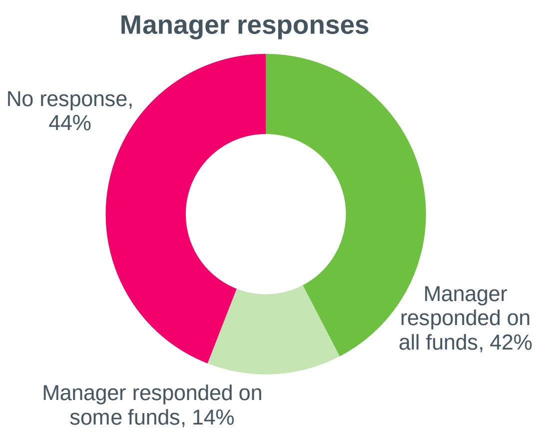
Research note

Our analysis demonstrates that the availability of climate data in private market strategies is poor with managers needing to improve the collection, reporting and disclosure of climate metrics to clients.

Managers of private market mandates seem generally unprepared to support clients looking to assess climate related risks and report in line with the requirements of the Task Force on Climate-related Financial Disclosures (TCFD). Data availability is particularly poor within private debt mandates, with no evidence that managers are currently able to report on carbon emissions. Improvements are drastically needed.

- As climate risk continues to climb the investor agenda and asset owners become increasingly subject to the reporting requirements of the TCFD framework, so the need for climate data becomes ever more important. Whilst the recent focus may have been on data in public markets, allocations to private market strategies have increased significantly over recent years, and hence there is a need to understand the quality of data available from asset managers.
- In early 2022, we asked the managers used by our clients for climate data. 59 managers and 137 different funds across private debt, private equity, real estate and infrastructure were approached and asked to complete a standard survey on their funds. We assessed the responses provided by the managers to gauge the current state of the market.
- A particular disappointment was the relative lack of response from managers. As illustrated in the image on the right, 45% of managers asked did not even respond to confirm that data was not yet available. This sends a poor signal to clients currently preparing for TCFD disclosures and needing to assess climate risk within portfolios.



- From the responses received, managers within real assets, such as property and infrastructure, are generally better prepared than private investors in corporate assets, through equity and debt mandates. Reasons for this may include disparity in the size of the underlying assets and differing regulatory reporting requirements.
- Where data was provided by managers, exposure and process-based metrics covering fund governance and strategy were more complete, with emission metrics lagging in availability. We were encouraged that some managers provided expected first measurement dates, with end-2022 being the most likely first measurement point. Formal reporting by managers on climate related issues is generally uncommon.
- It is understandable that data is poor. Requests such as ours remain relatively new and we expect that managers will need to develop data collection processes, needing to work with the underlying entities in portfolios to encourage measurement and facilitate reporting. Even then, we expect that progress may be slow.

Recommendations

- Asset managers should continue to work with underlying investee entities to improve data availability. Where data may be challenging or uneconomic to collect, be transparent as to the actions that can be taken to provide confidence that climate risks are being properly managed.
- Asset owners should consider adopting a data quality or data availability metric within their TCFD governance framework. The ability to challenge asset managers to improve data collection and reporting will allow the effective demonstration of stewardship and clearly measurable outcomes.
- Asset owners when selecting managers for new private markets mandates, to consider the use of minimum standards for climate data reporting to differentiate between providers.

Overview

In response to both growing regulation and an appreciation of the financial significance of social and environmental issues, there is a growing focus on getting better data to inform decision making. Climate change is in the spotlight as a global systemic risk and increasing expectation for different entities to report in line with the TCFD framework. Asset owners can naturally expect those responsible for managing their money to be taking steps to improve, but what action has been taken to date and what expectations should be set for the next few years?

Under the TCFD framework, asset owners need to be able to report on current emissions within their assets. They also need to be able to gauge the risks and opportunities within their portfolio; the implication here being the need to understand in greater detail what managers are doing, what processes they have in place to assess climate related risks and opportunities, and how they report on this to their stakeholders. Further, as asst owners are challenged to set net zero goals and associated targets, so the extent that change is already taking place is important.

