DEC0123

Written evidence submitted by BlackRock

1. In your evidence to the Committee, you stated that all building owners need to be investing in meeting net zero targets. What more could government/regulators do to encourage large-scale property portfolio owners to invest to reduce their buildings' carbon emissions?

BlackRock undertakes a number of measures to help property investors ensure their buildings are contributing to meeting zero-emission targets. Our approach is driven by a strong conviction that energy efficient buildings, and those with other strong sustainability standards, provide investment resilience and can enhance returns for our clients, in addition to bringing clear environmental benefits. Our measures fall into three broad categories, and include:

- Ensuring all of our new build projects are energy efficient, including making use of rooftop solar photovoltaics and other small-scale, on-site renewable energy opportunities. As an example, we have solar rooftop installations on several buildings in the United Kingdom, United States, Germany, the Netherlands and Singapore. We have also made use of Electric Vehicle (EV) charge points and other EV infrastructure, and have installed these at several logistics, retail warehouse and shopping centre properties. As the pricing of such technology falls, and tenant demand for these initiatives increases, we expect to continue pursuing such opportunities across our global real estate portfolios.

- Adapting existing buildings to drive efficiency improvements, such as introducing building management systems (BMS), and ensuring existing BMS are fully optimised to drive operational efficiencies. We have introduced LED lighting and other more sustainable and efficient lighting methods to many of our properties, as well as optimised heating, ventilation and air conditioning (HVAC) systems. We have also encouraged the utilisation of Automatic Meter Readings (AMR), to provide greater visibility on real-time energy usage (and wastage) and introduced innovations in energy and sustainability data management systems. This includes the use of Measurabl, an independent sustainability data management system, which enables the collation, analysis and reporting of asset- level energy consumption.

- Procuring energy from renewable and other low carbon sources, whilst also encouraging building occupiers to take a similar approach. We are increasingly shifting our energy contracts to green tariffs and those that prioritise the use of 100% renewable power. As an example, one of our largest UK property funds is now at 90% renewable energy supply for its energy consumption.

We suggest similar approaches could be followed by Government and regulators to complement efforts made by both public authorities and private investors to adapt to climate change priorities. In particular, we think it is imperative that Government set rigorous standards for energy efficiency in buildings, which should extend to standards for new construction and major redevelopments, but also, more importantly, address existing building stock and energy usage. International comparisons would be a good starting point in considering where and in what ways the UK might adapt to best practice. Secondly, in order to improve the energy efficiency of existing buildings, particularly those with a public use where local authorities already set standards - in health and safety for example - similar interventions at the local level could be undertaken. These would need to be in consultation with building owners and ensure any requests made were reasonable and proportionate. Finally, while occupiers could be encouraged to use more efficient sources of energy, it's difficult to discern what kind of intervention with building owners would be effective: this is more an issue for the energy and power markets. There could, however, be scope for Government funding to help with the installation of small-scale on-site renewable energy which could be implemented if shown to be beneficial for the taxpayer.

BlackRock recognises that a collective effort is required to drive the real estate sector towards net zero objectives. As a manager of real estate investments, our ability to act can be restricted in areas that we do not directly control or purchase energy, for example in tenant occupied spaces; as can our visibility on underlying property-level performance. Policies that drive greater collaboration between landlords and tenants in this regard could be beneficial to both parties and enable a more holistic understanding of the UK's commercial real estate carbon impact, from which appropriate performance targets can be set.

2. The shift towards passive investing has arguably created a situation where index providers, through the composition of the index, make investment decisions for large groups of investors including pension funds. In your evidence to the Committee, you suggested that firms can work with index providers to remove companies undertaking deforestation / other non-sustainable activities from the index. How much influence do major asset managers have on the make-up of indices, and what progress has been made to ensure the major index providers (S&P Dow Jones Indices, MSCI, and FTSE Russell) take climate financial risk into account on their major indices or offer climate-friendly alternatives?

