



 **Universal Owner Initiatives**

## Failure by Design

Is the Net Zero Asset Managers Initiative Broken?

October 2022

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[Universal Owner Initiatives](#) is a London and Edinburgh-based think tank that aims to transform the financial sector around climate change and biodiversity by providing systemically impactful data analysis. We are philanthropically funded and work closely with asset owners, asset managers and regulators.

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## Executive Summary

As things stand, the ‘net zero’ in NZAMI is a misnomer. Their headline ambition – a 15–26% cut in emissions by 2030 – is barely half of what is required for the world to stay on track with net zero. But once we take into account the initiative’s loopholes, we find that asset managers have on average made pledges that are consistent with aligning just a few percent of their emissions with net zero.

This report reviews the 43 targets released by the Net Zero Asset Manager’s Initiative (NZAMI) released in May 2022.<sup>1</sup> We break down these targets and assess potential effectiveness against emissions reduction goals and suggest areas to improve alignment. The analysis of the targets builds on [our November 2021 report](#)<sup>2</sup> analyzing the NZAMI’s first progress report.<sup>3</sup>

Asset managers have overwhelmingly set 2030 targets to either reduce their ‘portfolio emissions’, or to increase the share of their assets under management (AUM) invested in companies with ‘net zero targets’. We call these ‘portfolio emissions’ targets and ‘transition plan’ targets, respectively. But neither actually tracks real-world emissions reductions, which is what ultimately matters most.

We set this all out in detail, and suggest that the only path forward is a complete overhaul of the initiative.

### **NZAMI’s methodology is neither standardized nor rigorous**

This means that these targets are affected by ambiguity and confusion. We highlight this issue by looking at the targets of the ‘Big 3’: BlackRock, State Street, and Vanguard.

- **BlackRock sidesteps setting a binding target**, merely expressing what it ‘anticipates’. It draws on the SBTi methodology but omits one of its basic precepts. BlackRock says that *it* will decide whether a company has set a valid net zero target, whether or not the SBTi has validated their target.
- **State Street’s target is so ambiguous that it is virtually impossible to establish what it has committed to**. Its target *formally* covers only 14% of its AUM, but it *informally* suggests that its company transition target will apply to 100% of its AUM. State Street did not respond to our requests for clarification.
- Vanguard sets another non-target target, saying it ‘is expected’ that just 2% of its assets will be invested in companies on ‘a net zero glidepath’ by 2030. But Vanguard **does not explain** what a ‘net zero glidepath’ is, or how it will evaluate whether companies are following it.

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1: NZAMI, 2022, [Initial Target Disclosure Report](#).

2: Universal Owner, 2021, [Missing the Target: Why Asset Managers Have not Committed to Net Zero](#).

3: NZAMI, 2021, [Progress Report](#).

## Portfolio emissions targets are broken

22 asset managers released new portfolio emissions targets in May 2022. These targets have **four fundamental flaws**:

1. NZAMI allows asset managers to choose what percentage of their AUM to apply their targets to (from 0.5% to 100% of their AUM). But if we take a typical diversified asset manager, a small number of carbon-heavy sectors are responsible for the vast majority of their portfolio emissions. We estimate that **any target covering 50% of the typical asset manager's AUM could be consistent with the exclusion of up to 99% of its emissions**. The average AUM covered by the 22 asset manager portfolio emissions targets released in May 2022 was 50%. The **lower bound** ambition of these targets is thus likely <5%.

3. After asset managers choose what subset of their AUM to apply their target to (e.g., 50%), they commit to reducing a percentage of that AUM's emissions (i.e., 50%). If we combine these figures, we arrive at their 'effective decarbonization pledge'. In this example, it would be 25%. Suppose we perform this calculation for the 22 asset managers as a whole. In that case, they have committed to reducing **15% of their collective emissions**. This calculation assumes that the AUM covered has an emissions profile representative of their whole portfolio, which may not be the case as per (1). This is thus an **upper bound** on the ambition of these targets.

2. Portfolio emissions targets can take one of two forms. They can commit an investor to making an *absolute* reduction in their portfolio emissions. Or they can commit them to reducing the *intensity* of their emissions per \$ invested. The **vast majority** of portfolio emissions targets set under NZAMI are **intensity-based**. But investors can reduce their emissions intensity simply by increasing their investments in low-carbon companies while the emissions of GHG-intensive companies remain constant or increase.

4. Portfolio emissions targets **track the wrong thing**. They reflect an investors' exposure to emissions. But an investor reducing its exposure to emissions via divestment does not reliably reduce the emissions of the underlying companies. There is therefore a stark disconnect between these targets and the goal of net zero: reducing real-world emissions.

## **Asset managers are increasingly turning to transition plan targets, but they are little better**

26 asset managers released transition plan targets in May 2022. However, they have several shortcomings.

- They mirror two of the flaws of portfolio emissions targets. First, these targets cover an average of 63% of asset managers' AUM and are technically consistent with a **lower bound** emissions reduction of <5%.
- Second, asset managers then apply a target to this subset of their AUM. In this case, these investors have effectively committed to increasing the proportion of their assets invested in 'net zero' companies to **26% by 2030 (upper bound ambition)**.
- Under these targets, asset managers are pledging to increase the number of companies they invest in with 'net zero targets'. But the formulation of these targets mean that companies only need to *pledge* to net zero, **they do not need to act on net zero**. What is more, it appears that few of these targets have yet been submitted to the Science Based Target initiative (SBTi). If this continues, asset managers will be able to judge for themselves whether a company has a valid 'net zero target', and therefore fulfils their transition plan target.
- These asset managers are pledging (at their most ambitious) that 26% of their AUM will be invested in companies with net zero targets by 2030. But MSCI reports that 31% of the companies in their flagship global equity fund – covering 2900 companies – already have net zero targets. While these numbers are not directly comparable, this raises the possibility that **investors are setting targets that the market has already reached**.



