ESG Investing

ESG Investing Awards 2023 Interview

Fulcrum Asset Management

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Founded in 2004, Fulcrum Asset Management is a highly innovative, independent asset manager offering a broad range of investment capabilities. Headquartered in London, they also have offices in New York and Tokyo, with a growing presence in Europe and Australia. Fulcrum's people are at the heart of its business, with the partnership representing a team of over 90 people with approximately £5.1bn ($6.2bn) in assets under management. All investment management activities are carried out from their London headquarters.

> Fulcrum Asset Management was awarded Best ESG Investment Fund: Thematic (Climate Alignment) at the ESG Investing Awards 2023.

Thematic Team

Fawaz Chaudhry
Partner, Head of Equities

Joined Fulcrum in 2017

BlueCrest Capital (2016)
Moore Capital (2013-2016)
Hadron Capital (2011-2013)
Valorem Limited (2009-2011)
Macquarie Capital Advisors (2007-2009)

Citigroup (2003-2005)

Morgan Stanley (2001-2003)

London Business School,
MBA Finance (2005-2007)

Massachusetts Institute of Technology (MIT) M.Eng Electrical Engineering, SB Computer Science, SB Finance (1996-2001)

Natalia Chmielewska
Research Analyst

Joined Fulcrum in 2018

Amundi Asset Management, Analyst (2017)

Lyxor Asset Management, Analyst Intern (2016)

Sciences Po Paris, MSc in Finance (2014-2016), BS in Economics, Finance (2011-2014), PgD Mathematics, Statistics, Univ of London (2019-2020)

CFA charterholder since 2019

Rahil Ram, FIA
Research Analyst

Joined Fulcrum in 2019

Legal & General Investment Management, Multi Asset Strategist (2014-2019)

Cass Business, MSc in Actuarial Management (2014-2016)

Cass Business School, BSc (Hons) in Actuarial Science(2010-2014)

Fellow of the Institute and Faculty Actuaries (FIA) since 2017

Arthur Turner
Research Analyst

Joined Fulcrum in 2022

Cheyne Capital Management (2020-2022)

University College London, MSc in Machine Learning

University College London, BSc in Mathematics

Candidate for CFA Level 3

Neel Narayan
Research Analyst

Joined Fulcrum in 2022

Materials Science and NanoEngineering Research Scientist, Rice University (2018-2022)

Computer Science and Management Science & Engineering, Stanford University (2020-2023)

Iancu Daramus
Sustainability Analyst

Joined Fulcrum in 2021

Legal & General Investment Management, Senior Sustainability Analyst (2017-2021)

Carbon Tracker Initiative, Associate (2015-2017)

London School of Economics, MSc Philosophy and Public Policy (2013-2015)

University of Essex, BA Hons Philosophy and Public Policy (2010-2013)

CFA Institute, Lead co-author, Certificate in ESG Investing (2021)

Interview

Fund and Company Info

Can you provide a short overview of your company and your funds?

Founded in 2004, Fulcrum is a highly innovative, independent asset manager offering a broad range of investment capabilities. Headquartered in London, we also have offices in New York and Tokyo, with a growing presence in Europe and Australia. Fulcrum's people are at the heart of its business, with the partnership representing a team of over 90 people with approximately £5.1bn ($6.2bn) in assets under management. All investment management activities are carried out from our London headquarters.

Independently owned, the firm is large enough to enjoy economies of scale and a breadth of expertise, but equally nimble enough to be able to respond quickly to market events or alter course to adapt to new opportunities. Through a unique and transparent investment approach, the aim is to build lasting relationships based on the alignment of client interests with Fulcrum's own.

