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AN AFFILIATE OF NATIXIS INVESTMENT MANAGERS

SUSTAINABILITY

NEWSLETTER –FEBRUARY 2025

CONTENT

EUROPE SUSTAINABILITY REGULATION
OMNIBUS & THE EU TAXONOMY

01

EU Platform on Sustainable Finance Publishes Report on the Simplification of the EU Taxonomy

The Platform's report proposes five main simplification measures:

- **Refining the DNSH assessment and reporting obligations** by distinguishing between users (non-financial vs. financial), uses (turnover vs. CapEx), and geographies (EU vs. non-EU exposures).
- Introducing a materiality principle applicable to all entities, materiality thresholds for all non-financial company KPIs, and **a simplified DNSH assessment for the turnover KPI**, as well as clarifying the OpEx KPI calculation and limiting the mandatory scope to R&D.
- Defining **clear guidelines for the use of estimates** within the EU Taxonomy framework and establishing safe harbors for financial sector reporting.
- Allowing proxies and estimates across all assets in the context of the Green Asset Ratio (GAR) while introducing a simplified retail assessment and ensuring a symmetrical GAR.
- **Developing a simplified and voluntary approaches for listed and unlisted SMEs**, as well as banks and investors, to integrate the EU Taxonomy into their disclosures.

Go to the full article

02

The new 'Omnibus' package to exempt 80% of companies from CSRD reporting requirements

On the 26th of February, the European Commission released the first 'Omnibus' package, containing a series of proposals to reduce sustainability reporting requirements for companies:

- The proposal plans to **remove 80% of companies from the scope of the CSRD** and limit the sustainability information that large companies and banks can request from smaller companies.
- The new scope **would only include companies with > 1,000 employees** and with (i) revenue greater than €50 million net turnover or (ii) a balance sheet above €25 million, removing ~ 80% of companies from the scope of the CSRD.
- The Commission expects the new proposal to create approximately **€6.4 billion in administrative cost savings** for companies.
- The Commission also plans to revise the ESRS, notably with the aim of **not introducing planned sector-specific standards or requiring reasonable assurance** under the CSRD.
- The application of the CSDDD has also been delayed by a year for large companies to July 2028.

Go to the full article

EUROPE SUSTAINABILITY REGULATION
THE EU CLEAN INDUSTRIAL DEAL

03

The European Commission publishes the Clean Industrial Deal

The Clean Industrial Deal (the Deal) outlines the EU's roadmap for competitiveness and decarbonization following the Draghi report which was published in September 2024.

- The Deal is a commitment to a**ccelerate decarbonization, reindustrialization, and innovation**, with a focus on energy intensive industries and clean tech.
- The roadmap highlights **six key business drivers** (1) affordable energy, (2) lead markets, (3) financing, (4) circularity and access to materials, (5) global markets and international partnerships, and (6) skills.
- The Commission also adopted an **Action Plan for Affordable Energy** which includes measures to lower energy bills for industries, businesses, and households in the short term, while speeding up critical structural reforms.
- The roadmap also emphasizes the importance of boosting demand for clean products noting that 'building a business case for decarbonized products also requires measures on the demand side'. Notably, **the Commission will review public procurement policies** to help overcome barriers to market entry (i.e., targeted mandates, non-price criteria for sustainability).
- The Commission also plans to **adopt the delegated act on low carbon hydrogen in Q1 2025** to provide certainty to investors and clarify rules for producing low carbon hydrogen.

Flagship actions - Access to affordable energy and infrastructure	Timeline
Action Plan on Affordable Energy	Q1 2025
EIB pilot offering financial guarantees for PPA offtakers, with a focus on SMEs and energy-intensive industry	Q2 2025
Legislative proposal on the extension of the Gas Storage Regulation	Q1 2025
Clean Industrial Deal State aid framework	Q2 2025
Recommendation on network charges	Q2 2025
Industrial Decarbonisation Accelerator Act: • Speed-up permitting for industrial access to energy and industrial decarbonisation	Q4 2025
Recommendation on energy taxation	Q4 2025
Guidance on CfD design, including on combining CfDs and PPAs	Q4 2025
Guidance on promoting remuneration of flexibility in retail contracts	Q4 2025
European Grids Package	Q1 2026
KPI – Increase economy-wide electrification rate from 21.3% today to 32% in 2030[15] KPI - Annually install 100 GW of renewable electricity capacity up to 2030[16].	