## Portfolio emissions targets endure

When NZAMI released its [first batch](#) of targets in November 2021 to coincide with COP26, [we argued](#) that there were several profound problems with the fact that they were built around commitments to reduce portfolio emissions.<sup>4</sup> We therefore begin with a recap of these problems, before looking at whether the new portfolio emissions targets released by NZAMI do any better.

### The four flaws

Firstly, even on their own terms these targets showed little ambition. Members choose the percentage of their AUM covered by their target, and then the percentage emissions reduction they mean to achieve within that AUM. This slashes the scope of their ambition twice. If, say, their target applies to 50% of their AUM, and they are aiming to reduce the emissions of that subsection of their AUM by 50%, their effective commitment is to reduce 25% of their emissions. When we calculated the average effective decarbonization commitment across the targets released over COP26, it was just 20%. According to NZAMI itself, members are supposed to set targets “consistent with a fair share of the 50% global reduction in CO<sub>2</sub> identified as a requirement in the IPCC special report on global warming of 1.5°C.”

Secondly, even this overstates impacts because these targets contain an implicit loophole. Emissions are not evenly distributed across the typical investor’s portfolio. On the contrary, they follow a [Pareto distribution](#) where a small number of companies are responsible for the vast majority of emissions. We showed this empirically, looking at the equity holdings of BlackRock, Vanguard, State Street, Allianz and LGIM, and matching them to emissions data. We found that 10% of their holdings were responsible for 85% of the total emissions of their portfolio.<sup>5</sup>

Why does this matter? Because NZAMI gives its members the latitude to choose what fraction of their AUM to apply their targets to. If they decide to include less than 90% of their AUM, then their target is technically consistent with excluding 85% of their emissions. Our contention is not that asset managers will maximally exploit any loophole. It is that targets cannot commit asset managers to an outcome if they have loopholes.

Thirdly, these headline numbers overstate the reality in another respect. Portfolio emissions targets can take one of two forms. They can commit asset managers to making an absolute cut in their emissions. Or they can commit them to reducing the intensity of their emissions – their emissions per \$ of investments.

The decisive majority of investors have set intensity-based portfolio emissions targets. The problem is that intensity targets are consistent with an investor keeping their absolute emissions stable, or even increasing them. They could, for example, reduce their carbon intensity simply by increasing their investments in low-emitting companies. Further nearly all of these targets also exclude Scope 3 emissions, an enormous omission.

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4: Universal Owner, 2021, [Missing the Target: Why Asset Managers Have Not Committed to Net Zero](#).

5: These figures are limited to equity holdings, and should therefore be treated as approximations. At the same time, less diversified investors may show a different distribution of emissions across their portfolios.

Fourthly, investors should not be targeting portfolio emissions reductions in the first place. What this measures is an investor's exposure to emissions – the emissions of their portfolio companies (and potentially sovereigns) in proportion to their stakes in them. But an asset manager reducing its exposure to emitting companies is not a dependable proxy for reducing the real-world emissions of those companies.

This point requires further exploration. A majority of the assets held by the typical asset manager are equity and bonds traded on secondary markets. Payment for these assets has already been handed over to companies, and they are simply financial instruments traded between investors. Who holds these instruments makes no direct financial difference to the underlying companies.

Of course, selling out of high-emitting secondary market assets may lead to a higher cost of capital the next time the company in question decides to issue shares or bonds. But this depends on the liquidity of the market, the scale and number of actors divesting, and the company's other sources of capital. While divestment can therefore be a useful tool in certain circumstances, it is not a generic solution to curtailing financed emissions.

This argument was made forcefully in 2020 by 2 Degrees Investing Initiative (2Dii)<sup>6</sup>, and it has been stated more recently in a clear-eyed report by the team at the Oxford Sustainable Finance Group<sup>7</sup>:

“There is no robust evidence that aligning a portfolio with a given vision for the wider economy (e.g., Paris alignment, the EU sustainable finance taxonomy) or according to a general set of principles (e.g. recommendations of the Task Force for Climate- Related Financial Disclosure) is a compelling proxy for the real economy changes required to deliver that vision.”

GFANZ is far from oblivious to these problems. It has set up a working group to study the decommissioning – and not just the trading away from – high-emitting assets precisely because it is cognizant of them. The debut white paper of the group notes that:

“Neither the act of a financial institution reducing exposure to high-emitting companies, nor the act of a company selling a high-emitting asset, guarantees actual GHG emissions reduction. Counterintuitively, divestment movements may result in overall GHG emissions increases in the global economy, as high-emitting assets are transferred to companies and/or countries that are less sensitive to decarbonization pressures.”<sup>8</sup>

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6: 2 Degrees Investing Initiative, 2020, [“Science-Based Targets” for Financial Institution: Position & Consultant Deck](#).

7: Ben Caldecott et al., 2022, [Sustainable Finance and Transmission Mechanisms to the Real Economy](#), University of Oxford Smith School Working Paper 22-04, p.10. See also Julian F. Kolbel et al., 2020, [Can Sustainable Investing Save the World? Reviewing the Mechanisms of Investor Impact](#), *Organization & Environment*, 33(4), p.554–574.

8: GFANZ, 2022, [The Managed Phaseout of High-Emitting Assets](#), p.15. Another branch of GFANZ, the Net Zero Asset Owner Alliance, carefully marshals the evidence to conclude that divestment is not a generic mechanism for reducing real world emissions. See NZAOA, 2021, [Inaugural 2025 Target Setting Protocol](#), p.20.

