Collaborative investor engagement with policymakers: Changing the rules of the game?

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Abstract

A growing number of investors are engaging with policymakers on environmental, social and governance (ESG) issues, but little academic research exists on investor policy engagement. Applying universal ownership theory and drawing on eleven case studies of policy engagement, this article develops research propositions on what drives institutional investors to engage with government entities. We identify a trend that investors engage with sovereigns to fulfil their fiduciary duty, improve investment risk management, and create an enabling environment for sustainable investments. We encourage future research to further investigate these research propositions and to analyze potential conflicts of interest arising from policy engagement in emerging market jurisdictions.

1. Introduction

Institutional investor[1] engagement with companies on environmental, social and governance (ESG) issues increased substantially throughout the 2010s. According to the 2020 Global Sustainable Investment Review (GSRI, 2021), which maps the state of sustainable investment of major financial markets, total assets under management employing engagement strategies grew from US$ 8.4 trillion in 2016 to US$ 10.5 trillion in 2020. Moreover, the Climate Action 100+, one of the largest collaborative investor-led engagements to date, has over 700 investors engaging with 166 companies, which are responsible for 80% of global industrial emissions (Climate Action 100, 2023). Using their ownership position to influence corporate policy and practice, investors are engaging with companies through shareholder resolutions, voting, face-to-face meetings, and lawsuits. Still, huge differences in the level of engagement exist between different categories of investors and even within the same category of investor (OECD, 2013; Sjostrom, 2008, 2020).

Besides engaging with corporations, there are an increasing number of asset managers engaging with governments and government-related institutions (see, for example, Colchester Global Investors, 2020; Pictec Asset Management, 2022; Robeco, 2021) as well as investor associations and collaborative initiatives targeting government officials to change public policy, such as the Investor Policy Dialogue on Deforestation (IPDD), Shareholders for Change (SfC), The Investor Agenda, the Emerging Markets Investor Alliance (EMIA), the Seventh Generation Interfaith Coalition for Responsible Investment, and the Interfaith Center on Corporate Responsibility (ICCR). These initiatives may indicate that investors find it insufficient to engage only with companies to improve investment value, but the reasons are still unclear. As such, the importance of public policy has increased for investors since 2015, when governments committed to shift trillions of dollars to be consistent to the goals of the Paris Agreement and to increase investments in the Sustainable Development Goals (SDGs). Further, investors have accepted the influence of ESG factors on delivering financial returns, recognizing the need for well-designed and effectively implemented public policies to support national economic and sustainability objectives as well as to increase the attractiveness of countries as investment destinations (PRI, 2022a).

The growing importance of public policy for investors is not yet reflected in academic research. While the bulk of the literature on investor engagement focuses on companies as targets of activist investors, little focuses on engagement with policymakers such as parliamentarians, ministers and sovereign issuers. Further, there are a limited number of academic studies analyzing the public policy role of this particular interest group. Based on our literature review, exceptions include van Zanten, Sharma, & Christensen (2021), who provide guidance to sovereign debt investors in engaging with sovereign officials on sustainability challenges, and Robins (2006, p. 320), who argue that investors should extend their focus from the company level to that of the system so as "to create market frameworks that reward companies, and their investors, for high levels of social and environmental performance." In addition, several grey literature publications (e.g., PRI, 2014, 2020a; UN-convened Net-Zero Asset Owner Alliance, 2022) analyze the reasons why - and why not - investors seek to influence public policy

[1] The general term 'institutional investor' includes many different investor types. According to OECD (2013), these might be classified into 'traditional' institutional investors, such as pension funds, investment funds, and insurance companies. 'Alternative' institutional investors relate to hedge funds, private equity firms, exchange-traded funds, and sovereign wealth funds. Further, there are asset managers that invest in their client's name; these have grown in size and number since 2000. We recognise that the specifics of the investors might influence their policy engagement strategy. In this paper, we clarify the investor type if specified and considered as relevant.

and the strategies investors employ to attain this purpose. For instance, PRI (2014, 2022) note that PRI signatories were not yet engaging with policymakers at that time due to skepticism about whether public policy engagement would make a difference, a lack of understanding of how to influence public processes, the need for long-term commitment, and, despite being the largest fixed income asset class, sovereign debt investors face challenges other than equity investors as they do not own a stake in issuers.

Hence, the present article seeks to analyze and develop research propositions on what drives institutional investors to engage with sovereign entities on ESG issues by analyzing the existing literature and eleven cases of investor engagement. The case study research approach is appropriate for this research since investor policy engagement refers to an area "where there is little understanding of how and why processes or phenomena occur" and "where a phenomenon is dynamic and not yet mature or settled" (Darke, Shanks, & Broadbent, 1998, p. 279). We understand investor engagement in public policy as developing relations with governments and policymakers through different influence processes and intent as actions taken with the explicit aim of influencing public policies and practices (based on Goranova & Ryan, 2014). Considered a form of political engagement[2] (PRI, 2022d), investor policy engagement can be conducted directly or through third parties, working groups or collaborative initiatives and by different means, such as responding to policy consultations, providing technical input via government or regulator-backed working groups, participating in sign-on letters, or by directly communicating with policymakers (PRI, 2022a).

The increasing number of initiatives targeting policymakers as well as the need for developed and developing countries to attract private-sector investments to achieve their sustainability and climate-related commitments in line with the Paris Agreement underlines the practical relevance of our study, which we hope will contribute to a better understanding of the whys and hows of investor policy engagement. Further, our contributions lie in bringing together two strands of literature (section 2) - the literature on various interest groups influencing public policy and the literature on shareholder engagement with investee companies. First, we provide an overview of previous studies on public policy and corporate engagement, and what can be learned from it for investor engagement with sovereigns. We then analyze previous studies employing the universal ownership theory to understand the underlying factors driving investor engagement on public policy issues. Materials and methods we use are described in section 3. Eleven empirical case studies on investor engagement with policymakers are showcased in section 4. Based on the literature review and the empirical evidence, we present a set of research propositions (section 5) on the factors that drive investors to engage with government officials. Section 6 concludes.

