

# INVESTMENTS & WEALTH MONITOR

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## Surveys Show Advisors Underestimate Clients' Interest in ESG

*By Matt Belnap*



INVESTMENTS & WEALTH INSTITUTE®

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**C**erulli Associates observes several disconnects between the way financial advisors approach environmental, social, and governance (ESG) investing with clients and the willingness of retail investors to embrace this manner of investing. Advisors and asset managers must work to bridge these gaps and ensure that they understand the appetite for ESG investing among retail investors.

ESG investments have evolved from niche products that screen out certain companies or sectors, e.g., oil companies, to a range of investment methods that encompasses thematic products, ESG integration, impact investing, and active ownership. As the types of ESG investing broaden, responsible investing has made its way into the mainstream—and demand, especially among retail investors and financial advisors, has increased.

Asset managers have responded to the increased demand by doubling the number of ESG funds and exchange-traded funds (ETFs) from 250 in 2012 to more than 500 by the close of 2020. On the managed accounts side, asset managers are seeing increased demand from managed account program sponsors. In a 2020 Cerulli Associates survey, nearly two-thirds (59 percent) of managed account sponsors said that ESG investment solutions were the products they were most interested in adding to their platforms from an outside asset manager. Cerulli Associates anticipates that as sustainable investing becomes even

KEY POINTS	
<p>Advisors maintain a widely held belief that significant demand for ESG strategies among clients is a non-issue. Yet Cerulli Associates found that nearly half (44 percent) of households would prefer to invest in an environmental or socially responsible way. While by no means an overwhelming majority, this is a far cry from the “handful” of clients that advisors report proactively reaching out around the topic.</p>	<p>There is an opportunity for home offices and asset managers to better educate financial advisors about productive ways to broach the subject of ESG with clients. If home offices can show advisors that clients generally are open to discussing or implementing ESG solutions, and asset managers can provide them with tools and templates for successful conversations, fewer advisors will be held back by the “lack of client demand” hurdle.</p>

*More than half (58 percent) of surveyed advisors said this lack of investor demand was a significant factor preventing the adoption of ESG strategies, and an additional 14 percent reported that it was a moderate factor.*

more popular among retail investors, asset managers will look to capitalize with new investment strategies.

However, in conversations with financial advisors, surveys of asset managers, and surveys of retail investors focused on socially responsible or ESG investing, Cerulli Associates has noted several disconnects between the way financial advisors approach ESG investing with clients and the willingness of retail investors to embrace this manner of investing. For responsible investing to develop fully and grow in retail channels, advisors and

asset managers must work to bridge these gaps and ensure that they fully understand the appetite for ESG investing among retail investors.

## A CAUTIOUS APPROACH

In a 2020 survey, Cerulli Associates asked financial advisors about the reasons preventing them from adopting ESG strategies in their clients' portfolios. By far, the most prevalent response was a lack of investor demand. More than half (58 percent) of surveyed advisors said this lack of investor demand was a significant factor preventing the

adoption of ESG strategies, and an additional 14 percent reported that it was a moderate factor. Advisors maintain a widely held belief that significant demand for ESG strategies among clients is nonexistent.

Cerulli Associates believes that a possible reason for this belief is that most clients are not actively approaching advisors about ESG investing strategies. In numerous conversations with financial advisors about ESG and responsible investing, Cerulli Associates asked how many clients were proactively asking for ESG investment strategies or to implement responsible investing in their portfolios. Most advisors reported that only a handful of clients had reached out to them about ESG investing. In general, the experience was rare enough that advisors remembered vividly the few times it happened. As one advisor told Cerulli Associates, "I can count on one hand who has asked me about this." Cerulli Associates believes that this lack of proactive information-seeking by clients may fuel the perception among advisors that clients are not interested in ESG.

Advisors also report treading carefully around ESG and values-based investing due to potential political landmines with some clients. Several advisors, in conversations around ESG implementation at their practices, relate that they would hesitate to raise the subject of ESG investing with certain clients for fear of alienating them. This hesitancy springs from a belief among advisors (and by extension, their clients) that ESG investing is a liberal phenomenon and that bringing it up or implementing it with more conservative clients could have negative impacts on the advice relationship. As one advisor told Cerulli Associates: "At this point, it [ESG investing] wouldn't attract any clients for me. I'm not a conservative, I'm not a liberal, I am a libertarian. And most of my clients are the same." Cerulli Associates finds that many advisors see ESG

investing through a political lens, making it a non-starter for at least a portion of their client base.

### WIDESPREAD OPPOSITION TO ESG DOES NOT MATERIALIZE

In a survey of U.S. retail investor households, Cerulli Associates found that nearly half (44 percent) of households would prefer to invest in an environmental or socially responsible way. This is by no means an overwhelming majority, but it is a far cry from the "handful" of clients that advisors report proactively reaching out around the topic. Cerulli Associates believes that advisors generally underestimate the demand their clients have for ESG and should not interpret lack of proactive questions as a lack of client interest.

Additionally, Cerulli Associates believes that advisors need not fear alienating conservative clients if they decide to broach the topic of ESG investing with them. More than four-in-10 households (42 percent) report that they are neutral on whether they prefer environmental and socially responsible investing. Only 14 percent of surveyed households said that they oppose investing in an environmental and socially responsible way. Although there are certainly some clients who would oppose investing in this manner, clients are generally three times more likely to want to invest in an ESG manner than to not. Cerulli Associates believes that advisors need not fear alienating clients by having ESG investing conversations with them.

Cerulli Associates believes that there is an opportunity for home offices and asset managers to better educate financial advisors about the productive ways to broach the subject of ESG with clients. If home offices can show advisors that clients generally are open to discussing or implementing ESG solutions, and asset managers can provide them with tools and templates for successful conversations, fewer advisors will be held back by the "lack of client demand" hurdle.