## Has anything changed?

These were the problems as we saw them in November 2021 in our report [Missing the Target](#). Unfortunately, despite the weight of the case against them, portfolio emissions targets endure. NZAMI's May 2022 [report](#) announces that 20 asset managers have set portfolio emissions targets, and that another 2 have updated their targets from last year.

Do these twenty-two new targets at least show greater ambition? As a whole, no. On average these targets cover just 50% of asset managers' AUM. Based on our existing analysis of the distribution of emissions across the typical asset managers' portfolio, we estimate that the lowest emitting 50% of these portfolios accounts for approximately 1% of their emissions. In this sense the average targets are consistent a lower bound estimate for the emissions reductions these targets commit asset managers to: <5%.<sup>9</sup>

But what if this is not the case? What if asset managers choose to apply their targets to a subset of their AUM that is representative of the emissions profile of their entire portfolio? We can calculate what this would mean by taking the AUM coverage of these targets (50% on average), and then combining this with percentage reduction in emissions that they have committed to achieving over that AUM.

If we look at this on a case-by-case basis and then average it out, we reach an 'effective decarbonization target' of 26%.

But what matters is not so much the average decarbonization pledge, because this treats the targets of small, medium, and large asset managers equally. Smaller, climate-focused asset managers have tended to set more ambitious targets. While some large asset managers have pledged little. Vanguard, for example, the world's second largest asset manager by AUM, pledged to reduce its portfolio emissions by just 2%.

We want to look at the total AUM of the asset managers to set portfolio emissions targets, and then at what percentage of that total they have collectively committed to reducing the emissions of. This gives us our upper bound estimate of what these targets commit asset managers to do. If we do this aggregative calculation, we reach a figure of just 15%.

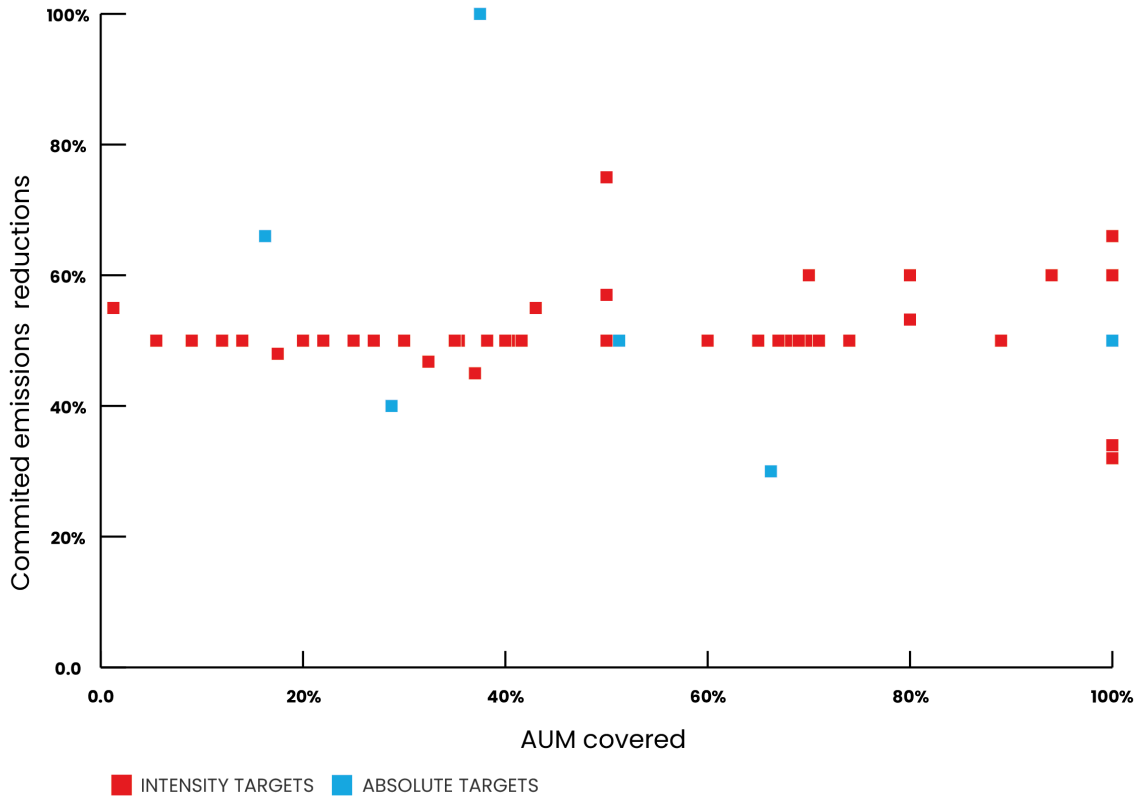
Of these 22 portfolio emissions targets, 19 were intensity-based, 2 were absolute, and 1 was ambiguous. Again, this is a problem: investors can meet intensity-based targets by increasing the proportion of their assets invested in low-carbon companies, without any commensurate decrease in their investments in high-carbon companies. It should also be noted that, with one or two exceptions, all of these targets exclude Scope 3 emissions.

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9: Because this underlying data is based on five (albeit large, representative) asset managers, looking only at their global equity holdings, we have decided to carefully avoid false precision. We are therefore using the approximate term '<5%' for these claims.