[2] In political engagement, interest groups contribute to, and participate in, the political process to shape laws, regulations, and policies that affect their business objectives, broader operating environment, and societal goals. It encompasses various channels of influence, such as lobbying, making political contributions, responding to policy consultations, using revolving doors (the movement of senior people between the private and public sectors), shaping public opinion through mass media and social media campaigns, as well as funding grassroot organisations and think tanks (PRI, 2022d).

2. Literature review

2.1 Stakeholder groups influencing public policy

Although there appears to be a gap in the academic literature concerning investor engagement with governments, the public policy academic field has studied more intensively how other interest groups and stakeholders, such as non-profits, think tanks, corporations, and churches, influence policy. In this article, public policies are defined as "the results of efforts made by governments to alter aspects of their own or social behavior in order to carry out some end or purpose" (Howlett, 2014, p. 281).

To influence public policy, think tanks in low- and middle-income countries employ both direct strategies – e.g., through participating in government advisory committees – and indirect ones – e.g., through publishing policy-relevant research (Bennett et al., 2012). In North America, the most commonly adopted tactic of policy engagement is direct, taking part in coalitions for the purpose of influencing policy (Mosley, 2011).

Churches prefer to rely on covert channels of policy influence; for example, by participating in policy committees and managing educational and welfare institutions (Busse, 2016). The media is found to use framing to portray, in a vivid manner, the need for policy change (Mwangi, 2018). Companies are more likely to avoid government intervention, campaigning in favor of self-regulation, lobbying against regulations (Mialon, Crosbie, & Sacks, 2020) and framing government intervention as unnecessary ("nanny state") (Thomas, David, Randle, Daube, & Senior, 2016). To illustrate, a survey by Ceres (2022) finds that, between 2018 and 2021, 26% of the S&P 100 companies have lobbied against Paris-aligned climate policies, advocating for policies that weaken GHG emissions standards and that continue the use of fossil fuels. Nonetheless, the same survey reflects ambiguity in investor behavior, as 50% of the respondents have lobbied for Paris-aligned climate policies, whether as individual organizations (8%), as part of a group (26%), or both (16%), advocating for GHG emissions regulation, clean energy measures, and government-backed emissions trading schemes.

Previous studies also examine those factors that contribute to successful policy engagement. One factor that helps think tanks to engage effectively in policy discussions are the personal links between institute members and policymakers, fostering trust and influence (Bennett et al., 2012). Business associations seem to have more success at influencing public policy when they have frequent contact with policymakers and advocacy skills (Irwin, 2015). By success, the author offers a broader definition, not only accounting for whether public policy bodies have changed policy, but also whether policy bodies have changed the way they see or have given a higher priority to issues.

Furthermore, the literature finds that certain features of the "engager" are associated with the level of policy engagement. For instance, companies are more likely to engage in lobbying activities when they are larger, older, internationally-exposed, in more concentrated industries, and have close relationships with state-level offices (Hill, Kelly, Lockhart, & Van Ness, 2013; Weymouth, 2012). Among non-profits, size, degree of professionalization and reliance on government funding are found to be correlated with participation in policy advocacy (MacIndoe & Whalen, 2013). We assume that some of the features also apply to investors when engaging with policymakers.

2.2 Investor engagement with investee companies and policymakers

The vast academic literature on investor engagement with investee companies analyzes different issues, including its antecedents (Karpoff, Malatesta, & Walkling, 1996; Smith, 1996), strategies (Becht, Franks, Mayer, & Rossi, 2008; Guercio & Hawkins, 1999) and outcomes (Bizjak & Marquette, 1998; Gillan & Starks, 2000; Guercio & Hawkins, 1999; Wahal, 1996). Systematic literature reviews on the topic are conducted by Cundill, Smart, & Wilson (2018) on different theoretical perspectives; Sjostrom (2020) on environmental and social issues with a focus on the efficiency and impact of the different active ownership strategies; and Goranova & Ryan (2014), adopting a multidisciplinary approach.
With regard to factors that encourage or limit investor engagement, investor size is considered a significant success factor because larger funds have greater ability to spread the fixed cost of engaging in activism across their asset base (Choi & Fisch, 2007) and are likely to possess the power (in terms of assets under management) necessary to gain access to, and be attended to by, directors and top managers (Rubach & Sebora, 2009). Larger investment funds are also more likely to have the resources to recruit and train in-house staff (Myners, 2001; Tilba & McNulty, 2013), while smaller funds find it more difficult to achieve best practice due to limited levels of personnel and resources (Myners, 2004). Investor collaboration is also found to influence corporate behavior since it increases shareholder salience and provides investors with material benefits including opportunities to share resources, build knowledge and skills, avoid duplication of effort, and share the workload (Dimson, Karakaş, & Li, 2015; Gifford, 2010; Gond & Piani, 2013; Santos, Sealey, & Onuoha, 2014). Increasing awareness of pension funds about the positive impact of ESG issues on long-term value and a pension fund ethos of responsible ownership are also found to encourage investor engagement (Clark & Hebb, 2004; Tilba & McNulty, 2013). On the other hand, the lack of investment expertise and pension fund reliance on external service providers act as barriers to engagement (Tilba & McNulty, 2013).

Corporate engagement can be classified as a form of investor political participation when investors express their political values through their investment decisions (O'Brien, Coneybeer, Boersma, & Payne, 2022). Besides engagement, there are four other tactics of investor political participation: (i) the use of shareholder resolutions at corporation's annual general meetings; (ii) negative and positive screening, in which investors proactively select investment options that align with their political values; (iii) legal action, for example, when a pension fund beneficiary legally requests their pension fund to provide information on its investment policies relating to climate risk; and (iv) divestment, where individual or institutional investors sell company shareholdings that conflict with their political values.

