Index Industry Association

2022 ESG Survey Report

KEY FINDINGS

- **Tried and tested:** Despite the global economic and geopolitical turbulence of the past year, ESG investment is here to stay, according to our survey of 300 investment fund companies in France, Germany, the UK, and US. An overwhelming majority say that ESG has become more important to their investment strategy since our 2021 survey.

- **ESG investment is set to accelerate sharply:** Compared with our 2021 survey, investment-fund companies are raising their projections of the likely future growth in ESG investing, predicting ESG investments to rise to 48% of portfolios 2-3 years from now, and to 57% in five years' time.

- **Fixed-income ESG investing is growing fastest:** The proportion of investors implementing ESG factors in fixed-income (bonds) portfolios has shot up from 42% in our 2021 survey to 76% in our 2022 survey. A large majority (over four fifths) expect the use of ESG criteria in all major asset classes—equities, bonds, and commodities—to increase over the next 12 months.

- **"E" is front-stage, while "S" and "G" are backstage...for now.** Environmental issues remain front and center for investment managers, with climate and carbon footprint issues dominating. This reflects in part the difficulties that investment fund companies face in evaluating the more diffuse and intangible aspects of social and governance performance by companies.

- **ESG tools, metrics and services are performing well, but there is room for improvement.** Asset managers believe that ESG measures are improving and keeping up well with recent world events, but that there is scope for further improvement. In particular, they continue to emphasize a need for greater public corporate disclosure of companies' ESG activities, as well as highlighting continuing challenges such as a lack of standardization of ESG measures across markets and sectors. They also see opportunities to incorporate more high-frequency data and geopolitical / region-specific risk factors into ESG measures.

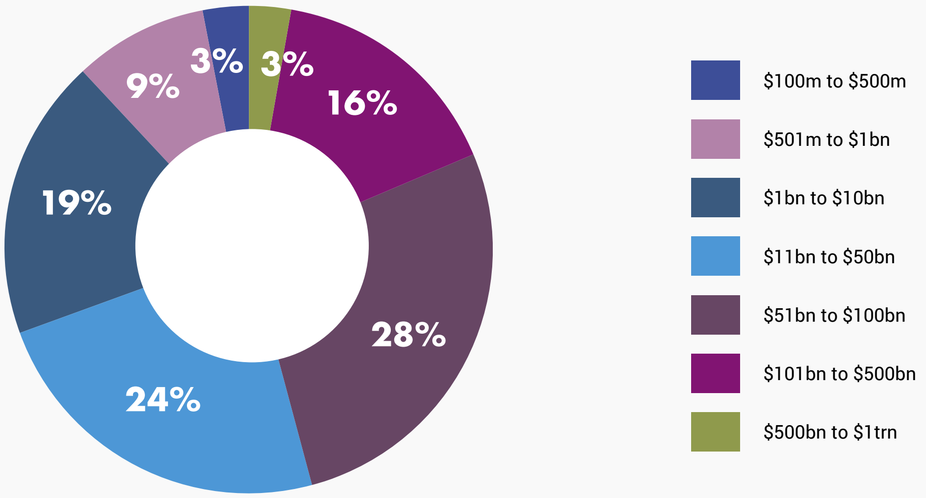
- **Indexes remain highly trusted for both investment and benchmarking purposes:** Our 2022 survey shows that ESG Indexes continue to be used by the vast majority of investment-fund companies, and remain highly trusted to do the job of helping with both ESG investing and ESG benchmarking. Respondents would, however, like to see more specialized indexes focused on specific aspects of ESG, and better risk metrics for individual issuers and markets.

TRIED AND TESTED: ESG INVESTING IS HERE TO STAY

Recent months have been testing times for the role of Environmental, Social and Governance (ESG) factors in business decision-making and investment management. The IIA's 2021 survey of fund-management companies across four major economies revealed the growing centrality of ESG factors to the investment management industry, with 85% of fund managers saying that ESG was a high priority for their business. Since then, the world has witnessed a series of destabilizing geopolitical and market events. The war in Ukraine has tightened energy markets and raised new questions around security of energy supply. Stock markets have been falling, putting pressure on both businesses and investors. On the regulatory front, the 2021 United Nations Climate Change Conference in Glasgow (COP26) resulted in new international pledges to combat climate change, and many international businesses have committed to becoming carbon-neutral by 2030.

Given this volatile backdrop, it seems timely to take another look at the role of ESG investment in the asset management industry and consider how views have evolved since our 2021 survey. To do this, the Index Industry Association (IIA) has once again commissioned leading market research agency Opinium to survey 300 asset-management companies in four major economies—France, Germany, the United Kingdom and the United States. As in 2021, our survey covers some of the largest firms in the asset-management industry. In the case of the US sample, for example, 19% of firms have assets-under-management (AUM) in the range of $1bn - $10bn, 24% in the range $11bn - $50bn, 28% in the range $51bn - $100bn, and 19% have AUM above $100bn (see Figure 1).

Figure 1: Distribution of US companies by size of AUM (US$)

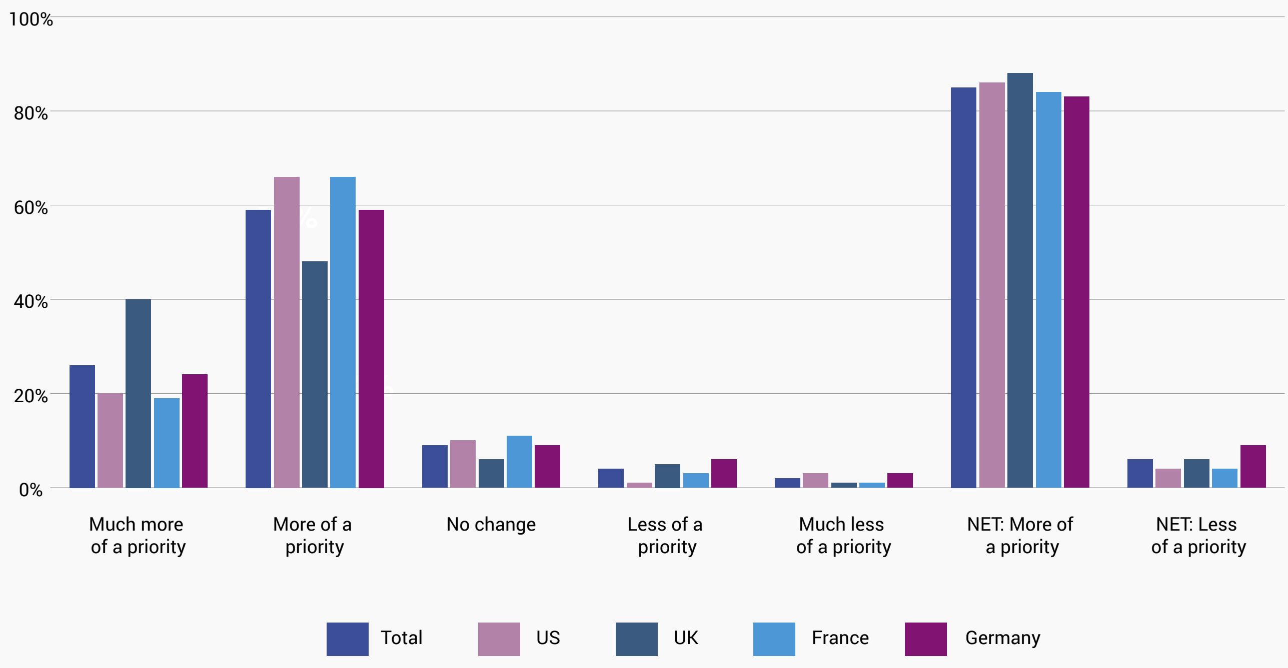


Base: 80 US respondents: NB: Totals sum to slightly more than 100% due to rounding.

