AIUSA Responsible Investment Beliefs

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1 Screening

Divestment can provide a simple but potentially costly way to avoid exposure to misaligned investments, though it removes the ability to advocate for change through stewardship.

- While investors tend to make divestment decisions for values-based reasons, from an investment perspective, we believe that divestment reduces the opportunity set and, on an ex-ante basis, it is likely to reduce expected portfolio return and increase risk.
- The magnitude or direction of the impact on returns will vary, depending on (i) divestment scope (i.e., excluding entire industries, countries or supply chains) and (ii) timing of divestment.
- If the goal is to change sentiment about the divested asset, and/or impact the cost of, or access to, capital for the divested asset, divestment is unlikely to accomplish those objectives. Divestment may simply transfer ownership to more misaligned investors, giving them more control than before.

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2 Integration

To improve expected long-term risk-adjusted returns, active investment managers should consider financially material ESG factors to inform their decisions.

- The performance of fundamental, active investment strategies will be influenced by an investor's skill in identifying and valuing under- or over-appreciated ESG risks and opportunities in asset selection, timing, and weighting decisions.
- Naively using widely available ESG data, such as third-party ESG ratings, is not expected to provide a competitive edge for performance.
- To help inform our investment manager research, we rate strategies on the quality of their integration of ESG risks and opportunities but recognize it may be challenging, if not impossible, to attribute how much performance comes from ESG integration skill.
- Rules-based indices that are constructed to over-weight highly rated ESG securities are not necessarily expected to offer an ex-ante performance advantage over standard indices, gross of fees.

3 Impact

Some investors may opt to seek both investment returns and positive environmental or social outcomes from their portfolio decisions.

- Depending on the investor's goal, impact and thematic allocations may be carved out or integrated into existing asset class buckets. For example, a mostly returns-first investor may allocate from existing asset class buckets and measure performance against traditional benchmarks but a strongly impact-first investor may carveout (because of the concessionary returns or higher risks).
- Impact investors should also consider:
  - **Investor contribution:** the wider change caused by their investment, not just the immediate impact of the enterprise and/or asset invested in.
  - **Trade-offs:** between contribution to impact versus other investment characteristics (e.g., liquidity, complexity, returns, asset class characteristics and investment structures).
  - **Flexibility:** designing impact mandates flexibly across theme, geography, and sector can improve sourcing and scalability and reduce the potential trade-offs.
  - **Measurement:** while it is challenging to accurately measure impact, deep diligence and monitoring efforts should be made to ensure impact outcomes are delivered.
- Investments with positive impacts, such as carbon reduction, energy efficiency, sustainable agriculture, and water, do not necessarily offer concessionary returns, and can be included in conventional portfolios based solely on their expected risk and return characteristics.

4 Stewardship

Exercising ownership rights can deliver tangible impact and help to protect and enhance long-term asset value.

- To effect long-term change on behalf of investee assets, a combination of dedicated resources, clear understanding of the issues, good communication and escalation processes are required. Ideally assets are controlled or ownership is concentrated.
- When deciding whether to, and when exercising ownership rights, including the voting of proxies, conventional investors must carry out their duties prudently and solely in the economic interests of the participants and beneficiaries.
- Stewards seeking impact can take a broader view of long-term value, including the externalities of investee assets.
- If delegating the exercising of ownership rights to asset managers and vendors of stewardship services, investors should evaluate if they are aligned with the delegate's stewardship policy and priorities and hold them to account for implementation.

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