Opportunity Knocks: How advisers can capitalize on growing ESG interest

IN RESEARCH

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Introduction: The Market for ESG Advice is Large … and Up for Grabs

As interest in Environmental, Social and Governance investing grows, so too has the business opportunity for advisers. The window to seize it remains wide open.

Perhaps the biggest finding in our third annual Calvert/*InvestmentNews* Research study on socially conscious investing is that the market for ESG investors is still up for grabs. Advisers who ignore this market segment are overlooking a substantial growth driver.

A few data points speak to the opportunity: Nearly 30% of Gen Xers and millennials expressed a high level of interest in implementing ESG strategies. Interest is also spread across the wealth spectrum, with nearly a quarter of mass affluent investors and 31% of ultra-high-net-worth investors expressing high interest.

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These investors are looking to the adviser community to channel their interest into action: A greater portion of individuals say they want to go about ESG investing through an adviser than through an online platform or do-it-yourself approach.

Advisers could do more strategically to capitalize on the opportunity, however. While advisers anticipate growing ESG demand from their clients, relatively few are using ESG to attract new clients or create a niche for their business. And fewer than half of advisers said they feel knowledgeable about ESG investing.

This report provides insight to help advisers harness the ESG opportunity. It explores investor intentions and motivations around ESG investing, and some of the impediments faced by investors along the way. The research also reveals nuances about ESG investors that some advisers may underestimate.

Finally, this paper provides a competitive analysis of the degree to which advisory firms are pivoting their business toward ESG investors.

To learn about these and other issues, *InvestmentNews* Research surveyed more than 300 financial advisory professionals and 400 investors. The following report details those findings and their implications for advisers.

An Opportunity Set That's Too Big To Ignore

Advisers can no longer afford to view ESG as a fad for younger investors. Value-based investing is now entrenched across demographic segments. A sign of its ubiquity, more Gen X investors now express a high level of interest in implementing ESG strategies than millennials.

ESG values are also prevalent across the wealth spectrum. Wealthier client segments tend to have a stronger desire to implement ESG investing strategies than other client segments. However, among the mass affluent, high-net-worth and very high-net-worth segments, at least half of investors express a moderate or stronger desire for ESG implementation.

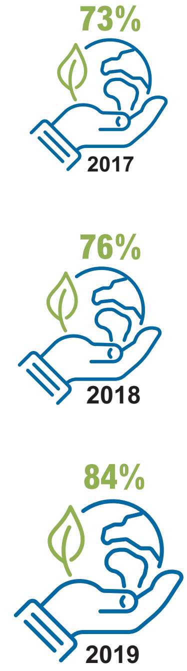
The ESG trend isn't likely to go away either. Only 4% of investors said their interest in ESG investing declined over the past year, while 45% said interest increased.

While interest is picking up, a gender gap still exists. Sixty percent of female investors expressed at least moderate interest in ESG implementation, compared to 48% of men.

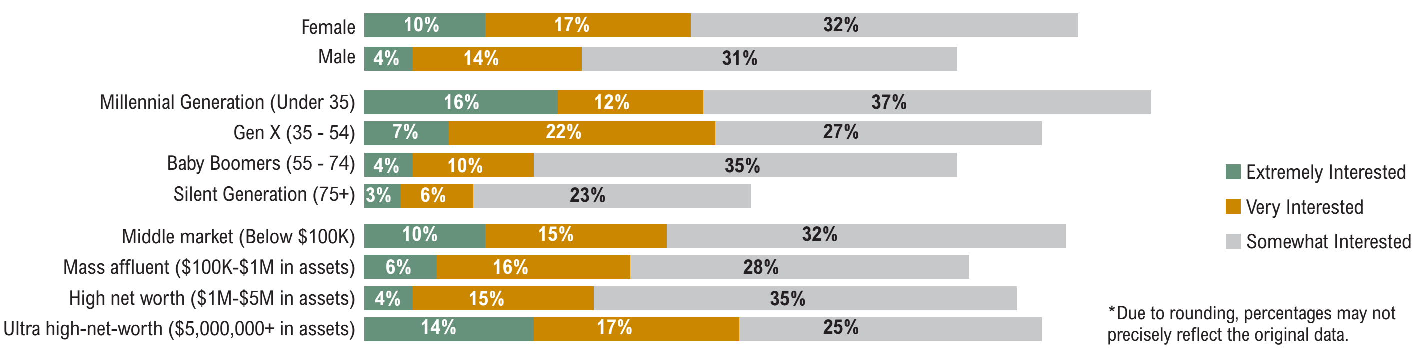
Advisers are experiencing the increased appetite for values-based investing firsthand, with ESG values influencing a growing portion of their current book of business. Eighty-four percent of advisers say ESG issues are important to their typical client, up from 73% in 2017. The percentage of clients carving out ESG allocations within their portfolio is also on the rise. By 2022, advisers expect more than a third of clients to direct some of their investments toward ESG strategies. The average allocation could comprise more than 40% of the client's portfolio by then, advisers project.

