FIDELITY INSTITUTIONAL INSIGHTS

# ESG Investing

## An Advisor's Guide to Strategies, Paths, and Approaches


**Rick Smyers**
Managing Director
ESG Pro and Fidelity Labs

**Inna Rivilis**
Director
Practice Management
and Consulting
Fidelity Investments

**Sarah Gelfand**
Vice President
FC Trustees Initiative and
Philanthropic Consulting
Fidelity Investments


ESG investing is far from a passing fad. In reality, it has evolved from being a specialized focus for a narrow subset of investors to an approach that has become a mainstream favorite. Morningstar CEO Kunal Kapoor put it aptly when he called ESG investing "the new normal." But even so, many firms have yet to learn to navigate the ESG landscape, and are uncertain about how to actually adopt and implement ESG investing. They want to be in a position to offer ESG to their clients—but are unsure how to get started in what seems like a complicated and evolving ecosystem.

With that in mind, this paper helps define ESG options for advisors (Exhibit 1), presents a snapshot of approaches for integrating ESG into one's business, and presents examples from firms that have made the transition to offering ESG to clients. In some cases, these firms offer ESG as a complement to their current investment approach and in others it is a larger focal point of their business.

### How Advisors Approach ESG Investing

There is not one ideal road map for incorporating ESG into your business. In fact, there are multiple paths advisors can take. Ultimately, the approach a firm chooses should be guided by their investment objectives and the needs of their clients. For example, some advisors offer ESG portfolios as one item on a much broader menu of investment offerings. Although ESG may not be their specialty, they develop the capability a la carte because it is a priority for some of their clients and prospects. In other cases, ESG is central to an advisor's mission: Most—if not all—clients are fully invested based on environmental, social, and governance factors. In this case, ESG is not a complement to, but instead is core to their offering and the firm's staff and advisors have special expertise.

**EXHIBIT 1: ESG investing incorporates environmental, social, and government factors into the investment process**

| **Environmental:** Sustainability and resource efficiency | **Social:** More equitable societies and respect for human rights | **Governance:** Accountable governance and transparent operations |
|---|---|---|
| Climate Change | Labor Standards, Health, and Safety | Executive Incentive Structure |
| Greenhouse Gas Emissions | Fair Treatment of Minorities | Board Diversity and Independence |
| Resource Depletion | Diversity, Employee Engagement | Transparency and Disclosure |
| Waste and Pollution | Supply Chain Management | Lobbying/ Political Contributions |
| Energy Efficiency | Local Community Impact | Bribery and Corruption |
| Alternative Energy | Data Protection/Privacy | Business Ethics |

Source: Compilation from United Nations Principles for Responsible Investment (UNPRI), CFA Institute, and the Sustainability Accounting Standards Board (SASB). As of Dec. 31, 2018.

Below, we will look at how four firms approach ESG investing, including where they fit along this continuum of delivery options and how they use ESG to meet their clients' investment needs.

## Offering ESG as a Capability

**Barry Investment Advisors, Headquarters:** New Bedford, MA
**AUM:** Approximately $602,000,000 as of 10/31/20

Patrick Barry, managing director of Barry Investment Advisors, started thinking seriously about values-based and ESG investing a few years back, when issues such as fossil fuels and climate change began creeping into more conversations with clients. "They occasionally would ask us to exclude a company, or even an entire sector that they felt was doing harm or didn't mesh with their values," he said. According to Barry, this desire to align values and investing was one that coincided well with his own preferences.

"Why wouldn't you want to have a better corporate citizen as an investment holding, compared to not having that?" he said.

"We have a suite of things that we do well. We look at ESG as one of our capabilities, one of our offerings for an important subset of our existing clients."

—**Patrick J. Barry**, managing director, Barry Investment Advisors

"We are not a firm that is known for ESG. But what we are known for is an ability to meet clients where they are and provide customized solutions that make sense based on what they care about."

—**Jennie Sowers**, partner and private wealth advisor, KORE Private Wealth

As a result, Barry added ESG as "an additional capability for clients who want it." While he wasn't in the market for a new guiding investment philosophy—the firm was already established with a value-oriented investment approach—that didn't stop him from finding a solution to satisfy clients who were interested in ESG.

