ESG Beyond Equities - Universities Superannuation Scheme Takes Broader View

Editor: Kathryn Saklatvala, Content Director, Institutional Investor

In the debate around long-termism and stewardship, an oversight that governments and thought leaders frequently make is the assumption that this a topic which entirely or primarily concerns listed equities." At Universities Superannuation Scheme, the Responsible Investment team has increasingly sought to take a broader approach that encompasses not just equity but unlisted assets, as Daniel Summerfield, explains.

On November 26 in Paris, Summerfield - Co-Head of Responsible Investment at USS - will be speaking at the **OECD / Euromoney Conferences Roundtable on Long-term Investment.** In a recent interview, he shared his views on pressing ESG-related themes that delegates will address.

Highlights include:

- **ESG can be even more relevant in private markets**: "The benefits of active stewardship can be much more significant in the unlisted space than in listed markets."
- **In listed markets, engagement may not always be the best strategy.** "Policymakers should not take it for granted that simply being an investor in a company's shares means that we should be engaged in that company."
- **European regulation should be more consistent**: "We do struggle with occasional inconsistent messages emanating from different regulatory bodies. ... while the EC speaks in favour of long-termism, other parts of the Commission are introducing rules that may discourage it."

For information about this roundtable, email raffaele.dellacroce@oecd.org and costrowski@euromoneyplc.com.

In interview: Dr Daniel Summerfield, Universities Superannuation Scheme

Asset allocation evolution

As our portfolio has evolved, so has our approach to ESG. When the Responsible Investment Team was founded, it was almost exclusively focused on listed equities and policy-related matters. Yet our remit has changed along with our greater exposure to alternatives. Although one cannot use exactly the same approach across all asset classes, I do believe that the same broad principles can be applied in terms of ownership and oversight responsibilities.

In fact, the benefits of active stewardship can be much more significant in the unlisted space than in listed markets. Thorough due diligence, oversight and engagement have always been essential in sectors such as infrastructure. There tend to be fewer owners and each investor is far more influential. The truth is that you're probably more in control of your own destiny in unlisted assets.

Policymakers, regulators and long-term investing

In the debate around long-termism and stewardship, an oversight that governments and thought leaders frequently make is the assumption that this a topic which entirely or primarily concerns listed equities. The UK stewardship code, for example, is very focused on equities. We've been trying to communicate to regulators and policymakers that we have a significant allocation to other asset classes which also require a stewardship approach.

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The stewardship code is also very focused on investing in the UK. Yet the reality is that we hold an increasing proportion of investments beyond the UK’s borders. Whilst we do still have a UK bias there is far more diversity in the equities portfolio than there was a few years ago. Whatever the stewardship code may expect from us, the truth is that local pension funds are no longer in the driving seat in UK equity markets. As domestic pension funds diversify overseas, international investors are holding a greater proportion of the country's equity markets.

There is also a tendency to assume that shareholders should fix the problems of the companies whose shares they own. Of course if there's a clear case where corporate governance can benefit us financially, through shareholder engagement, it can make sense to devote attention and exert influence to that effect. Yet policymakers should not take it for granted that simply being an investor in a company's shares means that we should be engaged in that company.

In general, policymakers have been reasonably responsive to some of our concerns. In particular the UK government does appear to want UK pension funds holding more of the country's infrastructure, so they're keen to encourage a focus on that area. The European Commission (EC) also speaks very supportively of long-term investment.

Yet we do struggle with occasional inconsistent messages emanating from different regulatory bodies. This is particularly the case when it comes to European regulation. For example, we're currently looking at the IORP directive and the scope for EIOPA to become involved in further development of a Risk Evaluation Process (REP) for pensions. There is a risk that this process could develop into a holistic balance sheet requirement which may make it more difficult to take on certain illiquid investments as there will be a desire to match liabilities measured on a risk free basis.

In other words, while the EC speaks in favour of long-termism, other parts of the Commission are introducing rules that may discourage it. Regulators and policymakers need to make sure that their messages and rules are consistent.

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