Transferring the findings from the public policy literature to institutional investors and the lessons learned from company engagement in public policy, we assume that investor engagement with governments might also be more successful when they are larger or act in collaboration due to resource availability. Other success factors could include closer relationships with policymakers and advocacy skills. Adding to O'Brien et al. (2022), public policy engagement could also be considered a form of investor political participation. Lastly, since companies are traditionally found to avoid or advocate against regulations, the literature also highlights an opportunity for investors to engage with policymakers so as to create regulations that demand improved corporate ESG performance, hence raising the bar for all investee companies.

Looking into the literature for arguments that would support the interest of investors in promoting changes in public policy, in the universal ownership theory we find a potential explanation since universal owner investors are interested in addressing systematic risks to reduce risks of their overall portfolio and which often require changes in public policy. We examine it in the next section.

2.3 Universal ownership as explanation for policy engagement

In previous studies, universal ownership theory is adopted to analyze investor engagement behavior on topics like climate change, labor rights, inequality, poverty, corporate governance (Hawley, 2002; Urwin, 2011), corruption (Gjessing & Syse, 2007), and drug pricing (Lippman, Rosan, & Seitchik, 2007).

Many institutional investors manage highly diversified and long-term portfolios that reflect global capital markets. According to the theory of universal ownership;[3] the high degree of diversification of their portfolios across sectors, markets, and asset classes, as well as their long-term investment horizon, means that the investment returns of these so-called 'universal owners' are inevitably exposed - and more closely linked - to developments in the economy than to the profits of individual companies or sectors. Therefore, for a universal owner and its beneficiaries, their interests align with the public at large, with long-term profit maximization not only involving enhanced returns on a firm-by-firm basis, but also improving the health of the economy (Hawley & Williams, 2000). As a result, and given that it is difficult to escape systematic risks only by divesting from a few externality-producing firms, they must take into account developments in society and the economy, thus having a natural interest in 'universal monitoring' (Hawley, 2002; Juravle & Lewis, 2008; Kiernan, 2007; Lydenberg, 2007). Reducing real-world negative externalities becomes more and more important as a major part of the universal owner returns can be attributed to market performance, or beta factor, which represents the effect of overall market movements on investments (Brinson, Hood, & Beebower, 1986; Hawley & Lukomnik, 2018; Ibbotson, 2010; Valdez, 2007). Approximately 75% of pension fund performance is typically due to market movements, while the remainder is split between asset allocation policy and active management (Ibbotson, 2010).

One of the challenges of monitoring a huge portfolio of shares is the high cost. Consequently, most investors only monitor or engage as a reaction to unusually poor performance (Keay, 2014), finding it more efficient to reduce risk by selling low-performing shares, using the strategy of 'exit' (divestment) rather than 'voice' (engagement) (Hirschman, 1970; McNulty & Nordberg, 2016; Otsuka, 2018). However, several authors conclude that divestment is less effective than engagement (Broccardo, Hart, & Zingales, 2020; Hirschman, 1970; Oehmke & Opp, 2019). They also claim that externalities produced by companies cannot be addressed through divestment; rather, policies and regulations are needed, with engagement being a tool to adjust the framework (Hansen & Pollin, 2022).

Generally, engagement is employed around corporate financial performance and ESG issues (Katelouzou & Klettner, 2020; Majoch, Hoepner, & Hebb, 2017; Sparkes & Cowton, 2004). The fact that universal owners hold large shares in portfolios that are representations of the overall economy encourages them to address issues that are originally governmental in nature by exercising ownership rights through constructive dialogue with companies and public policymakers (PRI, 2011). For many proponents of the universal ownership theory, public policy is a natural arena of engagement for the universal owner (Quigley, 2019), with some authors indicating ways in which they could advocate for policy changes that would benefit society, the environment, and the economy as a whole, such as

[3] For a systematic literature review on the universal ownership theory, as well as on its barriers and objectives, please see Quigley (2019).

applying active ownership practices and active investment strategies that integrate ESG considerations as well as collaborating with other asset owners to produce network benefits (Urwin, 2011).

The beta factor appears to be increasing in importance as more climate effects manifest themselves in costs to individual companies, sectors and the real economy (Quigley, 2020a). One alternative for universal owners to mitigate whole-system, systematic threats like climate change and inequalities, is effecting change in the real economy, for instance, through strategic engagement in public policy and standard-setting regimes (Quigley, 2020b). By engaging individually or in collaboration with other investors, investors could encourage public policymakers and regulators to not just reduce environmental impacts, but also foster the adoption of policies that establish regulatory frameworks for the internalization of externality costs (PRI, 2011).

There is evidence of the increase in the number of universal - or universal-like - owners. For instance, over 80% of institutional investment manager filers (i.e., investors with more than US$ 100 million assets under management holding equity securities that trade on a US exchange) own shares in multiple firms competing in the same industry (Amel-Zadeh, Kasperk, & Schmalz, 2022). Institutional investors are also significant investors in sovereign bonds. Given the size of the sovereign bond market, one can argue that investors carry a fiduciary duty to integrate sustainability topics in their investments and to engage with sovereigns on that matter (PRI, 2020a). According to the 2019 PRI survey, investments in fixed income represented US$ 38 trillion, 48% of which is in sovereign, supranational, and agency debt investments (PRI, 2020b). In turn, supranational and sovereign bonds account for approximately 70% (US$ 87.5 trillion) of the global bond market (US$ 128.3 trillion), which means that sovereign debt investors could have a significant influence (ICMA, 2020).

Drawn from this discussion, the universal ownership theory suggests that institutional investors are interested in engaging with policymakers to mitigate the systematic risks of their own portfolios, an assumption that we will investigate in the case studies.