Go to the full report

EUROPE SUSTAINABILITY REGULATION
FEBRUARY UPDATE

04

The Swiss Federal Council approves new emission reduction target of 65% by 2035 compared to 1990 levels

The Federal Council approved Switzerland's new GHG emission reduction target under the Paris Agreement during its meeting on the 29th of January in alignment with the Swiss Climate and Innovation Act and the recommendations of the IPCC.

- Switzerland should reduce its GHG emissions **by at least 65% by 2035 in comparison to 1990 levels** and by 59% on average between 2031 and 2035.
- The objectives to be achieved primarily through domestic measures and are to be set out in national laws, primarily in **the CO2 Act for the period from 2030**.
- The Federal Council's long-term emission reduction targets for individual sectors are based on **the Swiss Federal Office of Energy's Energy Perspectives 2050+** and include (i) reducing GHG emissions from the industrial sector by 90%; (ii) achieving building stock and land transport, with a few exceptions, that no longer generate GHG emissions, (iii) reducing GHG emissions from domestic agricultural production by at least 40%, and (iv) reducing the climate-impact of international travel from Switzerland.

Go to the full article

05

Spain becomes the first country in Europe to ratify the Global Ocean Treaty

On the 4th of February, the VP of Government and Minister for the Ecological Transition and the Demographic Challenge, Sara Aagesen, announced that **Spain officially ratified the Treaty on Marine Biological Diversity in areas beyond the National Jurisdiction** (the BBNJ).

- The BBJN establishes a robust legal framework for all activities in the ocean and seas by regulating human activities on the high seas, designating protected marine areas, and establishing a mechanism for equitably sharing the benefits derived from the exploitation of marine genetic resources.
- Notably, the BBJN assumes the commitment to declare 30% of the surface of the high seas as a protected area before 2030. The treaty plays a vital role in achieving the global 30 x 30 objective agreed during the Kunming-Montreal Global Biodiversity Framework.
- The treaty must be ratified by 60 countries to go into force; the first country to ratify was Chile in February 2024, which is bidding to host the BBNJ headquarters. In addition to Spain, 15 other countries have ratified the treaty.

Go to the full article

US SUSTAINABLE FINANCE REGULATION
FEBRUARY UPDATE

06

133 US Mayors and Local Elected Officials Call on Congress to Preserve Clean Energy Tax Credits

On the 10th of February, 133 mayors and local elected officials from 39 states **sent a letter to members of Congress calling on them to preserve all clean energy tax credits** available to state and local governments through elective pay.

- The signatories emphasized their concern that the repeal of clean energy tax credits could create economic uncertainty in their communities.
- Elective pay provides local governments, hospitals, schools, places of worship, and other organizations tax credits and cost savings to access clean, affordable energy, helping to save thousands of dollars on infrastructure improvements and energy projects. **A repeal could increase annual energy costs by $489 for affected families**, and result in job losses, reduced private financing, slowed economic growth, and diminished competitiveness.
- These credits have transformed cities such as San Antonio, Texas, which has installed 42 solar panel sites across the city, which are **expected to save up to $11 million in energy costs over the next 25 years** while creating full-time jobs and reducing pollution.

Go to the full article

07

Challenge to California Climate Disclosure Laws Partially Dismissed

The suit was brought in January 2024 by US industry groups, challenging California's Climate Corporate Data Accountability Act ('SB 253') and Climate-Related Financial Risk Act ('SB 261'). The laws require companies operating in California to disclose their direct and indirect GHG emissions, climate risk exposure, and mitigation initiatives.