In addition, he keeps his approach simple by using a third-party ESG specialty asset manager that uses data analysis and tools to personalize model portfolios based on values Barry is "excited" about. Even if ESG is not at the center of his approach, Barry believes that "corporate citizens are going to be better investments in the long run."

**KORE Private Wealth, Headquarters:** New York, NY
**AUM:** Approximately $4,000,000,000 as of 10/31/20

When KORE Private Wealth emerged from the private banking arm of a major wirehouse in 2018, the timing of their launch as an independent firm coincided with growing demand from clients for more in the ESG space. According to Jennie Sowers, a partner and private wealth advisor at KORE, the firm's desire to offer a robust ESG option was not necessarily aimed at broadening their array of services. Instead, it was meant to help them customize their offering to meet clients' specific needs.

"Historically, we always felt that the ESG or socially responsible investment options available to us were somewhat pre-packaged," Sowers acknowledged. "Essentially, clients were given products where the values were selected by someone else, and we wanted to find an opportunity to allow clients to tailor their ESG investments to fit their own values."

Sowers rarely uses the term ESG "because a lot of our clients don't know what it means. But many do know what's important to them in various aspects of life. We can tailor investments to their life values. And what better way to customize investments than to do so based on issues that mean something to them?"

"ESG data keeps you on track with relevant information about the company you are investing in. Investing without it is like driving without using your car's GPS. Why wouldn't you use it?"

—**Jeff Gitterman**, co-founder, Gitterman Wealth Management

In order to create portfolios based on ESG criteria without necessarily wading fully into the water with data management and a fleshed-out ESG rating system, KORE Private Wealth partnered with Ethic, a tech-driven asset manager that builds separately managed accounts (SMAs) aligned with a firm or client's investment allocation. According to Sowers, this capability has helped KORE Private Wealth's clients envision the value of ESG. "Very often a client doesn't necessarily come to us and say, 'Hey, my most important priority is ESG investing.' But when we talk about the concept of values alignment and the tools we have to bring them toward that—very often they want to head down that road."

### Leading with ESG

**Gitterman Wealth Management, Headquarters:** Edison, NJ
**AUM:** Approximately $529,000,000 as of 10/31/20

In 2009, Gitterman Wealth co-founder Jeff Gitterman released a book called *Beyond Success*, about bringing values and virtue back into business. In 2014, he helped produce a documentary film called Planetary, about the interdependence between people and the planet. Both of these projects were part of Gitterman's dawning awareness that "what I was doing in my business was different than what I was doing in my personal life. I realized they were not aligned around some of the things I really believed in, like addressing climate change."

A few years later, he started down the path of realigning his book of business so that ESG was fully integrated across accounts. Over an 18-month period, Gitterman converted his entire client base to ESG investing. It helped that the bulk of his clients were college professors who, he felt, were predisposed to accept the science behind ESG investing. It also helped that he had a clear rationale for embracing ESG.

"We say that ESG is about investment value ... whereas other approaches [like socially responsible investing (SRI)] are about personal values. Everyone wants value when they invest, but not everyone wants to put their values in their investments—and that's fine," he said. "When you look at it like that, then there's no reason not to do it."

"We've seen that people who invest in things they are connected to from a values standpoint are much more likely to be fully engaged, and many times they stay invested over the long term."

—**Steve Distante**, chairman and founder, Vanderbilt Financial Group

Gitterman considers ESG investing to be the foundation of a good portfolio, in part because he said it helps investors avoid the potential pitfalls and earnings risk associated with things like poor corporate citizenship and ethical or financial missteps by executives and organizations. To put that idea into action, he and his team do the hard work of building ESG factors into the core of their investment process, in part "by using information that is becoming more readily available every day, through big data and artificial intelligence (AI), to screen and make decisions about the stocks our clients want to own."

His approach appeals to his clients—and in some cases to their children, too. According to one Fidelity study, 77% of millennials are interested in ESG investing, something that Gitterman has witnessed firsthand: "When these next-generation kids see the work that we're doing," he said, "we've been able to retain some that normally would have left and gone with their own advisors."

Gitterman said that the appeal of ESG to younger investors is yet another facet of the value that ESG investing delivers for his firm.

**Vanderbilt Financial Group, Headquarters:** Woodbury, NY
**AUM:** Approximately $5,000,000,000 as of 10/31/20

Founded over 50 years ago and headquartered in Long Island's first LEED Platinum Office Building, Vanderbilt Financial Group is known as "the sustainable broker-dealer and RIA committed to investing with purpose." ESG (as well as impact investing and sustainable investing) is the firm's raison d'être.