3. Materials and Methods

To identify the drivers of policy engagement by investors, we analyze eleven case studies of policy engagement. There are four main roles for case studies (Ridder, 2017): the first is to build theory (e.g., Eisenhardt, 1989), following the ideal of 'no theory first' to capture the richness of observations without being limited by a theory, whilst cases offer insights into the phenomenon of interest. The second role is to specify a gap in existing theory with the goal of advancing theoretical explanations, often with 'how' and 'why' questions (e.g., Yin, 2009). The third role is to investigate the social construction of reality and meaning, with the direction of the case study shaped by the interest in the case (e.g., Stake, 1995). The fourth aims to identify anomalies, looking at what is interesting and surprising in a social situation that existing theory cannot explain (e.g., Burawoy, 1998). In the present research, the main purpose of the case studies here is a combination of the first and second roles: to develop theory, building research propositions on the drivers of investor engagement with sovereigns based on raw data from the case studies, and to add to the universal ownership theory by applying it to a phenomenon that is under-studied.

The eleven case studies on investor policy engagement analyzed were selected based (i) on whether investors were engaging with policymakers and other government representatives on ESG issues; and (ii) on availability of public information. This is because, although there exist several collaborative initiatives by investors[4] and an increasing number of net-zero finance sector alliances,[5] these either focus solely on corporate engagement or information on their policy engagement was not available for specific cases. As for data collection for the case studies, we relied on secondary data, analyzing the following documents: reports on the engagement initiatives; reports from investor associations; web sites of investors and investor coalitions; investor engagement policies; reports from specialized responsible investment media; investor letters to sovereign entities; and online news. The focus was to gather information on the perspective of the institutional investors on the phenomenon of public policy engagement. Still, the granularity of information publicly available differed widely, resulting in different levels of detail in the case studies.

For data analysis, we used content analysis, coding all documents analyzed from the case studies through an inductive and iterative coding procedure using software Atlas T.I. Codes. All arguments that appeared as motivations for engaging with policymakers (e.g., manage financial risks, create an enabling environment for sustainable investments) were transformed into codes, which were then refined along the coding process. Similar codes (e.g., manage sovereign credit risks, manage corporate reputational risks) were also grouped into a larger code (e.g., manage investment risks). A total of 98 quotations were coded.

4 Case studies on public policy engagement by investors

In order to find empirical evidence on what drives institutional investors to engage with sovereign entities on ESG issues and what could be the main challenges in this type of engagement, we analyze eleven cases of investor engagement: the Investor Policy Dialogue on Deforestation (IPDD) with Brazilian (case 1) and Indonesian government authorities (case 2); the engagement of Shareholders for Change (SfC) with the Namibian government to accede to the UN Biological Weapons Convention (case 3) as well as with Brazilian policymakers on deforestation (case 4); The Investor Agenda's public policy advocacy in Japan (case 5), Australia (case 6), the EU (case 7), the US (case 8), and with a set of governments prior to the Conference of the Parties (COPs) (cases 9 and 10), and the PRI-led engagement with Australia on climate change (case 11). Table 1 provides an overview on the policy engagement initiatives investigated in this study. As of the date of submission of this article, the engagement cases were still ongoing, except for case 3.

[4] e.g., Climate Action 100+, Nature Action 100, Investor Initiative for Sustainable Forests (IISF), Seventh Generation Interfaith for Responsible Investment's public policy advocacy

[5] Such as the Glasgow Financial Alliance for Net Zero - GFANZ, Net-Zero Banking Alliance - NZBA, Net-Zero Insurance Alliance - NZIA - and the Net-Zero Asset Owner Alliance - AOA

Table 1 - Case studies - Policy engagement initiatives

Engagement initiative	Launch year	Coalition[6]	AUM[7]	Targeted country[8]	Objectives[5]
Investor Policy Dialogue on Deforestation (IPDD)	2020	67 investors from 19 countries (for the IPDD initiatives)	US$ 10 trillion	Brazil (case 1)	Reduce deforestation rates, enforce Forest Code, prevent fires, public access to deforestation data, protect rights of indigenous peoples
	2021			Indonesia (case 2)	Encourage and enhance existing policies that contribute to the sustainable management of the forest assets and that reduce financial risks arising from deforestation and land degradation
Shareholders for Change (SfC)	2018	13 investors from Germany, France, Italy, Spain and Austria	€30bn	Namibia (case 3)	Join the UN Biological Weapons Convention
	2021	13 investors from Germany, France, Italy, Spain and Austria	€30bn	Brazil (case 4)	Protection of the Amazon rainforest and the rights of the indigenous population.

[6] Refers to the whole coalition unless indicated otherwise

[7] The AuM indicated refers to the overall coalition if information on the specific engagement case is not available.

[8] Refers to the specific engagement case under review in this article.

Engagement initiative	Launch year	Coalition[6]	AUM[7]	Targeted country[8]	Objectives[5]
The Investor Agenda	2021 and 2022	PRI, AIGCC, CDP	not specified	Japan (case 5)	Call for decarbonization of the energy sector and adoption of climate disclosure regulations
	2021 and 2022	IIGCC, PRI, AIGCC, CDP, Ceres, IGCC	AUS 100 trillion	Australia (case 6)	Ask for mandatory disclosure aligned with the TCFD
	2020, 2021 and 2022	CDP, Ceres and PRI	not specified	EU institutions (case 7)	Call on increasing climate ambition
	2021 and 2022	CDP, Ceres and PRI	not specified	US (case 8)	Call on key actions for climate transition
	2021	IIGCC, PRI, AIGCC, CDP, Ceres, IGCC, UNEP FI and over 700 signatories	US$ 52 trillion	Group of governments before COP26 (case 9)	Call on key actions for climate transition
	2022	IIGCC, PRI, AIGCC, CDP, Ceres, IGCC, UNEP FI and over 600 signatories	US$ 42 trillion	Group of governments before COP27 (case 10)	Call on key actions for climate transition
Collaborative Sovereign Engagement on Climate Change	2022	PRI signatories	Open for new members	Australia (case 11)	Support climate policy action

4.1. Investor Policy Dialogue on Deforestation (IPDD)

The IPDD collaborative investor initiative was set up in July 2020 with 34 investors, representing US$3.7 trillion in assets under management, with the aim “to ensure the long-term financial sustainability of investments, by promoting sustainable land use and forest management, and respect for human rights" (IPDD, 2022, p. 7). As of December 2022, the IPDD is supported by 67 institutional investors from 19 countries, representing nearly US$10 trillion. The group is co-chaired by Storebrand Asset Management and RBC BlueBay Asset Management, whilst the Tropical Forest Alliance, from the World Economic Forum, provides secretariat support (IPDD, 2022). The coalition mainly engages with representatives from Brazil, Indonesia, and a few consumer countries (e.g., UK, US, China).