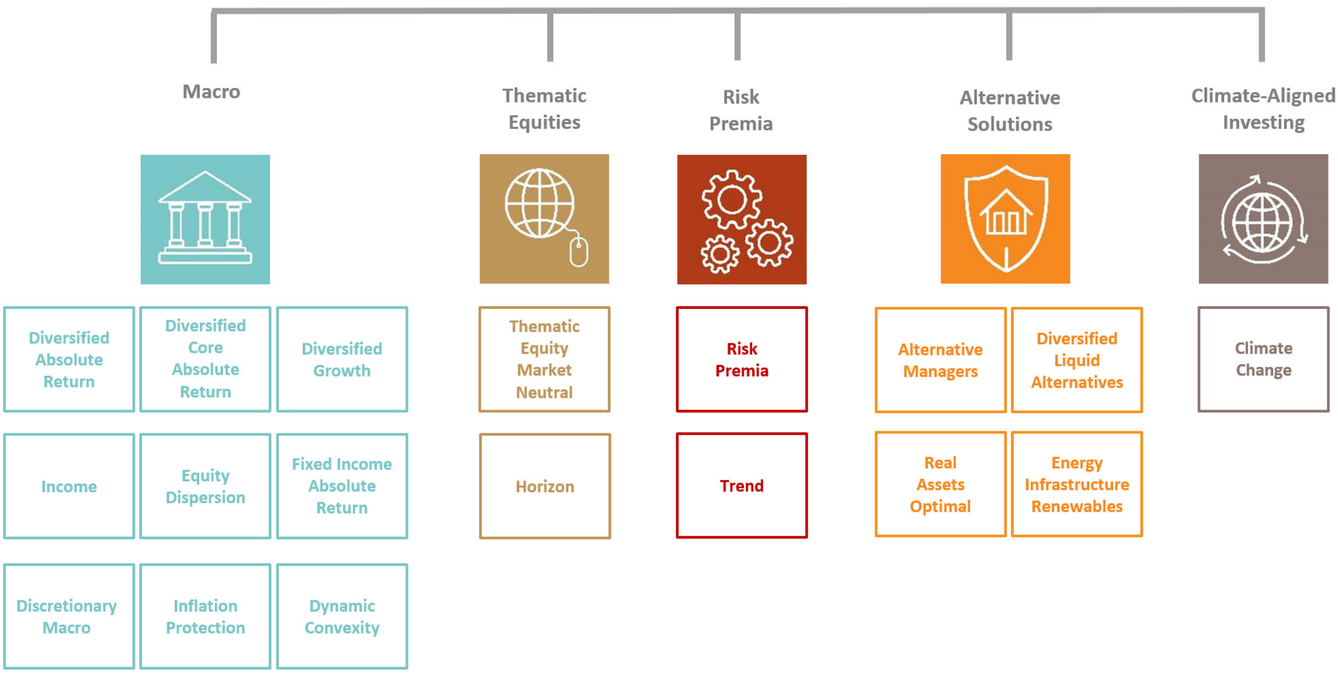
Fulcrum's five key investment capabilities include Macro, Risk Premia, Alternative Solutions, Climate-aligned Investing and Thematic Equities, spanning systematic and discretionary investments, managed both internally and externally. Through our Solutions Team we also manage bespoke mandates on behalf of pension funds, institutions, and charities. Our long-term goal is to work with clients that share our purpose and who seek expertise to help them meet their own objectives.

Innovation remains a key part of our DNA and our roots in macroeconomic research continue to provide a firm foundation to our broader investment thinking. At Fulcrum, our key strength is understanding the drivers of asset class returns and quantifying investment risk; we aim to maximise our advantage in capturing market movements through our research and rigorous investment techniques. Our solutions provide diversified, risk managed investments covering all the major global asset classes. Fulcrum's investment process is designed to deliver stable, positive outcomes for our investors over the long term regardless of the direction of global financial markets.

Strategy Description:

Macro	Thematic Equities	Risk Premia	Alternative Solutions	Climate-Aligned Investing
These strategies are designed to generate absolute returns, offer downside protection, and provide diversification.	We provide exposure to key megatrends throughs synthetic and physical equity investments.	A range of systematically implemented, quantitative investment strategies that includes trend following, volatility, carry, value and skewness	Our guiding objective is to support investor in overcoming the governance challenges of investing in Alternatives.	We invest in companies that are taking steps to align their business model to the net zero transition.
We invest globally via index derivatives across equities, bonds, commodities and currencies. These strategies also invest a substantial proportion in our other capabilities listed in this table.	This results in highly diversified long/short portfolios with global, cross-sector exposures to a wide range of socioeconomic themes.	We invest globally via derivatives across equities, bonds, commodities and currencies.	We offer a range of pooled and bespoke solutions with exposure to Real Assets, Alternative Credit and Diversifiers across the liquidity spectrum, largely accessed through external managers.	We aim to balance climate alignment, return expectations and diversification benefits.

Strategy Overview:



What is your AUM and size of the investment team?

The data below is as of 31st March 2023.

Firmwide Investment Team size: 38

The firm's assets under management are split across the following strategies and clients ($m):

Macro Strategies:	
Fulcrum Diversified Absolute Return & Discretionary Macro:	4677
Fulcrum Diversified Growth:	119
Fulcrum Fixed Income Absolute Return:	77
Fulcrum Equity Dispersion:	492
Inflation Protection:	142
Dynamic Convexity:	48
Thematic Equities:	
Fulcrum Thematic Equity Market Neutral & Horizon:	986
Risk Premia:	
Fulcrum Risk Premia:	703
Multi Asset Trend:	
Alternative Solutions:	
Fulcrum Diversified Liquid Alternatives:	383
Fulcrum Alternative Managers:	174
Climate-Aligned Investing:	
Fulcrum Climate Change:	154

What is your ESG strategy? Do you have an explicit exclusion/integration strategy? What are your exclusion/integration criteria?

Responsible Investment has been established as one of the key strategic priorities for our firm and sustainability is one of our core values. Being a top-down, macroeconomic investor, the consideration of ESG risks is integral to our success. Our approach includes ESG integration into our investment decision-making process, effective governance, and targeted engagement.

The assessment of ESG risks is conducted as part of our investment analysis and we also monitor these risks whilst we hold the assets. It is challenging to coherently integrate multiple ESG factors given our top-down focus. However, we have made significant progress and we expect this to continue in the years ahead. Based on feedback from our clients as to what is important to them, and as a consequence of our macro heritage, much of our work relating to ESG integration has focused on climate change. This is an expression of our inquisitive culture and our focus on this topic has been endorsed at our RIC and our Management Board. The depth of our work in this area reflects how important we believe it is to client outcomes and ultimately, achieving our purpose.

