

# Your Values, Your World, and Your Portfolio

*A snapshot of sustainable, responsible, and impact investing*

## KEY POINTS

- Sustainable, responsible, and impact investing (SRI) assets grew from \$3.74 trillion in 2012 to \$8.72 trillion in 2016
- Maintaining a financial and moral investment perspective can appeal to both individual and institutional investors
- SRI has evolved from targeted elimination (screen out), to include actively seeking to invest in companies that incorporate environmental, social, and governance criteria in their decision-making (screen in)



**In its broadest sense, sustainable, responsible, and impact investing (SRI) refers to an investment discipline that strives for strong financial performance while also seeking to create alignment of values.**

Since the concept of SRI first became popular in the 1960s, it's also been referred to in a variety of ways. But whether it's "socially conscious," "green," "values-based"—or today's more common monikers, "sustainable," "socially responsible," or "impact investing"—the concept is essentially the same.

The amount of assets devoted to doing good while also doing well has grown at quite a clip in recent years. In fact, SRI assets grew from \$3.74 trillion at the start of 2012 to \$8.72 trillion at the start of 2016, according to The Forum for Sustainable and Responsible Investment (US SIF).

### **Who are SRI investors?**

The group ranges widely—from individual (retail) clients of modest means to accredited individuals or those investing on their behalf, such as family offices for ultra-high-net-worth clients. The common thread is that they all seek to have their values reflected in their portfolio holdings. There are also institutional asset managers that invest on behalf of for-profits, or nonprofits such as foundations and charities, who may have a fiduciary responsibility pursuant to a nonprofit's mandate or mission, requiring that assets be invested in a certain way.

Although they initially grew popular in the 1960s with individual investors, SRI strategies are now very prevalent with institutional investors. The US SIF reports that institutional investors comprise \$4.72 trillion in ESG assets, a 17 percent increase since 2014.

### **The ABCs of SRI and ESG**

In the early days of SRI, the focus was more passive, and centered on eliminating corporations from investment consideration based on their involvement in certain activities (such as alcohol, tobacco, and/or firearms). Today, SRI strategies may examine the impact of a corporation's strategy and operations on the world, based on environmental, social, and corporate governance (ESG) criteria (see the table on the following page). ESG considerations are integrated into investment decisions, along with traditional financial analysis and securities selection calls.

Another means of seeing ESG criteria brought to life can be achieved by shareholders leveraging their authority. Through their combined voting power, stockholders of public corporations have the ability to influence a governing board to enhance disclosures and increase transparency and corporate responsibility in ESG matters.

Exerting pressure in this way may also incent a company to be a better corporate citizen, which in turn can help keep performance from being impacted by the kind of tarnished reputations that may result from questionable practices and subsequent public relations fallout.

### **Where principles meet portfolios**

Just like conventional investing, there are a number of investment vehicles and means of bringing SRI into a portfolio, with mutual funds being the most basic option. Exchange-traded funds (a stock-fund hybrid) are also an option; some are broad-based, while others are more narrow, centering on such goals as workplace equality, women in leadership, and ecological strategy. Socially responsible criteria have also become popular in the nontraditional, or alternative, investment space, with hedge funds and private markets (equity, debt, venture capital, and real estate). ESG assets in alternative investments stand at \$206 billion, according to the US SIF.

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Area of focus	Activity	Potential impact on performance
<b>Environmental</b>	<ul style="list-style-type: none"> <li>• Resource management and pollution prevention</li> <li>• Cut emissions/climate impact</li> <li>• Reporting and disclosure</li> </ul>	<ul style="list-style-type: none"> <li>• Avoid/minimize environmental liabilities</li> <li>• Boost profitability via efficiencies</li> <li>• Curb regulatory, litigation, reputational risk</li> <li>• Indicator of well-governed company</li> </ul>
<b>Social</b>	<b>Workplace</b>	<ul style="list-style-type: none"> <li>• Improved productivity and morale</li> <li>• Reduce turnover and absenteeism</li> <li>• Openness to new ideas and innovation</li> <li>• Curb potential litigation/reputational risk</li> </ul>
	<b>Product Integrity</b>	<ul style="list-style-type: none"> <li>• Create brand loyalty</li> <li>• Boost sales based on product safety</li> <li>• Reduce potential for litigation</li> <li>• Reduce reputational risk</li> </ul>
	<b>Community Impact</b>	<ul style="list-style-type: none"> <li>• Improve brand loyalty</li> <li>• Protect license to operate</li> </ul>
	<ul style="list-style-type: none"> <li>• Diversity</li> <li>• Health and safety</li> <li>• Labor-management relations</li> <li>• Human rights</li> </ul>	
<b>(Corporate) Governance</b>	<ul style="list-style-type: none"> <li>• Executive compensation</li> <li>• Board accountability</li> <li>• Shareholder rights</li> <li>• Reporting and disclosure</li> </ul>	<ul style="list-style-type: none"> <li>• Align shareholder/management interests</li> <li>• Avoid negative financial surprises</li> <li>• Reduce reputational risk</li> </ul>

Source: Pax World Management LLC

So how well do well-meaning investments actually do? As with non-SRI investing, performance varies widely among funds and due diligence is required. Some say it's difficult to quantify, due to inconsistent self-reporting and variation in agreement as to what qualifies as an SRI investment. Although the jury may still be out, we certainly think this is a starting point for further discussion.

**If you'd like to see how you can incorporate your values into your portfolio, please contact your Investment Advisor to see how we can help.**

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## The buzz on SRI performance

The positive effects of ESG criteria on performance may have been little-known at one time, but those days are long gone. Here are what some have to say on the subject:

- "There is increasing evidence showing that superior performance in managing climate risk is a useful proxy for superior, more strategic corporate management, and therefore for superior financial value and shareholder value-creation."  
— *RiskMetrics*
- "There is growing evidence that it is possible to find impact investing opportunities that deliver financial and social, double bottom-line returns."  
— *Darren Walker, President, Ford Foundation*
- "Demographic shifts, stakeholder advocacy, and government regulation are combining to create unprecedented demand for sustainable and impact investment solutions."  
— *Deborah Winsbel, Managing Director and Global Head of Impact Investing at BlackRock*
- "The premise underlying sustainable investing is elegant in its simplicity: companies that do a better job of integrating ESG standards into their business models are better positioned than their less-enlightened competitors to provide investment performance over the long term."  
— *Joe Keefe, President & CEO, Pax World Management*

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