You have finite resources and want to push regulation and policy where it can help, but equally, in areas like the US, you want to engage with corporates to lead with best practice.

You need to support your managers, because they are under pressure from where they operate, and yet be the constant voice that keeps them honest on managing and mitigating sustainability risks.

Bishop: But because there are so many different areas of focus in ESG, and managers do not hear the same from all investors, this message can be diluted versus the strong anti-ESG message from some parts of the US.

Gupta: Look at reproductive rights. How far have we gone back? There are shareholder resolutions asking how reproductive rights are being protected. This is where corporates can be supportive against the policies of the state.

Stewardship is across the capital structure. It's not equity ownership, it's asset ownership.

Michael Marks
Head of investment stewardship and responsible investment integration
LGIM

But we hear from companies that their investors have told them to avoid long termism or climate change at this point in time. Who are these investors? Where is the transparency? For example, some big oil and gas companies backtracked on their climate transition plan within a year. Feedback from investors is why, but who are the investors who supported that change. The companies won't name them. This is where there is a lack of transparency.

Thankfully, the Financial Conduct Authority and the Financial Reporting Council i are helping with the anti-ESG rhetoric coming from the US. It almost feels like it is on Europe to drive the world forward because Asia has its own challenges and there is the element of a just transition and large state ownerships, and the US has political headwinds as mentioned.

Christie: In Europe, the regulatory environment and the goals of so many asset owners mean that everybody is rowing in the same boat. A lot of change and progress is moving in the same direction.

But you have to look at America from a different perspective. The idea of stewardship and even voting shares is so different today from 10 years ago. Nobody was talking about engagement 10 years ago and there were perhaps a handful of resolutions. In the past four years, however, the number of resolutions has quadrupled.

Shareholders are now more active because they care. They are voting because they want to see change. There is always going to be a two-steps-forward-one-step-back situation, but you cannot put that genie back in the bottle.

The managers I cover are putting lots of resources and people behind stewardship. Some, of course, are using it to say they are doing things that they are not, and there has been a backlash. But clients care about engagement, as so much of this is financially material.

This is a generational change. There is going to be a huge transformation and the investment managers I speak to want in on these opportunities. Portfolios are changing because ownership is changing.

> **Portfolios are changing because ownership is changing.**
>
> Deborah Christie
> Managing director
> Cambridge Associates

Gilshan: There are structural differences in the US that are worth reflecting on. It does not have regulatory-backed corporate governance or stewardship codes.

Investors engaging with independent board members of US companies is a relatively newish concept, but I would be careful not to present Europe as a panacea.

Marks: We are talking about the influence shareholders can have through engagement, but as an asset manager, are we doing what our clients want us to do? Are we voting? The answer is yes.

If we see an appreciation of our influence and if it creates engagement with our clients on a subject that they care about then that can only be a good thing. In fact, we are doing what we should be doing: listening to our clients because we are stewards of their assets.

Rawson: On the point around not having the bandwidth to engage with everything, I am sympathetic to that. But there is a system failure. While it is true that individual investors do not have the resources to engage across the portfolio, there is also no effective collaboration. It is not just fears of anti-trust. You hear it among UK investors who have no concerns around collaborative engagement.

All investors have a responsibility to vote their shares, regardless of whether you have engaged or not. If you have a group of investors who have been thoughtfully and transparently engaging a company on an issue over a period of time you need to back them when they put forward a shareholder resolution or advocate for a vote against directors.

The number one reason investors say they cannot back a shareholder proposal is because they have not engaged with the company. Well, you cannot engage every company, but you can listen to your peers in a non-competitive way and support them. As a whole, we can drive the system transformation that we need to see.

Are unified voices more successful in driving change?

Gupta: We are talking about system change. If a significant body of investors are having the same conversation, their voice is amplified and is taken with a certain seriousness. It is more efficient, more practical and it's pulling in the same direction.

We have seen some success, but there is more work to be done. It is a fairly new concept and so there are lessons to be learned, but it is happening.

