

# Engagement – A tool to drive change and limit risk

Today, engaging with the management and boards of investee companies is required of all good asset managers – it is no longer the haunt of activist investors. Asset managers must act as good stewards of client assets, and not just ensure that investments provide steady financial returns, but also that they uphold minimum environmental, social and governance (ESG) standards. At RLAM, we value engagement as a versatile tool and use it in the pursuit of two key goals: delivering sustainable outcomes; and managing ESG risks and opportunities. Our

engagement spans both equity and fixed income funds because we think good stewardship should be applied regardless of asset class. This requirement is now included in the 2020 UK Stewardship Code and is understood as global best practice.

## Managing ESG risks and opportunities

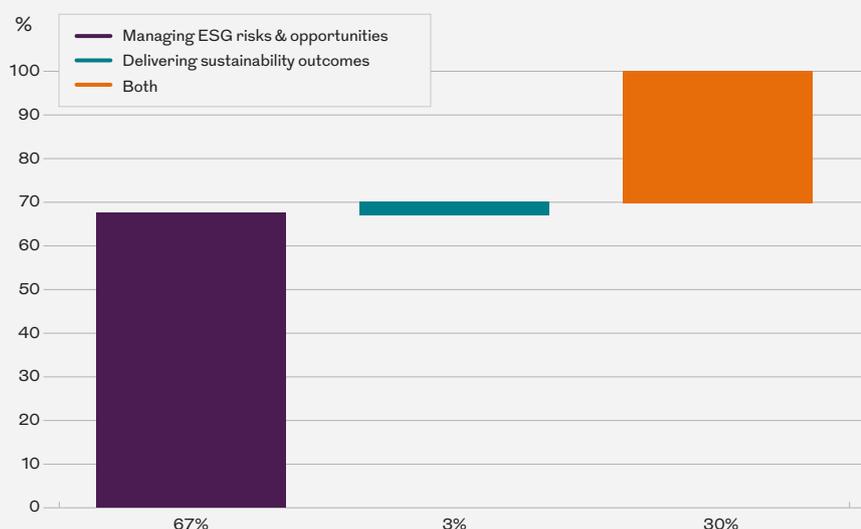
The majority of RLAM's engagement activity involves the management of ESG related risks and opportunities (97%), and a third aims to achieve a sustainable outcome at the same time – our engagement with energy utilities companies is a good example. Firstly, engagement with energy utilities

companies serves as a fact-finding mission, assessing their preparedness for the energy transition ahead, helping us to improve our decision making and reducing potential risks. The engagement also aims to generate a sustainable outcome by encouraging firms to plan for a 'Just Transition', minimising the negative social impacts of the energy transition.

## Just Transition engagement project in partnership with Friends Provident Foundation

Last year, in partnership with Friends Provident Foundation, RLAM launched a just transition project focused on investors supporting and working with energy and utilities companies – who contribute the biggest portion of emissions across our investment portfolios. The project, which remains ongoing, involved meeting seven companies with respect to a just transition. While most companies had detailed plans to address decarbonisation, none had plans regarding the broader social impacts of their actions. SSE was the first to publish its strategy late in 2020, with E.on following suit earlier this year and Scottish Power, Centrica, National Grid and likely EDF all publishing before the end of 2021.