All NZAMI portfolio emissions reduction targets (August 2022)

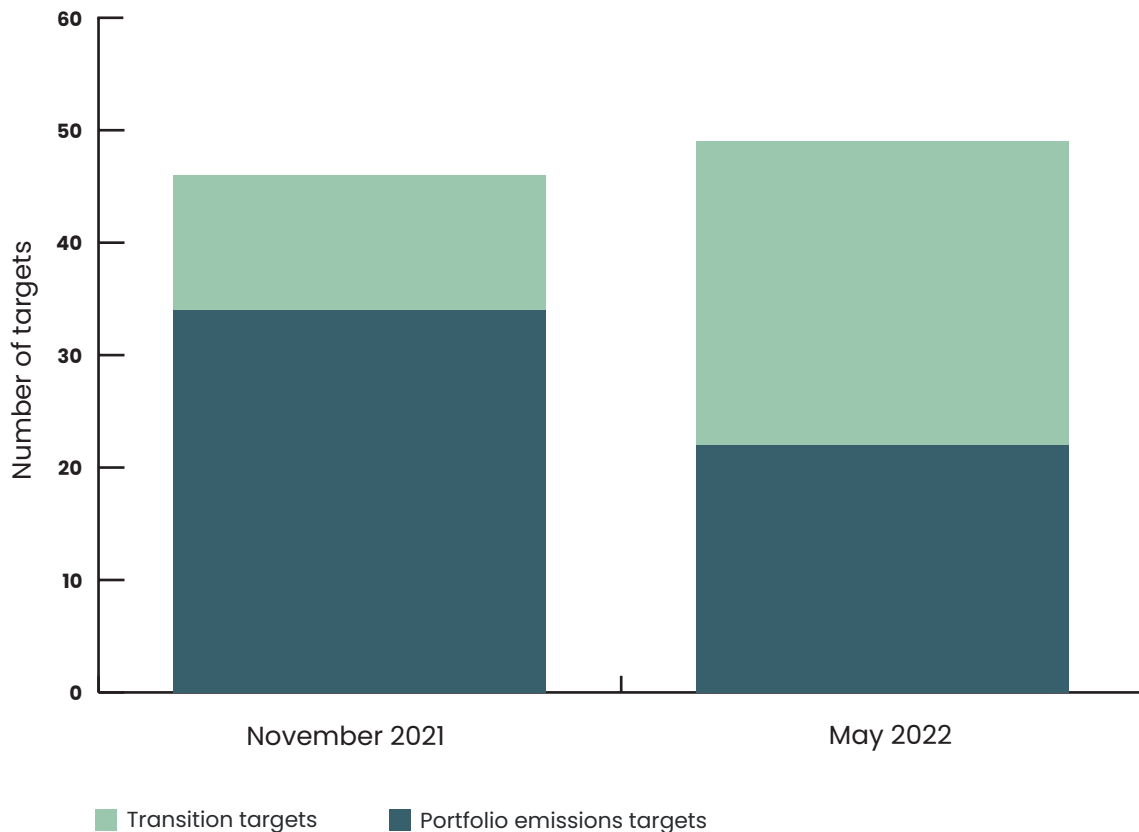


What this means is that these 22 asset managers have collectively committed to reducing their emissions by, roughly, somewhere by 1% and 15% by 2030. But of course, for the reasons enumerated above, *none* of these emissions pledges are likely to achieve even that. They are a poor proxy for reducing real-world emissions in the first place.

## Company transition targets, an improvement?

Although portfolio emissions targets continue to be set, it is clear that NZAMI is moving in a new direction. In its November 2021 report, 43 asset managers set targets. Within that group, 36 set portfolio emissions targets, and 12 set company transition plan targets (some set both, and a few set neither). In its May 2022 report, 43 asset managers set targets. 22 were portfolio emissions targets, and 26 were transition plan targets. What should we make of this change?

How NZAMI has moved toward transition plan targets



We can start with the raw numbers. On average asset managers chose to apply their transition plan targets to 63% of their AUM. We can look back to our existing analysis of the distribution of emissions over diversified asset managers' portfolios to estimate how these targets could be gamed. The lowest-emitting 63% of the equity portfolios we analyzed were responsible for just 2% of total portfolio emissions. We therefore estimate that the average transition target is consistent with the exclusion of AUM responsible for >95% of portfolio emissions. This gives us a *lower bound* approximation of what these targets commit asset managers to doing: a <5% emissions reduction.

A number of asset managers which have set transition targets do, however, specify that they will increase the percentage of their AUM in 'material sectors' invested in companies with net zero targets. This suggests that they will focus on asset which *are* representative of the emissions profile of their portfolio (though it will depend in most cases on the AUM they choose to apply the target to in the first place, reintroducing the possibility of a loophole).

What about if we take asset managers' AUM coverage, and then look at what percentage of this subset of their AUM they have pledged will be invested in companies with net zero targets by 2030? Again, we look at what percentage of the AUM of *all* the asset managers to have set transition plans targets are covered by these targets. If we just looked at the average, it would weight large and small asset managers equally. We find that collectively, they have pledged that 26% of their AUM will be invested in companies with transition plans by 2030. This is our upper-bound estimate.

It is crucial to note, however, that this is not a pledge to *increase* the percentage of their AUM invested in companies with net zero targets. A non-trivial proportion of asset managers' investee companies will already have transition plans. MSCI, for example, reports that of the 2,900 companies in the MSCI ACWI index, 31% (or 1330) have net zero targets.<sup>10</sup> While that may depend on a looser definition of a 'net zero target' than many investors intend to use – among other caveats<sup>11</sup> – it is still worrying that this number is *already above the target* that asset managers have set for 2030.

## Offloading risk onto companies

What accounts for this shift in strategy towards transition targets? An explanation could be that many of the problems afflicting portfolio emissions targets have filtered down to those asset managers who had yet to set their own targets, and inspired a change of direction.