That said, we have to be cognizant that there are instances where you might change tack.

We have fired managers who are failing to take material risks or opportunities into account.

Jen Bishop
Deputy CIO and head of responsible investment
Coal Pension Trustees

Sometimes when a group of investors are engaging, a company gets defensive.

It is then best to have those nuanced conversations one-to-one with a senior executive to find out what is happening within the business and how you can help.

Gilshan: There are a lot of great companies out there. Stewardship is about checking in and creating a long-term trustful relationship. But we have to acknowledge that not all companies are managing the transition or are diverse, and investors tend to focus on the ones where the most engagement is needed.

Stewardship, for me, is that long-term trustful relationship between investors and a company such that difficult conversations can be had and hopefully companies will respond.

Chapman: That's a good point. It is also good to change the tone of the conversation, which can sometimes be negative. For example, it feels combative when you are talking about the number of shareholders who voted against Shell's chair at the AGM.

There are positive conversations with companies, but they do not always come out when you are getting reports about how unhappy chairs are that nobody is knocking on their door to discuss the issues.

Marks: We want partnership-type conversations with the companies in which we are invested on behalf of our clients. There are also topics which we want to bring to their radar.

Roll back six or seven years, when we started our climate impact pledge, everyone was talking about the issue, but companies were not doing anything about it.

There is another issue which I do not believe companies across many sectors are paying attention to. It is financially material and is critical to our health: antimicrobial resistance.

We need more companies to think about it. We are talking to the World Health Organisation and the UN as much as we are to pharmaceutical companies, water companies and food companies.

It is shocking that prophylactic antibiotics are used in the food chain, weakening our resistance to diseases. The economic impact could be trillions of dollars if we find ourselves in permanent lockdown to protect us from a wave of diseases that we cannot treat.

Gupta: This goes back to what the role of an investor is. Fundamentally, it is to have that supportive dialogue and engender change.

Don't start with an antagonistic tone. It has to be one of togetherness. It is about collaboration, it is about the long term, but showing where to go next if there is not that clarity of mind.

At a fundamental level, it is about understanding the other side of the table. Everybody is on the hamster wheel of business as usual. They have to deliver what is in front of them and we are asking them to think about these deep issues that are entrenched in society that no organisation has an answer for.

In a practical sense, there is only so much bandwidth even the senior leaders have. It is all about culture. How do the senior executives look away from business as usual and start looking at the next five years, the next 10 years. For example, the whole concept of anti-microbial resistance and biodiversity are not even on their radar. Their current challenge, a big one, is getting to net zero and that needs considerable, and yet non-negotiable, effort.

Gilshan: I have attended many AGMs and spent most of my in-house career working for smaller investors in terms of their assets under management, so it is about efficiency, how best to get a message out.

Making a statement at an AGM on diversity or executive pay is not only a signal to the individual company but also the marketplace, as you cannot cover every company.

Marks: On the point about getting your voice heard, we can do that just as well on the positive side. You can name and shame or name and fame.

Gilshan: We need to re-frame some of this. We talk about levers or tools, but some of them are shareholder rights. You have the right to attend an annual general meeting. Making a statement is not seeking publicity. It is saying: "I have engaged, or engagement is ongoing, but I would like to escalate that through attending an annual meeting." I wish investors would use these rights fully to make change.

Chapman: Voting against directors is a powerful and underused tool, rather than raising a shareholder resolution where the threshold for it to pass is higher. If you don't believe that the transition plan is ambitious enough, then the unitary board structure in the UK means that you can vote against the board.

Gupta: Why do companies feel that shareholder resolutions are against them? You are a shareholder; you have rights and are putting across your point of view. Why is it considered so negative? It should be used as a tool that investors have.

Chapman: We have talked about the futility of engagement, but we should celebrate situations where it has worked. Engagement is about persistence, it's not a one and done issue.