Have the geopolitical and economic upheavals of the past year shaken the faith of asset-management companies in ESG investing, or otherwise lessened its importance? Not so, according to our 2022 survey. A resounding message from this year's survey is that ESG factors remain central to the asset management industry and seem set to play an even stronger role in the years ahead. Eighty-five percent of all respondents say that ESG has become more of a priority within their company's overall investment offering or strategy over the past 12 months, with just over a quarter (26%) saying it is "much more of a priority". This view is remarkably uniform across the four geographies of the US, UK, France and Germany.

A resounding message from this year's survey is that ESG factors remain central to the asset management industry

Figure 2: Overall, has ESG become more or less of a priority within your company's overall investment strategy over the past 12 months? By geography.

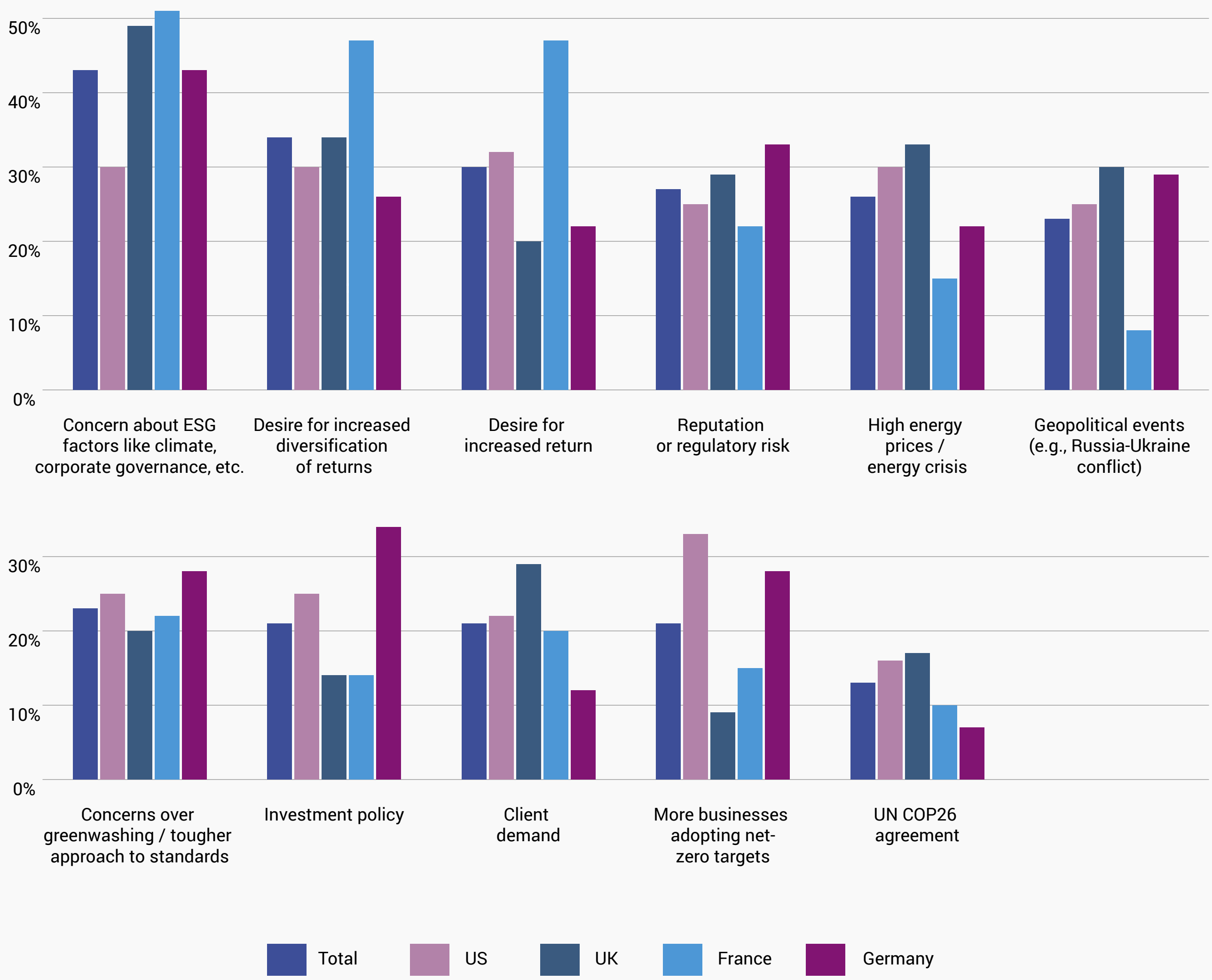


The resilience of ESG investing appears to be driven by the intertwining of ESG objectives with core financial performance considerations for fund managers. ESG investing is able to withstand shocks and setbacks because it is not seen as something transitory or done in response to external pressure, but as a core part of delivering financial returns.

Amongst the large majority of respondents who say ESG is becoming more important, the main driving force is a concern about ESG factors themselves (43%), followed by a need for increased diversification of financial returns (34%) and a desire for increased return (30%) (see Figure 3). Reputation and regulatory risk (27%), alongside high energy prices (26%) and geopolitical events (23%), are also playing a role. By contrast, the fact that more businesses are adopting net-zero targets seems less prominent a factor, perhaps reflecting the asset-management industry's already leading role in pushing for high ESG standards. Perhaps surprisingly, the UN COP26 Agreement featured relatively low in the list of drivers, mentioned by just 13% of respondents, but again this is consistent with the asset management industry's focus on ESG as a driver of value.

Some differences were also evident by respondent demographics. US respondents were more likely to highlight the adoption of net-zero targets by businesses as the primary driver (33%), compared with concern about ESG factors (30%) or desire for increased return (32%). Respondents from the UK and France were most likely to emphasize concern about ESG factors (49% and 51%, respectively).

