Impax chief Simm tracks trends in sustainable investing

By **Luke Jeffs**

More than twenty years after Ian Simm formed Impax Asset Management to invest in companies designed to expedite the transition to a sustainable economy, the chief executive has a lot to reflect on as the world faces life after COVID-19.

The London-based asset manager performed relatively well in the early part of the year, with inflows of almost £1billion in the three months to the end of June - the peak of COVID-linked volatility – to take its assets under management above £18bn.

The Aim-listed firm's share price fell in line with the market in March to about £2 but beat its peers by bouncing back to £4 by the end of May and staying there since.

The pandemic has posed some interesting questions about the robustness of the incumbent investment strategies. It has also cast the spotlight on the business of environmental, social and governance (ESG) investment which has in recent years become popular among firms keen to demonstrate their ethical investment credentials to increasingly discerning customers.

Simm, who launched Impax before ESG existed as a term, is understandably sceptical about the influx of 'ESG' managers because his message has been consistent for more than two decades: "We have a distinctive investment philosophy - focused on investing in companies and assets that are well positioned to benefit from the transition to a more sustainable economy."

Simm believes sustainable investing is not desirable, it is necessary.

"As the world's population grows from where it is today to a larger number, more and more people are consuming more and more resources to support higher standards of living and more people are moving to cities against the back-drop of a finite planet with increasingly vulnerable air and water quality, increasingly scarce resources and an unstable climate.

"Against that back-drop, it is necessary and, to a significant degree inevitable, that society will find a way to adapt to those constraints, to become more environmentally aware and more efficient in the way that resources are being used," he said.

One objective for investors is to spot firms that have the best solutions in sectors such as water supply, water treatment, recycling, energy efficiency or sustainable food.

Another is to divest those firms that are not prepared for the transition: "There are risks in other parts of the economy that are not sustainable, where companies may be threatened and ultimately go out of business. Obvious examples are businesses involved in the supply of fossil fuels, certain types of materials such as steel and cement that require a high degree of pollution for their manufacture or companies making chemicals that are subject to new regulation."

For Simm, the strategy is about delivering consistent returns: "What makes Impax special is our firm conviction that this investment philosophy is a clear way of signalling opportunities for outperformance."

Given every asset manager worth its (responsibly-sourced) salt has an ESG strategy these days, Simm may be forgiven for feeling his market is becoming over-crowded but he says Impax does not think of itself as a ESG shop: "I started the business before ESG was coined as a term. I started in 1998 whereas ESG was coined in 2004 so we have never described ourselves as ESG managers. We are pitching our investment philosophy into the mainstream market to say here is an insightful way to think about how to beat the market in terms of returns while having the opportunity to produce some great non-financial outcomes such as a better environment or social impact."

Simm is dismissive of the new breed of 'ESG' managers, questioning their credentials: "Many of them are just adding another layer to their process to check the three categories, to make

Mission Statement

- To generate superior, risk-adjusted investment returns from opportunities arising from the transition to a more sustainable economy for clients with a medium to long-term horizon.
- To make a contribution to the development of a sustainable society, particularly by supporting or undertaking relevant research and engaging or collaborating with others.
- To provide a stimulating, collaborative and supportive work-place for our staff.

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sure their investments have been made cogniscent of risk and opportunity factors in those three areas, but that's just an incredibly narrow interpretation of the transition to a more sustainable economy."

The Impax chief continued: "After the financial crisis of 2008, there was a lot of navel-gazing about what had gone wrong and ESG was grasped as a metaphor for what should have been thought about before the crisis - if the companies that had gone to the wall had been more aware of good governance and environmental and social issues, we wouldn't have had the financial crisis."

The crisis that began in late 2008 coincided with a big climate-change conference in Copenhagen the following year so there was a growing impetus behind ESG.

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"ESG became short-hand for "we've got to be more mindful of risk" and, by the way, there are portions of society that are not happy with how things are working so, if we think about ESG, we can signal to those group that we are being more thoughtful," said Simm.

"So, in that context, there are a lot of institutional investors interested in opportunities to deploy capital with an ESG badge a) because they think that offers good risk characteristics and b) they have a sense that such investments will allow them to communicate good corporate citizenship to their stakeholders like pension beneficiaries."

Simm said the influx of asset managers into ESG is a mixed blessing for Impax: "Ultimately it is a good thing that there is a lot more interest in ESG because Impax can slot its investment philosophy into that conversation quite naturally, particularly given our long history of working on these issues.

"Having said that, the more people there are shouting about something in the marketplace, the harder you need to work to get your voice to be understood."

