Has the Sustainable & Impact Investing Industry Reached an Inflection Point?

A Q&A with:

Peter J. Zuleba, III, CFA
Director of Investments,
The Glenmede Trust Company,
N.A., and Glenmede Investment
Management, LP

Amy T. Wilson, CFA
Director of ESG Investing
Glenmede Investment
Management, LP

Mark Hays
Director of Sustainable
& Impact Investing,
The Glenmede Trust
Company, N.A.

GLENMEDE
INVESTMENT MANAGEMENT

Sustainable and impact (S&I) investing describes a spectrum of approaches that draw on environmental, social and governance (ESG) criteria to help inform investment decisions and/or achieve environmental or social impact. Over the past several years, interest in — and application of — these approaches has grown significantly due to a convergence of factors, including increased cross-generational interest,[1] improved data availability[2] and more research showing that investors might help achieve strong risk-adjusted returns by incorporating ESG factors into investment analysis.[3]

However, the growth of assets in strategies prioritizing ESG in the investment process[4] slowed considerably in 2022 (Exhibit 1), including the second quarter's net outflow of $1.8 billion, the first quarterly outflow for sustainable strategies since 2017. In parallel, S&I investing as a discipline has faced increasing questions and scrutiny from major media outlets around its performance merits, its ability to produce measurable societal impact, greenwashing and even its political motivations.

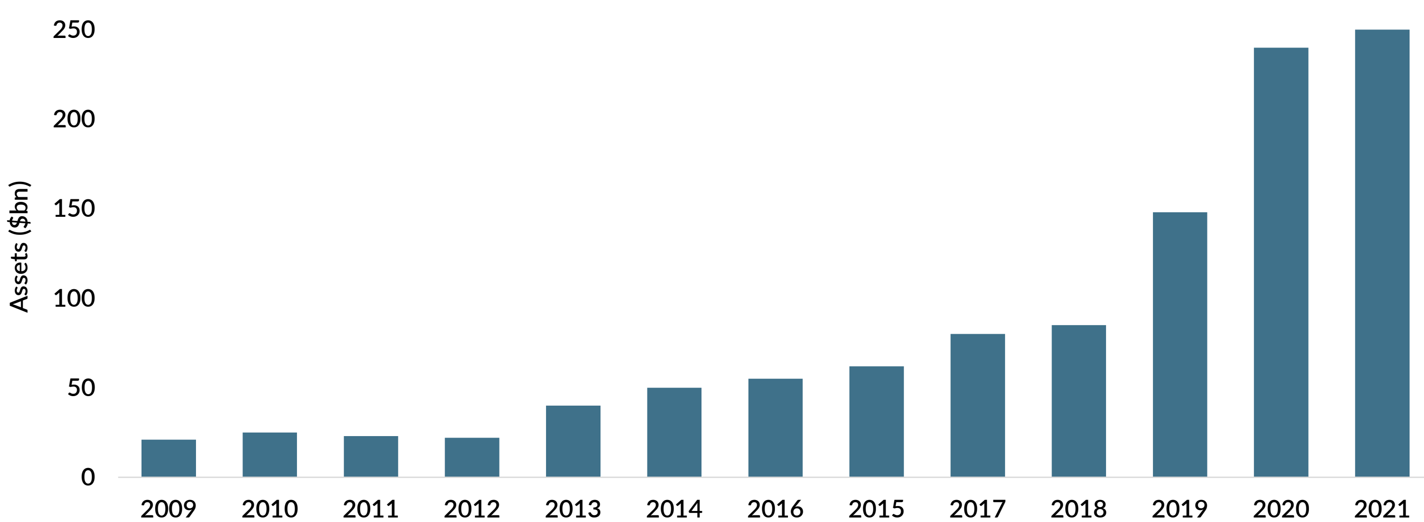
To help understand how S&I investors view this period of turbulence in the market, Glenmede's Director of Investments Peter Zuleba sat down with Mark Hays, Director of Sustainable & Impact Investing at The Glenmede Trust Company, N.A., and Amy Wilson, Director of ESG Investing at Glenmede Investment Management, LP, for a wide-ranging Q&A session.[5]

PETER: There is much noise in the marketplace related to ESG right now. Can you summarize any common threads you see amidst all the activity?

