Q&A

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The role of the asset management industry in a sustainable, open and competitive Europe

What is the role that asset managers are playing in the green transition? What is the extent of the impact of asset management activities on the green transition? Are further regulatory measures needed to support this role and do certain obstacles need to be addressed?

The success of the green transition will be predicated on the efforts of both policymakers and market participants. As to the latter, asset managers have a significant role to play and indeed, have been at the forefront of industry efforts. We have seen both individual commitments and industry-wide collaboration, with Climate Action 100+ and the Net Zero Asset Managers Initiative being powerful examples of asset managers working together to meaningfully drive forward the green transition.

While the role of the asset management sector is multi-faceted, there are three particular elements worth highlighting. First, asset managers can help educate and empower investors to take advantage of investment opportunities created by the green transition. Investors are increasingly vocal on the importance of ESG considerations in their investment objectives; it is now often a critical part of the discussion between asset managers and clients. The industry has responded in kind, helping clients to further understand the importance of the transition, as well as offering a variety of products and strategies across the spectrum of client ESG preferences.

Second, in seeking investment opportunities in line with investors' ESG objectives and, in doing so, factoring in the relevant risks during the investment process, asset managers can contribute to the appropriate pricing of climate-related risk by financial markets. Third, the stewardship activities asset managers undertake with portfolio companies helps to promote long-term shareholder value. Amongst other things, this dialogue may encourage investee companies to have robust transition plans and enables constructive engagement where progress is not fast enough.

On the role of policymakers and ESG regulation, we believe their primary objectives should be to set the appropriate standards for financial markets to facilitate the green transition and ensure investors have the necessary information to make informed decisions. The EU has been at the vanguard of global regulatory efforts and should be commended for bringing international attention to climate risk, as well as highlighting the importance of public-private sector collaboration. While Europe has enjoyed first-mover advantage, with certain elements of its framework becoming the industry standard, several challenges remain including, sequencing, insufficient clarity and lack of consistency with existing legislation. It is crucial these issues are addressed, in order to fully establish a well-functioning regulatory regime that delivers on the needs of all stakeholders.

Looking ahead, we note two additional considerations. First, we believe the focus of regulation to date has emphasised the channelling of capital to already green activities. However, the green transition will likely necessitate greater focus on the larger part of the economy that is not yet green but has the potential to be so in the future. Furthermore, to the extent possible, we continue to recommend international alignment of standards. The challenges presented by climate risk are global and will require a globally-coordinated response.

Is there a significant risk of greenwashing, what are the underlying issues in the asset management area and how to address them?

As investors' ESG considerations and the facilitation of the green transition more prominently influences the direction of capital, we acknowledge there is a material risk of 'greenwashing'. Greenwashing, as described by ESMA, are instances where the sustainability profile of a company, a financial instrument or a financial product that is disclosed does not accurately reflect the underlying sustainability risks and impacts. We believe that well-calibrated, unambiguous disclosures, which enable investors to assess and identify the most relevant financial products in line with their objectives, are critical to address concerns in relation to greenwashing. The EU has again been an early mover in this regard, through its SFDR framework. In addition, investor education will have a crucial role to play.

It is important to also recognise that discussions on greenwashing can be highly subjective. Given the diversity of views on what constitutes 'green' – for example, the classification of nuclear power – and there yet to emerge a consensus view, concerns around greenwashing are often scenarios where a product or strategy does not align with an individual party's definition of green. Similarly, all stakeholders are operating in a rapidly-evolving and dynamic environment. It is important that, in seeking to minimise the risk of greenwashing, policymakers do not proscribe new sustainable strategies and inadvertently stifle market innovation.

Do the proposed AIFMD amendments tackle the main areas where a further efficiency and integration of the AIF market is needed? Are the reviewed provisions of the AIFMD concerning delegation rules and liquidity management tools in particular likely to have a positive impact in terms of investor protection and financial stability?

The AIFMD review, which proposes changes to rules for both AIFs and UCITS, has come at an opportune moment. The investment funds industry, like broader financial markets, experienced a live stress test during the pandemic-related market volatility in March 2020. While we believe the funds industry broadly performed in line with expectations, it is prudent to assess whether there are elements of the framework that can be improved. We believe this has been recognised by the European Commission and we commend them for their targeted and balanced legislative proposal.

Regarding liquidity risk management, we strongly support harmonising the availability of liquidity management tools (LMT) across the EU, which we believe will directly contribute to improving financial stability. Nevertheless, we would urge caution in two areas. First, while we understand the desire for regulators to want to prescribe granular requirements, this should not come at the expense of the flexibility asset managers and fund boards have in selecting the most relevant tools for their circumstances and in the interests of investors. In addition, we continue to believe asset managers and the board are best placed to make the decision to activate LMT. As observed during March 2020, not all fund types faced the same set of challenges. Therefore, a decision by regulators to activate tools across a group of funds may introduce a contagion effect and procyclicality, thereby undermining market resilience.

On delegation, we welcome the acknowledgement from the European Commission of the contribution the current model has made to the global success of the UCITS framework and also, increasingly, for AIFs. The delegation model has been a critical feature in enabling the UCITS brand to permeate and appeal to investors on an international scale that is without comparison, and it is widely recognised as a best-in-class product. We appreciate the rationale and motivation behind some of the proposed changes, which we believe are driven primarily from a supervisory convergence perspective, rather than to address any material shortcoming in investor protection. In principle, we fully support efforts to ensure the consistent application of EU rules across Member States, although, in practice, we have seen few – if any – instances where this is not currently the case, in the context of delegation.

As such, we would urge caution when considering potential changes to the current delegation framework, which should be approached principally from the perspective of what is best for investors. We further encourage policymakers to avoid compromising the practical benefits in order to address theoretical concerns.

Are the measures proposed in the ELTIF review likely to position ELTIFs as a significant source of long-term finance for the EU economy and a key enabler of the CMU? Can revised ELTIFs become a significant investment vehicle for retail investors, and will they be easier to operate for AIF managers?

A core tenet of the updated CMU project, particularly in light of the effects of the COVID pandemic, is to encourage and facilitate a more sustainable and resilient economic recovery. We believe ELTIFs will have an important role to play in delivering this.

We welcome the ambitious approach taken by the European Commission in the ELTIF Review. ELTIFs have seen little uptake to date, largely as a result of the restrictive nature of certain provisions in the original framework. The new proposal seeks to amend some of these without compromising investor protection. In particular, we would highlight the revisions to the eligible assets requirements and, notably, the provisions relating to investments in other collective investment undertakings. We agree with the European Commission that these specific changes may facilitate fund-of-fund strategies, which we believe will help the scale up of ELTIFs and enable more diversified portfolio construction.

Regarding retail investor participation in ELTIFs, we believe the legislative proposal represents a step in the right direction. The most prominent example of this is the removal of the €10,000 'entry ticket' but we also believe the provisions that seek to align the ELTIFs regime with other EU legislation, notably the cross-border distribution of funds and MiFID suitability requirements, will be helpful. In addition, the provisions that seek to increase the liquidity profile of an ELTIF could also enhance retail investor participation.