In Brazil (case 1), the coalition has established dialogue with government-related entities and associations as well as with other stakeholders such as congress, embassies, financial organizations, companies, and members of academia and civil society to protect the rights of indigenous peoples, achieve a significant reduction in deforestation rates, enforce the country's Forest Code,[9] and establish public access to data on deforestation, forest cover, tenure, and traceability of commodity supply chains, amongst others (IPDD, 2022).

In 2020, a network of 34 investors sent letters to the Brazilian Embassy of their respective home countries raising concerns about deforestation and fires in the Amazon. In response to the letter, a video conference was arranged with the Minister of Foreign Affairs, Minister of Agriculture, Minister of Environment, and the President of the Central Bank (Spring, 2020). Further, the Brazilian government then announced a temporary ban on setting fires in the Amazon as some firms were threatening to put hold on additional investments in Brazil or to divest if the government then in office, led by Jair Bolsonaro, did not act (Paraguaçu & Spring, 2020). A second meeting with the Brazilian Vice President took place in January 2021 to discuss deforestation (van Zanten et al., 2021). Following that initiative, they also met in 2022 with the Governor of the Central Bank as well with the Ministry of the Environment to elevate investor concerns (IPDD, 2022).

In Indonesia (case 2), the IPDD seeks to encourage and enhance existing policies that contribute to the sustainable management of the country's forest assets and that reduce financial risks arising from deforestation and land degradation; e.g., disruption of ecosystem services undermining the country's agricultural productivity and inability of investee companies to meet consumer country regulations.

Since January 2021, the group has met with Ministries, Indonesian ambassadors, the financial markets regulator, the Indonesian stock exchange, multilateral institutions, banks, NGOs and academics to discuss, among others, actions taken by the Indonesian government to address and reduce deforestation. Co-chairs of this engagement chapter are the Church Commissioners for England and Robeco Asset Management. In 2022, they advanced partnerships with local actors by signing a Memorandum of Understanding (MoU) between the Indonesia Business Council on Sustainable Development (IBCSD) and the Indonesia Stock Exchange (IDX) to support the implementation of sustainable investment in Indonesia through capacity-building provisions and knowledge sharing. A second MoU was signed with the Indonesian Chamber of Commerce and Industry (KADIN) on supporting their Regenerative Forest Business Sub Hub (IPDD, 2022).

4.2. Shareholders for Change (SfC)

The European network Shareholders for Change (SfC)`, primarily a faith and values-based member organization, was founded in 2018 by institutional investors from Austria, France, Germany, Italy and

[9] The Forest Code (Law 12.651/2012) requires rural landowners to preserve/restore a portion of their land as Legal Reserve areas – the percentage varies from 80% in forested areas of the Legal Amazon region, 35% in areas of Cerrado of the Legal Amazon region, and 20% in other regions – and Permanent Preservation Areas from the property (e.g., mangrove areas and the surrounding bodies of water) (Brazil, 2012)

Spain. Since February 2020, the German Catholic Church Bank, 'Bank für Kirche und Caritas' (BKC), on behalf of Shareholders for Change, has been in dialogue with high-ranking Namibian state representatives and diplomats (case 3) to persuade the country to join the UN Biological Weapons Convention. Given the good sustainability indicators of the country, such as political rights, the bank saw an opportunity to engage with the country representatives on this topic rather than divesting from sovereign bonds. The background to BKC's efforts was their addition of the criterion "non-ratification of the UN Biological Weapons Convention" to the exclusion criterion for investments in government bonds at the time. Due to Namibia's positive positioning on basic sustainability criteria, such as "political rights and civil liberties" and ratification of the Chemical Weapons Convention, BKC saw an opportunity to engage with government agencies instead of divesting from Namibian government bonds. After two years of engagement dialogue, in February 2022, the country became a party to the Convention and BKC's plan proved successful (Shareholders for Change, 2021, 2022b).

The BKC is also engaging with the Brazilian government (case 4) since the beginning of 2021. Together with almost 100 Catholic investment institutions from 18 countries and the Global Catholic Climate Movement (GCCM), alongside domestic support from the Special Commission on Integral Ecology and Mining for the Brazilian Bishops' Conference (CNBB), BKC sent a letter in March 2021 to high-ranking Brazilian government representatives and officials with clear demands to protect the Amazon rainforest and the indigenous people living there. In 2021, they also met with the minority leader of the Brazilian Congress and several opposition politicians for an online hearing. In 2022, the intensive dialogue continued with high-ranking Brazilian state representatives, including the Brazilian Foreign Minister, the Minister of Foreign Affairs, and the Governor of the Central Bank. The initiative also gained support at the international diplomatic level from the Norwegian and German Ambassadors in Brasilia, who agreed to highlight the engagement and related concerns in exchanges with Brazilian and international diplomats and other stakeholders (BKC, 2022; Shareholders for Change, 2022a). In addition to maintaining pressure through follow-up letters to the National Indigenous Foundation (FUNAI), the Brazilian government agency responsible for indigenous affairs, and to the Ministry of Foreign Affairs, the coalition has been able to establish a dialogue with the Brazilian Central Bank on the issue of illegal gold mining and is trying to enter into an exchange with President in office Luiz Inácio Lula da Silva (BKC, 2022).