- The laws were challenged by the Plaintiffs on three grounds, alleging that they (i) violate the First Amendment to the U.S. Constitution; (ii) are preempted by federal law, therefore violating the Supremacy Clause of the U.S. Constitution, and (iii) violate constitutional limits on extraterritorial regulation by attempting to regulate GHG emissions beyond California's borders.
- The court held that **the challenges to SB 253 were not yet justiciable** because the California Air Resources Board ('CARB') has not yet put forth the regulations required under the law, and therefore no requirements have been imposed on the Plaintiffs.
- For the challenges made to SB 261**, the Court proceeded to dismiss grounds two and three,** notably stating that the Plaintiffs failed to plausibly allege discriminatory purpose or differential treatment of in-state and out-of-state economic interests.

Go to the full article

ESG MARKET INSIGHTS
2025 US BOARD MEMBER PRIORITIES

01

New corporate board member survey finds 76% of directors prioritizing growth opportunities in 2025, while directors prioritizing shareholder engagement falls to 11%

Corporate Board Member conducted a survey of more than 200 directors of publicly traded companies in the US on their board agenda for the year. The key findings include:

- Top priorities for 2025 include pursuing growth (76%), optimizing financials (50%), M&A transactions (37%), and improving CEO/C-suite and board succession planning (34%)
- **42% of directors see the potential of AI/generative AI to optimize operations and enhance workforce productivity and 51%** reported that their board has reviewed its process for identifying and disclosing cyber security incidents.
- **82% of directors believe that** a board should not encourage C-suite leaders to speak publicly on controversial issues.
- **Only 11% of directors consider shareholder engagement and activism a top priority**, a significant downshift from prior years.
- Moreover, **only 11% report that developing / implementing a sustainability strategy is in their top five priorities** for the year while only 10% report prioritizing the management of geopolitical risks.

Go to the full report from the Corporate Board Member

ESG MARKET INSIGHTS
OECD PUBLISHES ANALYSIS OF ESG METRICS

02

The OECD's new report *Behind ESG Ratings* highlights the significant imbalances across ESG topics and divergences in methodologies used by ESG data providers

The OECD assessed the scope and characteristic of over 2,000 ESG metrics from eight major ESG rating products, identifying four key findings:

1. **Imbalance between ESG topics:** There is a significant gap across coverage of ESG topics by ratings providers – less standardized / mature ESG issues typically lack comprehensive and granular metrics compared to established topics. For example, on average, over 20 different metrics are used to measure performance across topics such as business ethics and environmental management, while for biodiversity and business relations this is less than five metrics.

2. **Lack of comparability between ESG metrics:** the assessment found a significant divergence when comparing the scope of metrics used for the same topic across rating products. For example, one of the ratings uses 28 times more metrics to measure Corporate Governance performance than another. Another example is the measurement of corporate GHG emissions, for which the range of metrics varies from 1 to 47.

3. **Metric characteristics:** ESG performance is largely rated based on business' effort rather than the effect in the real-economy. 68% of ESG ratings products are based on input-based metrics which capture self-reported policies and initiatives put in place to address potential and actual ESG impacts, risks, and opportunities. In comparison, only a third of the metrics rely on output-based metrics, focusing on the outcomes of these policies and activities. The reliance on input-based metrics could be incentivizing a 'check-box' approach, rather than prioritizing risk prevention and actions in the real economy.

4. **The current metrics are insufficient to assess compliance with OECD standards on responsible business conduct:** OECD instruments on responsible business conduct promote risk-based due diligence, including the identification and prioritization of adverse impacts. In contrast, ESG rating products tend to measure how companies manage impacts, risks, and opportunities with respect to a specific topic – not across topics – irrespective of their interlinkages and interdependencies.

Moreover, most ESG rating products assess observance or 'violations' of the OECD guidelines through controversy-related metrics as a proxy, rather than evaluating a company's due diligence efforts and effectiveness in mitigating sustainability impacts.