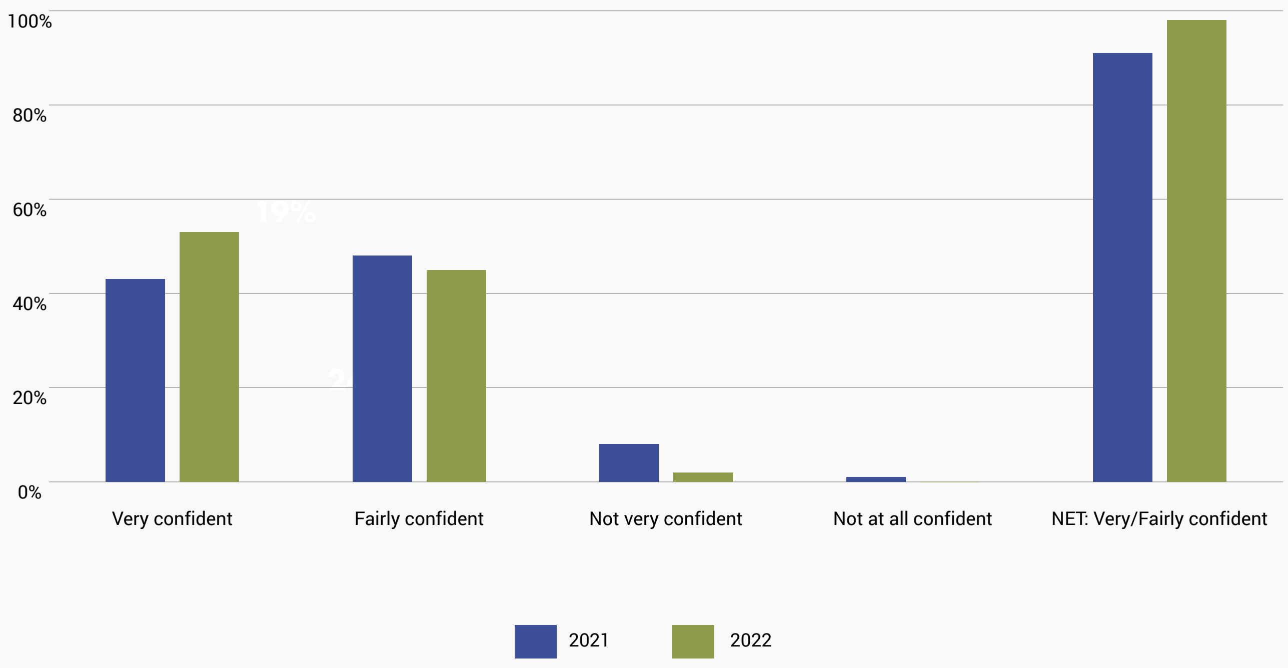
Figure 3: Reasons why ESG has become more of a priority in your company's overall investment offering or strategy over the past 12 months.



Base: 256 respondents who said ESG has become more of a priority in their company's overall investment offering or strategy over the past 12 months.

One further sign of the continued rise and growing resilience of ESG investing is that investment-fund managers are becoming more assured about their clients' personal knowledge and understanding of ESG investing, with 53% saying they are very confident in their clients' ESG knowledge, compared with 43% in 2021 (see Figure 4). Nearly all (98%) respondents from this year's survey are either very or fairly confident in their clients' knowledge of ESG, while only 2% feel "not very" confident.

Figure 4: How confident are you in your clients' knowledge and understanding of ESG investing?



Sample: All respondents (300)

Looking ahead, the growth of ESG investing seems set to increase dramatically over the next decade, with investment-fund companies in our 2022 survey accelerating their forecasts of likely growth (compared with their forecasts in 2021—see Table 1). In our 2021 survey, respondents expected that ESG elements would on average comprise 26.7% of their asset management portfolios in 12 months' time, rising to 35% in 2-3 years, 43.6% in five years, and 52.3% in ten years. From our 2022 survey, the forecast investment curve for ESG has notably steepened, with fund-management companies expecting ESG elements to comprise on average 40% of their funds in 12 months' time, rising to 48.2% in 2-3 years, and 57.4% in five years' time. By the early part of the next decade, investment fund companies we surveyed expect ESG elements to account for a staggering 64.2% of their asset management portfolios on average.

Table 1: Approximately what percentage of your asset management portfolios in your firm do you expect will contain ESG elements in the future?

Base: All respondents (300)

Weighted average	% 2021 Survey	% 2022 Survey
12 Months from now	26.7	40.0
2-3 years from now	35	48.2
5 years from now	43.6	57.4
Ten years from now	52.3	64.2

FIXED-INCOME IS THE FASTEST GROWING AREA OF ESG INVESTING

One of the main takeaways of our 2022 survey is the emergence of fixed-income (bonds) ESG investment as the fastest growing ESG asset class. As Table 2 shows, over three quarters of companies (76%) now implement ESG criteria in fixed income assets (bonds), compared with only 42% of companies that reported doing so in 2021. The growing focus on fixed income was particularly notable for those respondents using indexes for investment purposes (87%) compared with those using indexes for measurement and benchmarking (75%).

In fact, the growing role of bonds in ESG investing is part of a more general broadening of ESG investing beyond its traditional home in equities (which, incidentally, also saw an increase, from 53% of companies in 2021 to almost three quarters in 2022). Commodities are also getting more attention from ESG investors, with 47% of fund-management companies we surveyed now implementing ESG criteria for this asset class, compared with 37% in 2021.

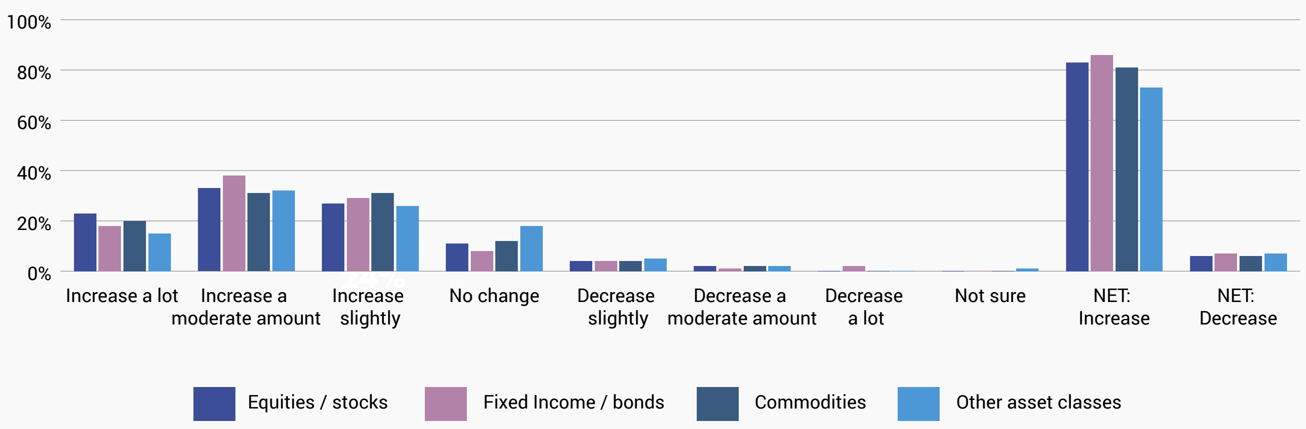
Table 2: In which asset classes does your company currently implement ESG criteria? (Percent of respondents)

Base: All respondents (300)

	2021	2022
Fixed Income / bonds	42%	76 %
Equities / stocks	53%	74 %
Commodities	37%	47 %

Looking ahead, a large majority of asset-management companies we surveyed expect the role of ESG in all asset classes to increase over the next 12 months—83% expect ESG to increase in equities, 86% in bonds, and 81% in commodities. Just under a fifth (18%) expect to see the use of ESG criteria increase a lot in bonds (see Figure 5).