MARK: The most consistent thread I am seeing across articles is the suggestion that so-called "ESG strategies" do not produce environmental or societal impact. Put another way, these strategies are accused of "greenwashing." I am also seeing an increased amount of content that suggests this type of investing is not motivated by financial returns but rather by political leanings.

AMY: Another common thread has been around the general underperformance of what are being

Exhibit 1: Assets under management in U.S. sustainable public funds and exchange-traded funds



Source: Morningstar

As of 8/30/2022

labeled as “ESG strategies” in 2022, raising questions around the long-term merits of such investments.

PETER: Let us unpack each of those factors. Are “ESG strategies” greenwashing if they do not produce “impact?”

MARK: In Glenmede Trust’s view, “ESG” is not the same as “impact.” ESG is a data set that helps inform investment decisions and, in some cases, can help create impact as a byproduct. We created our Sustainable & Impact Investing Taxonomy (Exhibit 2) to delineate four distinct approaches, which include applying ESG in investment portfolios, with very different outcomes. We find this taxonomy can help cut through what is still a definitionally blurry industry.

AMY: Glenmede Investment Management uses this taxonomy as well in how we organize our strategies and our thinking across integrated, mandated and thematic approaches — in all of which we still seek to produce competitive risk-adjusted returns. It is extremely important for us to be able to tailor our strategies to clients interested in their own motivations in using ESG in portfolios. For us, this is not a one-size-fits-all approach.

PETER: How do you think through the underperformance that some “ESG strategies” have experienced year-to-date?

AMY: In our experience, strategies that employ a broad ESG integrated approach often do not have specific sector underweights and therefore have not underperformed year-to-date. Similarly, strategies that use mandated or thematic approaches may not uniformly divest from full sectors, but instead focus on best-in-class names or use active ownership strategies that seek to drive change. Those strategies without a divestment approach have tended to be better protected from underperformance year-to-date.

MARK: For Glenmede Trust’s clients, we believe in approaches that go beyond divestment. Instead, we use strategies containing a blend of negative

Exhibit 2: Glenmede’s Sustainable & Impact Investing Taxonomy

Integrated

Explicit **consideration of material ESG factors** in the traditional investment decision-making process

Mandated

Use ESG screens to **avoid companies** with poor ESG criteria **and/or tilt toward companies** with strong ESG characteristics

Thematic

Dual goal to achieve at least **market-rate returns** and measurable environmental or social outcomes

Concessionary High Impact

Invest in **local opportunities** to **achieve impact**, while willing to sacrifice returns to do so

Source: Glenmede

and positive screens, alongside those employing active ownership via shareholder engagement to drive systematic change. For us, these approaches can aid in designing portfolios that provide similar sector exposure as traditional portfolios alongside seeking to impact the society or the environment.

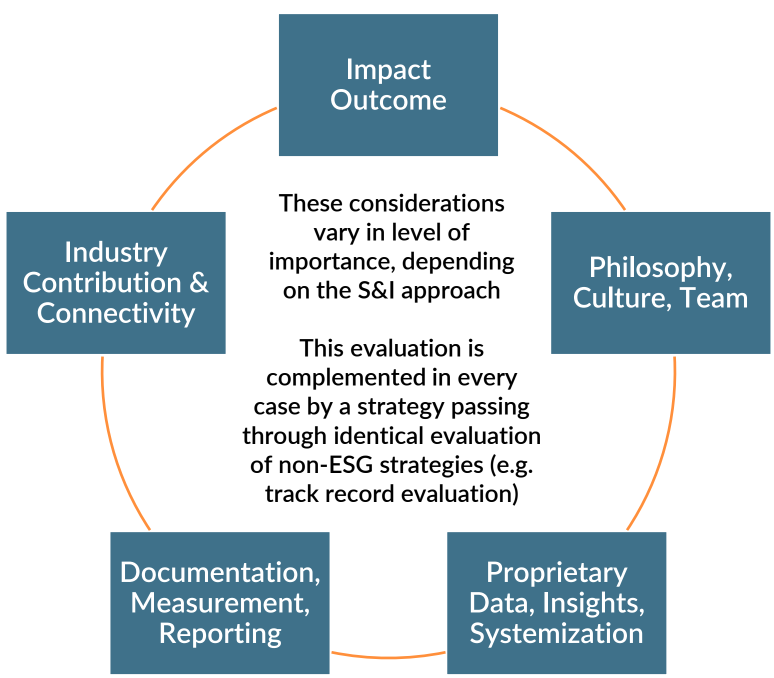
PETER: Amy, from an investment management perspective, how do you sift through which ESG factors are most meaningful?