BlackRock hints at this in the statement it released to accompany its NZAMI target.<sup>12</sup> "A portfolio fully divested of such [high-carbon] sectors in the near term", BlackRock cautions, runs counter to "a net zero economy in the long term". In short: divestment does not achieve decarbonization. But BlackRock also offers another, telling reason. Its portfolios merely "reflect the global economy", which more than anything, "reflect the regulatory and legislative choices of governments". In other words, it will not set a portfolio emissions target, because it does not have exhaustive control over the emissions of its investee companies. It is worth contemplating this rationale.

BlackRock's average stakes in the leading listed companies of advanced economies like the United States, the United Kingdom and Japan are huge, but still in the single digits. It is far from a controlling stake. Whether the emissions of the thousands of companies in its portfolio decline by 50% by 2030 is not something that it can unilaterally guarantee. That will depend on investors, policies, popular will, technology, market forces, geopolitics and much else besides. If BlackRock committed to that Paris-aligned 2030 target, it would therefore be exposing itself to the whims of fortune. That is a reputational risk and a [legal risk](#). It is worth keeping in mind that, according to Climate Action Tracker, the targets of the governments of the world currently put the planet on track for 2.4 C of warming.<sup>13</sup> What is true for BlackRock is *a fortiori* true for less powerful asset managers. This dynamic creates a perverse incentive for investors that set portfolio emissions targets to lowball their pledge, as insurance against the possibility that the world will lag behind net zero.

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10: See MSCI, June 2022, [MSCI Net Zero Tracker](#), p.5. MSCI's ACWI Index is its flagship global equity index, with stakes in large- and mid-cap companies across 47 advanced and emerging markets. MSCI claims that it covers "85% of the free floated-adjusted market capitalization in each market". It is therefore a fairly representative sample. It is also not far off BlackRock's disclosure that 25% of its AUM in corporate and sovereign issuers is invested in companies with 'science-based targets or equivalent'. See NZAMI, 2022, [Initial Target Disclosure Report](#), p.28.

11: Note that we are not comparing like-to-like here. 26% is the AUM asset managers have pledged to invest in companies with net zero targets. 31% is the *number of companies* in MSCI's global equity index that have net zero targets. These two things may not will track one another. The key 'unknown' factor here is how diversified the AUM is to which investors will apply their targets. If it is highly diversified, it will include a greater percentage of their investee companies than it does their AUM (and so will require more than the MSCI baseline). If it is less diversified, it will include a lower percentage of their investee companies than it does their AUM (and so will require less than the MSCI baseline).

12: BlackRock retroactively appended this statement to the end of its 2021 TCFD report upon releasing its target. BlackRock, [2021 TCFD Report](#), p.47-48.

13: See Climate Action Tracker's regularly updated [temperature scenario](#) for government policies.

A problem with transition plan targets is it is a lot easier to get a company to say that they will reach net zero than to get them to act in consonance with net zero. A target requires very little, while decarbonization often demands a new business model, a greened program of capital expenditure, and year-on-year emissions reductions. For this reason, a target does not reliably lead to action. Climate Action 100+'s latest update reports that 69% of the 166 major emitters that it targets have now adopted net zero plans, but it also notes that *none* of them have aligned their capital expenditure with net zero.<sup>14</sup>

Yet, this disjuncture between rhetoric and reality may well be the point. Transition targets offload the risk that companies might not actually line up with net zero onto the companies themselves. All the investor committed to was getting the company to set the target. If it then fails to live up to that promise, that accountability rebounds upon the company itself.

### **What do transition plan targets commit asset managers to doing?**

One of the two methodologies used by asset managers to set transition targets, the Paris Aligned Investment Initiative (PAII), appears to be designed to tackle this problem.<sup>15</sup> It tries to ensure that asset managers cannot claim that an investee company is 'net zero' just by virtue of its having set a target. It sets out a series of conditions that companies have to meet in addition to committing to the terminal goal of net zero by 2050.<sup>16</sup> Most notably, they have to:

- i) Set interim targets en route to 2050
- ii) Reduce their emissions intensity in a linear path to net zero
- iii) Demonstrably align their capital expenditure with the goal of reaching net zero

These are certainly powerful indicators of whether a company is acting upon their net zero target. But they are undermined in two respects. First, PAII does not provide any explicit guidelines on how to judge whether a company's emissions intensity and capital expenditure *are* net zero aligned. This bestows asset managers with the discretion to choose for themselves what this means. Second, PAII distinguishes between a company being 'net zero aligned' and a company being 'net zero aligning'. To be **net zero aligned**, a company has to meet (i), (ii) and (iii) of the above criteria. To be **net zero aligning**, however, it only has to meet (i): to set interim emissions reduction targets.

This is a vital difference because PAII recommends that asset managers should set 2030 targets to increase the percentage of their AUM invested in companies that are 'net zero aligned' *or* 'net zero aligned'. In other words, an investor can meet this target by just getting companies to set interim emissions targets. It does not require companies to take any material steps towards net zero.

Some asset managers have adopted an even looser standard. PAII suggests that investors set another, parallel engagement target. Investors should commit to a certain percentage of their AUM being invested in net zero aligned or aligning companies, *or* subject to 'direct or collective engagement and stewardship actions'. This is a low standard: it allows a company to be credited under a net zero target as long as it is subject to any kind of engagement or stewardship, which can range from the intensive to the trivial. Many asset managers have used this 'engagement target' as their primary NZAMI target. While with the SBTi, companies only need to set a long-term net zero target, and interim targets tracking a linear path to that terminal goal. Asset managers can fulfil their net zero goals without their investee companies actually doing anything to act on net zero.