Figure 5: Do you expect to see the use of ESG criteria in the following asset classes increase or decrease in the next 12 months?



Base: All respondents (300)

“E” IS FRONT-STAGE, “S” AND “G” ARE BACKSTAGE

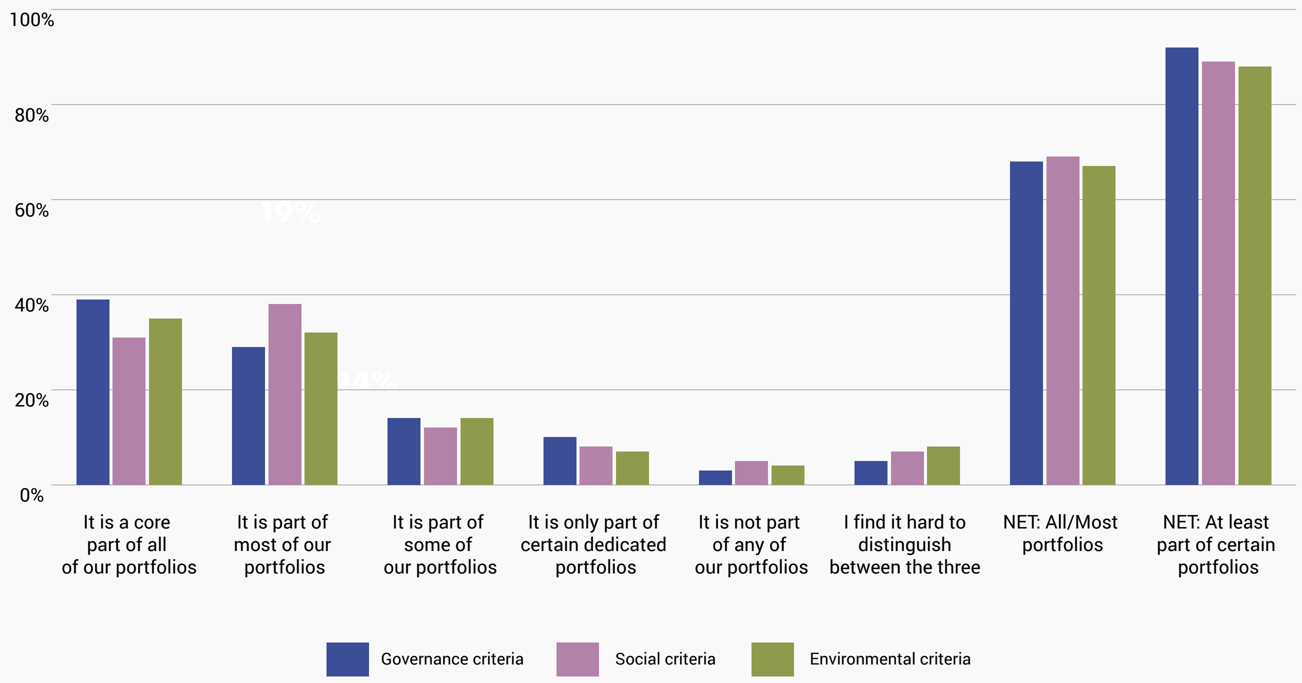
Investors are increasingly recognizing that ESG investing is not a monolithic category but instead represents a broad kaleidoscope of diverse issues and concerns. Some businesses may be leaders in sustainability, but do less well on social or governance criteria, and vice versa. Given the increasing range of issues across the ESG investment landscape, in this year’s survey we decided to look in greater depth at the views of asset-managers toward the different components of ESG in their investment portfolios. At first blush, our 2022 survey suggests that asset managers seem to be giving broadly equal weight to the incorporation of the different ESG elements in their portfolios. As Figure 6 shows, roughly 67% - 69% say that E (e.g., carbon emissions, environmental impacts, etc.), S (e.g., relationships with suppliers, employees, communities, etc), and G (e.g., transparency, probity, fairness, etc.) represent a core part of their portfolios or are part of most of their portfolios. Among these portfolios, a somewhat higher proportion (39%) say that environmental criteria are a core part, compared with social criteria (31%) or governance criteria (36%).

E, S, and G all factor in the views of respondents but their importance can vary depending on a number of factors

Looking at each component in turn, some significant demographic differences emerge. US respondents were more likely (51%) to say that environmental criteria are a core part of portfolios, compared with those in the UK (40%), France (37%) and Germany (26%). In general, larger funds were more likely than smaller funds to emphasize environmental criteria. Funds that use indexes for investment purposes were also much more likely (81%) than those who use indexes for benchmarking (64%) to say that environmental criteria formed a core part of all portfolios or were part of most portfolios.

Turning to the other dimensions of ESG, US (75%) and French (73%) respondents were more likely to agree that social criteria were a core part of all or most portfolios, compared to their counterparts in the UK (64%) and Germany (63%). Again, respondents who uses indexes for investment purposes (82%) were more likely than those who use them for benchmarking (69%) to be more actively incorporating social criteria. Governance criteria were particularly important for companies using indexes for investment, with 47% saying such criteria formed a core part of all of their portfolios, compared with 26% who use indexes for benchmarking purposes.

Figure 6: Which of the following best describes how each of the elements of ESG are incorporated into portfolios



Sample: All respondents (300)

While the above findings suggest that fund management companies seem to be giving broadly equal weight to the different ESG components, a series of attitudinal statements in our survey reveals that environmental concerns, at least at this point, tend to be more front-stage for investors, with social and governance criteria still in something of a backstage role (see Table 3). Four out of five respondents overall agreed that “environmental criteria almost always tend to be prioritized over Social and Governance criteria”. While that may simply reflect the current realities of ESG investment, almost the same proportion (78%) agreed that “environmental criteria should always be given priority over social and governance criteria”. To some extent this seeming backstage role could reflect the more diffuse, intangible and wide-ranging nature of social and governance issues, which makes performance on these factors harder to determine and measure accurately. Notably, two thirds of respondents say that they “find it difficult to evaluate the social and governance performance of companies”. As companies’ approaches to assessing and reporting social and governance factors start to mature and solidify, there may be more opportunity to increase the role of these criteria in ESG portfolios.