AMY: Within Glenmede Investment Management, we evaluate the ESG merits of companies in our fundamental integrated strategies by mapping key aspects of their business to our proprietary "financial materiality matrix." This enables us to hone in on sector-specific ESG criteria that may affect the financials of a company via revenues, margins or valuation, for example, focusing on privacy and data security risks which could lead to reputational risks for a communication services company, or human capital development in a healthcare firm where innovation is required to drive future growth. I will note that we consult a third-party ESG vendor for its raw data as one input to help inform our view, but we regard these ESG scores as an input amidst a wider mosaic of investment information.

PETER: Mark, through the Glenmede Trust lens, how do you sort through what is real and what may be greenwashing?

MARK: Within Glenmede Trust Company, we apply a proprietary five-pronged evaluation matrix to assess what we identify as the key differentiators in the manager's use of ESG information in the investment process (see Exhibit 3). To assess this, we issue a detailed request for information to managers on our platform, which helps us determine how consistently they apply ESG factors in their investment process, and how they document that application within investment memos or other systems. We use a third-party ESG vendor, but only as a monitoring tool to check a strategy's outcomes against its stated intentionality.

Exhibit 3: Evaluating S&I managers for greenwashing



PETER: What is your response to articles that suggest this type of investing is not motivated by financial returns, but rather by political leanings?

AMY: For Glenmede Investment Management, our motivation for ESG integrated investing is simple — we prioritize ESG-related factors in our analysis because of a data-driven view that these criteria can be financially relevant. Our job as asset managers is to seek to maximize risk-adjusted returns, and we believe the incorporation of ESG factors may help us do so.

MARK: Our role is to help build diversified portfolios that seek strong risk-adjusted returns alongside a diverse set of personal values and missions that go beyond any specific political viewpoints.

PETER: Let's wrap up — what do you think is next for the industry?

MARK: We believe the scrutiny of the industry could lead to more standardization and clarity in defining what ESG is and isn't. That is a positive development. This can enable us to reaffirm the value that we bring to clients who want to align their portfolios with mission — through our taxonomy, our evaluation process and our diversified approach to building portfolios that closely mirror the experience of traditional portfolios.

AMY: We are at an inflection point in the industry — increased scrutiny means increased interest and attention, for better or for worse, which could result in some really fascinating data sets and product capability developments in the industry. Ultimately the hope is that this period of scrutiny results in a more enduring, standardized industry fit for a larger proportion of institutional allocators' needs.