Stepping back, Simm has doubts about the efficacy of the ESG moniker: "One of the things that I've been saying for some time is that E, S and G don't obviously fit together. It's a hotchpotch of different ideas, particularly that governance is very different to environmental and social. Environmental and social are two risks facing firms, but we don't talk about changing technology, consumer behaviour or regulation?"

He added: "The way I like to describe ESG is that it should be a shorthand for doing a better job in investment

Regulation and Taxonomy

Impax Asset Management's day-to-day business is affected by environmental regulation, which is changing quickly, particularly in Europe.

To that end, the firm recently hired a full-time policy specialist to extend its research into policy matters.

One of the key initiatives in environmental regulation is the attempt by Europe to establish a single taxonomy to frame progress towards net zero greenhouse gas emissions.

Simm said these efforts are potentially risky.

"We've recently seen the rise of the green taxonomy from the European Union, a European-wide government-led venture to define and categorise what green means. They have produced documentation that goes into many hundreds of pages to define what green is. It was and remains pretty contentious because the taxonomy is ultimately going to be used for all sort of things such as regulation, compliance and reporting so there is a bit of a fight from different industries to get themselves included in this taxonomy."

Simm believes there are inherent problems with government-led definitions. "Firstly, there's no clearly defined boundary between "green" and "not green." For example, for some people nuclear power must be a key contributor to fighting climate change, while, for others, the pollution and safety risks are unacceptable. Second, boundaries or definitions change over time as our scientific understanding evolves."

The chief executive cites the example of diesel cars which were once promoted as green alternatives to petrol vehicles, but now we are told diesel is similarly harmful.

"Green is not a fixed thing, it's not a clearly defined concept so there is a risk in coming up with these centralised definitions. What I think is more effective is to see the healthy competition between different definitions provided by the private sector. FTSE Russell has a taxonomy that they call Green Revenues and there are half a dozen other similar classifications all of which have slightly different interpretations of the word Green, but they are all encouraged to stay on top of the issues and promote themselves to the market place."

Simm added: "I can see that there are benefits to this area being better classified, but I do feel strongly that those definitions are not seen as absolute, and they are better off being defined by consumer quality labels in the private sector."

The European example is important because it will likely become the global standard, Simm said.

"The UK and France have been leading the way in committing to net zero greenhouse gas emissions by 2050 and that is a relatively recent development. That sets a very clear goal for the whole economy to shift to low carbon and right now there is a lot of work underway to map out the sector transformations that are going to be required in areas such as energy, transportation and food to deliver on that target."

Simm said green regulation is not new but staying abreast of changing legislation is likely to become more challenging over time.

"We've had environmental regulation for about half a century so we have experience of what does and doesn't work, and we have now set a much more ambitious goal for the next 30 years and I think there's a good chance that we will be running pretty hard with new regulations to try to achieve that."

Simm concluded: "New regulations mean new opportunities, around electric vehicles, more comfortable homes or more interesting food, and so there are plenty of things for the consumer to look forward to as well. Of course, we invest time and to some degree money trying to anticipate where regulation is heading." ■

management particularly around risk assessment. So rather than thinking about three categories of risk, it is better to think creatively and broadly about what risks might be out there."

Simm believes ESG is a "sub-optimal, clumsy framework", adding: "The other thing that is confusing about ESG is that it has a history linked to ethics and values. The E and the S part can be traced back to the late 90s and what was called triple bottom line investing, focused on: people, planet, profit. ESG is still used by some people as a values-based idea to discuss moral issues whereas, for others, it's a values-neutral reminder to think more carefully about risk so it's quite easy for there to be crossed-wires as people have conversations around it."

The COVID-19 pandemic has highlighted issues with ESG strategies that seemingly over-looked the risk of a pandemic.

Simm said: "Pandemic risk is a good example. We are all experiencing it right now but it's not really environmental or social, it's more of a public health risk. You could say the same about cyber-risk – it's not really E, S or G but it is definitely a risk. If you are too blinkered or programmatic around interpreting ESG, you tend to have only three categories of analysis and can miss the point."

Simm argues that pandemics are not that unusual and firms should be better prepared for them: "We've had pandemics on an international scale since the 2000's. SARS was 2002-2003, Swine Flu was 2008-2009, so pandemics are not new. It's just that most people including governments had not really prepared for a really serious pandemic. So, in that sense, what COVID-19 has done is remind everyone how bad things can be if some of these low probability risks play out."

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The Impax chief said the COVID-19 pandemic has reminded investors to consider more broadly the factors that can affect their investments.