Go to the full report from the OECD

ESG MARKET INSIGHTS
SUSTAINABILITY & CLIMATE TRENDS FOR 2025 (1/2)

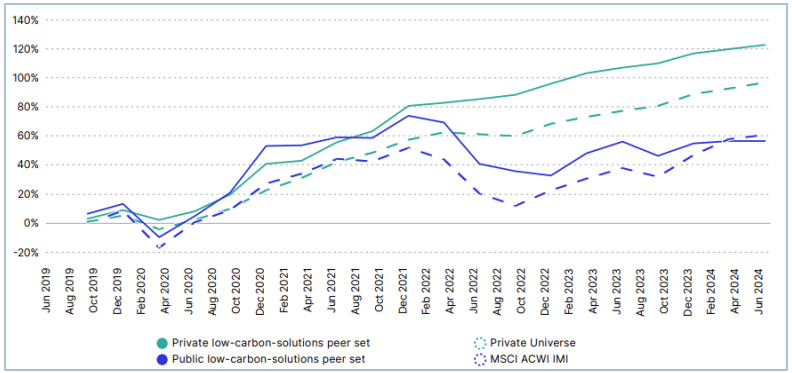
03 MSCI's new Sustainability & Climate Trends report for 2025 emphasizes focus on climate risk, energy transition, adaption finance for emerging economies, and AI

(1) Focus on private-market low-carbon solutions to drive the energy transition

MSCI identified companies with exposure to key energy transition themes in public and private markets, finding significant differences between the exposure and growth of the markets:

- In public markets, ~30% of the market value of the solutions peer set was in the consumer-discretionary sector, notably automobile manufacturers. In private markets, the solutions peer set was concentrated in utilities, with a focus on renewable electricity.
- The value of the public low-carbon solutions peer set (market cap of USD 4.4 trillion) was 23x larger than the private solutions set (NAV of USD 184 billion). However, the 5-year CAGR of the private solutions set was 17.0%, significantly higher than the 11.9% for public low-carbon solutions.
- Outperformance in private low-carbon solutions investments – The five-year cumulative returns from the private solutions peer set reached 123% by June 30th, 2024 – outperforming the returns of the asset-class-reweighted private-capital universe (97%), the MSCI ACWI IMI (61%), and the public solutions peer set (57%).

Cumulative return for low-carbon solutions peer sets vs. benchmarks in private and public markets



Data as of October 2024. Source: MSCI Sustainability & Climate Trends to Watch 2025 report. Data from the MSCI Private Capital data universe as of June 30, 2024. Data based on MSCI ESG Research, MSCI Private Capital.

Go to the full report from MSCI

ESG MARKET INSIGHTS
SUSTAINABILITY & CLIMATE TRENDS FOR 2025 (2/2)

03

MSCI's new Sustainability & Climate Trends report for 2025 emphasizes focus on climate risk, energy transition, adaption finance for emerging economies, and AI

(2) Climate risk and the impacts of extreme weather events on the economy in the short- and long-run

- 84% of the 350 surveyed financial-market participants agreed that damage to infrastructure from extreme-weather events would negatively impact regional economies.
- Managing physical risk is no longer a long-term concern; as we see the frequency and severity of extreme-weather events increase, businesses and homeowners may face rising insurance premiums, or in the worst-case scenario, find their properties uninsurable.

(3) Increasing corporate spending on AI while investors and regulators are more cautious with major concerns related to data privacy, copyright, and discrimination or bias.

- AI has shown significant promise for the health-care sector, from improving the efficiency of clinical workflows to drug discovery. However, this also poses several risks. For example, training a model on limited, poor-quality or biased data can lead to a biased product which is not applicable to general patient populations (e.g., IBM Watson Health) and expose the company to significant legal risks.

(4) Carbon markets: quality vs. quantity

- 2025 may be a turning point for carbon markets; in 2024, an analysis conducted by MSCI of more than 4,000 registered voluntary carbon projects found that 47% of used and claimed credits ('retired') up until July 2024 come from projects with an MSCI Carbon Project Rating of B or lower, compared to only 8% of projects between A and AA, with no projects qualifying for MSCI's highest rating of AA.
- New projects being developed appear to be of higher integrity, notably for engineered and nature-based projects that remove CO2 from the atmosphere.
- The standards for carbon markets are also increasing focus on quality; in June 2024, the Integrity Council for the Voluntary Carbon Market (ICVCM) announced the first set of carbon-crediting methodologies that qualify for its Core Carbon Principles.
- MSCI also found that of the 8,844 firms in the MSCI ACWI Investable Market Index, those that used carbon credits during 2017 and 2022 also performance better on a range of climate metrics, including transparency on disclosing their scope 1, 2, and 3 GHG emissions and the credibility of their emissions-reduction targets.