The use of 'passive' is not the most appropriate description of how investment decisions are made. All decisions around asset allocation and implementation strategy are active decisions. We are committed to giving our clients choice in how they wish to invest. We recognise that many clients will continue to prefer traditional strategies, particularly in market-cap weighted indexes. However, we believe all investors – and particularly the millions of our clients who are saving for long-term goals like retirement – must seriously consider sustainability in their investments. Moreover, our stewardship efforts are consistent across all the portfolios we manage for clients, whether index or active: We do not vary our approach to engagement with companies based on the investment strategy – in other words, our engagement work is 'mandate neutral'. Our fundamental underlying goal of aiming to ensure companies deliver long-term sustainable growth is beneficial to all clients, regardless of the strategy they are invested in.

I would also note that the index universe is highly diversified. There is a wide variety (millions) of indices created by index providers for asset owners and product manufacturers to choose from. Indices span all major asset classes, including fixed income, currencies, commodities and real estate, as well as geographies (global, regional, national markets). Each index provider uses its own, rules-based methodology to build indices.
Methodologies are used to define the scope of the index, such as which securities or financial instruments are included, their respective weightings and the geography.

The role of index providers is not to make investment decisions. Index providers, such MSCI and S&P Dow Jones Indices, are responsible for constructing and monitoring indices, which are then used by investors, including asset owners and asset managers, as a performance benchmark or as a tracking benchmark.

The role of asset managers differs from that of index providers and asset owners. Asset managers do not generally manage indices, but funds or portfolios on behalf of asset owner clients. Index providers license their indices to asset managers and other financial institutions for a variety of uses, including benchmarking investments.

Both active and index asset managers use the indices provided by index providers. Active fund managers seek to outperform a chosen benchmark or index. Index fund managers aim to track the performance of the index bin question as closely as possible. An important decision for the asset owners – such as pension funds or insurance companies, for example – is deciding which index is appropriate for them, in terms of the sectors they track, the risk and liquidity characteristics of the index and its constituent securities, as well as, increasingly, chosen investment 'themes' such as 'global water' or 'ageing population'.

Index providers do however have an important role to play in the green financial ecosystem. Bringing them in to the public debate, and into the industry frameworks being developed to support the Paris Agreement or net- zero commitments, will help us all make further substantive progress on 'greening finance'. The Committee may wish to engage directly with index providers to obtain information first hand from them.

As noted above, many clients continue to prefer traditional strategies, particularly in market-cap weighted indexes, with significant exposure to hydrocarbons. However, BlackRock believes society is in the early stages of a tectonic shift towards sustainable investing. This shift is spurring political pressure, a regulatory push and technological advancements to create the foundations of a more sustainable world, leading to a change in investor behavior and setting in motion a major yet gradual capital reallocation. To drive adoption of green finance, index providers must provide sustainable versions of their indices so that we and other financial institutions provide more sustainable investment options to end-investors. Some index providers are already doing so (for example, FTSE Russell with their Climate Risk-Adjusted Government Bond Index Series). As we have created more sustainable investment options, we've seen record adoption by clients.

Index users, such as ourselves and our clients, need to engage with them to ensure climate is a key consideration in their activities. As part of making sustainability our standard for investing, we said in January we would be engaging with index providers to expand and improve the universe of sustainable indices. Since then, we have worked with several index providers to further expand our iShares (which includes the exchange- traded funds (ETFs) and other index portfolios managed by BlackRock) sustainable product offering. For example, we have launched with S&P three new ESG Screened funds underpinned by well-known, flagship S&P indices. In launching a customised sustainable version of the S&P 500 index, we worked with Standard & Poor's to remove multiple companies and industries based on business involvement risks, including thermal coal, oil sands and shale energy. With FTSE Russell and Markit, we have worked to develop innovative sustainability integrated versions of their standard market benchmarks (i.e. the FTSE Russell Climate Risk- Adjusted Government Bond Index Series and the iBoxx MSCI ESG Liquid Investment Grade Ultrashort Series respectively). However, the ongoing decisions around index eligibility, composition, construction, and rebalancing remain with the index providers themselves.