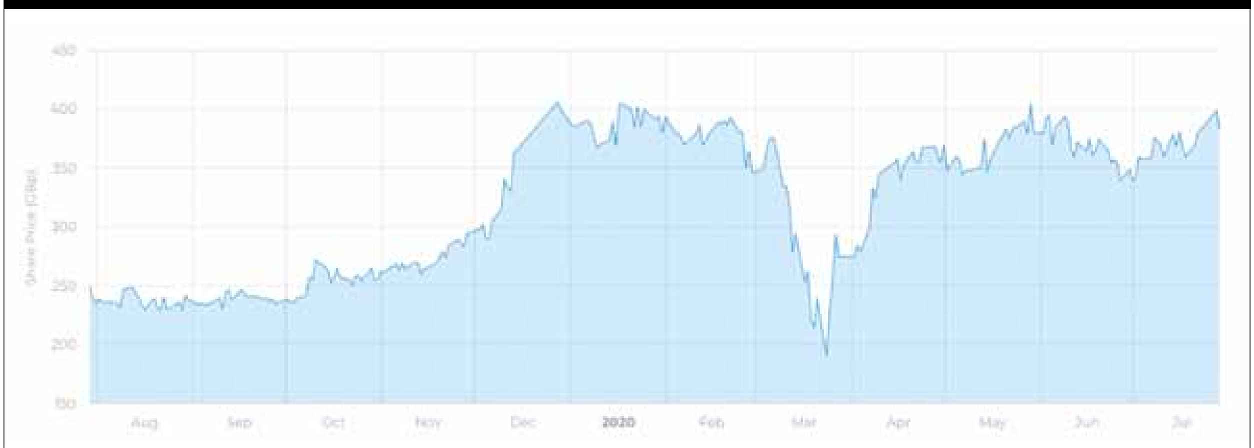
"That is quite good for people who are thinking about the world in an ESG framework correctly because they are on the look-out for low probability risks and thinking about how they would deal with them but it's not very good for someone who is interpreting ESG rigidly because, depending on where they draw the boundaries, they will miss pandemics."

But Simm said it is too early to understand the full effects of the pandemic: "There's a lot to reflect on and I don't think anything is certain yet. A lot of people are finding it quite comfortable working from home but, if you're a junior staff member without a network or a clear idea of your career plans, it's not sustainable to be working by yourself forever. The micro-conversations and encounters people have around the office cement the culture and the feel of the place, and you can't sustain that if everyone is dispersed in their homes."

Simm continued: "We are going to be quite cautious about a massive switch to working from home. That said, I think people will be more trusting of video and voice communications to some degree in the future, and business travel will take a long time to recover to where it has been."

He said there will likely be significant long-term effects for some industrial sectors: "I think there will be dislocation in some parts of the economy. Hospitality and leisure will take time to get back, transportation will suffer

Impax Asset Management: Share price, August 2019 - July 2020



with more people working from home and travelling less. But others will do well, such as telecommunications and healthcare, they should see a boom.

"The economy will recover and will probably recover relatively sharply but it will come back different and hopefully better and greener."

In terms of the Impax business, Simm said: "Today we have three business lines - listed equities, private equity and fixed income. They are all focused on the transition to a more sustainable economy. We have investment teams in London, North America, and Hong Kong, and we have institutional and wholesale clients all around the world."

He added: "Broadly speaking we are planning to extend our client footprint, serve more clients and serve our current clients with bigger amounts. We are not intending to proliferate a large number of new products, but we are carefully thinking about other ways that we can reflect our investment views in new portfolios."

Simm pointed to the launch in 2019 of an actively managed portfolio that takes stocks from a basket of companies that have significant levels of female representation on the board and/ or in management or leadership. The Global Women's Select Strategy is based on a long track-record of doing something similar in the passive space, Simm said.

He continued: "Historically Europe has been the place with the most interest in this type of investing which is not a surprise because European environmental regulations are more comprehensive than anywhere else in the world. European environmental industries are probably better developed than in other parts of the world. Having said that, we do see a sizeable and rapidly growing market in North America, so we have recently launched two new mandates in Canada and have a good pipeline of new business in the US."

Simm said the Asia-Pacific region has been slower to show interest but it is starting to pick-up in some countries such as Australia and Japan.

"The economic growth has been so strong in that region over the last 15-20 year period that citizens and governments are experiencing the kind of environmental problems that Europe and North America have been aware of for many decades and therefore there is much more interest in the Asia Pacific region about protecting the environment and protecting the social fabric."

Impax has been investing in Chinese companies for 15 years through its Hong Kong-based office. Simm said inflows from Chinese firms have been minimal but that market is one-to-watch because the Chinese government has made a strong commitment to resource efficiency and sustainable development.