Environmental concerns, at least at this point, tend to be more front-stage for investors

Environmental performance itself can also cover a multitude of different issues, including carbon emissions, land use, water and resource depletion, air pollution, micro-plastics, among many others. Thus far, within the "E" dimension, climate change issues seem to hold greater sway for ESG investors. Three quarters of survey respondents agreed that "environmental performance tends to only be focused on climate change and /or carbon footprint", while 74% said that "most of our ESG portfolios are climate only".

Table 3: Thinking in general about ESG in your company, do you agree or disagree with the following statements?

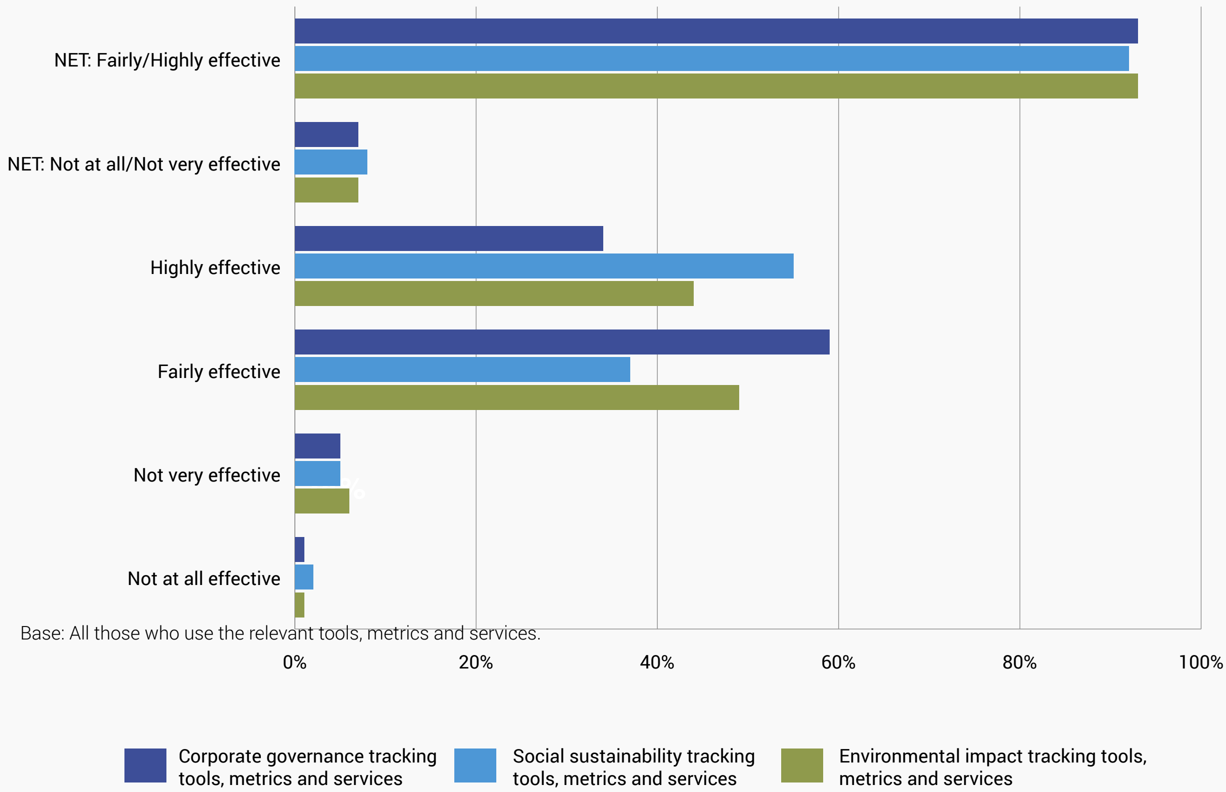
	Environmental criteria almost always tend to be prioritized over Social and Governance criteria for ESG investing	We find it difficult to evaluate the Social and Governance performance of companies	Environmental performance tends to only be focused on climate change and/or carbon footprint	Environmental criteria should always be given priority over Social and Governance criteria	Most of our ESG portfolios are climate-only
Strongly agree	30 %	33 %	33 %	36 %	36 %
Agree	50 %	32 %	41 %	42 %	38 %
Neither agree nor disagree	14 %	17 %	12 %	15 %	14 %
Disagree	4 %	10 %	9 %	4 %	10 %
Strongly disagree	2 %	7 %	3 %	2 %	2 %
NET: Agree	80 %	66 %	75 %	78 %	74 %
NET: Disagree	6 %	18 %	12 %	6 %	12 %

Base: All respondents (300)

TOOLS, METRICS AND SERVICES: GOOD, BUT ROOM FOR IMPROVEMENT

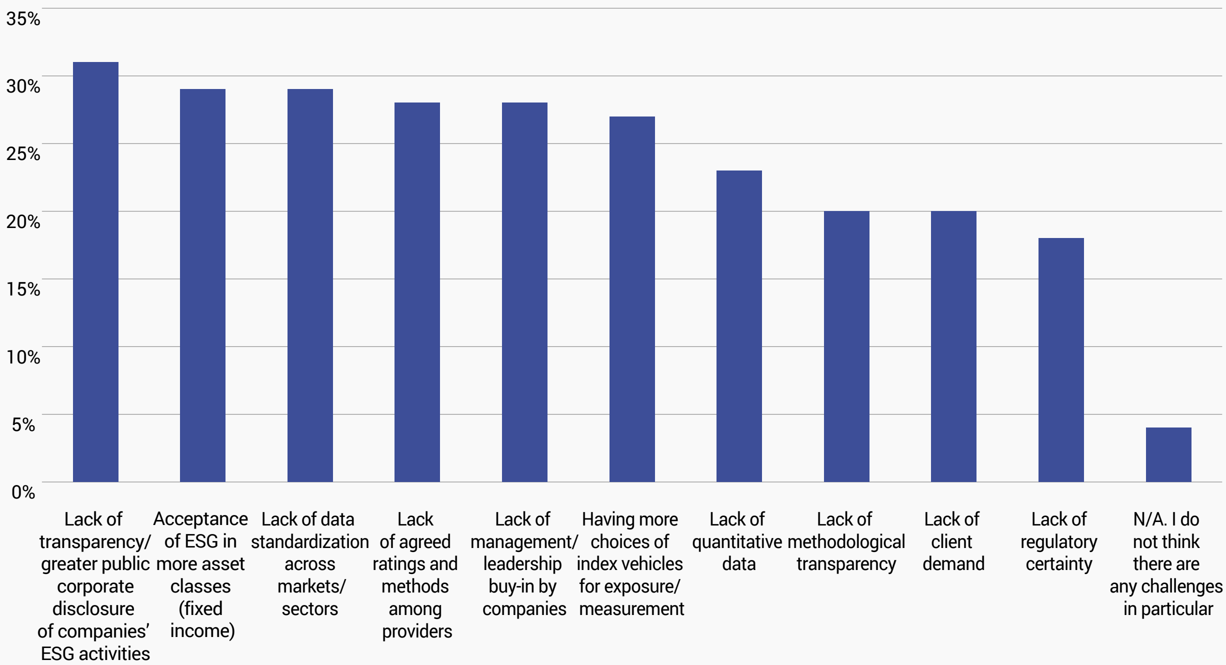
As in last year's survey, we explored the extent to which fund management companies consider that they have effective tools, metrics and services at hand to make effective ESG decisions (see Figure 7). The findings suggest significant improvements in the ESG toolkit compared with last year. More than nine in ten (93%) of respondents agreed that environmental impact tracking tools, metrics and services were either highly effective (34%) or fairly effective (59%), a significant improvement on the 66% net effective response recorded in 2021. Ninety-two percent agreed that social sustainability tracking tools, metrics and services were either highly effective (55%) or fairly effective (37%), again a major improvement on the 66% net effective response in 2021. Similarly, 93% of survey respondents found corporate governance tracking tools, metrics and services either highly effective (44%) or fairly effective (49%), compared with a 69% net-effectiveness recorded in our 2021 survey.

