



IMAP Independent Thought Podcast

Episode 46: The IMAP Australia's Best - Managed Account Award Winner Series: Navigating Politics and Performance Pressures in RI Portfolios

Join our host **Emily Barlow (Perpetual Private)** and **James Harwood of Russell Investments** to discuss:

- Have political pressures been driving an ESG rollback?
- Testing RI strategies
- How rising conflict risk has pressured RI portfolios, prompting some investors to reallocate away.
- How AI and unprofitable tech have been a mixed blessing for RI strategies.
- Is Geopolitics helping clients reframe their long-term RI expectations?

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Emily Barlow

Hello and welcome back to the IMAP Independent Thought Series Podcast, a podcast dedicated to helping managed account and advice professionals stay up to date with views from across the industry.

My name is Emily Barlow, and today we're taking a pragmatic look at responsible investing (RI).

RI has moved firmly into the mainstream over the past few decades, but more recently it's entered a period of challenge and reassessment.

Political pressure, changing market dynamics, and performance headwinds have all tested conviction, particularly for advisors trying to balance client expectations with long-term portfolio outcomes.

So today isn't about revisiting why RI exists, it's about how it's evolving, what's changed, and what advisors should be paying attention to right now.

And with that as a backdrop, I'm delighted to be joined by James Harwood, head of multi-asset APEC at Russell Investments. James brings a global perspective to responsible investing across markets and cycles.

Thank you so much for joining me today.

James Harwood (Russell Investments)

Thanks, Emily. Thanks for having me. It's great to be here.

Emily Barlow

So let's start with the global landscape. As I indicated in the introduction, we've been seeing a visible rollback of RI and ESG commitments driven by political, regulatory, and legal pressures.

From a global investor's perspective, what impact has this had on the RI opportunity set and capital allocation decisions?

James Harwood (Russell Investments)

I think, as you say, there's been a lot of pressure, particularly from the US. And you know, Russell is a US investment manager and has definitely seen some of the pressures, particularly in the United States and North America. But I would say here in Australia and also in Europe, that there's still a lot of demand for responsible investing or sustainable solutions.

A lot of retail advisors are looking for those solutions, and I think increasingly looking for help as well, because as you know, there's been this change in regulatory backdrop. And that's something that I think advisors are looking to their partners, to help them navigate some of those challenges.

Emily Barlow

And one of the slightly newer issues advisors are now faced with is "green hushing". It's become apparent that some managers haven't necessarily abandoned responsible investing, but they have become far more cautious about how they're talking about it.

How is it you think advisors should interpret this shift? Is it largely a change in language or labelling, or are there cases where it reflects genuine change in investment approach?

James Harwood (Russell Investments) 2.52

Yes, look, I would say that that most managers have not changed their investment approach or strategy. I think it's one really responding to some of the regulatory changes and focus from our regulator, but there's been a number of fines in our industry for greenwashing.

And I think managers are naturally more cautious in terms of what they're saying in literature or marketing pieces. So, I think it is it's much more a case of tightening up language and wording rather than a change in investment approach. That's certainly the case from Russell Investments perspective.

Emily Barlow 3.38

And you mentioned caution around language, and this is also sharpened scrutiny, particularly around whether funds are actually truly delivering what they claim. (So, sort of the other end of the spectrum).

From a practical standpoint, what should advisors be looking for to test whether a strategy is aligned with their clients' expectations?

And perhaps one example of this is the misalignment when Russia invaded Ukraine. Many investors were surprised to find that their RI portfolios did hold some allocations to Russia, be it bonds or securities.

James Harwood (Russell Investments) 4.15

Yes, I can probably mainly speak from Russell's perspective. I don't think a lot of advisors want to get into the weeds and look in under the hood of investment products. They're looking for partners that they can rely on for their ESG and sustainability expertise. I think that's probably the starting point, you know, working and finding a partner that has strong ESG credentials and experience in running these strategies over a number of years. I think that that's a key thing.

There's definitely been cases that that I've seen in the market as well, like Russia as you've highlighted. And yes, I think it's something that partnering with an investment provider that's been doing ESG for many years can help.

We launched (over 10 years ago in Australia), some of our sustainable strategies in the equity space. And we've stayed true to a lot of the ways we approach responsible investing throughout that time. And I know there's been several providers that have stepped away from sustainability products. We've seen that globally and also here in Australia.

Some providers have removed their sustainable options from menus, etc. But we're very committed to sustainable products and you know it's an area we continue to invest in.

Emily Barlow

And James, given you take a multi-asset, you know, you're building multi-asset portfolios. Do you have to take different approaches for different asset classes?

James Harwood (Russell Investments) 5.46

Yes, that's a good question. I think the easier asset class to review from a sustainable perspective is equities. You know, that's where the data is best, and there's a lot of different options there to invest in sustainable equity products.

As you say, we do look at you know across asset classes and for our sustainable SMAs, for example, we're always looking for a sustainably themed product.

And yes, we have a strong manager research capability where we're looking to add the best of breed sustainable strategies into our SMAs.

One of the challenges is that you know not all managers have the same approach to say things like exclusions. That's something we've had to ensure that our product PDSs, et cetera, kind of reflect. But we are looking for best of breed sustainable strategies where we can and trying to mix those to provide good levels of diversification across the asset classes.

Emily Barlow 6.47

So if we move on to performance, which is also very topical, and you know, periods of underperformance across any strategy always influence investor sentiment. But the backdrop does feel a little bit different today.

Rather than a single shock, we're seeing a rise in global conflict risk with tensions across multiple regions and more recently the war in the Middle East feeding directly into markets. And as mentioned, for many RI portfolios, this has been a difficult environment and for many other portfolios as well.