4.3 The Investor Agenda

The founding partners of The Investor Agenda are seven major groups working with investors: Asia Investor Group on Climate Change (AIGCC), CDP (formerly known as Carbon Disclosure Project), Ceres, Investor Group on Climate Change (IGCC), Institutional Investors Group on Climate Change (IIGCC), Principles for Responsible Investment (PRI), and UNEP Finance Initiative (UNEP FI). They advocate collectively for public policy aligned with delivering a just transition to a net-zero economy by 2050 or sooner, coordinating investor and finance sector initiatives on climate change issues.

In Japan (case 5), they engaged several times with government representatives, such as the Minister of Economy, Trade and Industry and the Prime Minister. to call for decarbonization in the energy sector and the adoption of mandatory climate-related disclosure regulations (The Investor Agenda, 2022). In Australia (case 6), the group engaged with the Australian Treasurer and the Reserve Bank of Australia Governor as well as with the Parliamentary House to ask for mandatory disclosure on climate change risks aligned with the Taskforce on Climate-related Financial Disclosures (TCFD), and for adopting the standards issued by the International Sustainability Standards Board (ISSB) (The Investor Agenda, 2022).

Engagement also took place with the EU Commission (case 7) on the EU's 2030 target and sustainable recovery package after the pandemic as well as on the EU "Fit for 55" package. In the US (case 8), policymakers and the US Congress were engagement targets for effective action to address the climate crisis, including improved support for an inclusive and just transition to achieve net zero with ambitious climate investments. In 2022, a response from global investors was submitted to the consultation on the draft climate rule of the Securities and Exchange Commission (SEC).

In addition, in 2021 and ahead of COP26, the group issued the Global Investor Statement to Governments on the Climate Crisis, which was signed by more than 700 investors collectively managing over US$52 trillion in assets, calling governments (case 9) around the world to take key actions for climate transition (IIGCC, 2022; The Investor Agenda, 2022). In 2022, ahead of COP27, The Investor Agenda together with over 600 investors launched again a Global Investor Statement (case 10) that urged governments to rapidly implement priority policy actions that will enable them to invest the trillions needed to respond to the climate crisis.

4.4 Sovereign engagement on climate (PRI)

The Collaborative Sovereign Engagement on Climate Change is one of the most recent collaborative engagement cases, having started in autumn 2022. The PRI-coordinated investor initiative is pushing governments to take action on climate change, starting with Australia as a pilot (PRI, 2022b). In 2022, the country introduced its Climate Change Act, which sets out Australia's greenhouse gas emissions reduction targets. The coalition recommends that Australia's policymakers update standards and guidance to clarify investors' duties to address sustainability risk; adopt a reporting framework; strengthen regulatory support for investor stewardship; implement an Australian sustainable finance taxonomy; and address the effects of product heatmaps and financial performance tests on investors' actions on sustainability outcomes (Turner, 2022).

5. Results and research propositions

From the literature review and publicly accessible documents of the case studies, we develop four research propositions regarding the drivers of investor engagement with policymakers. We classified them separately for analytical reasons, but one driver was often mentioned in combination with others in the case studies analyzed. We separate, in different columns, the number of quotations and the number of codes because some of the quotations mentioned more than one code.

Table 2 - Number of quotations and number of mentions of policy engagement drivers in quotations

Drivers	Number of quotations	Number of mentions in quotations
Comply with fiduciary duty	11	11

Drivers	Number of quotations	Number of mentions in quotations
Enabling environment for sustainable investments	49	
Enabling environment (unspecified)		39
Seize opportunities		27
Increase level playing field		8
Manage investment risks	56	
Manage investment risks (unspecified)		34
Enhance corporate transparency		13
Manage corporate market risks		8
Manage corporate operational risks		2
Manage corporate physical risks		4
Manage corporate regulatory risks		8
Manage corporate reputational risks		5
Manage sovereign credit risks		6
Manage systematic risks		13
Ethical reasons	2	2

5.1. Complying with fiduciary duty

Eleven quotations are found supporting that investors engage in public policy to comply with their **fiduciary duty**. According to the IPPD coalition (IPDD, 2022), financial institutions have a fiduciary duty to act in the best long-term interests of their beneficiaries and tackling deforestation is increasingly recognized as part of good fiduciary duty. In the 2021 Global Statement to Government on the Climate Crisis, The Investor Agenda (2022) argues that “investors are urgently seeking to decrease their exposure to climate risk as a core fiduciary duty.” The Australian Council of Superannuation Investors explain that their fiduciary duty includes engaging with policymakers because “the rules that govern investment markets and the conduct of individual companies do not always operate in the best interests of long-term fiduciary asset owners and their beneficiaries” and, therefore, “asset owners have an opportunity and responsibility to engage with policymakers to better align the operation of their financial system with the interest of beneficiaries” (PRI, 2022a, p. 21). Given the evidence, our first research proposition is the following:

RP1: Investors engage in public policy to comply with their fiduciary duty.

5.2. Creating an enabling environment for sustainable investments

Engagement with policymakers is also justified by the need to create an enabling environment for sustainable investments (49 quotations), allowing investors to seize investment opportunities (27 mentions), and creating a level playing field that rewards companies and investors for higher levels of social and environmental performance (eight mentions).

An **enabling environment for sustainable investments** is sought, for instance, by the IPDD (2022, p. 16) who state that it engaged with Brazilian authorities due to concerns that “weakening environmental and human rights policies as well as lack of effective enforcement” would create “widespread uncertainty about the conditions for investing in or providing financial services” in countries like Brazil. In an open letter to the EU Council, investor CEOs also highlight that “accelerating 2030 climate ambition will reduce the risk of carbon lock-in and increase certainty for investors, supporting them to deliver private investment in the low-carbon economy” (The Investor Agenda, 2022).