### ESG IS NOT JUST A HIGH-NET-WORTH SOLUTION

Another common refrain that Cerulli Associates hears in conversations with advisors is that interest in ESG investing is limited to high-net-worth (HNW) clients. This sentiment is also shared by asset managers. As shown in figure 1, a Cerulli Associates survey found that two-thirds (66 percent) of asset managers expected high demand from HNW investors (those with more than \$5 million in investable assets). Another one-quarter of asset managers expected moderate demand from HNW investors.

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*Only 14 percent of surveyed households said that they oppose investing in an environmental and socially responsible way.*

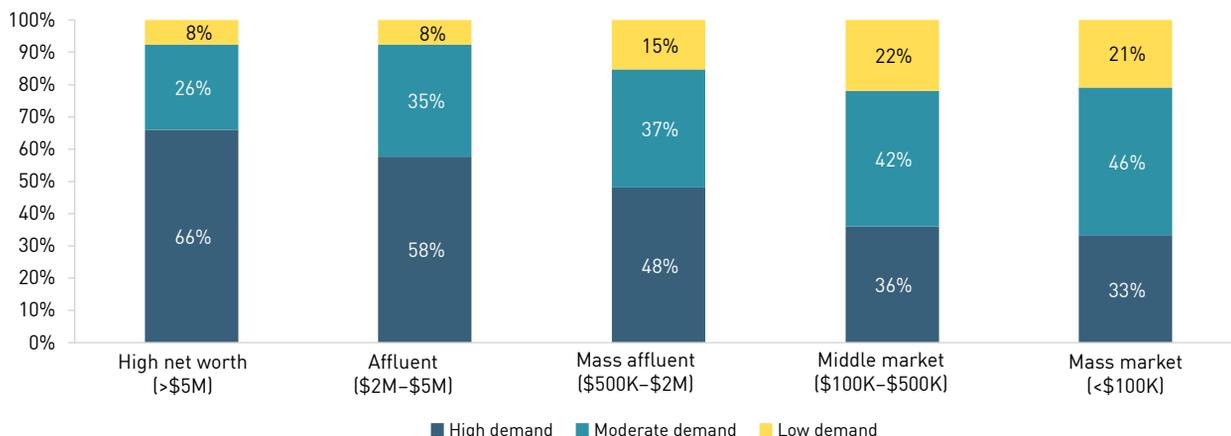
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Asset managers anticipate much less demand for ESG investment solutions from middle- and mass-market investors. Only 36 percent of asset managers anticipate high demand from middle-market investors (those with \$100,000-\$500,000 in investable assets), and only one-third of asset managers expect mass market investors (those with less than \$100,000 in investable assets) to demonstrate high demand for ESG investment strategies.

Table 1 presents survey data that shows that the expectations of asset managers and financial advisors do not necessarily match the preferences of retail investors. More than half (56 percent) of households with between \$100,000 and \$250,000 in investable assets agree that they would rather invest in companies that have a positive social or economic impact, and more than the 44 percent of all households agree that they would prefer ESG investing. HNW households were, in fact, the least likely wealth tier to prefer environmental and socially

Figure 1

### ASSET MANAGERS: EXPECTED DEMAND FOR ESG STRATEGIES IN THE NEXT TWO TO THREE YEARS BY WEALTH TIER, 2020



Asset managers view high-net-worth investors as the most likely to prefer ESG strategies; however, Cerulli Associates believes that this view discounts significant demand from lower wealth tiers.

Source: Cerulli Associates

Table 1

### HOUSEHOLDS PREFERRING ENVIRONMENTAL AND SOCIALLY RESPONSIBLE INVESTING, 2019

Prefers Environmental and Socially Responsible Investing	Household Investable Assets						All Households
	\$100K-250K	\$250K-\$500K	\$500K-\$1M	\$1M-2M	\$2M-\$5M	>\$5M	
Agree	56%	42%	44%	43%	41%	26%	44%
Neutral	35%	45%	43%	43%	41%	43%	42%
Disagree	10%	13%	14%	15%	17%	32%	14%

Despite the perception that ESG investing is a HNW phenomenon, Cerulli Associates has found significant interest exists among investors in lower wealth tiers.

Analyst note: Respondents were asked how they feel about this statement, "I would rather invest in companies that have a positive social or environmental impact."

Sources: Phoenix Marketing International, Cerulli Associates

responsible investing, with just more than over one-quarter (26 percent) of surveyed HNW households agreeing they would prefer to invest in that manner. By viewing ESG investing as merely an HNW solution, asset managers and advisors are discounting the interest from a broad swath of the investing public. Both asset and wealth managers should seek to make ESG investing more accessible across wealth tiers and not limit it to HNW investors.

#### OPPORTUNITIES FOR ALIGNMENT

A significant number of new ESG products that have come to market over the past half-decade provides ample opportunities for alignment among asset

managers, financial advisors, and clients. Advisors now have multiple ways to access ESG products and strategies, be it through an ETF, mutual fund, or separately managed account wrapper. This should provide advisors with an extra degree of comfort. Instead of having to use an unfamiliar vehicle, they can access ESG investments using the wrappers they are used to.

Most of the aforementioned product development has happened in domestic U.S. equities, which present the easiest point of entry for advisors looking to unlock the ESG space in client portfolios. Advisors who are more sold on ESG have an opportunity to use core equity offerings, and those who want

to dabble around the edges can use tactical allocations to specific ESG factors that may be in favor, e.g., solar power or board diversity. As product development continues in the space, and data on foreign companies' ESG practices comes into greater focus, advisors should monitor these developments and be prepared to make greater allocations to international equity products in the future as more investment options become available. 🟡

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