Go to the full report from MSCI

NEW IN RESEARCH
STATE OF CLIMATE & NATURE IN 2025

01

The World Economic Forum's *State of Nature and Climate* briefing paper for 2025 finds only 35% of companies globally on track to meet climate targets

The paper provides a global stock take on the health of planetary systems and the state of corporate action in addressing the nature and climate emergency to drive transparency, accountability, and comparability.

- The Planetary Health Check, based on the planetary boundaries, found that **annual global warming reached a record 1.54°C above the pre-industrial average in 2024.**
- The Corporate Health Check found that **only 10% of corporates demonstrate tangible action to address the climate and nature emergency**, with only 1% performing at the highest assessment level defined by the CDP* (including having a net zero / SBTi approved target).
- Globally, **only 35% of companies are on track to meet their climate targets**; Europe leads with 46% of companies on track, followed by North America (33%) and Asia (32%).
- **Disclosure on nature remains limited**; although water a material issue for 75% of companies, only 48% disclose data on water-related risks.

*the companies analyzed under CDP's Corporate Health Check represent 67% of the global market capitalization

Figure 3 **Company emission disclosures**

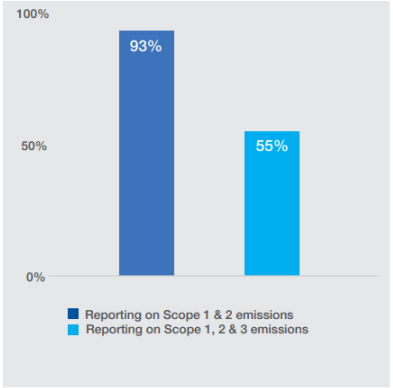


Figure 4 **Company nature disclosures**

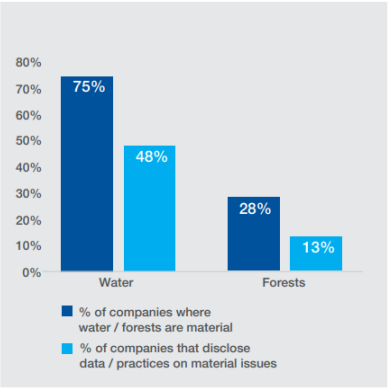


Image source: State of Nature and Climate 2025, Centre for Nature and Climate, Briefing Paper, January 2025, World Economic Forum.

Go to the full report from the World Economic Forum

NEW IN RESEARCH
EXECUTIVE BENCHMARK ON INTEGRATED REPORTING

02

97% of executives agree that a strong sustainability reporting program will give businesses a competitive advantage in the next two years finds Workiva survey

97%
of executives believe integrated financial and sustainability data helps identify performance gaps that enhance financial opportunities

85%
of executives who were intending to disclose GHG emissions will move forward with disclosures irrespective of any political developments within their country

97%
of investors are more likely to invest in companies with assured integrated reporting

73%
of executives believe that their reporting technology is insufficient for complying with new climate regulations

Workiva polled 1,601 executives as well as 222 institutional investors globally on their expectations for integrated financial and sustainability reporting:

- The survey found that regardless of any potential fallout from the elections held in 100+ countries in 2024, **85% of executives still intend to move forward with their existing plans to disclose GHG emissions.**
- Of the 286 executives who said that they do not need to comply with the CSRD, **75% still intend to at least partially align their reporting with the mandate.**
- The new standards have exposed a gap between investor priorities and executive confidence – **92% of investors rank data accuracy as foundational for evaluating an organization**, while 29% of executives are not fully confident in the reliability of their ESG/sustainability reporting.
- **92% of executives say that their organizations adhere to 'responsible AI' practices**; however, 77% of executives also believe that their organization's current approach to the adoption of AI tools could introduce risk.
- Investors are embracing AI, with 72% using generative AI for summarizing data, 71% to evaluate a company's financial performance, and 67% to evaluate a company's sustainability performance.