This all requires data. Whilst data in public asset markets is generally widely available, can the same be said of private market assets and if not, what steps are being taken to improve this? Earlier in 2022, we undertook an exercise to establish a baseline for climate data from private market asset managers and their respective funds in order to help build an understanding for our clients. Drawing on different sources including the Investment Consultants Sustainability Working Group data template, TCFD guidance and our own research requirements, we asked private market managers where we had some client exposure to report their currently available climate data. The aim of this exercise was threefold, being to:

- Establish the current state of data provision within private markets
- Collect data to support client reporting and manager evaluation
- Build a dialogue with clients and managers to drive expectations for change.

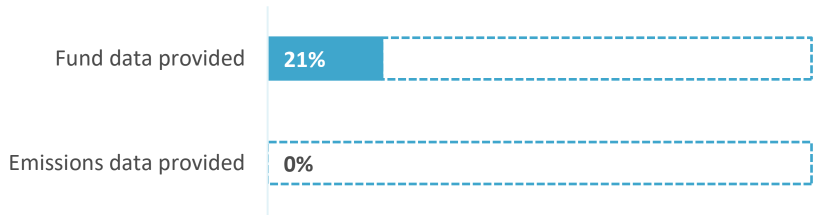
Whilst supporting client reporting is clearly important, we view this as an area where we and our clients can have significant influence. We can highlight areas that need improvement, identify the managers and funds that are leading the market, as well as those in danger of falling behind. This ongoing engagement is a key action that all asset owners can take to push for change.

Our analysis

We were surprised that the responses overall indicated no correlation between size of fund and amount of information provided within the responses. Larger managers who should be in a position to provide leadership and set an industry standard provided just as much (or little) as smaller managers suggesting that the challenge may either lie within the asset class or be a function of the level of attention and effort put in by the manager. Furthermore, as the responses varied drastically from asset class to asset class, it is sensible not to compare private markets as a whole. So, whilst it is difficult to identify any patterns at this preliminary stage, we have summarised some conclusions within private debt, equity, property and infrastructure in a little more detail below.

Private debt

Across 20 managers, only 4 managers responded to our request and even these responses had no emissions data provided.



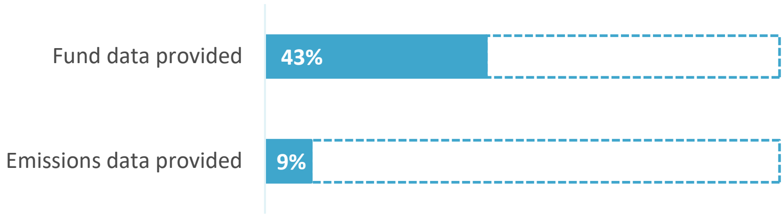
The ten funds that responded had a **total fund value of £2,344m,** as at 31 December 2021, and held 673 assets between them. Where there was an expected first measurement date provided, this is expected to be at the end of 2022. Until then, there is little insight to be drawn about emissions attributed to credit funds. It was noted by a number of the private credit managers that there is a heavy reliance on the reporting of underlying companies – many of which are not yet producing their own climate metrics. So, there is a strong likelihood that progress in this space will be slow and laborious.

From the responses provided, there was only little information provided on exposure and engagement. Disappointingly, funds either had no data on companies with climate transition plans in place or confirmed that 0% of thier portfolio did. Only one fund responded that there was engagement with underlying entities on climate change during the year and only one of the ten that responded had a fund level climate strategy in place.

Evidently, the data both collected and shared at this point is minimal, so it is hard to draw solid conclusions outside of the obvious – that it has to get better. But in the first instance, we should focus on managers getting fund level strategies in place, thereby focusing their actions and formulating a path that guides them to both engage and make improvements.

Private equity

We issued questionnaires to ten managers covering a total of 23 funds. The responses covered total assets of £5.2bn. Of those that responded, a couple of funds noted that data would be available in the coming year, suggesting that measurement of climate risks was beginning, but responses were generally lacking detail.