Figure 1: Purpose of engagement activity, 2021 year-to-date

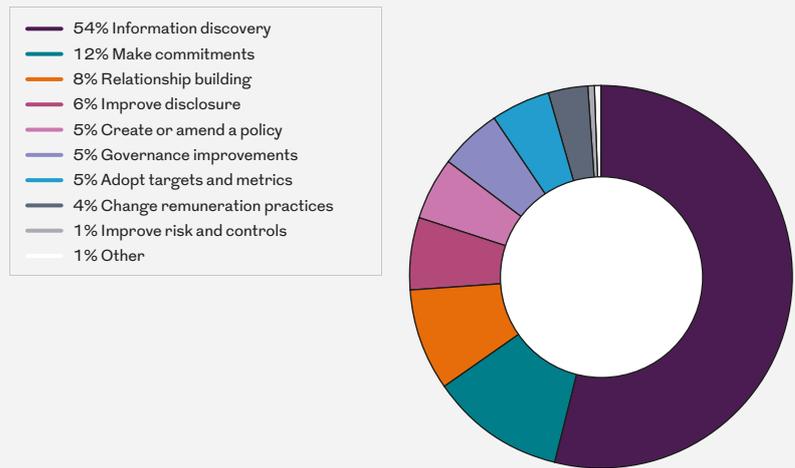


Information discovery is the most common objective of engagements at RLAM (see figure 2). The reason for this is simple; more information allows for better decision making and more effective risk management. Fact finding is especially important when it comes to non-financial information, as the quantity and quality of disclosure varies broadly. Private companies, for example, which have far fewer reporting requirements than their publicly listed counterparts, often lag in data coverage. This can make sourcing ESG data to improve the decision making within fixed income funds very difficult, as bond issuers are often private companies.

RLAM has found that fixed income data coverage from typical ESG data vendors is often very low. Furthermore, due to the relative immaturity of non-financial reporting, there is an absence of universally agreed reporting guidelines which means that when companies do disclose information, it often follows different guidelines and is incomparable.

When it comes to assessing carbon emissions data in fixed income, RLAM overcame this issue by engaging with

**Figure 2: Objectives of engagement activity, 2021 year-to-date**



Source: RLAM. Figures are subject to rounding and therefore total may not equal 100%.

issuers to plug a shortfall in emissions data. In 2020 we developed an in-house carbon intensity tool, extending carbon emissions data for our fixed income holdings from 70% to 84% coverage of our portfolio. Although some investors assume that engagement is best left to equity markets, we believe that targeted engagement by bondholders is not just possible, but beneficial to all

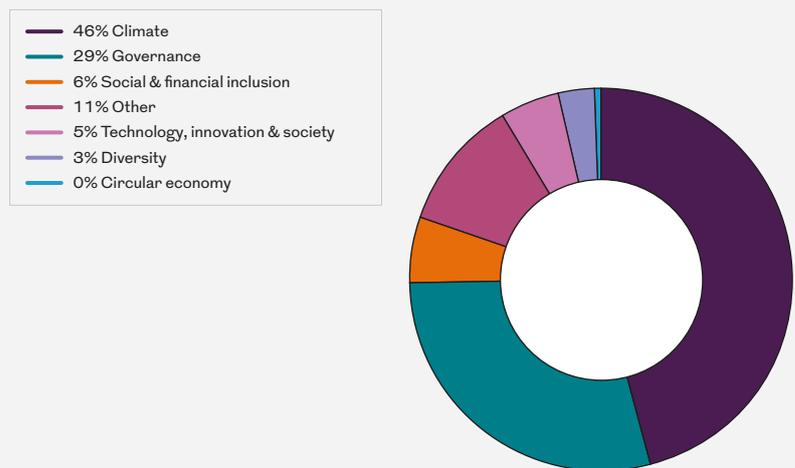
stakeholders. Although our points of influence are more limited in relation to large global companies, RLAM's focus on secured debt and more highly covenanted issues gives us greater access to the 'decision makers' and consequently allows us to have greater impact both in relation to bond structures and ESG considerations.

## Delivering sustainable outcomes

RLAM engages on both a reactive and proactive basis. Our reactive engagement is largely driven by market events such as rights issues, governance issues, company announcements, ESG risk events or company requests. Under these circumstances, while we endeavour to respond to as many engagement requests as possible, given the size of our investment portfolios and the large number of different firms and issuers we invest in, we usually prioritise our reactive engagements by the size of our holding or the severity of our concerns.

On a more strategic basis RLAM engages proactively with investee companies, taking the view that good company engagement has a positive cumulative effect. We believe that through ongoing discussions with company management we can have a positive influence on corporate

**Figure 3: Engagements by theme, 2021 year-to-date**



Source: RLAM

behaviour and help companies to improve internal practices, governance and oversight, and impact on society and the environment.

Faced with an ever-growing list of ESG issues and company requests, we undertake a full review of our engagement themes every two years

in a process which involves extensive consultations with our fund managers, responsible investment analysts, clients and other stakeholders. In 2019, we assessed our portfolio exposures, reviewed academic evidence on engagement, and surveyed external research on new and emerging issues and risks. From this we selected the six themes that we felt were most material to our holdings, fit with our company's culture and values, were of importance to our clients, and represented significant: climate risk; governance; circular economy; innovation, technology and society; diversity; and social and financial inclusion.