We recognise that more sustainable markets must pay due regard to people, as well as the planet. We therefore do not invest in activities that we believe have a disproportionately negative social impact, including predatory lending, tobacco, and controversial weapons. And we seek to constantly improve our own internal practices and policies, creating a workplace where employees feel valued and supported.

More specifically, an overview of how ESG risks are currently considered across each of our capabilities is outlined below:

- **Macro:** Our Macro capability allocates to our other capabilities as well as implementing a range of tactical views across a variety of different asset classes and time horizons using derivatives. ESG risks can also be an element of overall risk assessment for certain discretionary positions within our Macro portfolios, for certain commodities and countries where it is most relevant.

  One of our biggest challenges is to work alongside the market to develop best practices in this strategy. We are cognisant that derivatives form a large part of our investment universe. While we continue to participate in market discussions in this space (through our work with climate investor network IIGCC), we are also working internally to move our derivatives to physical equities and thus better integrate and engage from an ESG perspective.

- **Risk Premia:** We have now systematically integrated ESG risk data from third-party vendors into our quantitative models for the directional parts (e.g. Trend Following) of our risk premia strategies. This has involved augmenting our risk assumptions across all instruments according to certain ESG risk metrics and will ultimately have the effect of reducing our maximum position sizes in those assets with higher unmanaged ESG risks.

- **Alternative Solutions:** We use a proprietary scoring system for each of the alternative investments we review as part of our due diligence process. This includes a detailed review of an external manager's policy and approach, asset allocation, portfolio construction, stock selection and any asset class specific considerations. We use third- party ESG risk data for certain aspects of this work, including carbon emissions and country risk scores. In addition, we have developed an engagement framework with bespoke engagement objectives for our third-party managers, and have seen examples of managers stepping up following our requests (for example, improving their reporting or joining ESG initiatives).

- **Climate-Aligned Investing:** We regard climate change as one of the largest risks facing investors over the medium- to long-term, and we believe that climate-aligned investing can boost risk-adjusted returns as well as shift financial flows to fund the green transition. We launched our flagship, long-only climate-aligned global equity strategy in August 2020. The Fulcrum Climate Change strategy invests in companies that are taking steps to align their business model to the net zero transition. The strategy invests only in companies that are below 2°C, thereby focusing on a forward-looking metric that incorporates historical, present, and future potential emissions (as opposed to "low-carbon" portfolios that focus on a backward-looking historical emissions measure). We believe that climate-aligned solutions must be able to play a core part of investors' equity portfolios, and have therefore designed our climate strategy with a view to maintaining diversification, and controlling tracking error and factor exposures.

  After extensive due diligence, as the Fulcrum Climate Change Fund approaches its 3-year anniversary, we were comfortable allocating to it the majority of Fulcrum's long-only dynamic equity holdings across our flagship strategies. The climate alignment of equities thus strengthens the integration of sustainability considerations also within our macro capability, and represents a key milestone in Fulcrum's commitment to net zero.

- **Thematic Equities:** The relevance of ESG issues is assessed when new themes are researched and monitored. In the theme idea generation process, the exposure to ESG risks as well as ESG-related opportunities is considered (particularly long-term trends such as climate change) and ESG risks can be considered both an attractive investment opportunity or a risk signal. We assess the ESG implications within a theme based on external research, company meetings and sell-side analyst meetings. A number of the themes within the strategy are designed to take advantage of sustainability-related tailwinds (e.g. long clean energy) in our long holdings or positioned to benefit from headwinds in the short exposures (e.g. short 'gig economy' stocks that are facing scrutiny as regards labour practices and human rights). In addition, across our equity book, where we are able to vote, we have implemented a voting policy that aims to hold companies and their directors accountable for progress on sustainability, as illustrated here: https://www.fulcrumasset.com/inst/uk/en/fulcrum-blog/adjusting-the-resolution-reflections-on-the-2022-proxy-season/

How do you assess a firm's ESG criteria? How dependent are you on third party ratings?

Our approach is to combine third-party data with our own proprietary analysis, with the combination depending on the capability under consideration. As climate change has been the biggest thematic focus of our stewardship efforts, we have relied most heavily on 'E'-related data, drawing on multiple data providers to give us a more rounded view of companies' policies and progress. We are working on expanding this dataset to a broader range of ESG themes. We are working on developing Principal Adverse Impact indicators, currently in development with our data provider, Sustainalytics, alongside EU sustainable finance directive guidelines.

In certain areas where we believed data and tools were lacking, we have also collaborated on the development of new resources, such as the 'ESG for Investors' initiative, which provides free-to-use tools trying to assess the potential upside for companies if they were to improve ESG performance in line with peers, with carbon emissions identified as the most material ESG variable: https://esgforinvestors.com/.