Figure 7: How effective would you rate the tools, metrics, and services available in the following areas?



Base: All those who use the relevant tools, metrics and services.

Figure 8: Which, if any, of the following aspects are the biggest challenges to ESG implementation for fund and asset managers?

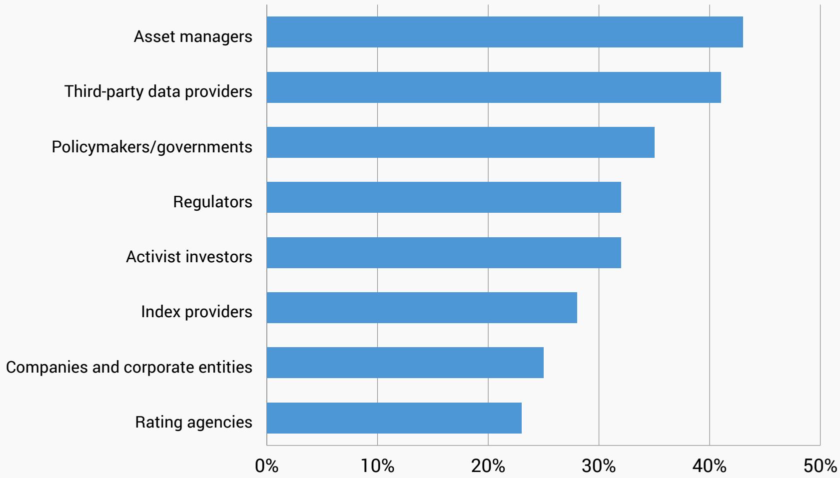


Sample: All respondents (300)

Nevertheless, despite these improvements, the "data vacuum" identified in our 2021 report remains a significant obstacle to improved ESG investing (see Figure 8). Asked about the biggest challenges to ESG investing, fund managers highlighted the need for greater public corporate disclosure of companies' ESG activities, as well as pointing to a lack of data standardization across organisations and sectors. We also asked fund-managers who they believed should be doing more to develop and improve ESG criteria and strategy for the fund management industry. It is clear that they see this primarily as a role for asset managers themselves (43%), followed by third-party data providers (41%) and policymakers and governments (35%) (See Figure 9). Perhaps surprisingly, companies and corporate entities (25%) and rating agencies (23%) come somewhat lower down the list of responsible entities.

Figure 9: Which, if any, of the following do you believe should be doing more to develop and improve ESG criteria and strategy for the fund management industry?

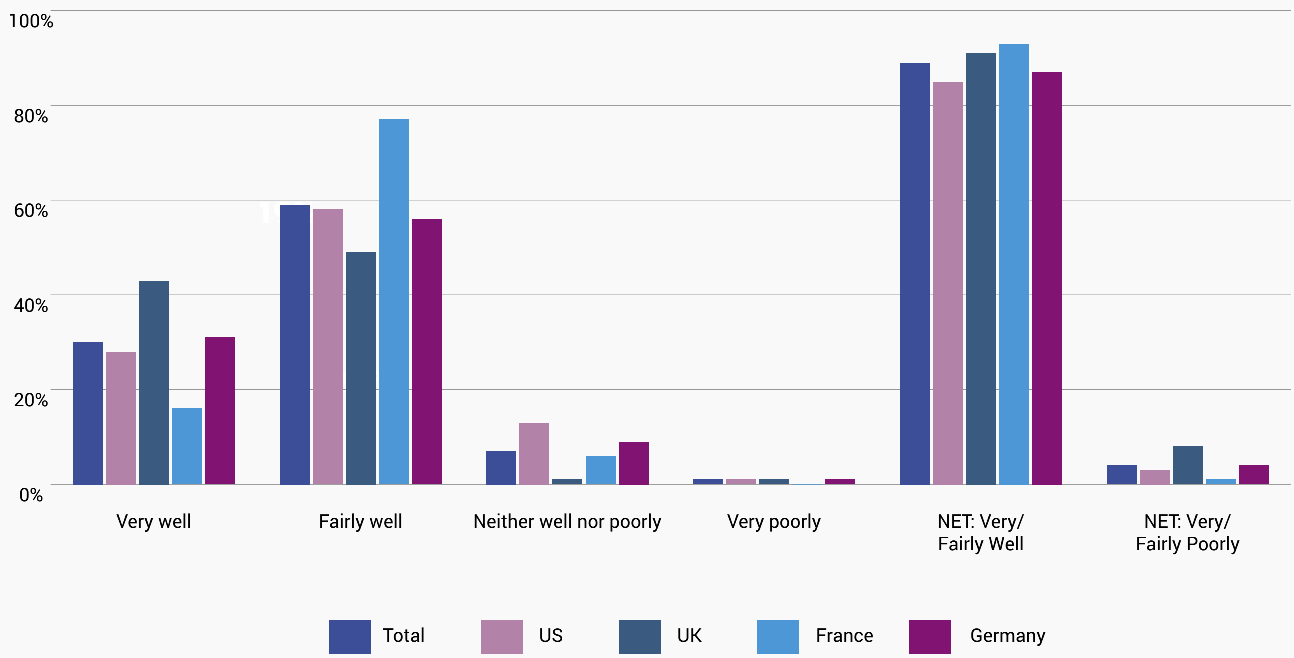
Base: All respondents (300)



Keeping up with world events

Given the geopolitical and economic turbulence of recent times, our survey explored the extent to which ESG measures are keeping pace with world events (see Figure 10). Perhaps surprisingly, a large majority of respondents indicated that ESG measures are keeping up very (30%) or fairly (59%) well with world events over the past 12 months. Some regional differences were evident. UK respondents were significantly more likely to say that ESG measures are keeping up very well (43%), compared with those from the US (28%), France (16%), and Germany (31%).