It is no surprise, then, that Vanderbilt's founder and chairman, Steve Distante, is a public advocate and vocal proponent of ESG and global impact investing.

"The world's changed in that we value companies now not only from a profitability perspective, but also based on the practices that they're incorporating in their business," Distante says. "[The ESG factors] are important, in large part because they have a bearing on how successful a company will be in the long-term."

As part of Vanderbilt's mission "to be the most Impactful BD and RIA in the industry," he suggests that advisors can align ESG criteria with the United Nations Sustainable Development Goals (SDGs), which are 17 areas that address issues such as human rights, gender equity, health care, and education, as well as preservation and conservation. Why the SDGs? In part because about 40% of the G250 (the world's largest 250 companies) acknowledge the SDGs in their corporate reporting. But even more, Distante says, "because they provide a framework and common language for companies to integrate sustainability information into their reporting cycles."

Vanderbilt's advisors use screening tools as well as active engagement with companies to help deliver on clients' individual objectives. Distante himself is embarking on a project that uses artificial intelligence (AI) to create ESG portfolios that align with the specific issues clients are interested in.

According to Distante, "ESG investing is about giving people choices and giving them a vision of the future. What are the outcomes our clients want to help effect? Whatever they are, it gets them engaged in the process and creates common ground between them and their advisor."

## Steps for Getting Started

### 1. Decide on a rationale for ESG

Getting over the starting line with ESG investing requires articulating your rationale—including how ESG fits into your existing offering and investment approach and why it will help your clients.

For example, KORE Private Wealth went through a structured process to develop a mission statement and value set as part of their process for getting started in ESG investing. Their rationale was simple: to meet clients where they are and present personalized solutions that coincide with their values.

Jennie Sowers put it this way: "Many of our clients are thinking about the defining issues of our time, like climate change and racial justice. To the extent that we can have a tool to invest in companies that are doing their part there, it's fully in keeping with our overriding mandate to make ESG a component of what we offer."

KORE Private Wealth went on to select six pillars that encompass key ESG themes clients can use to personalize their portfolios. In particular, the strategy centers on issues relating to climate change, women's rights, health and wellness, education, pollution, and racial justice.

KORE Private Wealth structured their ESG offering in a way that was consistent with how they were building out their overall firm—its early adoption of and alignment with Ethic is one of many innovative solutions that the firm is offering their clients. For some other advisors, particularly those that specialize more exclusively on sustainable investing, ESG itself may be at the core of their value proposition, as opposed to playing a supporting role. Regardless, the rationale for ESG needs to be clear and form the basis for how the firm structures their investment offering.

**Three questions about rationale**

- Why do you want to offer ESG investing as a firm, and what goals will it achieve? Do you want to add an offering to stay relevant to evolving investor needs?
- How does it align with your firm's existing philosophy and approach?
- How will you define success with respect to your firm's ESG strategy?

3 Approaches to ESG Investing

- Leverage existing resources
- Partner with a specialist
- Build your own solution in-house

## 2. Approaches to ESG Investing

After determining your rationale for ESG investing, moving forward requires some exploration and set-up to guide implementation. While this may be an ongoing pursuit, firms can begin by weighing the benefits and deterrents of a DIY, go-it-alone approach; partnering with specialists that deliver ESG solutions; or finding that "middle ground" and utilizing existing, publicly available tools and models to customize an approach for investors.

### Leveraging available resources to build a customized approach

For some firms, the "dip our toes in the ESG pool" method is the right first step. Firms can start small by engaging with fund partners, identifying thematic products, and exploring existing ESG mutual funds (sometimes through model portfolios offered by other providers). There are technology tools and solutions available that allow you to scan the universe of existing, publicly traded mutual funds for ESG criteria, giving advisors the ability to identify and customize their offering to investors.

### Partnering with a specialist

Some firms may decide to partner with a specialist to offer ESG investing to a subset of their clients. While not relevant to every account under management, these firms (like KORE Wealth and Barry Investment Advisors) view ESG as one of several important priorities in their investment portfolio.