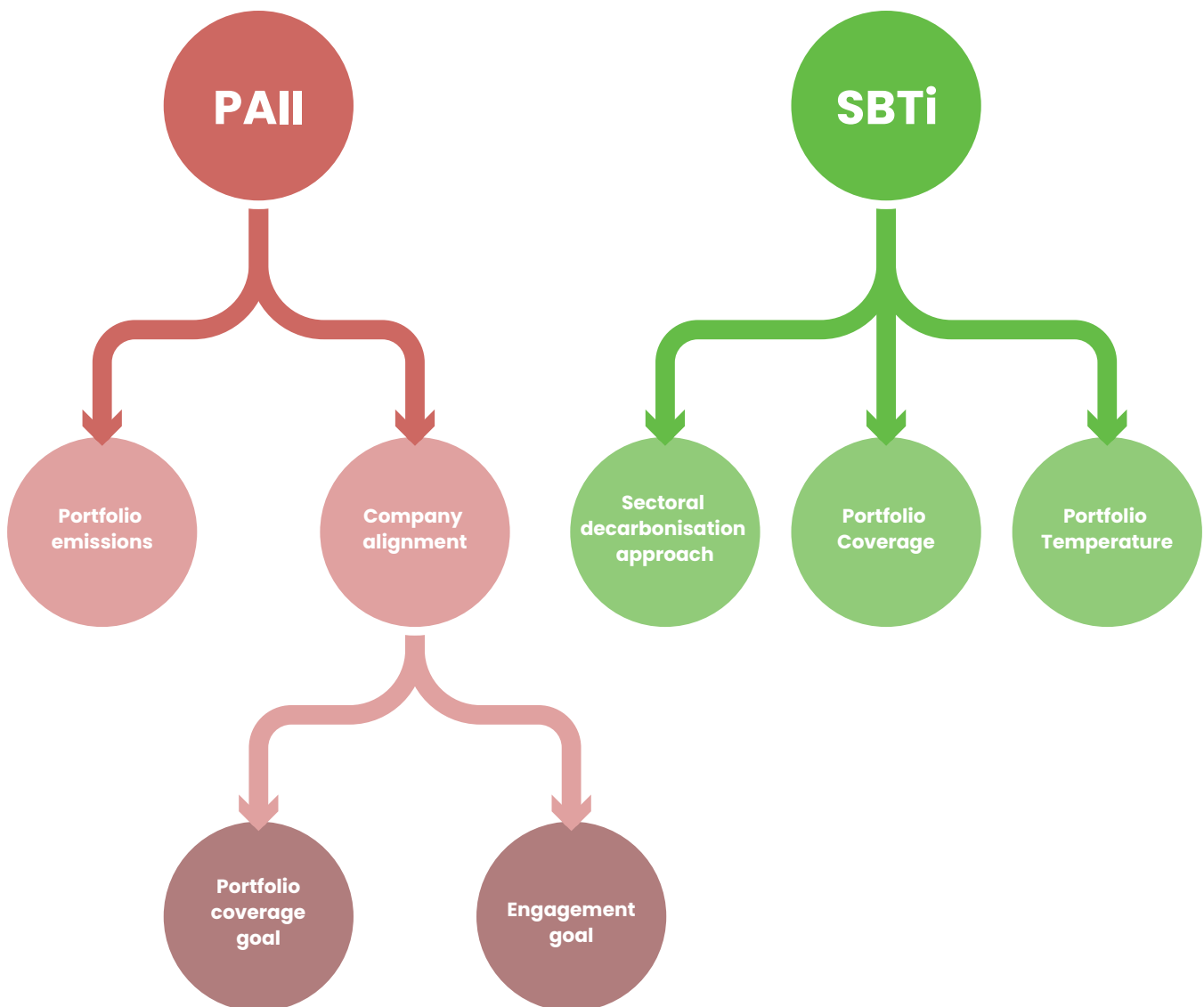
14: CA100+, 2022, [Climate action 100+ Net zero Company Benchmark Summary](#).

15: PAII, 2021, [Net Zero Investment Framework 1.5C: Implementation Guide](#).

16: Ibid., p.16-17.

## The methodological maze

The NZAMI does not have a prescriptive, standardized, and rigorous target-setting approach. Its members set targets using three methodologies: set out by the PAII, SBTi and NZAOA. Given that only a handful of asset managers have set NZAOA targets – and have done so in quite different ways – we focus on the PAII and SBTi frameworks. First, we explain how asset managers use these two frameworks. Next, we look at the NZAMI targets of the Big 3 asset managers in more depth, to draw out just how loose the initiative’s rules are for target-setting.