The ESG for Investors platform also has portfolio optimisation tools that aim to quantify the trade-offs and synergies between reducing transition risk (e.g., by reductions in the implied temperature of a portfolio) and the risk/return/volatility characteristics of a portfolio. Fulcrum and Arvella Investors won the award for 'Best Sustainable Investment Education Initiative' at Investment Week's Sustainable Investment Awards 2022 for our work on this project.
https://esgforinvestors.com/articles/detail/23/

More information on our approach can be found in our dedicated fund-level sustainability reports.

What has been the performance of your funds against its index since their inception?

The fund is up +19.2% from inception (3rd August 2020) to 28th February 2023 while the benchmark is up +17.8% over the same period. The quoted performance record represents the live fund performance returns from Fulcrum Climate Change Fund F Share Class USD, which charges fees. Source: NAVs provided by official third party fund administrator.

Do you have an explicit commitment to Net Zero? If so, how does this manifest itself in your engagement with companies you invest in?

Fulcrum is a signatory to the Net Zero Asset Managers Initiative and committed to support the goal of net zero greenhouse gas ('GHG') emissions by 2050. We are signed up to the Net Zero Asset Managers initiative and will be providing them with an annual climate action plan, which will be submitted to their investor agenda. As a member of the Net Zero Asset Managers Initiative, we have committed to reach net zero across our assets, with initial work focused on aligning many of our directional, long-only holdings of corporate equity and debt to a climate-secure outcome. We have also implemented restrictions around companies expanding thermal coal and oil sands exploration, in select funds.

We have developed an engagement strategy focused on encouraging companies to set net-zero/ science-based targets, focused on c. 40 large global companies in different sectors. By setting targets, companies are more likely to be included (or remain) in the growing share of our assets managed to net zero. We have also implemented a voting policy that sanctions the directors of companies lacking (ambitious) emissions targets.

We joined the Glasgow Financial Alliance for Net Zero (GFANZ) in 2022, and are contributors to the working group on portfolio alignment measurement. Our climate-aligned strategy was featured as a case study in GFANZ's flagship report in November 2022.

What is your policy regarding engagement and proxy voting?

Please refer to our proxy voting policy here.

Could you provide an example how you have engaged with a company that scored poorly on ESG?

We have been discussing climate strategy with mining giant Glencore. The company has made progress on the issue in recent years, including by adopting a comprehensive 2050 net zero target. However, we remain concerned that the company's interim emission targets (particularly for the phaseout of its coal assets) are not aligned with science-based pathways for fossil fuel production – which we have raised directly with the company. We have since opposed the company's energy transition strategy and the re-election of four directors at the 2022 AGM, where almost a quarter of shareholders also voted against the transition plan. We have since been engaging with other investors that have co-filed a resolution on the alignment of the company's coal assets to be voted at the 2023 AGM.

The company is held within a concentrated engagement equity strategy, where the names have been chosen due to a belief in potential upside from specific sustainability-related improvements. We have also been collaborating with other investors on joint engagements with some of the other investee companies in the strategy, such as BNP Paribas – where we joined a campaign to encourage the company to cease its new fossil financing. Our Head of Equities was quoted in Bloomberg about our engagement expectations, please see quote at the link below.

https://www.bloomberg.com/news/articles/2023-02-10/bnp-barclays-among-banks-in-crosshairs-over-new-oil-gas-loans

Voting sanctions currently remain our main avenue for escalation – we may vote against management or the election of specific directors both in response to ongoing engagements (see example below), but also to encourage the adoption of certain principles across markets, regardless of whether we were able to engage with the underlying issuer.

In the 12 months to the end of June 2022, there have been 751 votes against management for environmental reasons, 168 of which were specifically due to the lack of (ambitious) emissions targets.

Our voting policy will also codify broader expectations, with regards to governance (e.g., the independence of directors, or their remuneration) and social aspects (encouraging improvements in gender diversity or in practices relating to labour standards or human rights). During the same period, we have cast 191 votes against management for social reasons.

We also pay attention to the interplay between E, S and G elements as manifested in the incentives offered to the directors and employees of investee companies. There have been 315 votes against pay where it was considered the proposed pay arrangements provide insufficient incentives to manage of material environmental and social risks. In general, we have cast at least one vote in opposition to management at 48% of companies over this period.

How do you measure the impact of your investments in relation to the UN SDGs?

We focus on encouraging companies to set science-based decarbonisation targets. Our research, in collaboration with environmental engineers and a third-party investor, led us to develop an investment strategy aligned to the sub-2ºC temperature target of the Paris Agreement. For this strategy, which is 100% invested in listed equities, we use several levers including direct engagement, collective engagement, and proxy voting (through Glass Lewis). We are in direct contact with our holdings through letters, calls, and company meetings. in 2020-21, we supported circa 70% of environmental and social proposals, compared to an average of 35% for the world's 6 largest asset managers.

By way of example, we have repeatedly discussed the sustainability strategy of industrials company Air Liquide. In May 2022, we were pleased that the company informed us they are the first in their industry to receive validation from the Science-Based Targets initiative for their targets to 2035.