Firms may look to specialists to:

- Provide tools to implement a customized set of exclusions/tilts based on a client's values
- Help with construction of pre-defined ESG portfolios
- Provide consolidated financial and ESG reporting data

### Delivering ESG solutions in-house

Other firms, like Gitterman Wealth and Vanderbilt Financial, consider ESG and values-based investing to be a priority or even a core purpose of the firm. In this case, most or many of their client portfolios are ESG-integrated.

In addition, many or all of their advisors are "all in" with ESG. The transformation to an "all-in" ESG firm doesn't happen overnight. Over time, these firms have gained the expertise, and invested in the data management and due diligence systems—as well as the operational infrastructure—to become ESG specialists.

### Making a direct impact

Oftentimes, ESG is lumped underneath the bigger, socially responsible impact investing umbrella. Advisors and clients need to be really clear about how they want to move forward in this space. If an advisor's goal is to help clients reflect their values using their wealth and resources, they may have to go further than ESG investments.

Contributing directly to non-profit organizations, businesses, or charities that clients care about may satisfy the client's goal of having a direct impact on an important cause. Consider engaging with philanthropic specialists to help clients take that next step.

### Thoughts to consider when choosing an approach

Most firms will be closer to the left side of the spectrum. Regardless, it is important to identify where you want to be on the continuum in order to proceed appropriately to build an ESG capability.

### Three questions about approach

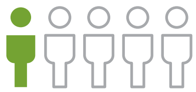
- Where does your firm see itself on the ESG spectrum: Will you outsource ESG investing, use a do-it-yourself approach, or help investors make a direct impact?
- What resources will you need to be successful? (Presumably, you will need more resources and expertise if you are not working with a third party.)
  - Are you willing to hire more staff, train and educate them differently, buy new data sources, etc.?
  - What is your time frame for launching even a "minimum viable product" ESG offering?
- How will you measure success?

## 2. Get your firm ready for ESG

According to a 2020 survey by the Financial Planning Association, nearly one-third of advisors plan to increase their use and recommendation of ESG funds over the next 12 months, up from 19% in 2019. Still, that leaves most advisors on the sidelines. Why is that? According to Vanderbilt's Steve Distante, ESG investing still isn't on the radar as a priority for many advisory firms. Some advisors may also be reluctant or uncomfortable raising the topic with clients and discussing values.

"While most of us are aware that ESG is out there and rising in prominence, many don't have it at the top of their list just yet," he said. "And you can't just force it. Advisors need to get there themselves."

That's where training and education come in, focused on generating excitement around ESG offerings while offering insights that will establish a comfort level for advisors with value-based investments. Distante is something of an expert on the topic. He founded a free, online community for investors, financial advisors, and entrepreneurs. The platform offers online training modules, and certification for those who are inspired to dive into ESG and impact investing.



**1 in 5 investors** are willing to pay more for an advisor who offers more socially responsible, or ESG, investing.

Source: The 2019 Fidelity Investor Insights Study

Training and education are also available through industry conferences, including the Sustainable Investment Conference hosted annually by Gitterman Wealth Management, which began in 2016 with 120 participants and grew to 1000 participants in 2019. Other avenues for training include peer coaching and support from other advisors, as well as outside consultants and coaches who are steeped in the ESG landscape.

In fact, when Gitterman was first transitioning his own business fully over to ESG, he brought in consultants to help educate advisors and coach them through the change.

Even beyond education, Distante believes that client demand is what may ultimately nudge many advisors over the edge.

"My advice for advisors who are not currently taking this trend into account yet is this: Even if it has not been a priority for you in the past, your clients care about having sustainable impact [through ESG] and they want it reflected in how they invest."

**Three questions about approach**

- Are my advisors on board with ESG investing? What concerns might they have?
- How do you plan to get your advisors ready to discuss these topics?
- What training and education is needed for all staff (process and operations, new intake forms, new workflows, etc.) to generate excitement within the team and help them be successful?

### 3. Introducing ESG to Clients

Some advisors may be tentative in their approach to ESG investing because they are less accustomed to having conversations about values with clients. They may not know where to begin or how to avoid the political and cultural landmines that come with discussing a client's specific ESG orientation and priorities. Patrick Barry, of Barry Investment Advisors, suggests that it's wise to take your cues from the clients themselves.

"Clients who have been investing a certain way for decades may feel that a shift to ESG would be a big change," Barry says. He prefers approaching the topic in an organic way: "Talk to them about the causes they're into. What are their special interests and the things they care about? Do they have any exclusions or companies they don't like? It's a natural part of getting to know them."