So, James, my question or my first question on this is when this conflict risk rises, what part of RI portfolios tends to feel the pressure first?

James Harwood (Russell Investments) 7.30

I think it's fair to say that war is generally not good for sustainable strategies. They tend to be underweight to things like mining or energy. Obviously oil companies that most ESG strategies will have some kind of fossil fuel type exclusion, and definitely I feel that there was pain felt back when Russia invaded Ukraine and more recently with the conflict in the Middle East.

So, it definitely has short-term challenges for sustainable strategies. And Aussie equities are probably a good example because the material sector is a big part of the benchmark.

if you're underweight a like stock like BHP or some of the oil names, that's going to detract versus a portfolio that doesn't have sustainable focuses. So Aussie equities would be the most obvious area, but yes, I think it does affect global equities as well.

And probably the one other theme is that sustainable strategies do tend to have more of a growth bias and less of a value bias, given the exclusions that many strategies employ. And that's another area that can add to some of this volatility as well.

One of the reasons why in our global equity product we look for a value-based sustainable strategy as well. They're actually quite hard to find. But that is one thing that we've included in in the portfolios.

Emily Barlow 9.12

And given this period of more challenged performance, have you seen any meaningful reallocations away from these types of strategy?

James Harwood (Russell Investments) 9.22

No, to be honest, we continue to see strong demand from our advisors that we're working with and in sustainable SMAs, for example, that there's a much smaller opportunity set than in the core space, where there are a lot of providers, there's far fewer in the sustainable space.

So, I think we are a natural call for a lot of advisors when they're looking for those types of solutions. But I think most advisors, most clients, accept there will be some short-term headwinds, and when you have these kinds of trends in the market and conflicts such as war, they have proven to be fairly short-lived.

You know back in 2022 with Russia-Ukraine, that would that was a short-term headwind, but within a couple of years, sustainable strategies have caught up again. So, I think it's understanding what's driving the performance, and being prepared to wear those short-term deviations for those sustainable principles that investors in these products have.

Emily Barlow 10.34

So if we change tack a little bit, but still sticking on performance and AI. While markets have returned or markets have started to broaden in terms of returns outside of those mega cap tech stocks, clearly AI is a very strong and persistent thematic.

In many cases, the market has been rewarding companies with very long-dated growth expectations, even where current profitability is weak or non-existent. Has this thematic been a help or a hindrance for RI strategies?

James Harwood (Russell Investments) 11.09

Yes, it's a great question. I think AI is probably ... well, you can't avoid AI in any discussion, but it's probably the biggest unknown, I would say in terms of where it's going to, or how it's going to impact companies.

As you've mentioned those high PE multiple businesses have really been challenged, and particularly the software companies have really suffered some significant selling pressure in the last six months or so.

I mentioned before that a lot of ESG strategies tend to have a higher tech or a higher growth bias., and that's something that when we're building our portfolios, we're trying to manage and provide some balance to our portfolios and the global equity value manager that we have in our ESG sustainable ETF helps provide some balance during these fairly extreme times.

Emily Barlow 12.17

And bringing it back to geopolitics, which you know is such a key feature at the moment, energy security and technological disruption are now arguably structural features of markets and not temporary noise. What does this mean for the outlook of RI strategies?

James Harwood (Russell Investments) 12.36

Yes, look, I'd say all three of those factors are here to stay. Geopolitics has been something that a lot of market commentators have spoken about for a number of years in terms of challenging markets, and markets have been incredibly resilient, And you know the S&P 500 hitting recent highs is a good example that despite all the geopolitical challenges we've got, markets can still look through that and look to the future.

Yes there's a lot of question marks, at the moment around how AI is going to affect jobs. And we've seen a lot of job cut announcements from big corporates due to AI. I think that's going to be an important trend to follow. But in terms of ESG strategies, I think they're naturally going to be exposed to those areas, and you know there's a there's certainly a strong argument that that AI is going to introduce a lot more productivity improvements and that that should be good for equities.

We're about to get some earnings reports from four of the Magnificent 7 in the next 24 hours. So, I think that's going to set the tone for equities in the tech sector for the next few months.

Emily Barlow 14.16

And finally, to wrap up, we've covered politicisation scrutiny, and performance challenges. Do you have any thoughts on how advisors can better ensure they're guiding clients into the right solutions so that values and portfolio behaviours are genuinely aligned?

James Harwood (Russell Investments) 14.33

Yes, the way I think about that there's a spectrum about ESG for some clients. For some clients it's all about sustainability and they're completely comfortable wearing performance volatility. Others want a more balanced type of approach to sustainability.

And that's where we've landed with a lot of our solutions. We're not the greenest type of solution. It's more mid-level in terms of the solutions we're trying to produce.

So, I think that's probably the key conversation advisors need to have with clients. Where are their clients on this this ESG spectrum? And that will help them determine what's the right risk characteristics and what's the best provider for that particular client with regards to sustainable solutions.

Emily Barlow 15.35

Thank you, James. This has been a really great discussion. And I mean, from my perspective, it's clear that responsible investing is continuing to evolve. And advisors are being asked to be clearer and more deliberate about how it's implemented and explained to their clients.

Thank you so much for joining us and sharing your perspective.

James Harwood (Russell Investments)

Thanks, Emily.

Emily Barlow

And to our listeners, thank you for tuning in to the IMAP Independent Thought Series podcast.

If you enjoyed this episode, please share it and keep an eye out for more conversations with industry leaders shaping the future of portfolio construction.

See you next time.

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