The Sustainable Development Goals (SDGs) are a helpful and user-friendly framework that we use for mapping our ESG practices. An example of this is SDG 13: Climate Action which we specifically focus on in relation to our equity themes. Climate change is an issue that will have dramatic consequences for nature and society, and touches on many of the other SDGs, it is also an area that Fulcrum has prioritised from a risk and investment perspective.

An overview of the alignment of our climate strategy (alongside firm-wide considerations regarding SDG alignment) can be found on the next page:

The Strategy supports various SDGs in particular SDG #13 (climate action) and #7 (affordable and clean energy)

	5 GENDER EQUALITY	6 CLEAN WATER AND SANITATION	7 AFFORDABLE AND CLEAN ENERGY	13 CLIMATE ACTION	8 DECENT WORK AND ECONOMIC GROWTH	16 PEACE, JUSTICE AND STRONG INSTITUTIONS	14 LIFE BELOW WATER	15 LIFE ON LAND	17 PARTNERSHIPS FOR THE GOALS
Firm-wide approach	Multiple initiatives to increase levels of diversity in the organisation		**Climate- aligned investing** is one of Fulcrum's core capabilities Dedicated climate research team UK office energy use backed by renewable electricity guarantees		Multiple initiatives for staff health and wellbeing; Development programmes, mentorship and volunteering opportunities; Competitive remuneration				
Investment process	Developing equity scoring frameworks to reflect levels of gender diversity	Thematic investments in providers of clean water and waste solutions	**Climate-aligned strategy** **Thematic investments in providers of clean energy and climate solutions**		Firm-wide exclusions on providers of controversial weapons, tobacco and predatory lending; Developing equity scoring framework to include datapoints on human rights and adherence to international standards Tactical thematic positions reflecting concerns around labour standards (e.g. short 'gig economy')		Developing equity scoring frameworks to include datapoints on water use, deforestation and biodiversity		Collaborations with other investors in support of system-wide action (e.g. Glasgow Financial Alliance for Net Zero, Diversity Project)
Stewardship	Voting sanctions on companies with low levels of diversity		**Direct and collective engagement on climate change** **Collaborations** with industry and policy-makers in support of climate action **Voting sanctions** for companies, directors and/or their pay in the case **of insufficient disclosures and targets around sustainability**		Voting policy sanctions companies falling short of expectations around governance (e.g. board independence), remuneration (e.g. pay structures misaligned with long-term value creation), or alignment with international standards (e.g. UN Global Compact Principles or OECG Guidelines for Multinationals)				

Source: United Nations, Fulcrum Asset Management LLP

Do you actively attempt to measure the climate risk associated with your funds?

As mentioned earlier, we prefer using a range of metrics to hold us accountable. These include frameworks such as Weighted Average Carbon Intensity (WACI) and temperature metrics. We are also in the process of developing KPIs in line with our SFDR requirements, which we will use to monitor our progress on ESG.

Quantitatively, we are calculating a suite of climate and ESG metrics on a daily basis, available on request.

Illustrative carbon metrics currently calculated for equities:

Column	Name
Exp_pct_GR	Gross Exposure %
Exp_pct_Net	Net Exposure %
Carbon_Int	Carbon Intensity Net (tons CO2e/$M revenue)
Carbon_Int_GR	Carbon Intensity Gross (tons CO2e/$M revenue)
WACI	WACI Net (tons CO2e/$M revenue)
WACI_GR	WACI Gross (tons CO2e/$M revenue)
Tot_Em	Total Emissions Scopes 1&2 (tons CO2e)
Tot_Em_GR	Total Emissions Gross Scopes 1&2 (tons CO2e)
Em_1_2_3	Emissions Scope 1&2&3 (tons CO2e)
Em_1_2_3_GR	Emissions Scope 1&2&3 Gross (tons CO2e)
Em_3	Emissions Scope 3 (tons CO2e)
Em_3_GR	Emissions Scope 3 Gross (tons CO2e)
Tot_Em_Mln_Inv	Total Emissions per Mln Invested (tons CO2e/$M invested)
Em_Mln_Inv_1_2_3	Emissions per Mln Invested Scope 1&2&3 (tons CO2e/$M invested)
Em_Mln_Inv_3	Emissions Mln Invested Scope 3 (tons CO2e/$M invested)

We are seeking to add ESG data on 'principal adverse impacts' (as defined by EU sustainable finance regulation) as part of these regular reports.

Qualitatively, we produce a firm-wide stewardship report, with case studies of engagement, and statistics on proxy voting and other fund metrics, supplemented as of 2022 by fund-specific reports; a report for the TEMN strategy expected by the end of the year.

We include a broad range of the below information in our materials (policies, annual reports and more regular client reporting on specific investments) to clients and on our website:

- Commitment to being a UK PRI signatory
- Impact reports where appropriate/applicable (for example in our Climate Change and Liquid Alternatives solutions).
- Industry- and asset-class-specific criteria we follow (TCFD and GRESB for real estate investments)
- Our Responsible Investment policy
- A description of the investment process and ESG integration.
- A list of our main investments and holdings.
- ESG case studies/examples of existing strategies.

A sample report is included in the submission for Fulcrum Climate Change. There is a strong degree of overlap between the investment process and companies invested in. We are currently finalising the TEMN Annual Sustainability report and can send that on in due course.