Microfiber plastics in the oceans is a significant problem, with one million metric tons entering the seas every year, affecting the feeding patterns and reproduction of marine organisms as well as human health.

Every time you wash your gym kit, 700,000 of these particles are discharged into wastewater. First Sentier Investors led an engagement with 30 other investors to engage 13 washing machine manufacturers. They also engaged with governments, with France passing legislation from January 2025 where new washing machines have to be fitted with filters that capture these fibers.

The coalition's other successes include convincing Grundy and Electrolux to produce machines that have these filters fitted as standard.

Bishop: This feels less controversial. Nobody disagrees with not putting plastics in the ocean, so it is easier to sign up to versus issues that feel more politically charged.

Marks: It is an interesting point because language matters. We were talking about the US. Right-wing politicians in the US may not find it controversial to talk about nature conservation, but if you say re-wilding...

We need to think about the language and the way we have the conversation. In our everyday conversations, we think about who you are talking to and how they will receive it. As investors, we need to bring that mindset: what outcome are we seeking? What's the approach we want to take? How will we understand the milestones along the way?

Gilshan: Sometimes a lot of the outcomes we look at are often through the lens of the company, such as CEO pay. We should look at these outcomes through the lens of beneficiaries and other stakeholders, such as employees and customers.

> **Effective stewardship should be demonstrated irrespective of how your capital is invested.**
>
> Claudia Chapman
> Head of stewardship, regulatory standards division
> Financial Reporting Council

> **The ability for owners to influence managers depends upon good transparency on their practices.**
>
> Simon Rawson,
> Director of corporate engagement & deputy chief executive
> ShareAction

Coal Pension Trustees outsources its engagement function. What do you look for in people to represent you?

Bishop: We use managers to engage with companies, but it doesn't mean we cannot engage with companies ourselves.

We see it as our role to engage with our asset managers. It is about efficiency. We can compare them and tell them that these are the areas you are doing well in, and these are the areas you are not.

We do not often engage with individual companies, although we have tried to support a few more resolutions, but we are resource constrained.

Chapman: Choosing managers who align with your investment objectives and philosophy and then checking that is being followed, that is your stewardship role.

Bishop: Then we escalate concerns within those relationships. We have withdrawn voting rights from managers and added voting rights to those we previously with-

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> Shipra Gupta
> Investments stewardship lead
> Scottish Widows

drew them from. We have fired managers who are failing to take material risks or opportunities into account.

We have had conversations about what is good stewardship in Asia and now we are having conversations around what is good stewardship in the US. We set a bar; do we now have to lower it?

Gupta: We are having the same conversations. As an asset owner we engage ourselves in a limited way, either directly or through collective measures. A lot of this is about showing best practice, about monitoring our managers, challenging them on how they voted and showing them what others are doing.

Rawson: The ability for owners to influence managers depends upon good transparency on their practices. This comes back to stewardship reporting, where, while weak globally, the UK is leading the way.

Asset owners that have the conviction to then fire their managers are terrific. We have a number of asset owners in our collaborative initiatives and the influence they have in getting managers to back a resolution or sign a statement is tremendous.

Yet we also face cases where asset managers refuse to vote. It is when you hit those barriers and are not able to resolve them that you have to be prepared to move a mandate. That is the stewardship superpower asset owners have.

Gupta: Our role is to influence the market. If we can move a manager's vote, and therefore how all their clients' shares are voted, we have played a bigger role than just moving our votes. That is where the difference is. This market is fast evolving and there will be variations on how to make progress using shareholder rights.

Bishop: We have been having conversations around fixed income and asking: how is buying a new issuance different from voting? It is saying yes or no to a company's strategy every time it comes back to you.

You can do it below the radar in that it does not have the same level of scrutiny as voting. If your manager is finding it hard to vote against a company, perhaps they could refuse to buy the next debt issue unless changes are made. Fixed income feels more opaque than equities if they want to do the right thing.