Go to the full survey from Workiva

NEW IN RESEARCH
PHASING-OUT COAL IN EMERGING ECONOMIES

03 The World Economic Forum's new white paper on financing the phase-out of coal in emerging economies provides financial levers for early-phase out

- The phasing-out coal-fired power generation is particularly challenging for emerging markets, which make up 80% of global coal consumption:
- Two key financial levers for early phase-out include **(1) lowering the cost-of-capital (WACC)** to free up cash flows and enable the asset owner to realize equity value earlier (often achieved through a blend of commercial and concessional financing) and **(2) transition credits** compensating asset owners for retiring CFPPs early.
- The credibility of CFPP phase-out plans can be evaluated across three levels:
  - **Government & systems-level:** national transition strategy, enabling market environment, just transition provisions, etc.
  - **Entity-level:** science-based pathways for CFPP phase-out (e.g., is the plan sector- and/or region-specific?), additional financing needs, etc.
  - **Asset-level:** details of forecast BAU CFPP operations profile (i.e., is it climate ambitious), measures to ensure the CFPP will close in line with the phase-out plan, and additionality.

Considering the number of operational CFPPs globally, scaling coal phase-out through concessional capital and transition credits will be challenging. The World Economic Forum completed an analysis of the opportunities and limitations for Coal Retirement Mechanisms (CRMs) using cost-of-capital levers, based on 10 real-life plants in the Philippines. Key findings from the analysis:

- CRMs leveraging large concessional financing are costly and have limited scalability.
- Cheaper debt, financial re-gearing and extended loan tenors can be used to enable early retirement by allowing asset owners to realize equity value faster and lowering the cost of capital. In addition, financial re-gearing offers higher payouts to asset owners than concessional financing, providing a better incentive for early retirement.
- Newer, larger CFPPs are better suited to market-based CRMs given the remaining equity value and abatement potential, while concessional financing is a preferable option for older, smaller CFPPs given that less concessional capital goes further.

Go to the full white paper

IN FOCUS: ARTIFICIAL INTELLIGENCE
OPPORTUNITIES & CHALLENGES FOR SUSTAINABILITY

01 Opportunities, risks, and regulatory frameworks for AI use – what are the sustainability benefits and impacts of AI?

As AI is increasingly adopted across sectors and regions, numerous frameworks and use cases for AI have emerged to achieve sustainability objectives. For example, **the AI for Good initiative, supported by the UN, which provides a framework for the ways in which AI can be leveraged to achieve the SDGs.**

Use cases for how AI for Good initiatives align with the SDGs include:

- Healthcare (SDG 3) – AI can enhance diagnostics and enable treatment personalization, allowing early detection of disease and outbreak management through data trend analysis.
- Environmental conservation (SDGs 13, 14, 15) – AI can be leveraged for biodiversity monitoring, climate modelling, and the development of environmental protection and conservation strategies.
- Education (SDGs 4, 5, and 10) – AI can be used to create more personalized learning platforms that cater to individual student needs, improving education outcomes and increasing access to learning content.
- Agriculture (SDs 2, 12, and 15) – AI can be used to make agriculture techniques more precise and efficient, for example by using satellite images and sensors to optimize water, fertilizer, and pesticide use.

However, there are also significant risks and sustainability concerns associated with the use of AI across the lifecycle of AI systems.

Key issues linked to the environmental footprint of AI include:

- **Energy consumption:** AI models require substantial computational power, resulting in high energy use, particularly during the training phase of AI models. The significant energy required also results in considerable GHG emissions, especially if the energy source is non-renewable.
- **Water consumption:** Large data centers, which are the core infrastructure required to train AI models, need cooling systems that consume significant amounts of water for cooling.
- **Hardware & e-waste**: hardware such as servers, GPUs, and other specialized equipment also contribute to the carbon footprint of AI systems. The production and disposal of specialized equipment can have a significant environmental footprint, including the extraction of raw materials, GHG emissions from manufacturing, and disposal of electronic waste.