We also disclose all our votes via a dedicated platform, the day after the AGM, available online at https://viewpoint.glasslewis.com/WD/?siteId=Fulcrum.

Where does most of your data and information come from? Which sources do you rely on for the latest research related to climate change?

We aim to constantly enhance our Climate Change strategy's alignment with the Paris-Agreement goals by using the most relevant and cutting-edge data sets. These data sets are sourced both internally and externally. More specifically, our investment and research teams aim to stay at the forefront of the climate alignment space by working closely with different industry working groups and shaping the industry's thinking. Our goal is to enable investors to use metrics that enable them to have maximum impact on emitters via two channels: the cost-of-capital channel and the engagement channel.

Moreover, we intend to publish our research in an academic journal and present the research at academic conferences.

We have also continued to develop our capability to report on a suite of carbon and climate metrics, using both absolute measures (e.g. the total Scope 1,2, and 3 emissions associated with equities; total territorial emissions associated with government bonds), and relative metrics (which scale emissions relative to another measure – for example, the amount invested in a security, the revenues of a company or the GDP of a country). We are currently expanding this to include a broader range of sustainability metrics, in line with EU regulation. In addition, we are strong believers in the importance of adopting a forward-looking perspective in analysing the climate alignment of an issuer, as illustrated below.

Implied Temperature Rise (ITR) metric:

Mitigating climate change is a long-term economic challenge that is likely to remain on political agendas for decades to come and we believe that Climate-Aligned investing can boost risk-adjusted returns, especially relative to an approach that minimises backward-looking carbon emissions.

The scale of the challenge is captured by the fact that a majority of the world's listed companies and major equity indices* are not aligned with the goals of the Paris Agreement, if measured in terms of implied temperature rise.

At the same time, this challenge represents an investment opportunity – as climate change is "priced" into financial markets, investors may seek to capture "transition alpha". We have already seen this in the aftermath of Covid-19 (where a growing share of fiscal spending was geared towards the green transition) and in the increased focus of policy-makers on accelerating the shift away from fossil fuels.

As mentioned previously, our Climate-Aligned strategy – Fulcrum Climate Change – is explicitly designed to contribute to making financial flows aligned with the Paris Agreement's temperature target by having a weighted average portfolio temperature of below 2°C, with no individual company exceeding 2°C. The strategy is based on a rigorously researched ITR metric developed by environmental experts. This means that the investment process is geared towards a forward-looking approach, rather than the backward-looking methods (focused on historical carbon emissions) that are often used in the market.

As a result of our commitment to net zero emissions across assets under management, we have built on this strategy by expanding the proportion of our assets that are invested in Climate-Aligned securities by the end of 2022. We will seek to expand this, with further announcements to be made under the regular Net Zero Asset Managers Initiative reporting timelines.

In terms of ESG data providers, our approach is to combine third-party data with our own proprietary analysis, with the combination depending on the capability under consideration. As climate change has been the biggest thematic focus of our stewardship efforts, we have relied most heavily on 'E'-related data, drawing on multiple data providers to give us a more rounded view of companies' policies and progress. We are working on expanding this dataset to a broader range of ESG themes. We are working on developing Principal Adverse Impact indicators, currently in development with our data provider, Sustainalytics, alongside EU sustainable finance directive guidelines.

Data provider	Purpose
Sustainalytics	ESG Country Risk data (used in certain systematic strategies), activity involvement (used for firm-wide exclusions), carbon data (used for reporting); Principal Adverse Impact
MSCI	Activity involvement (currently relating to tobacco, controversial weapons, and predatory lending, used for firm-wide exclusions)
S&P Global Trucost	Temperature alignment
SBTi	Corporate climate targets
CDP	Carbon data, corporate climate targets and policies
Urgewald	Data on fossil fuel expansion (primarily thermal coal mining and oil sands expansion), used to support Fulcrum's net zero commitments and restrict exposure to misaligned activities in relevant funds
InfluenceMap	Data on companies' lobbying efforts on climate change to support stewardship
Bloomberg	Data on the sustainability profile of executive pay structures and company activities, to support stewardship
ESG for Investors	Publicly available data on potential share price upside from improving corporate sustainability used to support engagement

In certain areas where we believed data and tools were lacking, we have also collaborated on the development of new resources, such as the 'ESG for Investors' initiative, which provides free-to-use tools trying to assess the potential upside for companies if they were to improve ESG performance in line with peers, with carbon emissions identified as the most material ESG variable: https://esgforinvestors.com/.

The ESG for Investors platform also has portfolio optimisation tools that aim to quantify the trade-offs and synergies between reducing transition risk (e.g., by reductions in the implied temperature of a portfolio) and the risk/return/volatility characteristics of a portfolio. Fulcrum and Arvella Investors won the award for 'Best Sustainable Investment Education Initiative' at Investment Week's Sustainable Investment Awards 2022 for their work on this project. https://esgforinvestors.com/articles/detail/23/#.

More information on our approach can be found in our dedicated fund-level sustainability reports.