Even though advisers are experiencing rising client demand, they may be underestimating the opportunity set. As the chart below shows, older generations have a much higher interest in ESG than most advisers believe. Advisers are also miscalculating the interest among wealth groups, particularly high-net-worth and ultra-high-net worth investors.

FIGURE 2: How important are social and environmental issues to your typical client?

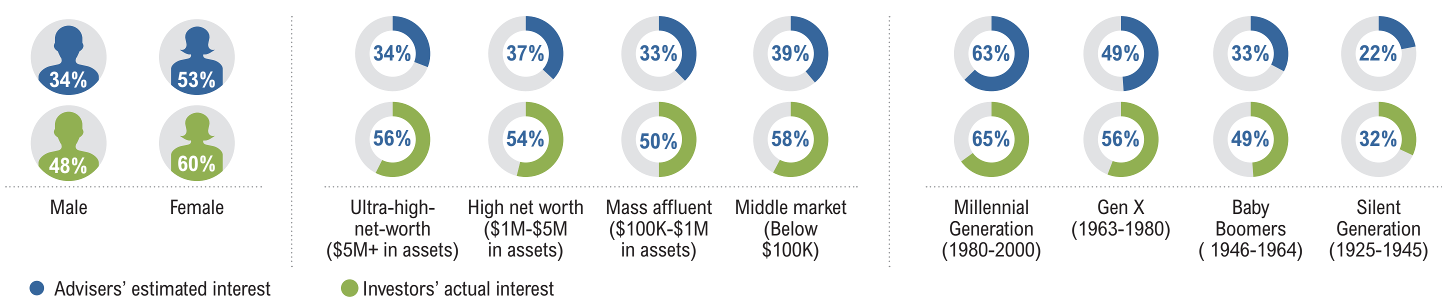


How interested are you in implementing ESG (environmental, social and governance) investing strategies in your own portfolio?*



*Due to rounding, percentages may not precisely reflect the original data.

Advisers' Estimated Investor Interest in ESG vs. Investors' Actual Interest



Challenges to Incorporating ESG Into the Adviser's Business

ESG demand is growing, and most investors see financial advisers as the main avenue of implementation. Yet few advisory firms have been strategic about the opportunity. Only 32% of advisers use ESG to attract new clients and only 25% utilize it to create a niche for their business. Further, only 44% of advisers take ESG factors into account when constructing portfolios, which is in line with last year's survey.

Often, advisers leave ESG discussions up to the investor. Only 21% of advisers said their firm is proactive in initiating ESG conversations, while 26% of advisers said clients initiate the discussion and 35% said it depends on the situation.

Advisers may shy away from leading discussions because many do not see themselves as ESG subject matter experts. Less than half (47%) of advisers say they feel knowledgeable about socially responsible investing.

Support from the top is also lagging at many advisory firms. Only 45% of advisers say their firm is "extremely" or "very" supportive of ESG. The lone exception may be wirehouses, as 68% of wirehouse advisers said their firms offer high levels of support.

Advisers who claimed their firms were highly supportive were asked what sets their firms apart. Longer lists of investment options, company-sponsored ESG marketing materials, personal ESG updates from upper management, model portfolios based on ESG factors and the creation of internal ESG advisory groups are a few of the ways these firms are differentiating themselves.

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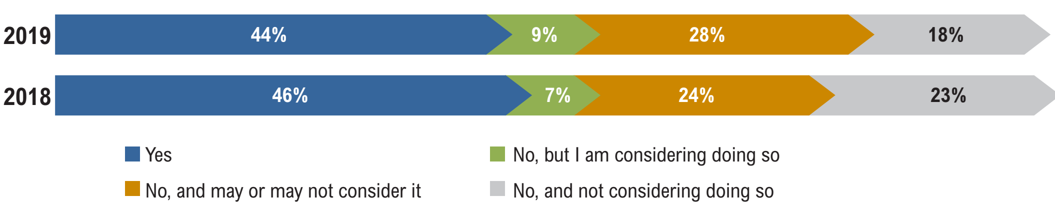
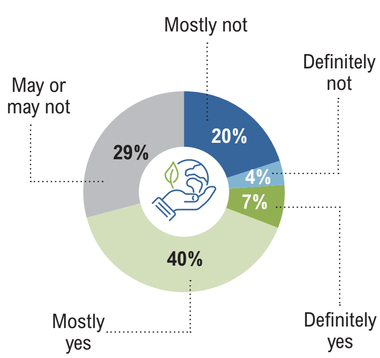
Do you take ESG (environmental, social and corporate governance) factors into account when constructing your clients' portfolios?*

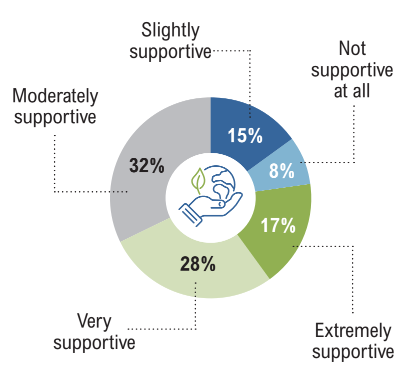


*Percentages may not add up to 100 due to rounding.