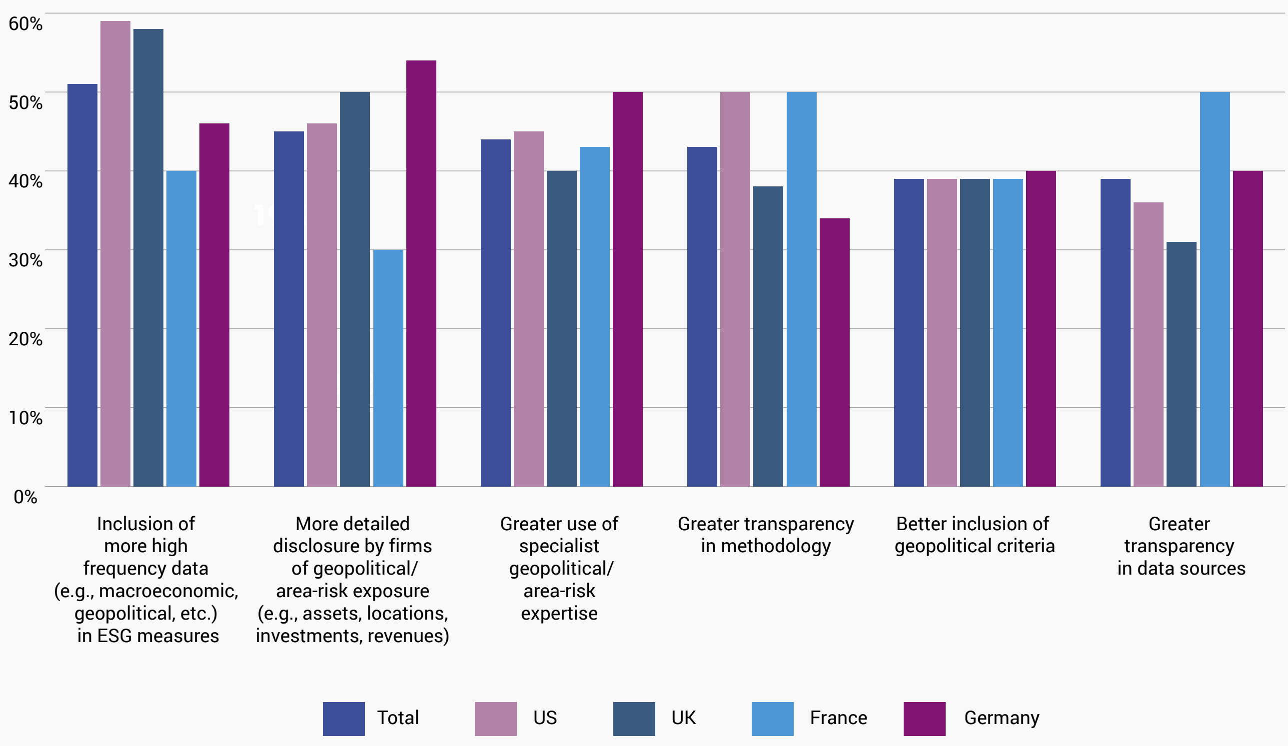
Figure 10: In general, how well or poorly do you think ESG measures are keeping up with world events over the past 12 months?



Base: All respondents (300)

Nevertheless, despite the perceived currency of ESG measures, asset managers do see some room for improvement, particularly around the need for better integration of geopolitical risk factors (see Figure 11). Asked what measures would better help ESG measures keep pace with world events, over half of respondents (51%) cited a need for inclusion of more high-frequency data (e.g., around macroeconomic and geopolitical trends) in ESG measures. US and UK respondents (59% and 58%, respectively) were more likely to point to the need for such high-frequency data compared with their counterparts in France and Germany. Just under half (45%) of all respondents would like to see more detailed disclosure by firms of geopolitical and area-risk exposure in their ESG reports, for example relating to assets, business locations, investments or revenues. Forty-four percent see a need for greater use of specialist geopolitical or region-risk expertise in the development of ESG measures, and 39% would generally like to see better inclusion of geopolitical criteria in such measures.

Figure 11: Which, if any, of the following would most help ESG measures better keep up with world events?



Base: All respondents (300)

Indexes remain critical

Our 2022 survey once again confirms the central role that indexes play in ESG investment and benchmarking. Nearly all (99%) of those surveyed use indexes in some form, with 41% (40% in 2021) using them for measurement / benchmarking purposes, and 31% (39% in 2021) using them for investment strategies. Just over one quarter of respondents (27%; 19% in 2021) use indexes for both measurement and investment strategies.

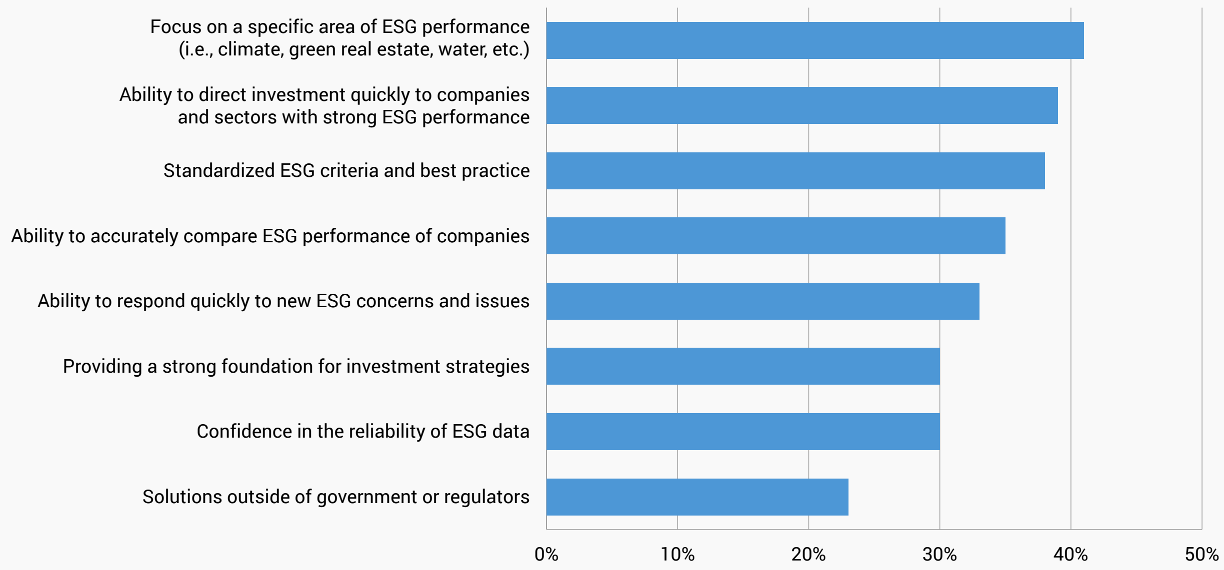
As before, index providers remain highly trusted by asset-management companies (see Table 4). Almost nine in ten respondents trust index providers a lot (45%) or somewhat (44%) to push financial services ESG innovation and standards. In this respect they are on a par with regulators and the asset management industry itself (both 91%).