ESG Insights

How do you foresee ESG investing changing over the next few years? Are there any other emerging ESG issues you are looking at?

Key changes in the Responsible Investment policy in the last 12 months include addition of our commitment to the UK Stewardship Code, inclusion of our engagement policy (itself strengthened with regards to escalation), becoming signatories to the Net Zero Asset Manager alliance and thus considering how ESG is integrated from that stand point as well as embedding our Principal Adverse Impact considerations.

Please see our recent RI policy (which is reviewed quarterly) for more details.

What impact will new regulation have on ESG funds and their viability?

We see regulation as improving transparency and strengthening the sustainability credentials of certain funds. We were pleased that our climate change strategy has retained its classification as "article 9" under EU sustainable finance regulation, even as many funds in the industry have become downgraded. In our view, part of the problem stems from an undue focus in the market on average portfolio metrics (such that a fund can include both 'brown' and 'green' companies) – by contrast, we have designed our climate strategy such that every issuer selected for the fund is considered 'climate-aligned'. (We have explored this in more detail here and here).

One of our strategies in the Alternative Solutions team is also registered as article 8; following the completion of the climate alignment of directional long-term equities, mentioned above, we will also be exploring article 8 incorporation for our flagship diversified absolute return strategy.

We have also welcomed regulatory developments in the UK – in particular, the introduction of the 'long-term asset fund' (or LTAF), and we are developing a solution in this area with a strong focus on sustainability https://www.fulcrumasset.com/inst/uk/en/fulcrum-blog/a-new-world-private-market-innovation-for-dc/

Do you think the UN SDGs provide an adequate guide to sustainability?

The Sustainable Development Goals (SDGs) are a helpful and user-friendly framework that we use for mapping our ESG practices. An example of this is SDG 13: Climate Action which we specifically focus on in relation to our equity themes. Climate change is an issue that will have dramatic consequences for nature and society, and touches on many of the other SDGs, it is also an area that Fulcrum has prioritised from a risk and investment perspective. Additionally, our strategies align to the SDGs to varying extent (such as SDG 6, 7, 9, 11 and 17).

However, we prefer using a range of metrics (in addition to the SDGs) to set targets, measure progress and hold us accountable. These include frameworks such as Weighted Average Carbon Intensity (WACI) and temperature metrics. We are also in the process of developing KPIs in line with our SFDR requirements, which we will use to monitor our progress on ESG.

Has the quality of ESG ratings improved in recent years? Is there any evidence that ESG ratings have a direct impact on share price?

Improvement has occurred in recent years and that is evidenced by the recent downgrading of funds from SDFR Article 9 to 8 however, we feel more work can be done in this space.

We use different ratings and metrics for our own funds however in certain areas where we believed data and tools were lacking, we have also collaborated on the development of new resources, such as the 'ESG for Investors' initiative, which provides free-to-use tools trying to assess the potential upside for companies if they were to improve ESG performance in line with peers, with carbon emissions identified as the most material ESG variable: https://esgforinvestors.com/.

The ESG for Investors platform also has portfolio optimisation tools that aim to quantify the trade-offs and synergies between reducing transition risk (e.g., by reductions in the implied temperature of a portfolio) and the risk/return/volatility characteristics of a portfolio. Fulcrum and Arvella Investors won the award for 'Best Sustainable Investment Education Initiative' at Investment Week's Sustainable Investment Awards 2022 for their work on this project. https://esgforinvestors.com/articles/detail/23/.

Are you happy with the standard of ESG reporting and disclosure by companies? Are some sectors better at reporting than others?

How long is a piece of string? This has always been a bone of contention. For where we invest in listed equities we have in place a Proxy Voting Policy and we have also published our statement of support of the UK Stewardship Code on our website.

Other than through our voting efforts (examples below) we do not engage directly with companies. This is mainly due to the limited exposure we have to listed equities and the size and holding period of such holdings. However, from an ESG point of view we request and receive ESG metrics from our agreement with Sustainalytics and their work of collecting sustainability data from companies encourage increased disclosure and can influence corporate practice.

Case study – Glencore: voting escalation

We have also been discussing climate strategy with mining giant Glencore. The company has made progress on the issue in recent years, including by adopting a comprehensive 2050 net zero target. However, we remain concerned that the company's interim emission targets (particularly for the phase-out of its coal assets) are not aligned with science-based pathways for fossil fuel production (with the latest Intergovernmental Panel on Climate Change assessment report estimating coal usage must drop by 65-80% by 2030 in 1.5°C-consistent pathways with 'no overshoot') – which we have raised directly with the company. We have since opposed the company's energy transition strategy and the re-election of four directors at the 2022 AGM, where almost a quarter of shareholders also voted against the transition plan. Under the UK Corporate Governance code, the company is expected to formally respond to and consult with shareholders to better understand the rationale for voting dissent; we will be monitoring the response as part of future engagement.

Case study: Net zero collaborations

There is significant collaboration between the financial institutions that are members of the Glasgow Financial Alliance for Net Zero (GFANZ) – the umbrella organisation that co-ordinates the sector-specific net zero initiatives (such as the Net Zero Asset Managers Initiative, which Fulcrum joined at the beginning of 2022).