Marks: Stewardship is across the capital structure. It's not equity ownership, it's asset ownership. When we engage, we engage with corporates on all aspects of their strategy. It is just as relevant, if not more so, when we are supplying primary capital via debt issuance than voting on secondary capital in the equity market.

Bishop: It is a decision you make more often. Equity managers invest for 10 years while they have to decide about debt every six months.

Gupta: In fixed income this is not used enough. Whenever we engage with our managers in this area, we rarely find examples of where the fixed income desk has led such stewardship. It is usually the equity and fixed income desks coming together to do it.

Bishop: We have met fixed income managers who have told us: "Stewardship doesn't apply in fixed income."

Gilshan: But it is also about optimising the points at which you have the most power. One of the most fascinating engagement meetings I ever had was with a US company. All the risks we were worried about came to fruition because of a combined chair and CEO. When they appointed an independent chair, we told him that our economic exposure was beyond our equities and he had a lightbulb moment. It is about not having these systems working in isolation but optimising the positions that we have.

Voting decisions are often binary. It is yes or no, for or against. How we capture the nuance of that decision is why I believe that vote reporting needs to improve and is why I am delighted to be leading the working group the Financial Conduct Authority has convened to look at that. We have all these rights, but it is about optimising them to the best of our ability for savers.

The Stewardship Code is under review, so what will it look like going forward?

Chapman: We are not overhauling it. It is fit for purpose following the 2020 review. What we will look at is clarifying, streamlining and raising expectations in some areas. We want to focus on the role of systemic stewardship. Today we have talked about system change and the role of collaboration and what that means, especially if you are a universal owner.

We are also looking at a common language for stewardship. We see a wide interpretation of engagement in reporting and that makes it difficult to compare and assess the efforts of investors.

Rawson: What about focusing on outcomes?

Chapman: We have a focus on outcomes. We talked about attribution sometimes being difficult to achieve. There is a strong focus on this and perhaps we need to look at the quality of some of those outcomes.

Marks: When we start a stewardship engagement, we should always be thoughtful of the change we are seeking, why we are seeking that change and how we will know we are achieving change.

If you don't get the outcome that you were seeking, it does not necessarily mean that the engagement was not worthwhile.

Deborah, what do you think of the quality of stewardship reporting?

Christie: It is improving, but transparency is key and we are not always getting that.

I talk to boutique managers all the time, who tell me anecdotes in person, but they do not report on anything. Again, the US is further behind Europe. It has some requirements and is moving towards more, but it currently still is a mixed bag.

Gupta: We are not the police, but we are investigating in a measured way. For example, we are asking companies if deforestation has happened and if are they monitoring it.

Thankfully, there is now special data coming, which we have to see how reliable and credible it is, but it is hard when you are sitting through a desktop as companies come prepared with good anecdotal examples for meetings with investors.

It is hard. I don't know exactly what level of reporting will give us that level of disclosure, but advances are being made.

Rawson: What is the quality of the advice consultants provide asset owners? It is my impression that there is a lot more they could do to provide objective information about the quality of stewardship, particularly for some of the environmental and social outcomes.

Christie: I do not know what my peers are doing on a day-to-day basis, but I can tell you that we are actively engaging with all asset managers on behalf of our clients.

We have, particularly in the United States, huge initiatives behind diversity, equity and inclusion because we have clients who care about this topic. They have created escalation policies for their managers and want to know where they stand in terms of diverse ownership.

Clients are asking what their investment managers look like in terms of diversity today. Where do they want to be in five years? How are they going to get there? What's our manager's escalation policy? If the investment firm is made up of five white men who are managing this boutique, is that okay with us? What are they doing to change this and achieve a diversity of thought? What are their policies? Do they have a diversity, equity and inclusion policy? How often is this policy reviewed and updated? Who is involved in that process?

We are having these conversations with investment managers – then the client has to decide for how many years they are willing to have this conversation.

Bishop: Do you rate managers on stewardship and diversity?

Christie: Stewardship and diversity are aspects of how we evaluate managers. Some clients care about this, some don't.