Throughout 2020, under stress from Covid-19, reactive engagement took precedent. With companies experiencing overwhelming financial strain, the focus of RLAM's engagement shifted to executive pay (a sub-set of the governance theme – see figure 3) – we wanted to ensure that employees were treated fairly through a difficult period, which disproportionately affected the lower paid. In 2021, however, the level of our strategic engagement activity has increased, and now more closely reflects our most pressing priorities. In 2021 to date, RLAM has engaged more on climate than any other theme.

## Engaging at scale

In 2020, our RI team engaged with over 200 companies on a total of 413 occasions, a significant uplift in engagements compared with activity in 2019, and we are on target to maintain this level of activity during 2021. We have invested heavily to improve and enhance our engagement offering to clients, and now have a team of nine responsible investment professionals working alongside our investment teams and client teams. Our engagement activity has expanded to new markets, which has helped us to extend our research and analysis to focus on all the companies and issues that are most material to us.

However, we understand that the current scale global social injustice, ecological degradation, and broad inequality means that lasting resolutions are outside of RLAMs immediate

## Delivering our Net Zero commitment through engagements with a targeted focus

As part of our strategy to deliver on our commitment to decarbonising our investment portfolio to Net Zero by 2050, through real economy emission reductions, we are ramping up our engagements on investee companies' climate strategies.

**Purpose:** To ensure the largest greenhouse gas emitters set targets aligned with a 1.5°C warming ambition, work to address policy, technology and stakeholder considerations in the journey to Net Zero and demonstrate action now to minimise their impact on climate change.

### Expectations sent to companies:

1. Set target aligned with 1.5°C ambition:  
Reach Net Zero emissions at the earliest feasible timeframe, with 2050 as the backstop date. Include in your target all scopes of emissions and only offset residual emissions following Net Zero aligned offsetting principles.
2. Bring along the system to Net Zero  
Commit to scaling-up technology and solutions required to achieve Net Zero. Lobbying for a policy that accelerates the transition. Engaging with the complete business value-chain, communities, and workers to ensure a just transition.
3. Demonstrate action now:  
Setting ambitious short-term targets. Aligning the Board, management and employees' incentives to achieving Net Zero targets. Developing an action plan with specific operational implications and any business model transformation to becoming a Net Zero business. Aligning capital expenditures with Paris goals, accounting practices to the delivery of Net Zero. Being transparent about targets and climate transition plans, by including them in advisory shareholder votes. Investing in adaptation measures to ensure resilience against locked-in climate impacts.

grasp. Nonetheless, we can still help. We believe that it is essential, as a responsible investor, to engage with regulators, governments, standard setters and NGOs to advance good governance and responsible investment on a global scale. By doing this, we not only drive impact within our own investment portfolios, but we also help to shape a fairer and more sustainable future for the next generation.

For further detail on RLAMs engagement process, and information on the local, regional and global change projects we are involved in, please visit [rlam.co.uk/SRI](http://rlam.co.uk/SRI) to read our Stewardship and responsible investment 2021 report.

The views expressed are the author's own and do not constitute investment advice.

## Contact us

For more information about our range of products and services, please contact us.

### Royal London Asset Management

55 Gracechurch Street  
London EC3V 0RL

### For advisers and wealth managers

bdsupport@rlam.co.uk  
020 3272 5950

### For institutional client queries

institutional@rlam.co.uk  
020 7506 6500

### Responsible Investment team

esg@rlam.co.uk  
www.rlam.co.uk

### For Professional Clients only, not suitable for Retail Clients.

This is a financial promotion and is not investment advice. Telephone calls may be recorded. For further information please see our Privacy policy at [www.rlam.co.uk](http://www.rlam.co.uk)

All information is correct as at September 2021 unless otherwise stated.

Issued in October 2021 by Royal London Asset Management Limited, 55 Gracechurch Street, London EC3V 0RL. Authorised and regulated by the Financial Conduct Authority, firm reference 141665. A subsidiary of The Royal London Mutual Insurance Society Limited.

Ref: AL RLAM PD 0110