We were honoured to be invited to join the Portfolio Alignment workstream Group in GFANZ, highlighted by the UK Government as one of the 'key' workstreams within GFANZ. Members of our Management Board, investment and research teams have taken part in regular, weekly or bi-weekly meetings and workshops, alongside other representatives from leading financial institutions. This culminated in several publications throughout the year, including the publication of a significant new report: Measuring Portfolio Alignment: Enhancement, Convergence, and Adoption. The report aims to offer guidance on multiple technical aspects of aligning portfolios to a net-zero trajectory. We wholeheartedly welcome the report's emphasis on the importance of forward-looking metrics, and are proud to have our approach to equity portfolio construction featured as a case study in the report.

Case study: Driving the derivatives discussion

We have, since Q4 2021, joined the working group on derivatives and hedge funds from the investor practices programme of the Institutional Investors Group on Climate Change (IIGCC). The group's initial efforts focused on defining the avenues through which hedge funds can make a positive contribution to the low-carbon transition, and on specifying guidelines to help prevent 'greenwashing' in the reporting of emissions associated with long and short positions. We have contributed to the consultation that culminated in the publication of a discussion paper and report (available on their website here)and are seeking to expand our reporting to more explicitly incorporate the main recommendations of the working group. Going forward, we have suggested that the working group build on the initial report by looking more closely at specific types of derivatives (e.g. index options, or commodity futures).

Case study – Unlocking voting

We recognise, in line with the principles of the Stewardship Code, the importance of exercising the rights and responsibilities associated with our investments. One area we have identified relates to the synthetic exposure to equities (via derivatives). This asset class does not offer investors the ability to vote the underlying shares and therefore exercise the rights and responsibilities in a similar way to physical equities. At our company level, we are tackling this by an ongoing project to increase the percent of physical equities we own.

At the same time, we recognise one of the broader, market-wide ramifications of this issue – cases where no-one ends up voting on what can be a significant percentage of a company's outstanding share capital, if prime brokers do not instruct votes for the shares they nominally retain ownership of (although economic ownership has been passed onto other investors via derivatives). We have therefore been engaging with one of our main brokers on finding ways beyond this deadlock, not just for our derivatives shareholding, but potentially for a broader proportion of the broker's book. This is a complex issue without simple solutions (indeed, in certain markets, regulators explicitly require such 'broker non-votes'), and we are discussing ways to collaborate with different market participants on it.

Case study: Exploring the effects of market-wide risks

A risk may be pervasive, and yet impact sectors and industries differently. We were invited to explore the question of how climate change risks can affect derivatives and central counterparties, with Fulcrum contributing to a panel discussion organised at the World Federation of Exchanges' 2022 Clearing and Derivatives Conference, alongside speakers from the Financial Conduct Authority, the Bank of International Settlements and other industry participants.

What is the best way to avoid greenwashing from fund providers? How can an investor best differentiate greenwashed funds from the genuine article?

We believe intentionality and measurement are key concepts. For example, whether climate considerations are genuinely placed at the heart of portfolio construction, and whether they play a significant role in capital allocation. Our climate strategy imposes a climate 'filter' on each security selected, for example, rather than merely relying on the portfolio being green 'on average'. As explored in our papers on 'the tracking error error' and the 'carbon half-time show', an undue focus on portfolio averages creates the potential for greenwashing, whereby seemingly climate-aligned securities are in fact comprised of a majority of misaligned stocks. See more on this at the two links below:

https://www.fulcrumasset.com/inst/uk/en/fulcrum-blog/the-carbon-half-time-show/

https://www.fulcrumasset.com/uploads/2022/03/2c4d8387bb886c791ffc11d093ece137/fulcrum-the-tracking-error-error-why-climate-alignment-calls-for-bolder-steps.pdf?v=1648121160

Thorough due diligence is required here.

Is the quality of ESG data and company reporting/ disclosure an issue?

Standardising reporting will make a big difference.

We include a broad range of the below information in our materials (policies, annual reports and more regular client reporting on specific investments) to clients and on our website:

a) Commitment to being a UK PRI signatory
b) Impact reports where appropriate/applicable (for example in our Climate Change and Liquid Alternatives solutions).
c) Industry- and asset-class-specific criteria we follow (TCFD and GRESB for real estate investments)
d) Our Responsible Investment policy
e) A description of the investment process and how ESG is integrated.
f) A list of our main investments and holdings.
g) ESG case studies/examples of existing strategies.

We also produce an annual Sustainability report for a number of funds and an annual Stewardship Code submission.

Biodiversity is a hot topic at the moment. Have you done any work on this and what conclusions can you share?

We are looking at avenues to add green space, which promote biodiversity as well as designing the office to include more social and collaborative areas. We are looking at reducing this even further by engaging with our building manager on renewable energy, understanding the waste management of the firm and improving firmwide sustainability practices.

We are in the midst of creating KPIs at the back of Principal Adverse Impact Indicators (aligned with SFDR regulation). We have signed a contract with our data providers and will aim to roll this out towards the end of the year. Please refer to our Stewardship report here.

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