First and foremost, we are looking for a high return for all of our clients, but their needs and unique goals have to be taken into consideration.

They not only want a return, but they might also look for more manager diversity or to be moving towards net zero.

Clients need to understand all of these issues, so we do the due diligence for them. We provide the information so clients can make the best decision for their specific, and unique needs.

Gilshan: One of the most powerful statements I have seen from an asset owner on diversity, equity and inclusion was a letter from the late David Swensen, who at the time was chief investment officer of the Yale Endowment Fund. He wrote to all of the fund's external managers to highlight the collective responsibility on diversity, equity and inclusion, in terms of making financial services and investment more diverse.

It was so insightful and demonstrative of the power of asset owners to use the levers they have to drive change. I applaud him for doing that.

Stewardship is about checking in and creating a long-term trustful relationship.

Deborah Gilshan
Adviser, investment stewardship & ESG
Founder of The 100% Club

Lucrecia Tam is a senior investment director at Cambridge Associates.

STEWARDSHIP: A LONG-TERM STRATEGY

Lucrecia Tam, a senior investment director at Cambridge Associates, discusses the importance of stewardship with *Andrew Holt*.

What for you are the key component parts of effective stewardship?

The way we approach stewardship is to evaluate the culture that is set in the context of long-term ownership – our clients are invested with a long-term view and that is how we build their portfolios.

As part of our thorough due-diligence process, we look for asset managers who have a clear purpose and clear objectives aligned with their stated mandates, especially those that are sustainability labeled.

We also check that adequate resources are being allocated to address the stewardship function.

It is important that asset managers have a policy to put clients first and they must be able to respond to market systemic risks.

And finally, the ability to review policies and processes to ensure managers align with the relevant codes – the UK Stewardship Code is probably the most progressive.

Culture and strategy are therefore important. What initiatives are key to ensuring that the culture and strategy promote effective stewardship? And what actions have Cambridge Associates taken in this regard?

Stewardship sits at the heart of everything we do for our clients.

Clients rely on us to invest their capital responsibly. We engage with asset managers who in turn need to be regularly engaged with companies. This creates a stewardship ecosystem strengthened by capital allocation.

We consider ourselves to be pioneers in sustainable investing. We have taken several steps in our stewardship practices and challenge ourselves to create change with our managers through our stewardship. We have our own reporting on stewardship responsibilities too.

To do all this, we have established a special section of of our research platform to track manager engagement oversight.

The UK Stewardship Code has shifted the dial on stewardship. Is it effective and all embracing?

We are global investors and see different stewardship codes and, although it is not all embracing, the UK Stewardship Code is the most progressive. Particularly in reference to the reporting on certain asset classes: real estate, infrastructure, fixed income, etc. More importantly, it sets the bar high for asset managers to report. As a global investor we tend to apply best practices everywhere. So we have the same high expectations of managers in the US and Asia, as well as the UK and EMEA.

How important is stewardship to Cambridge Associates' clients?

It has become increasingly important. It is something clients are asking for on a higher than ever level. A big factor in this has been the alignment with net zero, a difficult and complex task and our clients have needed more stewardship to get the transparency they need in this regard. We work with our clients to create a net-zero pathway that offers that same alignment. It is fair to say that since net zero has come into play, stewardship has become increasingly important.

How do you include stewardship metrics in your due diligence process when assessing managers?

We look at different aspects. We look at stewardship reports, the activities managers have been involved in, and how they have been voting. More importantly, we are supporting managers in helping companies to move to a better position. We are here to help and steer managers.

Do you see any parts of stewardship that investors are failing to address and why?

One example that hasn't been addressed, which is topical at the moment, is artificial intelligence (AI). We need to understand and address the ethical and ESG implications and challenges from AI. As an issue it is moving very quickly. We have to be careful about how managers are using AI, but it is early days.

How can stewardship be improved going forward?