He said: "Over time, as the Chinese capital markets and their interest in overseas investment grows, we are hoping to be well-placed to tap into Chinese clients, but we are not doing that at the moment."

Simm said Impax, which has 170 staff of which 55 are analysts or fund managers, is looking to increase its presence in targeted areas: "Our business has been growing quite rapidly recently and is expected to continue to grow - moving forward we will certainly look for more investment opportunities and to cover more areas. Therefore, we would anticipate wanting and needing to hire a few more specialist investment staff."

"From an investment perspective we are pretty well covered in the three key geographies. Over time we would probably want to add more people in the Asia-Pacific region as our business activity grows there. Whether that is through another office or more people in the Hong Kong office, we can't really say."

Simm added: "In the US, if we were to open another office it would be to get closer to certain groups of clients rather than to provide an additional research hub."

The majority of Impax's investments are in publicly-listed markets but it has a growing private equity arm focused on renewable energy: "Our preference in the private markets is to own 100%, whether we start the company or buy it from someone else. Generally speaking, there is so much demand now for built assets, the way to make money in our view is to get those assets built and sell them on to long-term demand. So, we have a fairly short ownership period because it normally takes a year or so to build the assets."

Simm added: "We may be buying it a year or two before construction starts

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so our typical hold period is three or four years by the time we've got in and got out."

The chief executive said Impax has worked in this way with 25 firms over the past 15 years.

A recent success for Impax was the April 2020 renewal of its Queen's Award for sustainable development, which Impax first won in 2014.

Simm said: "It is described as the UK's most prestigious business award and it does account for a large number of factors including business success, particularly around international expansion, and, in this case, around environmental practices."

The chief executive said the award reflects the firm's travel and office environment policies as well as its welfare and charitable efforts.

Impax supports a charity called Ashden, which works with charities and start-ups in the clean energy space, and Client Earth, an environmental law group that holds governments and companies to account over their environmental footprint.

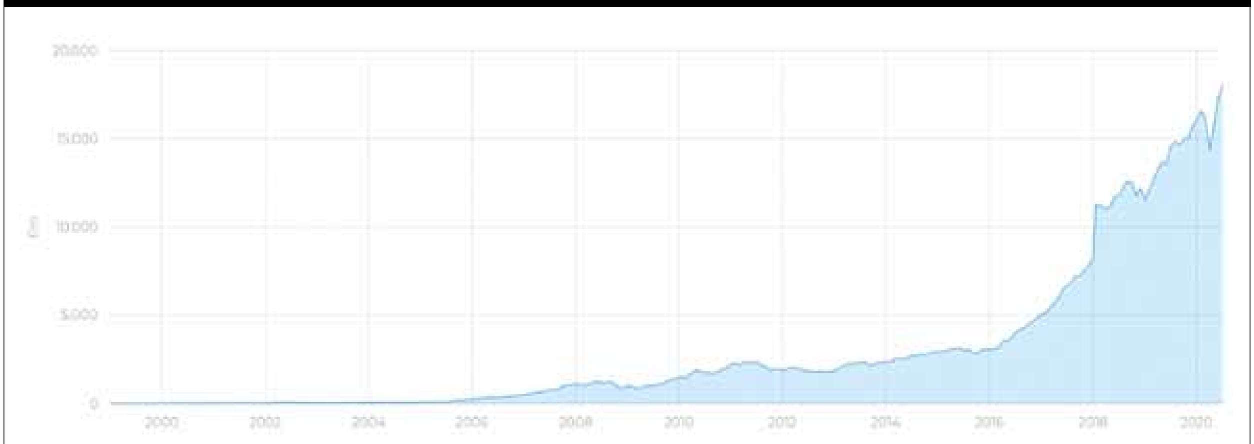
Simm is also pleased with his firm's performance over the first half of this year: "Companies that have been consistent with the transition to a more sustainable economy have out-performed this year quite considerably, whether that's because they are deemed to be more resilient or they are in sectors that are less prone to earnings downgrades