---

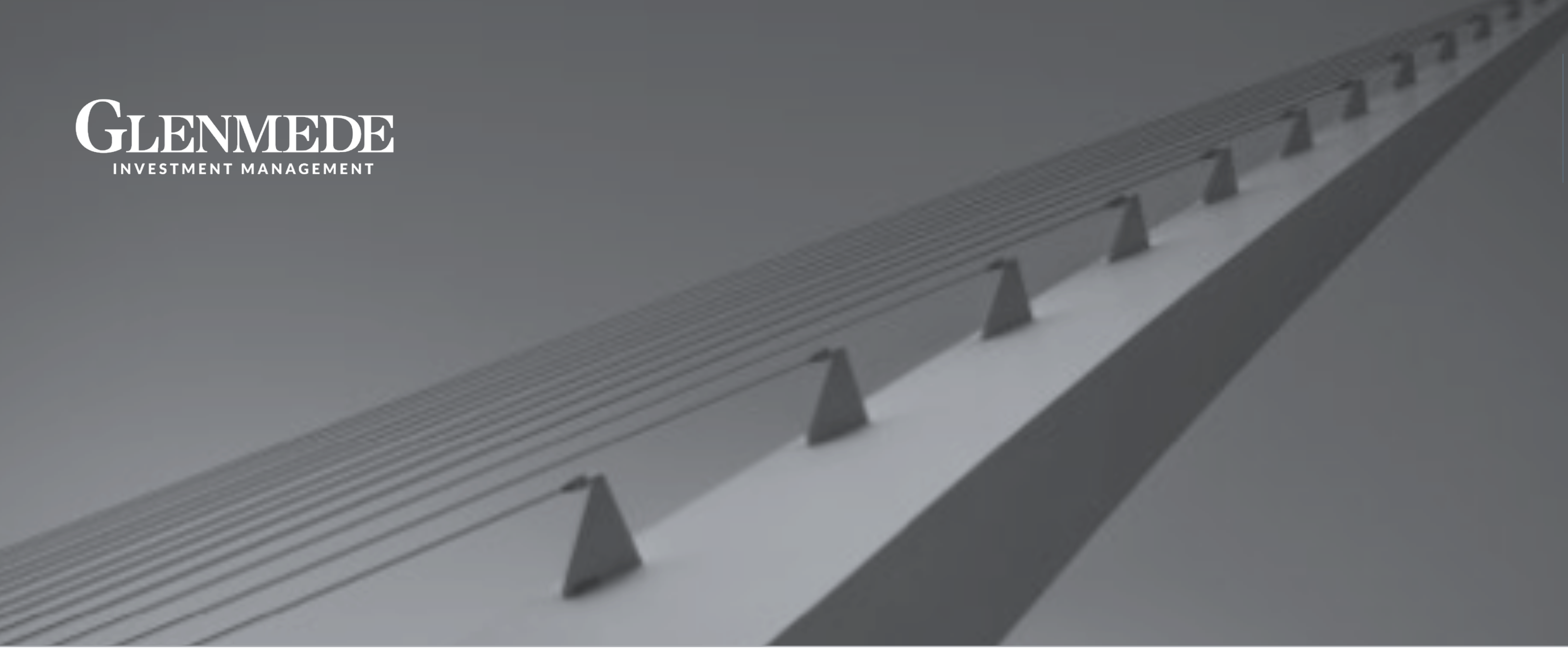
[1] Source: Forbes 2020, DeVere Group.

[2] Foubert, A.-L. "ESG Data Market: No Stopping Its Rise Now." Opimas, March 9, 2020.

[3] "ESG Factors and Equity Returns – A Review of Recent Industry Research." PRI, June 17, 2021.

[4] Morningstar "sustainable" categorization is a proprietary Morningstar data point and is assigned based on the underlying securities in each portfolio. The Morningstar Sustainable funds universe is determined by Morningstar and includes mutual funds and exchange-traded funds in the U.S. across three categories defined by Morningstar: ESG integration, sustainable and impact approaches.

[5] The Glenmede Trust Company, N.A. is a trust company headquartered in Philadelphia with multiple offices, providing wealth and investment solutions for individuals and families, institutional investors, nonprofits and foundations. Glenmede Investment Management, LP is an institutional asset manager advising various strategies available as mutual funds and separately managed accounts. The firms are affiliated.



Contact us

Institutions and Sub-Advisory

Edward Hart
Director of Consultant Relations
Direct: 215-419-6119
Email: edward.hart@glenmede.com

Platforms & Advisors

Jason Laird
Business Development Officer
Direct: 215-419-6902
Email: jason.laird@glenmede.com

Jarrett Naiden
Business Development Associate
Direct: 215-419-6793
Email: jarrett.naiden@glenmede.com

Glenmede Investment Management

www.glenmedeim.com

1650 Market Street, Suite 1200
Philadelphia, PA 19103-7391

215.419.6662

gimclientsupport@glenmede.com