There are some changes needed. There is a gap in the various stewardship approaches in different countries. Particularly, more clarity is needed in collective activism. Our clients invest globally. They don't just invest in the UK and there is a gap between different geographic areas.

Stewardship should be applied as best practice. Our clients will continue to demand more effective stewardship which will help accelerate change in the future.

Anything else you would like to add on the issue of stewardship?

There is an issue around the size of the asset manager. Niche and boutique managers do not have the capital power and allocation that speaks to emphasise their purpose and their goals. There needs to be more co-operation, so smaller players can have a say.

Michael Marks is head of investment stewardship and responsible investment integration at Legal & General Investment Management (LGIM)

WHY WE BELIEVE SUCCESSFUL ESG ENGAGEMENT MUST BE MULTILATERAL

In today's inter-dependent global economy, we believe effective engagement activity should consider the whole value chain, not only individual companies.

To truly address systemic, long-term ESG risks and capture potential opportunities, we believe investors must consider the complex web of the whole market, not just a single entity within it. This is the foundation of how we approach stewardship and responsible investment at LGIM.

Each individual company we invest in on our clients' behalf is inextricably linked to the societies, markets and economies in which it functions. To drive sustained and tangible change with our ESG-related engagement activity, we believe it is insufficient to influence only the views of individual companies.

Rather, sustainable, long-term change is more likely if the whole system supports and drives towards the desired outcome. Therefore, when we consider how best to use our stewardship voice, we look across the whole value chain of stakeholders to leverage common interests and seek to influence for tangible change.

Seeing the bigger picture

So, what does this value chain look like?

Let's take the topic of climate. Investors will often focus on engaging with the companies that generate the biggest carbon emissions. This makes sense, but we believe this type of bilateral engagement alone overlooks several pertinent factors:

– Industries with lower levels of operational carbon intensity are nonetheless responsible for a large percentage of greenhouse gas emissions. Examples include agriculture, forestry and real estate
– The supply and demand drivers in the value chain for carbon-intensive products
– The policy barriers standing in the way of change

When we structure our engagement activities at LGIM we consider not only our direct exposure to the companies held in portfolios, but also other inter-linked stakeholders in this value chain. This includes other investors, suppliers, customers, regulators, civil society and more.

For example, consider a simplified supply chain for one part of the automobile sector. Coal is shipped and used to power mills that produce steel. This steel is then shipped again to factories where it is used to manufacture cars, which are then sold to consumers.

Setting out this simplified supply chain shows why engaging with automobile manufacturers alone may not be the most effective way of encouraging positive change. In our view, the inter-dependencies of the supply chain means that to bring a permanent and positive change to the real economy, we should target the entire supply chain, whether or not such companies are held in an individual portfolio.

We believe supporting companies in their own discussions with their customers and suppliers is an effective way of bringing a permanent shift in market practices.

AMR engagement in action

We apply this concept of value-chain engagement across other ESG themes. Let's take antimicrobial resistance (AMR) as an example, which we believe may be the next global health event with significant financial implications.

Here, the value chain encompasses drug manufacturers, developers of new anti-microbials, the major users of anti-microbials – such as those involved in animal husbandry – and the 'spreaders' of antimicrobial-resistant bacteria and genes in, for example, the water system. Therefore, our engagement looks to use our investor voice as effectively as possible across pharmaceuticals, animal husbandry, food companies and water utilities.

Where barriers to change are identified, our engagement with policymakers, regulators and other collaborations comes into its own. A good example of collaboration is our work with Citi and other AMR experts to raise the profile of this systemic risk. We have also published our expectations for policymakers with regards to AMR in the water sector, and initial steps we believe should be taken.

A global, multilateral approach

Our aim on the investment stewardship team is to improve global ESG standards across the markets in which our clients are invested. We believe that our multilateral approach, looking across the full value chain, is the most effective way to encourage the positive change we are looking for.

We follow this approach across all our ESG engagement activities, guided by our global themes, helping us to gain an in-depth, global understanding of the issues we want to

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