Impax Asset Management timeline

1998:	Impax Asset Management founded with mandate from the International Finance Corporation (IFC)*
1999:	First listed equity strategy launched with advisory contract for Alm. Brand Invest in Denmark
2001:	Floated on the London Stock Exchange's Alternative Investment Market (AIM) and subsequently renamed Impax Asset Management Group Plc
2002:	First own-label listed equity fund launched: Impax Environmental Markets Plc
2004:	Launch of Impax Funds (Ireland) plc, a self-managed umbrella UCITS
2005:	Launch of first private equity infrastructure fund
2007:	BNP Paribas Asset Management Holding became a shareholder; Hong Kong team established; Advisory relationship with Pax World Management LLC established
2008:	SEC registration; UN PRI signatory
2010:	Launch of second private equity infrastructure fund
2012:	New York Metro office established
2014:	Portland (OR) office established; Impax received the Queen's Award for Enterprise: Sustainable Development
2015:	Impact methodology launched; Global Opportunities strategy seeded
2016:	SmartCarbon research published
2018:	Impax acquired Pax World Management LLC which was subsequently renamed Impax Asset Management LLC
2019:	Impax received World Economic Forum's Circulars Investor Award

*Corporate finance advisory firm Impax Capital Ltd was established in 1994. Ian Simm was working at Impax Capital prior to founding Impax Asset Management Ltd in 1998. Impax Capital Ltd ceased operating in September 2007.

Impax Asset Management: AUM 2000 - 2020



depends, but we have definitely seen a solid performance."

Simm said the company has seen positive inflows each month this year, which makes Impax unusual among its peer group.

"Assets under management at the end of April were $20bn. We are a publicly held stock and that is a metric that the market looks at and is keen to see improvement on. Having said that, we are investment people rather than asset gatherers, so our overwhelming priority is to make sure that the investment performance comes through, and staff are happy and committed. The number matters but is not the be-all-and-end-all."

As a boutique manager at a time when the largest asset management groups are keen to establish their sustainable credentials, Impax could become a takeover but Simm is cool on the prospect of M&A activity.

"We are committed to being in this business in perpetuity because we believe in our investment philosophy. What that means for the ownership of the firm is much less relevant because we feel if we do a good job in delivering great returns for current clients, the business will grow much more easily than if we try to be clever and do lots of acquisitions to create growth."

He added: "We are happy to be public and have been since 2001. We are not angling for any change in ownership. I have satisfied shareholders as far as I am aware and there is plenty of potential for further expansion."

Looking more broadly, Simm is also tracking secular trends in the asset management business.

"What is the future of the investment management sector? There is plenty of evidence that the growth in passive is going to carry on but, at the same time, there is plenty of evidence that specialist investment managers, the boutiques that have differentiated ideas also have great prospects if they are able to deliver on their promises."

He added: "The concept of Impax as a boutique with a differentiated idea that it has been pursuing for a couple of decades puts us in a very good place. At the same time, there is yearning in the industry for investment managers to embrace more diverse sources of talent and to engage more with society. We are committed to doing that through our own diversity and inclusion practices but also our outreach to policymakers, charities and educational charity groups."

Impax has active programmes to recruit women and from ethnic minorities, screens recruitment shortlists and runs a diversity and inclusion working group which has a number of projects to promote diversity.

Simm said: "I do think asset management still has got some way to go to get to where it should be because it is not really reflective of the population that it is serving." ■

Memberships

Impax Asset Management is a member of or signatory to:

Principles for Responsible Investment (PRI): Aims to help investors integrate ESG considerations into investment decision making and supports sharing best practice in active ownership.

Institutional Investors Group on Climate Change (IIGCC): A forum for collaboration on climate change for European investors.

Investor Network on Climate Risk (INCR): Partners with investors worldwide to advance investment opportunities and reduce material risks posed by sustainability challenges such as global climate change and water scarcity.

The Carbon Disclosure Project (CDP): An independent organisation holding the largest database of corporate climate change information in the world.

Council of Institutional Investors (CII): Promoting strong governance and shareholder rights standards at public companies.

UK Sustainable Investment and Finance Association (UKSIF): Provides services and opportunities to align investment profitability with social and environmental responsibility.

USSIF: A US based membership association promoting sustainable, responsible and impact investment.

Global Impact Investing Network (GIIN): The largest global community of impact investors (asset owners and asset managers) and service providers engaged in impact investing.

Task Force on Climate-related Financial Disclosures (TCFD): Develops voluntary, consistent climate-related financial risk disclosures for companies providing information to investors, lenders, insurers and other stakeholders.

The UK Stewardship Code: Aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities.

PRI Sustainable Stock Exchanges Working Group: A peer-to-peer learning platform for investors, regulators, and companies. Looking at enhancing corporate transparency, and ultimately performance, on ESG risks and encourage sustainable investment.

ACGA: Focuses on collaborative engagement with companies and policymakers to improve governance structures and practices in Asia.

A Just Transition: Looking at challenges faced when moving to a more sustainable economy and why investors need to integrate a social dimension into their climate strategies.