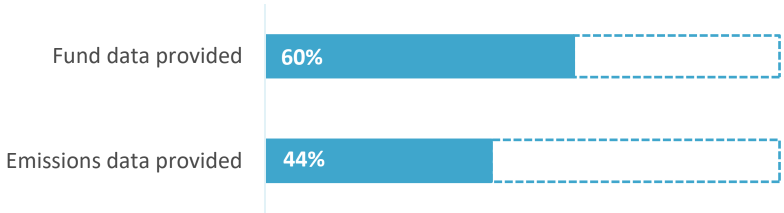


All but one of the funds that responded had exposure to the fossil fuel extraction section. However, no detail was provided on whether underlying companies had climate transition plans in place and only one manager had engaged with underlying entities on climate change during the year – even then engagement was limited. Only one fund had a fund level climate change strategy in place and had produced a fund level climate report.

The closed-ended nature of private equity funds means that many of the funds in the sample are likely to be at different stages in their maturity, with some ramping up exposure whilst others may be in run-off. It is therefore unsurprising that the data is patchy as priority may not be being given to climate risks within more mature funds. That one fund within the sample was able to provide data suggests that reporting barriers can be overcome.

Property

15 of the 25 managers covering property funds of a total value of £23.8bn responded to our request and in general, responses were more comprehensive than in other asset classes. In total, there were 20 funds that provided some emissions data.

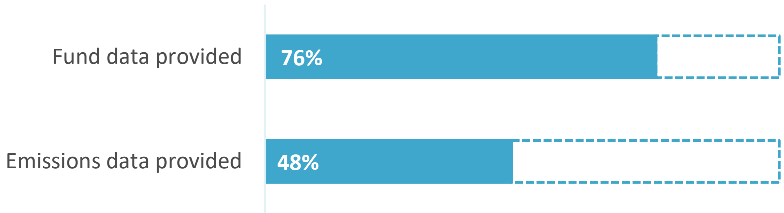


No funds that responded had exposure to the fossil fuel extraction sector, although we would note that this would most likely be through office buildings, rather than operational assets in any event. Three funds had climate transition plans in place for 100% of their portfolio and 14 funds had a fund level climate strategy in place.

The carbon emissions data collected varied quite significantly, with some funds noting that, due to the nature of the properties involved, scope 1 and 2 emissions were wholly owned by tenants and therefore nil for investors. However, this scope 1 and 2 data is therefore included in scope 3 emissions for investors – much of which is not yet measured or estimated. Further analysis will be possible as more data (including scope 3) becomes available.

Infrastructure

Infrastructure was the most responded to category within our request, with responses for 16 of the 21 funds (corresponding to 11 of 14 managers with infrastructure funds). Given the generally larger nature of the funds, responses covered a total underlying asset value of £56.4bn.



In general, reporting on climate issues was good with around 50% of funds providing emissions data, with absolute carbon emissions the most regularly reported data item. However, our analysis of responses suggests there is more work to be done in understanding data and improving data quality so as to allow comparisons to be drawn.

Data on underlying asset exposures is generally available to investors although there is perhaps lesser transparency in fund-of-fund structures. Unsurprisingly, given the asset class, this is an area retaining high exposure to the fossil fuel sector. This suggests that there may be risks arising as climate action progresses, although we also note that climate transition plans were more common in this sector. Several funds reported having plans in place for 100% of assets.

In contrast, only a small number of funds reported having a fund-level climate change strategy in place. This should perhaps not be viewed as an immediate negative; given the idiosyncratic nature of the individual assets, asset level plans may be considered to be more beneficial, although we would also expect considerations to be made at a strategic level.

Next steps

Our climate data assessment was a first step in establishing a baseline and we will be repeating this survey in early 2023 to establish what progress has been made. We expect to expand and improve our survey to provide additional clarity on expectations and improve the consistency of responses. We will be progressing our own engagement with asset managers over coming months on this issue.

Our recommendations for asset managers are:

- To engage with asset owners to understand their requirements and outline the steps that are being taken to improve data collection and reporting.
- To work with underlying investee entities to improve data availability. Where data may be challenging or uneconomic to collect, be transparent as to the actions that can be taken to provide confidence that climate risks are being properly managed.

Our recommendations for asset owners are:

- Consider adopting a data quality or data availability metric within the TCFD governance framework and use this to drive engagement with managers. Challenging asset managers to improve data collection and reporting will allow the effective demonstration of stewardship and provide clearly measurable outcomes.
- When selecting managers for new private markets mandates, consider the use of minimum standards for climate data reporting to differentiate between providers.

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