3rd Sir Oliver Hart Conference on Sustainable Investing

The Engagement Channel

Paper: Are all ESG funds created equal? Only some funds are committed

Lowry, Wang & Wei

Remarks: Jessica Jeffers

HEC Paris, CEPR

Roadmap

1. My takeaways
2. Three questions
3. Engagement in private markets

“Are all ESG funds created equal?” – Key Takeaways

1. Talk of “ESG funds” is too broad
   - Conflating different models of sustainable finance is misleading when assessing impact, process
2. Funds vary widely in engagement
   - Some engage a lot, others don’t. Why? Incentives
3. Engagement is a suite of behaviors
   - Voting; asking questions; gathering information; holding long term; holding concentrated shares
4. Engagement is a critical channel through which to influence companies
   - Sizable effects on company behavior, especially after a scandal (much more than exit)

1. Who sets the incentives?

- Only funds with incentives to engage have impact. What determines these incentives?
- "Incentive-to-Engage" measure depends on concentration and flow sensitivity
  - Not specific to ESG! Although within ESG funds, concentration and sensitivity in ESG holdings
- Is concentration a deliberate strategy, to align with engagement model?
  - Or can non-strategic constraints or factors create the incentives, which then drive the engagement?
- Does not seem random: committed funds have more ESG words in prospectuses
  - Also higher ratings on Morningstar Commitment and other measures

2. Why do different ESG models coexist?

- Different beliefs that manifest in investment strategies

- Whose beliefs? Fund managers, or capital providers?
  - Equity portfolio managers report feeling constrained on ES they can do (Edmans, Gosling & Jenter 2025)
  - But same paper highlights manager beliefs are more important than fund label for degree of ES

- Other constraints from underlying investors, fund families, markets served, or target impact?

- To create a more complete market?

3. Is sustainability special?

- If we sorted on a different investor preference, would takeaways be the same?
  - Incentive-to-Engage is not specific to ESG
  - Is the engagement channel equally important for any shareholder preference?

- Prior: engagement is especially important for sustainability

1. Wide dispersion of preferences and beliefs → grounds to engage
2. Rapidly evolving environment → unforeseen circumstances (Gilson, Sabel & Scott 2010)
3. Incomplete markets → no “homemade leverage” equivalent for most ESG preferences

Engagement in Private Markets

- Private markets present unique opportunities for sustainable investing
  - Relatively small amounts of capital can be pivotal
  - Culture of investor involvement in portfolio companies
  - Financing for next generation of companies and emerging markets

- Conditions are conducive to engagement
  - Relatively long term (funds typically have 10-year horizons, hold deals for several years)
  - Concentrated holdings
  - Information can be hard to obtain ex ante, but can contract for information rights

Engagement in Private Markets

- LPs in impact funds contract heavily around engagement (Geczy, Jeffers, Musto & Tucker 2021)
  - Advisory committees are ubiquitous; weigh in on investment strategy, due diligence, approve investments…
  - Relate this to braiding theory (Gilson et al. 2010) but also need for flexible contracting (e.g. Hart & Moore 2008)

- Different models coexist and target different impact (Brown, Cole, Jeffers & Klein 2025)
  - E.g. impact-first funds that target social issues in emerging markets and intervene less in PCs, vs "collinear" funds that target clean tech and intervene more in PCs
  - Incentive to engage may depend not only on incentive structure but also on nature of PC and impact target

Conclusion

- Engagement is an important channel for incorporating shareholder preferences into capital allocation
  - Manifests across markets (publicly-listed and private), but not for all funds
- What determines incentives to engage?
  - Beliefs (whose)?
  - Type of company, target impact?
  - Other investment features, e.g. access to exit, information, holding period?
- Looking forward to a great discussion!