As for specific reasons for seeking to create an enabling environment, first, investors engage in public policy to enable investors to **seize investment opportunities** associated with the transition to a net-zero emissions economy. In the Global Statement to Government on the Climate Crisis, The Investor Agenda (2022) notes that “full implementation of the Paris Agreement will create significant investment opportunities in clean technologies, green infrastructure and other assets, products and services needed in this new economy.” Therefore, to accelerate and scale up private capital flows for a climate resilient, net-zero transition, investors require effective climate policies. In Japan, The Investor Agenda coalition requested that the Japanese Ministry of Economy, Trade, and Industry support the country’s achievement of a carbon neutral goal for 2050 and adopt measures like an action plan to decarbonize electricity production and carbon pricing, so as “to increase investor confidence in mobilizing private capital towards the net-zero emissions energy transition in Japan,” giving them long-term planning security (The Investor Agenda, 2022). In addition, as The Investor Agenda argues in the engagement with EU governments, “the ability of investors to provide the funding needed for the net zero transition is dependent on government’s credible commitments and policies” and “all relevant [EU] parties need to show strong policy action and political will to negotiate the political framework and translate ambitious targets into action for net zero and the green transition” (The Investor Agenda, 2022). The Investor Agenda concludes by noting that countries that "set ambitious targets in line with achieving net-zero emissions, and implement consistent national climate policies in the short-to-medium term, will become increasingly attractive investment destinations." On the other hand, "countries that fail to do so will find themselves at a competitive disadvantage" (The Investor Agenda, 2022).

Secondly, investors engage in public policy to create a **level playing field** for higher levels of social and environmental performance (seven quotations). As stated by the CEO of Storebrand Asset Management, and IPDD co-chair, "sovereign engagement is something complementary to company engagement - companies alone can't change systems, they need enabling environments… regulations and policy enforcement can change how companies are operating in a country" (IPDD, 2022, p. 25). Hence, investors want governments to create an investment environment in which they are rewarded for their sustainable investment practices and that public policies elevate the minimum requirements to give them and their investee companies a competitive edge against players that do not feature the same level of ESG performance.

RP2: Investors engage in public policy to create an enabling environment for sustainable investments, allowing investors to seize investment opportunities, and creating a level playing field that rewards companies and investors for higher levels of social and environmental performance.

5.3. Managing investment risks

There are 56 quotations supporting the fact that investors engage in public policy to manage various types of investment risks from their own portfolios.

First, encouraging the creation of public policies that require improved **corporate disclosure and transparency** for the management of investment risks is mentioned 13 times. For example, in Australia, The Investor Agenda engaged with Australian authorities to call for alignment of corporate disclosure requirements with the TCFD. The investor group argued that voluntary disclosure is "insufficient in delivering transparency, consistency and comparability of disclosures that are required for informed and efficient asset allocation," and that investors are spending unnecessary resources trying to reach best practice, resulting in reporting burden (The Investor Agenda, 2022). In the 2021 Global Investor Statement to Governments on the Climate Crisis, The Investor Agenda defended that investors "need access to adequate information on how companies are assessing and managing the risks and opportunities presented by climate change," and requested that the targeted governments implement mandatory climate risk disclosure requirements aligned with the TCFD recommendations (The Investor Agenda, 2022).

Secondly, 12 quotations are found supporting that investors engage in public policy to manage investee companies' market (eight mentions), operational (two mentions), physical (four mentions), regulatory (eight mentions), and reputational risks (five mentions), solutions that rely on solving market and policy failures (PRI, 2014). There is some evidence that **ESG factors,** such as climate change and deforestation, have an increasing impact on the ability of investee companies to deliver long-term returns. For instance, the IPDD shows concern that investee companies' exposure to deforestation in their operations and supply chain increases **market and regulatory risks** as it can make it more difficult for them to access international markets, "as a result of [the] inability of local companies to meet consumer country and regional regulations and standards relating to finance, ESG factors, deforestation and human rights" (IPDD, 2022, p. 18). As an example of consumer country regulations, the European Union reached a regulatory agreement ensuring that a set of key goods sold within the EU market, including palm oil, cattle, and soy, does not contribute to deforestation or forest degradation in the EU or elsewhere in the world (BMZ, 2022; European Commission, 2022).[10] Shareholders for Change (2021) are also concerned about deforestation-related risks in Brazil, arguing, in a letter sent to the Brazilian government, that "more and more consumers are boycotting Brazilian products" and "investors are refraining from further investment in securities of such Brazilian companies" as they see "deforestation and the associated impacts on biodiversity and climate change as systemic risks to their reputation and portfolios."

Thirdly, **acting on ESG systematic risks** is mentioned 13 times as a reason for policy engagement. As noted earlier, a great share of financial performance derives from beta (market movements) (Brinson et al., 1986; Hawley & Lukomnik, 2018; Ibbotson, 2010). Deforestation is considered a systematic risk by the IPDD that is increasingly financially material to investment portfolios (IPDD, 2022), requiring a "holistic, multi-pronged approach" (PRI, 2023). Likewise, the Seventh Generation Interfaith Coalition for Responsible Investment deems many issues, such as climate change and human trafficking, as systematic in nature, thusly unable to be adequately addressed without changes to public policy (Seventh Generation Interfaith, 2023).

Finally, managing ESG systematic risks from their own **sovereign bond investments** is mentioned six times as a reason for policy engagement. For instance, Colchester Global Investors (2020, p. 2) engages "with sovereigns helping to inform, promote and potentially drive best practices delivering better social and economic outcomes" since they "believe that countries with stronger governance, healthier and more educated workforces, and higher environmental standards tend to produce better economic outcomes," leading to "more stable debt and currency paths, and ultimately better risk-adjusted returns." In the case of deforestation, IPDD investors are concerned about the conditions for investing in, or providing financial services to, countries rich in such natural resources, as the violation of the rights of indigenous peoples might potentially increase reputational, operational, and regulatory risks resulting in a higher risk valuation of the sovereign bonds of these countries, impacting their creditworthiness (IPDD, 2022; TFA, 2023). In this context, issues like climate change, income inequality, and human rights become more prominent in risk assessment, potentially affecting sovereign bond valuations (PRI, 2020a, 2020b).

RP3: Investors engage in public policy to manage investment risks.