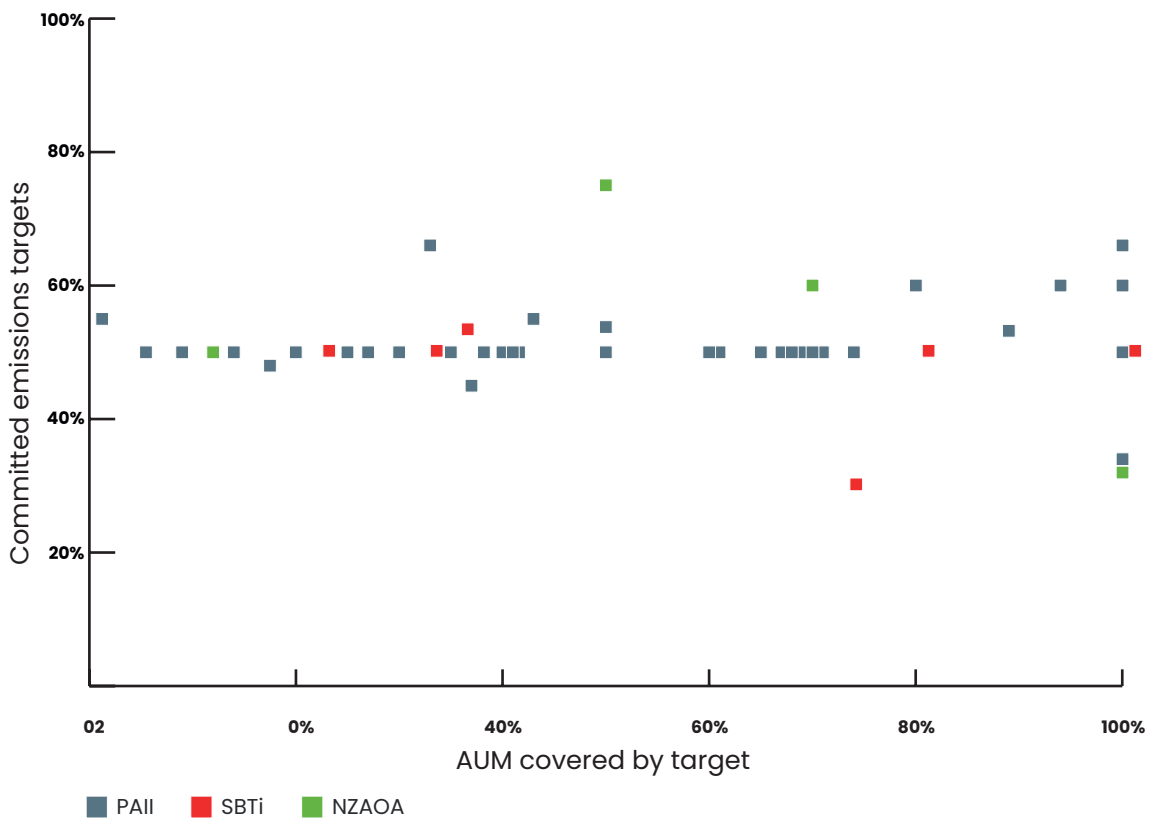
## Paris Aligned Investment Initiative

PAIL is a framework developed primarily for asset owners, and only encourages “asset managers to implement the Framework across their funds under management to the greatest extent possible”.<sup>17</sup> At its core, it suggests that investors adopt three kinds of targets:

1. A goal to reduce its emissions, either on an absolute or intensity basis (portfolio emissions target)
2. A goal to increase the percentage of their AUM invested in companies that are net zero, aligned with net zero, or aligning with net zero (portfolio coverage goal)
3. A goal to increase the percentage of their AUM invested in companies that are net zero, aligned with net zero, or subject to direct or collective engagement and stewardship actions (engagement goal)

One problem, however, is that asset managers have tended to pick and choose which of these three targets to adopt. Some investors (like APG) have adopted the first, but neither the second nor the third. Other investors (like MFS) have set targets using the second approach, but neither the first nor the third. And, finally, others (like ATLAS) have used the third approach, but neither the first nor second. Though, to add to the complexity, ATLAS uses the SBTi methodology to also set a carbon intensity target. The result across the whole of NZAMI is a series of uneven, criss-crossing targets.

### NZAMI company transition plan targets



17: PAIL, 2021, [Net Zero Investment Framework 1.5C: Implementation Guide](#), p.24.

## Science-Based Targets Initiative (SBTi)

SBTi is different from PAll in that it is a formal framework that requires investors to follow their often-exacting guidelines and only accredits a target as ‘science-based’ once it has been validated.<sup>18</sup> It gives investors the option of choosing from three target-setting approaches:

1. Sectoral Decarbonization Approach. Targets using sector-specific decarbonization pathways.
2. Portfolio Coverage Targets. Targets commit an investor to ensure that a certain proportion of their portfolio is invested in companies with science-based targets.
3. Portfolio Temperature Rating. Targets to align investors’ portfolios with a Paris-aligned temperature scenario.

Nearly all of the asset managers to have issued targets under NZAMI using SBTi’s methodology have used the second of these approaches. But it is unclear how many of them intend to submit their targets to SBTi for validation. Only a couple of asset managers (DigitalBridge and FSN) have their NZAMI targets listed on the SBTi website.

One clear issue is that SBTi requires financial institutions to apply their targets to 100% of their listed equity and bonds. The decisive majority of asset managers to set SBTi targets under NZAMI have not yet done that.

Without SBTi validation, several things are unclear: the details of the targets, whether investors will only count a company as having a science-based target if the SBTi validates it or not, and whether and how often they will disclose their progress vis-à-vis their target. Certainly, these targets are less binding without SBTi’s validation.

## A closer look at the Big 3: BlackRock, State Street, and Vanguard

It is only possible to understand how loose the NZAMI’s rules for target setting are by working through the details of specific targets.<sup>19</sup> We do that by looking at the NZAMI targets submitted by the Big 3 asset managers: BlackRock, State Street, and Vanguard. To be clear, the problems we highlight are not unique to the Big 3. We focus on them because they are the most well-known and consequential asset managers.

To clarify that these problems are endemic, we briefly consider sampling the ambiguities of other NZAMI targets. Lombard sets an SBTi temperature alignment target, but uses in-house ‘custom benchmarks’ to model the scenario it is aligning with. Macquarie sets a transition plan target, and then carefully sidesteps setting a formal portfolio emissions pledge. Instead, it says that its portfolio coverage targets are *anticipated* to lead to emissions intensity reduction of at least 50% by the year 2030’. Mirova, a sustainability investor, submits a target that reads, simply: ‘Mirova has consistently sought net zero alignment of all its investments for several years and continues to do so.’ Many more examples could be cited.