Do you feel knowledgeable and fully informed when discussing ESG investments and strategies?



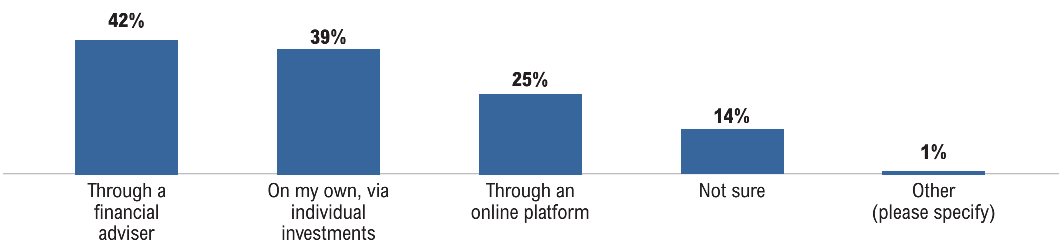
How supportive is your firm of its advisers who are embracing ESG investing?



A Closer Look at Investors' ESG Motives and Impediments, and Where Advisers Fit In

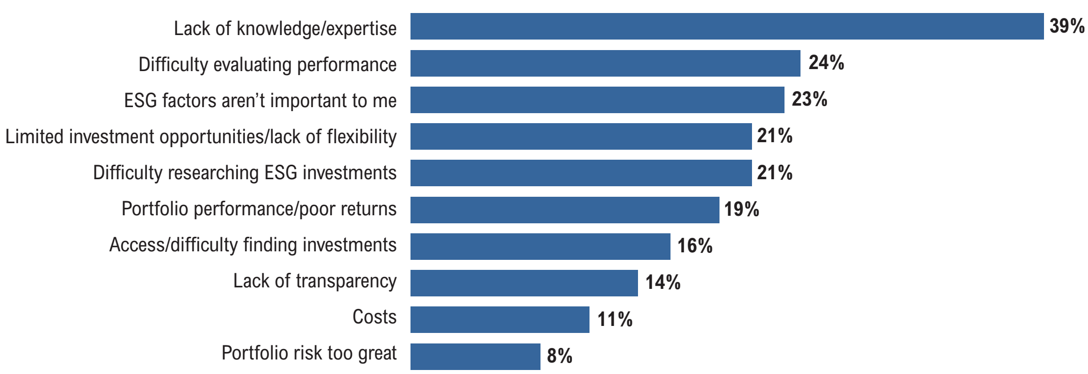
The ESG movement could prove constructive for the advisory industry. While some individuals are using new online platforms to take a do-it-yourself approach to retirement planning, ESG is an area where many prefer an adviser's guidance. Far more investors (42%) say they want to pursue ESG strategies through an adviser than via an online platform (25%).

How might you be interested in going about investing in ESG (environmental, social and governance) strategies?



This is because many of investors' biggest perceived roadblocks toward ESG investing are problems that advisers are well-equipped to solve. Four of the five biggest impediments investors cite toward ESG implementation include lack of knowledge, difficulty evaluating performance, limited investment opportunities and difficulty researching ESG investments. These are areas where an adviser could fill the void.

Why don't you currently utilize ESG (environmental, social and governance) investment strategies, or what might prevent you from doing so?



