MANAGED FUNDS ASSOCIATION

AIMA

April 1, 2019

Ms. Raluca Tircoci-Craciun
International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
Spain

Re: **AIMA and MFA Response to IOSCO's "Sustainable finance in emerging markets and the role of securities regulators" Consultation Report**

Dear Ms. Tircoci-Craciun:

Managed Funds Association[1] ("MFA") and the Alternative Investment Management Association[2] ("AIMA") (collectively, the "Associations") welcome the opportunity to respond to IOSCO's consultation report on sustainable finance in emerging markets and the role of securities regulators. Sustainable finance is an important topic for the alternative investment management industry, and the role of emerging markets in this area has too often been overlooked.

Alternative investment managers are often an important source of investment for many emerging markets, investing in everything from their currencies to their start-up companies. At the end of 2018 roughly 17% of global hedge fund assets under management were invested in strategies focused on emerging markets.[3] Further, sustainable finance and responsible investment are growing

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1 MFA represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

2 AIMA is the global representative of the alternative investment industry, with more than 1,900 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programs and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council ("ACC") to help firms focused in the private credit and direct lending space. The ACC currently represents over 100 members that manage $350 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialized educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

3 BarclayHedge, *Hedge Fund Industry Assets Under Management*, 2019. https://www.barclayhedge.com/solutions/assets-under-management/hedge-fund-assets-under-management/

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The Alternative Investment Management Association Ltd

in importance as topics for the alternative investment management industry. In AIMA research published last year half the alternative investment managers surveyed indicated that they had experienced increased interest in responsible investment from their investors in the preceding 12 months.[4]

Investor Driven Approach

While many asset managers and asset management strategies have incorporated environmental, social and governance (ESG) factors in their investment process, not every investor and not every investment strategy incorporates ESG. Rather than recommending that ESG factors be incorporated by asset managers, we encourage IOSCO to develop guidance that will assist interested investors in selecting investments that include ESG factors.

We believe that policymakers can best achieve this result by creating incentives for investors on the demand side of the asset management process rather than imposing requirements (especially any proscriptive requirements regarding factors which must be applied as part of an asset manager's fiduciary obligations) to asset managers on the supply side of the asset management process. When designing incentives for investors to incorporate ESG factors into their investments, policymakers should recognise it may be impracticable to incorporate all ESG factors into every investment. We believe any approach should balance the goals of capital markets efficiency, financial stability, and sustainability over time.

To help facilitate this investor driven approach, we suggest adopting a framework for investment managers to provide a client or prospective client with general information on what the composition of a fund or portfolio managed by that investment manager might look like in practice. This would then lead to a more detailed discussion with the client around whether that investment strategy would meet the prospective investor's investment objectives and ESG preferences. When an investor does not have such preferences, this approach would permit the investment manager to continue to provide products or services to the investor consistent with the investor's non-ESG preferences.

Because ESG-related issues can be important for some, but not all institutional investors, we suggest a slight amendment to Recommendation 10, and request that IOSCO recommend that institutional investors incorporate ESG-specific issues *when relevant*.

ESG Data

Even with respect to investors and asset managers that have adopted or are seeking to adopt ESG into their investment strategies, the adoption of sustainable investment faces several hurdles. IOSCO is right to highlight one of the greatest of those hurdles: the lack of reliable data on ESG factors. At present even companies in developed markets are only required to release some ESG data. Given the clear downsides to voluntarily releasing such data, issuers cannot reasonably be expected to reliably release it of their own accord.

This has created a situation in which the data necessary for the implementation of sustainable finance is expensive, inconsistent, or simply unavailable in even the most developed markets. Academic research has shown that the most common challenge to adopting sustainable finance is the lack of comparability between the reported ESG data of different issuers; ratings by third-party data providers can also be inconsistent. Without widely available, consistent data

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[4] AIMA, *From Niche to Mainstream: Responsible Investment and Hedge Funds*, 2018. https://www.aima.org/educate/aima-research/from-niche-to-mainstream-esg.html

alternative investment managers are often left with the choice of developing research capabilities in-house or paying for third-party data; both approaches involve costs that may be ultimately be borne at least in part by investors.

Further, a relative scarcity of ESG data in emerging markets could dissuade investment. As sustainable finance becomes more common more investment managers will need ESG data before making an investment decision. Should such data be relatively difficult to acquire in emerging markets, investment managers may be deterred from investing in them. This could cause serious damage to emerging economies and undermine the United Nations Sustainable Development goals.

As such, we are glad that IOSCO has recognised the necessity of ESG disclosures on the part of issuers. Sustainable finance—and regulation mandating it—cannot progress without a foundation of ESG data. Further, investors and asset managers must be able to have confidence that the sustainable products to which they allocate are indeed sustainable. Transparent, efficient markets benefit all participants. Securities regulators in emerging markets should be encouraged to require disclosure ESG data, with allowances made for the particularities of their individual markets.

I. Conclusion

Ensuring that investment managers have the data they need to invest in a sustainable manner in emerging markets is crucial not only to the development of sustainable finance, but also to the wider development of emerging markets. It is essential that emerging markets are involved in the formulation of global sustainable finance standards and that their needs are taken into account. We support IOSCO's drive to make ESG data more readily available, and to ensure transparency and accountability in the market for sustainable products worldwide. We look forward to working with IOSCO to accomplish this goal. Please do not hesitate to contact Benjamin Allensworth, Carlotta King, or Mark Epley of MFA at (202) 730-2600, or Adam Jacobs-Dean of AIMA at +44 20 7822 8380 should you have any questions.

Respectfully submitted,

/s/ Michael Pedroni

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