3. **In your evidence to the Committee, you stated that BlackRock has added new products to allow consumers to invest more sustainably and that these funds are labelled on carbon intensity. Could you provide more detail on these products, how carbon intensity labels work, and how these assist clients to make climate-friendly investment decisions?**

In January 2020 we made several commitments related to sustainable products addressed to retail investors. First, we committed to enhancing the transparency of sustainable characteristics, including the carbon footprint, for all BlackRock investment funds. Second, we committed to increasing access to sustainable investing for retail investors by building the largest suite of ESG ETFs. In the year to date, iShares has added 38 sustainable ETFs globally and we intend to continue creating more offerings, including sustainable versions of flagship index products. Finally, we advocated for a clear and consistent naming convention for 'sustainable' products across the industry, so that end-investors can make informed decisions when they invest in a sustainably labeled fund, which I mentioned in my hearing.

In terms of enhanced sustainability disclosures, we now provide reporting on the sustainability characteristics of all our EMEA funds already (see for example, the reporting for MyMap 5, a BlackRock ESG multi-asset fund for retail investors, or iShares MSCI Europe ESG Enhanced UCITS ETF, a BlackRock ESG ETF).

Regarding the carbon reporting specifically, the data we provide online is the fund's Weighted Average Carbon Intensity (WACI), in other words the estimated greenhouse gas emissions per $1 million in sales across the fund's holdings (tCO2e/$M sales). WACI is a well-established indicator of carbon intensity. The Task Force on Climate-related Financial Disclosures recommends for both asset owners and asset managers to use this metric, for products or investment strategies, to disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities. The sustainability characteristics disclosed of BlackRock-managed funds, including carbon footprint, is based on the MSCI ESG Rating and the MSCI WACI reporting.
These are not labels, but methodologies built and licenced by MSCI to financial institutions.

Public and easily accessible information of sustainable products is a key to enabling end-investors make better-informed investment decisions. Providing fund sustainability characteristics, including their carbon intensity, helps meet the growing demand for transparent information about sustainable investing and demonstrates our commitment to increasing investor access. Having the information available on the homepage of each of our funds, means end-investors are able to compare funds in terms of (i) their carbon intensity, comparing it with the ETF tracking the benchmark, and (ii) can look at the overall peer rating of the fund on an aggregated ESG metric by MSCI. Such transparency also enables clients to make their own climate- related reporting to their beneficiaries.

Two more ways to assist clients make climate-friendly investment decisions are the establishment of an industry-wide sustainable classification for naming products, which I mentioned during my hearing, and product innovation.

One challenge that has been consistently pointed out by public and private sector officials in advancing sustainable finance has been the need to address 'greenwashing'. Today, the term 'sustainable' encompasses what are in fact a wide range of different investment strategies. One approach to addressing greenwashing is to come up with a single framework that all products must meet in order to be called 'sustainable' – while this would provide clear boundaries, it may also discourage innovation. A step the industry can take now, more so with public sector encouragement, is to more clearly segment and name 'sustainable' products so that investors can better understand exactly what it is they offer. Industry groups such as the Institute for International Finance and the Investment Company Institute have put forward a high-level classifications system. Importantly, these systems first define 'ESG integration', which is the increasingly mainstream incorporation of ESG factors into an investment process alongside other material factors, as distinct from 'sustainable investing,' which involves products geared towards achieving a specific sustainable outcome. Within the universe of sustainable investing, these frameworks further divide products into (roughly) those that
(i) exclude particular investments to help end investors align their investments with specific sustainability preferences or beliefs (e.g. exclusionary or screened products), (ii) orient their portfolios towards some ESG- related objective (e.g. inclusionary, thematic, or ESG broad products), or (iii) pursue a strategy with the aim of creating a quantifiable positive impact in line with a particular sustainability goal (e.g. impact products). BlackRock strongly supports these efforts and believes clearly understood product naming is an important step towards addressing greenwashing concerns and giving investors confidence to differentiate between available investment products.

With the increasing demand by UK pension schemes and the regulatory efforts to progress climate integration in these asset owners' investment policy, we are developing products to support the investment needs of our UK clients. This year, we launched the ACS Climate Transition Fund, a vehicle which allows UK pension schemes to invest in the transition to a low-carbon economy. Climate Transition is a new data driven investment approach developed by BlackRock that measures a company's exposure and management to transition risks and opportunities, seeking to provide investors with a broad market approach to invest in the transition to a low-carbon economy.

Sandy Boss

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