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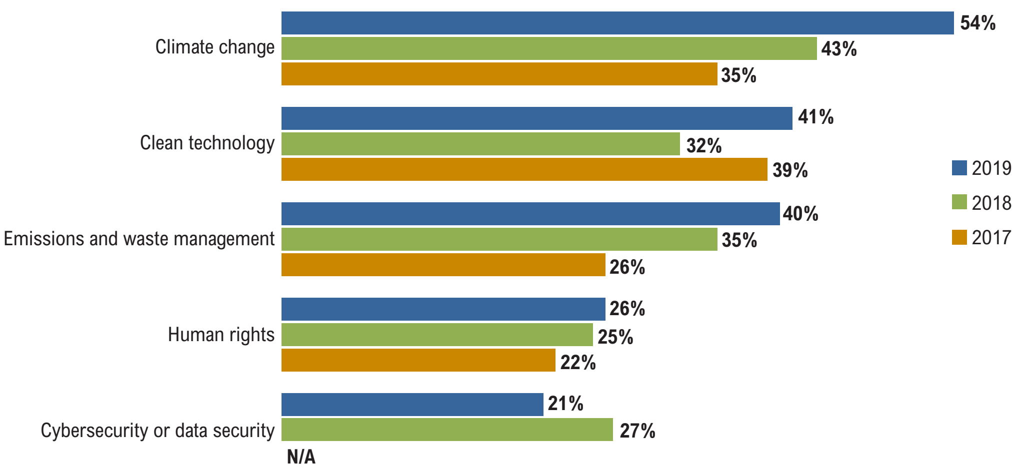
Environmental Issues Garner the Most Attention

When it comes to what motivates ESG investors, environmental issues are the biggest catalyst. Investors rated climate change as their most important ESG criteria, followed by human rights and corporate transparency. Separately, climate change, clean technology and emissions and waste management were the three criteria that advisers say clients bring up most. The jump in the percentage of clients bringing up those issues was significant this year, as the chart below shows.

What are the most common ESG criteria brought up by your clients?



The political climate likely played a role in moving environmental criteria to the forefront of investors' minds. Many respondents in this year's anecdotal survey noted that the current administration's environmental policies are a reason their interest in ESG investing increased.

Another important nuance about investors' ESG views is how they determine investment success. For most, success is not defined purely by returns. Fifty-seven percent of ESG investors say that impact is of equal or greater importance than performance when evaluating ESG investments.

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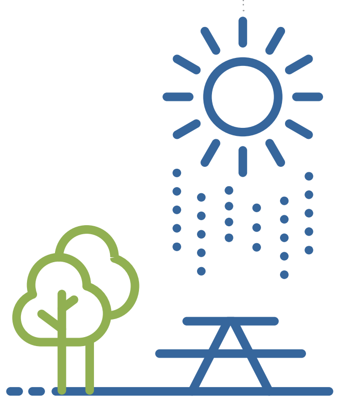

Next Steps: How Advisers Can Differentiate Their Practice with ESG

Momentum around values-based investing continues to build. A substantial portion of investors across age and wealth groups are now demonstrating a high level of interest in ESG investing. These same investors want advisers to help them achieve their socially responsible investment aspirations. Who will show them the way?

While advisers readily acknowledge growing client interest, few are pivoting their business toward ESG as a strategic growth opportunity. Those advisers who are willing to become informed, embrace values-based investing principles and engage clients on ESG, can establish themselves as leaders in a growing area of client interest.

The following insights can help advisers improve their ESG practices:

- **To attract clients interested in ESG, advisers must become educators.** Investors' ESG interest is growing, but that doesn't make them experts. A lack of knowledge remains the largest impediment to ESG implementation. Advisers who ramp up their knowledge base will be the ones who can answer questions, lead discussions and win over the growing portion of clients who want to incorporate socially responsible investment principles in their portfolios.

- **Don't discount the value of impact.** Clients aren't determining ESG investment success solely by returns. For many clients, impact is just as important. Leading advisers will need to demonstrate how an ESG portfolio is affecting positive change.

- **Advisers may be overlooking ESG interest among some demographic groups.** ESG is not just a millennial issue. A substantial portion of Gen Xers and baby boomers are also interested. Advisers should not dismiss the opportunity among these generations. Similarly, advisers should be attuned to heightened interest among wealthier clients and females.

- **Advisory businesses could take a leadership position in ESG by showing more support at the firm level.** Less than a quarter of advisers believe their firms are strongly supportive of ESG. Advisers who work in highly supportive environments named several factors that set their firms apart: longer lists of options on investment platforms, company-sponsored ESG marketing materials, ESG updates from upper management, model portfolios based on ESG factors, and the creation of internal ESG advisory groups.

- **Start the conversation.** This year's Calvert/*InvestmentNews* Research study shows that while most investors are interested in ESG issues, advisers start the ESG conversation with clients less than a quarter of the time. Advisers can establish themselves as socially-responsible thought leaders by initiating dialogue.

About Calvert

Calvert Research and Management is a recognized leader in Responsible Investing. Our mission is to deliver superior long-term performance to our clients and to enable them to achieve positive impact.

Calvert Research and Management traces its roots to Calvert Investments, which was founded in 1976 and was the first to launch a socially responsible mutual fund that avoided investment in companies that did business in apartheid-era South Africa. Today, the Calvert Funds are one of the largest and most diversified families of responsibly invested mutual funds, encompassing actively and passively managed strategies, U.S. and international equity strategies, fixed-income strategies, and asset allocation funds.

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