5.4. Ethical reasons

We also find two quotations mentioning ethical and/or faith-based reasons to engage with governments. In the context of engaging with the Brazilian government on deforestation, the leader of the SfC engagement, BKC, wrote in their letter to the Brazilian government, that "this devastating environmental damage is in stark contrast to the Catholic guiding theme of preserving creation and

[10] Other examples: In Germany, the Supply Chain Act, which entered into force January 1, 2023, obliges companies with 3,000 or more employees – from 2024, companies with 1,000 or more employees – with a registered office or branch in Germany, to fulfil their due diligence obligations in their supply chains with regard to respecting internationally recognized human rights and certain environmental standards (such as the UN Guiding Principles on Business and Human Rights) (Bundesgesetzblatt, 2021). A European Supply Chain Act is currently under discussion (European Commission, 2022).

the call of his holiness Pope Francis to protect the climate and the environment in the encyclical Laudato Si'" (BKC, 2021). In their general statement on why they do policy advocacy, SGI writes on their website that "SGI members believe that the perspective of faith-based investors needs greater visibility in public policy debates and can be critical in advancing social justice and environmental sustainability" (Seventh Generation Interfaith, 2023).

As noted, these statements are solely brought forward by faith-based investors and in combination with other reasons, such as managing investment risks and/or seizing investment opportunities and creating an enabling environment for sustainable investments.

RP4: Values-based investors engage in public policy for ethical reasons.

6. Discussion and conclusion

According to the literature review and the cases analyzed, investors are encouraged to engage with policymakers in order to not just comply with their fiduciary duty and manage investment risks, but also create a level playing field and an enabling environment for sustainable investments. Faith-based investors are also concerned with ethical values.

Drawing on the universal ownership theory, our initial hypothesis is that investors started engaging with policymakers to manage the systematic risks of their portfolios, given the increasing impact of ESG issues to the long-term health of whole economies and, therefore, to beta performance. However, the research findings indicate that this is only part of the explanation.

From a corporate investment perspective, one reason why investors are engaging with policymakers is to create enabling conditions for investments in companies with good ESG performance. If externalities are not required by the rule of law to be internalized, then ESG laggards have a competitive advantage in comparison to proactive companies that have incurred in costs, whether, for example, to reduce their GHG emissions or to combat human rights violations. By acting as such without the right conditions and incentives, these ESG-leading companies tend to compromise their financial returns and those of their investors. On the other hand, the enactment and enforcement of public policies that require companies to internalize externalities contribute to levelling the playing field for all businesses and to creating more rewarding conditions for leading companies and their investors; which Eurosif (2021, p. 10), claims works "by making harmful investments more expensive and sustainable investments more competitive." Additionally, it favors the appearance of new investment opportunities that would be otherwise not financially viable.

Investors are also found to engage with policymakers to manage ESG risks that they deem financially material. Having regulations that require investee companies to report on ESG issues in a comprehensive, periodic, and comparable manner will help investors to monitor and manage the ESG risks of their own portfolios. Moreover, having enforced regulations requiring companies to properly manage material ESG risks (e.g., climate risks) improves investee companies' management, avoids the need for investors to engage with individual companies on the same ESG issues, and protects investor portfolio value.

From a sovereign investment perspective, sovereign bond investors are also encouraged to engage with policymakers to reduce reputational, operational, and regulatory risks that arise from failing to address ESG issues that have the capacity to affect the valuation of the sovereign bonds of these countries. However, engagement with sovereigns is not a "one-way street." Governments and investors are already engaging in the context of green bond issuance frameworks, with policymakers and sovereign issuers beginning to understand that their debt will increasingly be valued based on ESG criteria and their performance on the SDGs. Channels and processes for dialogue might be less well established in the sovereign debt markets so far, but this is beginning to change.

Thus, universal ownership theory does not seem to fully explain why investors engage with policymakers. It appears that other theories, like institutional theory, might be complementary theoretical frameworks that help explain policy engagement. According to the economic approach of institutional theory (North, 1990), the institutional framework of a society serves to regulate economic activities by providing the 'rules of the game,' which include formal rules (e.g., laws, policies), informal rules (e.g., norms of behavior and conventions) and enforcement. By encouraging the creation of the regulatory conditions under which corporations and investors are likely to integrate ESG factors, policy engagement seeks to facilitate the channeling of financial flows to sustainable activities. This is also beneficial to countries interested in improving their business environment, reducing risk perception, and attracting private investments.

This study makes several academic and practical contributions. This research contributes to the academic literature related to investor engagement, analyzing a new form of investor activism: sovereign engagement. It also contributes to the public policy literature by identifying a new stakeholder influencing public policy that has not been the focus of academic research so far. As for practical contributions, this study offers insights to governments on the demands of the investment community, providing inputs on how sovereign entities can attract private investments to achieve their national climate and SDG commitments.

Given that transparency on engagement activities is low, with only a few investors engaging via a third-party or directly and/or indirectly with policymakers disclosing public information (PRI, 2022a), we encourage future research to further investigate our research propositions by collecting primary data. Since public data availability is limited, it would be recommended to complement data collection by interviewing investors involved in the case studies analyzed. Additionally, future research could analyze what challenges investors find in engaging with policymakers. As mentioned in the introduction, the still limited investor engagement with policymakers might reflect general skepticism about its effectiveness as well as a lack of public policy knowledge and resources. It would be interesting to verify whether these challenges are still perceived by investors, given the increase in policy engagement initiatives and the employment of strategies to overcome these barriers, such as collaborative engagement. Further research could also investigate the policymaker perspective, including their perspectives of why investors are engaging in public policy. Additionally, we suggest future studies analyze the implications of policy engagement and eventual conflicts of interest related to national sovereignty, arising from developed country actors seeking to influence public policy in emerging market jurisdiction, since the targeted country could interpret engagement as questioning its right to act within its borders, particularly on sensitive topics like human rights. Finally, further studies should analyze the weight of beta in investment returns, thus providing further insights on the importance of systematic risks.

Research shows that investors started engaging in order to change the rules of the game. Evidence will show if they can play a constructive and effective role in policy debates on sustainability issues.

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