Go to the full article from EY

IN FOCUS: ARTIFICIAL INTELLIGENCE
OPPORTUNITIES & CHALLENGES FOR SUSTAINABILITY

01 Opportunities, risks, and regulatory frameworks for AI use – what are the sustainability benefits and impacts of AI? (cont'd)

- Research on how AI models and supply chains can be made more efficient and sustainable is ongoing; this includes optimizing energy use, using renewable energy sources, and developing water-efficient cooling technologies.
- Other solutions include education on the impacts of AI. For example, **image generation is more energy and carbon intensive than text generation** and large language models such as ChatGPT are more energy intensive than small language models designed for specific tasks.
- In addition, regulations related to AI should include considerations of the environmental and social impacts of the entire AI lifecycle. **The EU AI Act, which was adopted in June 2024,** became the first regulation on AI, providing a framework for regulating AI-related risks:
  - Under the Act, certain AI uses are classified as 'unacceptable risk', such as AI applications that are used for biometric identification and categorization of people.
  - Models not classified as 'high risk' will need to comply with the Act's transparency requirements, including disclosing content created by AI and publishing summaries of copyrighted data used for training.

Social risks associated with AI use:

AI also poses social and business ethics related risks, including (Forbes):

- **Bias and discrimination** – AI systems can perpetuate existing societal biases if they are based on biased training data or algorithmic design.
- **Data privacy concerns** – AI models collect and analyze large amounts of personal data, leading to issues related to data privacy and security and exposing companies implementing AI models to regulatory risks related t data access laws.
- **Job displacement** – AI-driven automation could lead to job losses across various sectors, particularly for low-skilled workers. However, there are also studies indicating that AI will create more jobs than it eliminates. The key is to ensure a just and inclusive transition, including upskilling employees.
- **Economic inequality** – AI may disproportionately benefit wealthy individuals and large corporations as smaller firms and low-income households may face barriers to implementing AI (access, training, etc.).

To address these issues, various organizations have developed principles to guide the responsible use of AI, which are synthesized on the next page.

Go to the full article from EY

IN FOCUS: ARTIFICIAL INTELLIGENCE
PRINCIPLES FOR RESPONSIBLE AI

02

Seven Key Principles for Responsible AI – Synthesis of Findings Across Frameworks

#	Principle	Sub-dimensions
1	**Accountability**	• Auditability: ability to assess AI applications (algorithms, data, design) • Responsibility: oversight of various stages and activities involved in the deployment of AI across people, roles, and departments
2	**Diversity, non-discrimination, & fairness**	• Accessibility: design of AI systems to make them accessible and usable for everyone • Bias: biased results can perpetuate existing human biases in society that can lead to harmful outcomes
3	**Human agency & oversight**	• Human review: the right of a person to challenge a decision made by AI • Human well-being: AI must include human well-being as a central measure of success during development 4
4	**Privacy & data governance**	• Data quality: accuracy of data set • Data privacy: considerations of data privacy throughout the data lifecycle • Data access: national and international rights laws for AI data access
5	Technical robustness & safety	• Accuracy: ability of AI systems to make correct judgements • Reliability: AI system's ability to work under a range of inputs / contexts • General safety: safety rules and fallback plans established for AI systems • Resilience: protection of AI systems against vulnerabilities (i.e., hacking)
6	Transparency	• Explainability: ability to explain the technical processes of an AI system and related human decisions • Communication: human right to be informed in advance to interacting with an AI agent • Traceability: tracking of data and processes that yield AI system's decisions
7	Social & environmental well-being	AI systems should be developed with the objective of addressing global challenges, including: • Social well-being: Impact of AI across all areas of society, including jobs and education (i.e., job displacement) • Environmental well-being: sustainability and ecological responsibility of AI systems embedded in design of AI models

Source: Emmanouil Papagiannidis, Patrick Mikalef, Kieran Conboy, Responsible artificial intelligence governance: A review and research framework, The Journal of Strategic Information Systems,Volume 34, Issue 2, 2025,101885, ISSN 0963-8687, https://doi.org/10.1016/j.jsis.2024.101885.