Gitterman suggests beginning with the basics when it comes to uncovering client needs: "Do they get involved in specific philanthropy? Do they have a donor advised account where they are looking for impact, yet the investments are not very impactful? What are their kids interested in?"

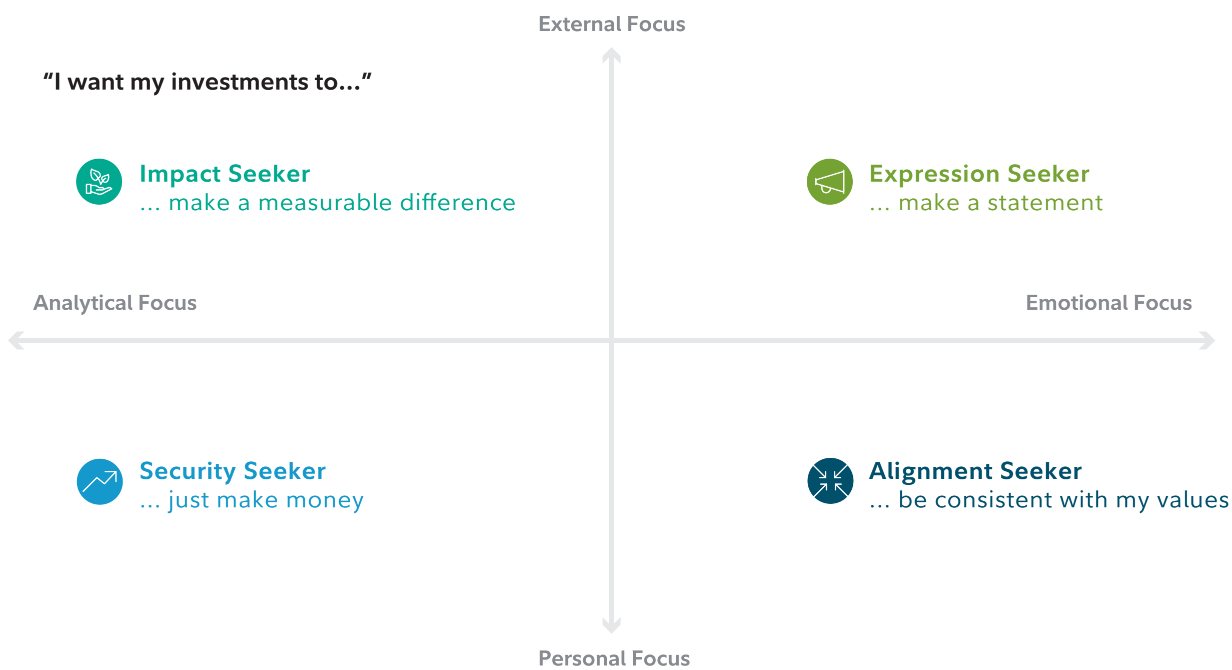
You have to get to know what your clients want and understand what they're looking for, Gitterman asserts. After that, "it's up to you to add value to the conversation through your expertise." For instance, "You can have a low carbon portfolio that has [an oil company] as a top holding. But try giving that to a client that actually asked for a fossil fuel-free portfolio? These are two different things."

### Understanding clients' values

It's important that advisors recognize that their clients might be on an ESG journey, too, and it can be helpful for an advisor and client to work together to clarify which assets (e.g. retirement, charitable, other) are the best place to start, how much is the right amount to start with, and what would the client need to see to allocate more assets over time. Fidelity's four "ESG mindsets" can help advisors understand their clients' motivations for ESG and value-based investing, and guide them to have more productive, meaningful, and engaging client conversations.

These mindsets are featured in Fidelity's latest software solution, ESG Pro, designed for the independent financial advisor to help build an ESG investing practice.

**EXHIBIT 2: Fidelity's ESG Mindsets Can Help Advisors Understand Their Clients' Motivation Around ESG Investing, Allowing Them to Tailor Their Conversations to Be More Meaningful and Relevant**




Source: Fidelity Investments.

Gitterman also advises being able to articulate to clients and prospects why your firm is offering ESG investing. "You should be able to tell that story," he said. For Gitterman, telling that story happens not only through the conference the firm hosts, but also through speaking events and interviews, content on their website, blog posts—some with over 20,000 views as well as social media posts on LinkedIn.