Table 4: To what extent to you trust the following to push financial services ESG innovation and standards: 2021 and 2022 compared

	Index providers		Regulators		Asset management industry		Other data providers	
	2021	2022	2021	2022	2021	2022	2021	2022
Trust a lot	33 %	45 %	36 %	45 %	41 %	44 %	26 %	35 %
Trust somewhat	51 %	44 %	47 %	46 %	47 %	47 %	44 %	46 %
Trust a little	16 %	10 %	16 %	7 %	11 %	9 %	28 %	18 %
Do not trust at all	0 %	1 %	1 %	2 %	1 %	0 %	2 %	1 %
NET: Trust a lot/ Somewhat	84%	89%	83%	91%	88%	91%	70%	80%
NET: Trust a little/ Not at all	16%	11%	17%	9%	12%	9%	30%	20%

What do asset-management companies specifically value about the services that index providers offer? From our survey, an important role played by indexes is their ability to assist in ESG capital allocation decisions (see Figure 12). Just over two fifths (41%) of respondents highlighted the role of indexes in focusing on a specific area of ESG performance (e.g., climate, green real estate, water, etc.), while 39% noted the ability of indexes to direct investment quickly to companies and sectors with strong ESG performance. Other benefits include the provision of standardized ESG criteria (38%), and the ability to respond quickly to new ESG concerns and issues (33%).

Figure 12: Thinking specifically about ESG Indexes, which, if any, of the following do you value about the services that index providers offer?



Base: All respondents (300)

The survey found that indexes play an important role assisting in ESG capital allocation decisions

Asked what, if anything, they would like to see ESG indexes provide more of, survey respondents highlighted the need for more specialized indexes focusing on specific aspects or components of ESG (41%) and better ESG metrics for individual users and markets (40%). These findings are consistent with respondents' indication that there is a need for ESG to better incorporate risks, as noted earlier, and underscore the increasing diversification of ESG components. Respondents also highlighted the need for more information about the underlying ESG data used in indexes (39%), greater transparency in how indexes are compiled (39%), help improving ESG capabilities (37%), a greater selection of ESG indexes (32%), and more standardization of metrics and methods across providers (29%).

FUTURE DEVELOPMENTS

Finally, we explored the views of fund-management companies around likely future developments in ESG investing, with a snapshot of quotes provided in the Box below. A number of common themes emerged from this snapshot of views. First, fund managers see achievement of ESG goals becoming increasingly interwoven with business performance metrics such as delivering greater return on equity and increasing the stability of financial returns. Second, they see a growing role for new technologies such as big data, carbon accounting analytics, and automation to help deliver net-zero carbon emissions in the future. Third, fund managers noted the increasing variegation of ESG issues, encompassing concerns such as biodiversity and natural capital, supply chains, labor standards, firm competitive behavior and business ethics.

FUTURE DEVELOPMENTS

"ESG is projected to increase at a rapid pace in the foreseeable future since ESG funds have lower volatility while delivering a good return on equity as well as longer lifespan."
CIO, UK.

"It will increase significantly, partly because of regulatory changes, but more to meet the growth needs of our organization."
Portfolio Manager, UK.

"A shift to quantitative and systematic accounting data is required to identify sources of carbon emissions and address the challenge of reducing carbon emissions."
Portfolio Manager, Germany.

"Investors will further use data mining to discover companies that are leading the transition to a zero-carbon economy."
Portfolio Manager, US.

"Add new technologies and diversity of investment projects and instruments and that's how investment will change over the next five years."
Portfolio Manager, US.

"Companies will pay more attention to ESG and increase environmental investment based on big data analysis."
Portfolio Manager, UK.

"Existing ESG scoring mechanisms increasingly focus on a subset of ESG factor selection and weighting to enhance a company's financial resilience."
Portfolio Manager, Germany.

"Natural capital and biodiversity will continue to rise and companies need to be prepared to assess materials."
CFO, UK.

"Regulatory mechanisms should be transferred from the firm to the individual, and investment technologies should better evolve towards all aspects of the industry."
Portfolio Manager, France.

"Fair treatment of the unemployed, reskilling programs, full consideration of the company's impact on the community, decarbonization as quickly as possible throughout the value chain." Portfolio Manager, Germany.

"Business ethics, competitive behavior, supply chain management, etc. are related to the stability and reputation of the company."
Portfolio Manager, Germany.

"Focus on supply chain availability and be keenly aware of vulnerability to resist human rights and labor violations."
CIO, UK.

"ESG assets are becoming more automated through modern technology implementations." CIO, Germany

"Greenhouse gas emissions, water and wastewater management, biodiversity and other pollution prevention and control."
Portfolio Manager, Germany.

CONCLUSION

Our 2022 survey of 300 investment-fund companies across Europe and the US helps track the evolution of key ESG investing trends over the past year, as well as pointing up emerging issues and future patterns of change. The survey confirms that ESG investing has withstood the turbulence and uncertainty of the past 12 months, remains central to investment decision making, and if anything seems set to surge even further in the years ahead. It highlights the continued need to resolve some perennial issues—such as a lack of data standardization across markets and sectors— as well as respond to emergent issues such as the role of world events and geopolitical risk in ESG measures. It also highlights the need for better understanding and measurement tools in relation to the “S” and “G” aspects of ESG.

ABOUT THE IIA

The Index Industry Association (IIA) is the global trade association for the index industry.

A not-for-profit organization serving the global community of independent index providers, IIA membership is open to independent index businesses worldwide. For more information about membership, please contact CEO Rick Redding.

28 Liberty Street, 58th Floor
New York, NY 10005

media@indexindustry.org
r.redding@indexindustry.org

OUR PURPOSE

The purpose of the Index Industry Association (IIA) is to represent the global index industry by working with market participants, regulators, and other representative bodies to promote sound practices in the index industry that strengthen markets and serve the needs of investors.

ABOUT THE AUTHOR

Mark Purdy is managing director of Purdy & Associates, an independent advisory and thought leadership firm focused on issues at the intersection of economics, technology and business. He has over 25 years' experience as an economist in business and government. His recent work has focused on ESG and the economic and business impact of next-wave technologies such as AI. He has published widely in tier-1 media and business publications such as Harvard Business Review and Sloan Management Review. He speaks on economics and technology issues at conferences, client workshops and seminars around the world.

www.purdyassociates.com

METHODOLOGY

The IIA commissioned Opinium, an independent strategic insight agency, to survey 300 Chief Investment Officers, Chief Financial Officers, and portfolio managers across four markets: the United States, United Kingdom, France, and Germany. There were 80 respondents from the US, 80 from the UK, 70 from France, and 70 from Germany. Fieldwork was conducted from May 3rd to May 25th, 2022.

Opinium is an award-winning, independent strategic insight firm built on the belief that in a world of uncertainty and complexity, success depends on the ability to stay on pulse of what people think, feel and do.

www.opinium.com

iia
index INDUSTRY ASSOCIATION