Go to the full article on responsible AI governance

IN FOCUS: ARTIFICIAL INTELLIGENCE
AI IN EU INVESTMENT FUNDS

03

ESMA publishes new study on the adoption, strategies and portfolio exposures of AI in the EU investment management industry

The study focuses on two main ways in which AI impacts fund managers: the operational use of AI in the investment process and portfolio investment in AI by EU funds.

Operational use of AI by Fund Managers

Since the first generative AI (GenAI) tools based on large language models (LLMs) became commercially available in 2022, asset managers have shown renewed interest in understanding how AI is deployed across investment management and what the opportunities are for the fund management industry.

- According to surveys conducted by Mercer Investments and PwC in 2024, a majority of asset and wealth managers believe that disruptive technologies (i.e., AI and GenAI) are improving operational efficiency (84%), driving revenue growth (80%), and boosting employee productivity (72%).
- However, only a few investment managers currently view AI as a key part of the investment process (14%); fund managers are implementing AI to augment existing capabilities (e.g., investment research), rather than to make investment decisions.

EU investment funds' use of AI

ESMA identified the funds that disclosed their use of AI or machine learning (ML) in their communications to investors to assess how fund managers are implementing AI in the investment process:

- The results indicated that most funds don't explicitly advertise the use of AI; out of the 44,000 EU investment funds, 145 funds indicated leveraging AI (specifically, ML) in their investment strategies.
- In only 30% of the funds AI appeared to play a key role in the investment decision (often smaller funds, accounting for only 5% of the original sample's AUM).
- Funds using AI have a mixed success among investors, having experience mostly net outflows over the past 3 years, fairing almost always worse than other EU investment funds when normalized by the funds' AuM.
- ESMA's findings conclude that most funds that use AI have not yet adopted a systematic approach to implementing AI-based models, and that many funds that take advantage of AI tools to carry out intermediate steps (e.g., investment research) largely omit references to their use of AI.

Go to the full report from ESMA on the adoption of AI

IN FOCUS: ARTIFICIAL INTELLIGENCE
AI IN EU INVESTMENT FUNDS

03

ESMA publishes new study on the adoption, strategies and portfolio exposures of AI in the EU investment management industry (cont'd)

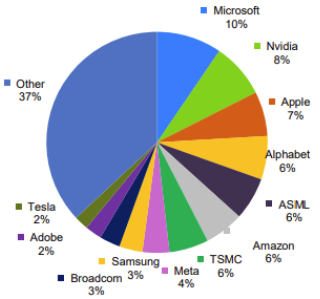
Increasing investor interest in the impact of AI on sectors such as healthcare, finance, and manufacturing has led to the creation of numerous indices that aim to track AI's high-growth opportunities. ESMA evaluated seven indices that focus on AI* finding that:

- These indices tend to offer a more diversified exposure to the sector than the one that would result if the selected companies were weighted by their market capitalization, with the largest index constituents not weighing beyond 4-5%.
- The 'Magnificent Seven' stocks, along with a few other large tech companies, appear in all the indexes. However, the rest of the companies that represent the AI sector across the indexes are highly diversified.
- The diverse composition of AI-focused indices reflects the wide range of companies included under this theme. Most of the indexes aim to include companies using AI at various stages of their value chain, defined as AI 'enablers', 'developers', 'engagers' or 'enhances', reflecting the uncertainty and subjectivity related to what exactly encompasses 'AI' technologies.
- ESMA also highlights the need for increased vigilance in risk management and diversification strategies as funds allocate larger portions of their portfolios to AI-related companies.

Conclusions:

- While investors believe that AI has significant potential to drive future growth and operational efficiency, few EU funds have embedded AI as a key part of their investment strategy.
- New risks may arise from third-party dependencies on AI, services provider concentration, cyber threats, model and data governance, and increased market correlations.
- Especially less liquid markets, such as PE, should pay attention to such dependencies.

EU funds' investment in AI companies
Large tech companies dominate exposure



*Nasdaq's CTA AI Index, WisdomTree's AI & Innovation Index, ROBO Global's AI Index, Solactive's Generative AI Index, Morningstar's Global Next Generative AI Index, Indxx's AI Index, and S&P Kensho Global's AI Enablers Index.

Go to the full report from ESMA on the adoption of AI

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