### Communicating and Marketing Your Offering to Clients

- Clearly articulate your ESG investment offering on your website

  Different firms position ESG for different audiences and mindsets. ESG tends to be associated with more progressive themes, but it can also work well with more conservative clients. Think about concepts that are important to all of your clients. Words like "stewardship," "community," "preservation," and "values" can resonate with a wide audience and may be less politically charged.

- Develop a social media strategy that shares ESG-related content with investor audiences
- Schedule frequent communications to clients and prospects through email campaigns, newsletters, etc.
- Hold virtual events, webinars to discuss ESG investing, or small client seminars to discuss relevant ESG topics

Through all of this, Gitterman says: "I am able to tell clients why sustainable investing is so important to me, and I think they find it interesting and compelling from an investment standpoint."

**Talking to Clients and Prospects about ESG Investing**

The more familiar you are with the issues that are most meaningful to clients and prospects, the easier it will be to talk about values-aligned investment strategies, including ESG. It's not a one-time conversation, but an ongoing part of your deepening relationship with the end investor. Conversation starters can include:

- What types of philanthropy or charities mean the most to you?
- Are there social issues that are important to you and your family?
- As a consumer, what do you find important in the businesses and platforms you frequent?
- What do you enjoy doing (hobbies, pastimes, etc.)?
- What else is important to you?

Regardless of where ESG investing fits within your value proposition—be it central or peripheral—using it as a conversation starter with prospects and a way to serve existing clients better can only help to clarify the value you offer as a firm.

**Three questions around introducing clients to ESG**

- Do you know your client's interests and the issues they care about?
- Do you have values-based questions as part of the client intake process or as part of your regular conversations with existing clients?
- Can you articulate to clients why you are offering ESG and why it is an investment option that might be right for them?

There are many ways to incorporate ESG investing options into your practice. If you're looking for additional guidance, you can read Fidelity's white paper, *ESG Investing for Advisors: Having Better Conversations with Clients*.

Fidelity also has several values-based investing and philanthropic products and solutions that advisors can access. To learn more, contact your relationship manager.

## ESG INVESTING TERMINOLOGY

ESG Investing: ESG stands for environmental, social, and (corporate) governance. While ESG investing encompasses varying terms and methodologies, Fidelity defines it as an investment discipline that incorporates ESG factors into an investment approach or decision-making process.

ESG Integration: Incorporates ESG factors explicitly into investment decisions to help better identify risks and opportunities.

Greenwashing: Conveying a false impression or providing misleading information about how sustainable or environmentally sound a company's products or practices really are.

Materiality: The Sustainability Accounting Standards Board (SASB) defines materiality as "information that would be considered decision relevant to investors." ESG's focus on materiality enables investors to align investing strategies with the ESG issues that may impact the performance of a company or industry.

Negative screening: Excludes investing in companies with practices that clients disagree with, often industries related to tobacco, gambling, fossil fuels, and weapons, among others. This approach was first popularized by socially responsible investing (SRI).

Positive screening: Maximizes investments in companies with high ESG ratings and positive environmental, social and governance practices.

Socially Responsible Investing: Socially Responsible Investing (SRI): Also known as sustainable investing, SRI uses screening to eliminate or selecting investments according to specific ethical guidelines that promote ethical and socially conscious themes.

## Authors

**Rick Smyers**

Managing Director
ESG Pro and Fidelity Labs

**Inna Rivilis**

Director
Practice Management
and Consulting
Fidelity Investments

**Sarah Gelfand**

Vice President
FC Trustees Initiative and
Philanthropic Consulting
Fidelity Investments

**ENDNOTES**

[1] How Advisors Can Tap into the Growing $23T ESG Market By Tobias Salinger Financial Planning, June 14, 2018, https://www.financial-planning.com/news/how-financial-advisors-are-using-esg-investments

[2] Get study citation from the exhibit shown in the 2020 ESG Webinar with Dave King and Nicole Connolly

[3] https://corpgov.law.harvard.edu/2018/10/04/un-sustainable-development-goals-the-leading-esg-framework-for-large-companies/

[4] https://www.financialplanningassociation.org/sites/default/files/2020-06/2020-Trends-in-Investing-Report-v5.4.pdf



953724.1.0 1.9899726.100