ERIG Index Performance Survey: **Performance of Active Managers Enhanced Through Consideration of RI**

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Established investment consultant, Evergreen Consultants, has released their latest performance review for Australian and global equity funds with Responsible Investing (RI) characteristics. The review compares both Australian and global equity funds with their corresponding benchmarks, as well as a broad representation of managed funds available to Australian investors.

While the year to June 2024 has been a difficult year for active management, funds with some consideration of RI principals outperformed the general universe of equity managed funds over the 6-month to end June period in particular, while FY numbers remained broadly in line globally and generally stronger in Australia.

Across three and six month periods to end-June, funds with a first-quartile Evergreen Responsible Investment Grade (ERIG) score broadly outperformed the cohort of second-quartile funds, while both first and second quartile ERIG rated funds outperformed the broader peer averages For the financial year, second-quartile funds outperformed both peers and first-quartile ERIG funds globally, while in Australia first-quartile funds outperformed second-quartile and peers.

Nonetheless, it is important and interesting to note that each of these actively managed categories underperformed their market-cap weighted indices (the S&P/ASX 200 and MSCI World ex Australia) over the most recent financial year. The only period where any of the actively managed categories outperformed the index was found in the 6-month to end-June period, where first-quartile ERIG Australian equity funds outperformed the index fairly significantly.

The disconnect between active and passive management in global equities can in part be explained by the astounding contribution of the 'Magnificent 7' (NIVIDIA, Microsoft, Amazon, Meta, Alphabet, Apple and Tesla), which generated nearly 50% of the S&P/500's return for the financial year. Many managers are significantly underweight these stocks, given their extraordinary valuations. Similarly, stocks such as Novo Nordisk are generally underweight in active fund manager portfolios, due to high valuation. Novo Nordisk is benefitting from the development of the GLP-1 drugs, which are touted as the solution for the global obesity epidemic.

While global investors have been piling into potentially society-changing technology and medicine, domestic investors have been loading up on the cyclical giants. Of the S&P/ASX 200's total return over the year, about 70% can be attributed to 8 of the Index's largest companies (BHP, CBA, CSL, NAB, ANZ, WBC, WES and MQG).

Given an environment which ostensibly appears poor for banks – aggressive interest rate hiking, high inflation, anaemic economic growth – it was difficult to foresee a situation where a stock such as CBA would become the world's most expensive bank! Similarly, weakness in the Chinese economy did not forebear strong performance from large resource companies. As a result, active managers across the board have generally been underweight in those stocks and have underperformed the ASX200 as a result.

From an RI lens, many of these AI or banking-related companies, with their low carbon footprints and their potential to contribute to multiple of the UN SDGs, appear more attractive than they might otherwise. As a result, it is likely that many RI biased funds could have had higher exposures to those types of stocks.

Below appears performance after fees for first and second quartile ERIG rated funds, as well as the broad peer universe and the corresponding index.

The ERIG Quartile portfolios below are comprised of an equally weighted allocation to all managers within their respective sector's quartile group. The Australian Managed Investments (AMI) Equity Australia and AMI Equity Global sector representations are maintained by FE fundinfo and contain a universe of 374 and 446 constituent funds respectively – providing a strong benchmark for managed fund performance.

In global equities, second quartile managers outperformed first quartile funds by about 0.4% and the average manager result by nearly 0.3% after fees for the year ended June. The index significantly outperformed all cohorts.

In Australian equities, first quartile ERIG rated funds outperformed both their second quartile counterparts and the average manager by over 1.5%.

In summary, there is ongoing evidence that RI does not lead to poor performance outcomes for investors. These results continue suggest that, although performance patterns may be slightly different to managed funds in general, overall performance is not impeded by a consideration of RI principles.

Total Return in Australian Dollars (%) at 30/06/2024	3m	6m	1yr
Index: MSCI World ex Australia	0.42	14.67	20.49
ERIG: Q1 Global Equities Managers	-0.69	11.77	14.28
ERIG: Q2 Global Equities Managers	-0.72	10.75	14.73
Sector: AMI Equity Global	-1.14	10.59	14.48
Index: S&P ASX 200	-1.05	4.22	12.10
ERIG: Q1 Australian Equities Managers	-1.21	5.54	10.63
ERIG: Q2 Australian Equities Managers	-2.39	3.99	8.89
Sector: AMI Equity Australia	-1.78	3.43	9.06

Source: Fe fundinfo, Evergreen Consultants

About the ERIG Index

The ERIG Index aims to empower financial advisers and their clients to find and compare investment products that suit the end investors needs and preferences with regard to RI.

Built using the Responsible Investment Association of Australasia’s Responsible Investment Spectrum as a foundation, ERIG scores are based on all seven categories and approaches to RI; ESG integration, negative screening, norms-based screening, active ownership, positive screening, sustainability themed investments and impact investing are all scored for a given product regardless of its asset-class or individual approach. Quartile scores are then provided based on the sector a fund operates in through combining the overall scores across each approach to RI. This allows investors to understand and identify products relevant to their individual requirements.

As opposed to focusing on holdings (a ‘bottom-up approach’ to RI analysis), ERIG scores the sophistication and depth of a fund managers investment process itself (a ‘top-down’ approach). This method allows for the evaluation of managers that take more nuanced or flexible approaches to RI, for example aiming to improve a company through time via active ownership or other strategies, as opposed to the blunt removal of companies which appear ostensibly weak on an ESG basis - perhaps due to their industry or sector - from their investment universe. It also allows for the inclusion of asset classes that may be more difficult to asses than equities.

About Evergreen Consultants

Evergreen Consultants is a long-standing boutique investment consultant, committed to providing our financial advisory clients with both an eceptional level of client service and best-in- class investment solutions.

Evergreen is an industry founder and leader in investment consulting and managed account services, having provided our clients with solutions since 2015. Over that time, we have built one of the largest and most experienced consulting teams in the Australian industry.

Central to our value proposition is the tailored approach we take to each client: we are here to build long-term, deep and strong relationships that provide significant value to an adviser’s business.

Managed accounts are an important ingredient in maximising the value of a financial planning business, and we are a leader in providing superior, tailored and high performing managed accounts solutions for businesses.

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