What about the Big 3, then? Of all of them, BlackRock has set the most ambitious target. It applies its target to 77% of its AUM, pledging that 75% of that AUM will be invested in companies with transition plans by 2030. But it has a few notable quirks. One is that it is not a formal target at all. BlackRock, like Macquarie, is careful not to actually commit to an outcome. BlackRock only expresses what ‘we *anticipate*’ by 2030, it does not say what it *will* achieve, or what it is *making a binding commitment* to achieve. This is not a small

<sup>18</sup>: SBTi, 2021, [SBTi Criteria and Recommendations for Financial Institutions](#).

<sup>19</sup>: Here, we work through targets reported in NZAMI, 2022, [Initial Target Disclosure Report](#).

difference. Although it uses the SBTi methodology, its full statement also discounts two important parts of that methodology<sup>20</sup>. It declines to apply its target to 100% of its listed equity and bonds, as the SBTi requires.

And, more significantly, 'BlackRock may consider issuers aligned if they follow another science-based framework'. But what frameworks, using what criteria? This inserts a degree of discretion into what a viable company transition plan is. BlackRock may use that discretion reasonably, but the point of a commitment structure like NZAMI is surely to bind investors to specific courses of action. It should not depend on trusting asset managers to self-define the details of their targets.

State Street's submission to NZAMI is one of the most ambiguous. It declares that its target pertains to 14% of its AUM. It then pledges that, by 2030, 90% of those assets will be invested in companies which, following the PAll framework, are net zero, net zero aligned, or the subject of direct or collective engagement. This is clear enough, however unambitious it might be. But it then goes on to say that it will 'increase AUM invested in assets in material sectors that are achieving net zero or aligned to net zero to 100% by 2040'. It is very unclear what this means.

Does it mean that, taking the 14% of its AUM that its target formally applies to, it will increase the fraction of that AUM invested in net zero, or net zero aligned companies?<sup>21</sup> Or does it mean that it will slowly expand its target to include an ever-greater proportion of its total assets? Its following explanation of its NZAMI target confirms that it really does only apply to 14% of its AUM. But then on its website, State Street claims that it has a 100% portfolio coverage target.<sup>22</sup> As with BlackRock, this equivocation may well be purposeful.

*Formally* its target only applies to 14% of its AUM, but *informally* it claims that it will achieve much more.

Either way, it speaks to a problem that runs through NZAMI's progress reports. The targets submitted by asset managers admit an enormous amount of ambiguity. This kind of loose, equivocal language makes it harder to accurately assess what asset managers have committed to, and for observers to hold them accountable.

Vanguard provides us with another case study in ambiguity. Its target applies to an underwhelming 4% of its AUM, but the wording of that target is, once more, less than binding. Vanguard explains that it '*is expected*' that the 50% of the 4% of its AUM covered by its target will be invested in companies with 'a net zero glidepath' by 2030.

But what exactly is 'a net zero glidepath'? It is not clear whether this is a portfolio emissions target, a transition target, or something else entirely. Vanguard says that it is employing SBTi's methodology, but doesn't specify which of its three approaches it is using or how. It does say 'targets are considered "science-based" if they are in line with what the latest climate science deems necessary to meet the goals of the Paris Agreement', which suggests that this is a transition target. Perhaps. But that is an unhelpfully vague description of what it considers a valid company transition plan to be. Vanguard goes on to suggest that Scope 3 emissions cannot be included in a carbon intensity target because of the quality and coverage of data on Scope 3 emissions. This suggests that it is a portfolio emissions target. No further details are given.

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20: BlackRock, [2021 TCFD Report](#), p.47-48.

21: We contacted several personnel at State Street to try and clarify this but received no response.

22: This statement is currently found on State Street's website [here](#).

## Conclusion

We believe NZAMI is weighed down by such a multitude of problems that it is currently unfit for purpose. The only way forward is a major overhaul of the initiative. We thus conclude with some abbreviated reflections on what that might look like.

One option would be to work with and strengthen the initiative's direction of travel, towards company transition targets. This could be done in two principal ways:

1. Ensure that the emissions profile of the AUM covered by targets reflects the emissions profile of the investor's entire portfolio. Otherwise, low-carbon, easy-to-abate sectors can be prioritized.
2. Mandate that transition plan targets cannot rest on companies simply committing to net zero, but must be backed up by material steps towards net zero.

The problem with (2) is that this would reintroduce one of the flaws of the portfolio emissions target. Asset managers cannot unilaterally guarantee that companies will act, and binding themselves to that outcome exposes them to the whims of fortune. One possibility might be a third reform:

3. Establish metrics for company change that are benchmarked against how much progress the world at large is making on net zero. Investors could, for example, have to achieve some percentage alignment of their AUM above the baseline of national targets, policies, and emissions.

The details of (3) would be all-important. While a transition plan target risks committing investors to an outcome they cannot guarantee, a metric of this kind risks committing them to less than they could achieve. The common problem in all these cases is *tying net zero targets to external outcomes*.

There is a simpler alternative, however. The initiative could redefine net zero in terms of the *internal policies* that asset managers can introduce to help bring it about. The role of the NZAMI would then be *to audit* if and how asset managers are applying these policies.

Broadly, policies might cover three areas:

1. Capital allocation to increase the cost of capital to the fossil fuel value chain, in sync with a Paris-aligned phasedown of fossil fuels
2. Commensurate investments in clean solutions
3. Strong stewardship and escalation policies to bring corporate political lobbying into line with net zero

This would achieve two things. First, it would focus attention on how asset managers can affect real-world emissions reductions on the all-important question of *impact*. Second, it would sidestep a key problem with portfolio emissions and transition plan targets. Investors would not be pre-committing themselves to an outcome the fulfilment of which they cannot guarantee. Whatever the wider state of the world, investors *can* implement efficacious, net zero policies.