ESG Philosophy

Materiality – We believe that material environmental, social and governance (ESG) factors can have an impact on investment returns and client outcomes. The umbrella of ESG is a complex set of factors, from board composition to supply chain resilience, and from political lobbying to environmental management. It covers the full spectrum of leadership, strategy, operations, products and services, and stakeholder management. Establishing the ESG credentials of a company essentially entails making a judgement of the factors an observer considers to be most important, on a relative and absolute basis.

ESG integration – ESG factors without question have a material impact on the success or failure of businesses. Their inclusion enriches and completes the investment process and through this, paired with our voting and engagement activity, we aim to deliver enhanced investment outcomes. Diverse and engaged boards make better strategic decisions. Robust governance systems better protect investor rights and returns. Employee welfare impacts operational efficiency. However, while important, ESG indicators are not the whole story. A company's security price performance is ultimately also driven by other investment considerations, such as balance sheet strength, product quality, competitive differentiators, demand dynamics and macroeconomic drivers. This means that ESG's value is linked to the robustness of the fundamental investment process it is embedded in. Our ESG approach is systematic and tailored for individual strategies. Our process generates investment actionable insights with demonstratable impact on investment outcomes. A culture of deep collaboration between portfolio managers and our ESG specialists ensures ESG is the bedrock of our approach.

Driving the transition – Our transition philosophy is integrated into our investment approach through several layers, and the touch points and applicability of each vary by sub-fund. These layers include firstly the macro transition – all of our investment teams and portfolio managers are cognisant of the global transition and how this impacts markets and the value of investments, and they use this insight to drive better investment outcomes for clients. Secondly, industry and issuer transition – this is where the investment teams utilise insights at both an industry and issuer level around specific transition pathways to inform investment decisions by managing risks and identifying opportunities. Finally, driving the transition through engagement activity – Aviva Investors does this through voting, company engagement and macro stewardship.

Driving positive change – While the purpose of ESG integration is tightly defined – to improve risk-adjusted returns – ESG does help drive positive change in issuers. Investors' ability to deliver value does not stop at asset allocation and security selection. Voting and engagement enables investors to hold management and boards accountable for performance, while directly influencing the sustainability of business models and strategy. It is our preference to engage and drive a transition of the economy to a sustainable footing wherever possible. Boycotting the old economy is not an option. Crucially, we believe that engagement should "have teeth." Our engagement activity has a direct feedback loop into our investment decision-making, with the ultimate sanction of divestment always a possibility. ESG also encourages longer-term investment thinking, a helpful counter to markets' tendency to react disproportionately strongly to shorter term developments.

Changing the rules of the game – ESG integration can help identify mispriced risks and opportunities and direct capital towards companies that have more sustainable business models, however it cannot remediate sustainability-linked market failures. Certain systemic risks are the result of fundamental gaps in the regulatory environment meaning that it is governments and regulators that must act to tackle market failures. This will in turn cascade back into adjustments to business models, valuations, and allocations. Our Sustainable Finance Centre for Excellence also helps drive the transition to a more sustainable future through what we call macro stewardship. This refers to engaging with regulators, governments and other entities to change “the rules of the game” in favour of those businesses that are providing solutions to sustainability problems or supporting the transition to a sustainable future.

Client empowerment – ESG also provides informed choice for clients, enabling the alignment of investments with sustainability preferences. An asset manager’s ESG principles, such as firmwide sector exclusions, net zero ambitions and commitments to human rights, allow clients to determine whether those values align with their own. We believe there are certain sectors that have no place in a sustainable future and screen these companies out through our baseline exclusions policy. We are committed to universal enjoyment of human rights, being a founder of both the Corporate Human Rights Benchmark and the World Benchmarking Alliance. We are determined to play a leading role in decarbonising the global economy, as evidenced by our net zero 2040 ambition. Asset managers are also responsible for designing products and solutions that cater to the full spectrum of client needs. We have created a suite of solutions with a high baseline of ESG integration to address this range of needs.

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