Whitechurch Securities Ltd
WEALTH MANAGERS

A Guide to Socially Responsible Investing

Making an Impact with your Investments

Would you like to be able to align your investment choices with your social and environmental beliefs? If so Socially Responsible Investing (or SRI as it is commonly known) may be something you would like to look into.

Socially Responsible Investing is a term used to describe investments which take into consideration social, ethical and environmental factors as part of the investment decision making process. Many other terms, including Ethical Investing, are also used.

In this short guide we will take you through how this area of investment is developing; why we think it is becoming more important and explain some of the terminology and processes used to help you decide if this is an area you would like to explore further.

Contents

The History of Socially Responsible Investment

The Origins of Ethical Investment can be traced back to religious orders such as the Quakers and Methodists who sought to exclude 'sin stocks' such as Alcohol, Tobacco and Gambling.

Charities and some individuals adopted this exclusionary method of investing to ensure they were not invested at odds with their charitable or personal beliefs.

1971 - *The PAX Fund* was launched in the US inspired by anti-war activists during the Vietnam War.

1983 - *EIRIS (Ethical Investment Research Services)* was established as the UK's first independent research for ethical investors.

1984 - Saw the launch of the first ethical fund in the UK - ***The Friends Provident Stewardship Fund***

Increasing availability of news started to highlight to people the environmental impact of things such as deforestation and Human Rights abuse by companies within the supply chain.

End of the 90's - approximately £3.3 billion invested in 50 ethical funds.

Increased newsflow, aided by increasing use of social media brought issues to people's attention and ethical consumerism grew.

The Paris Climate Agreement (COP 21) really brought climate change and carbon emissions to the forefront and environmental issues are becoming a central issue for many companies and investors.

By the end of 2015 *EIRIS* stats showed the UK ethical fund market size was £13bn and growing.

Shades of Green – How Ethical is My Investment?

Funds are often classified using shades of green to help investors identify how strict the criteria are likely to be.

Light green funds

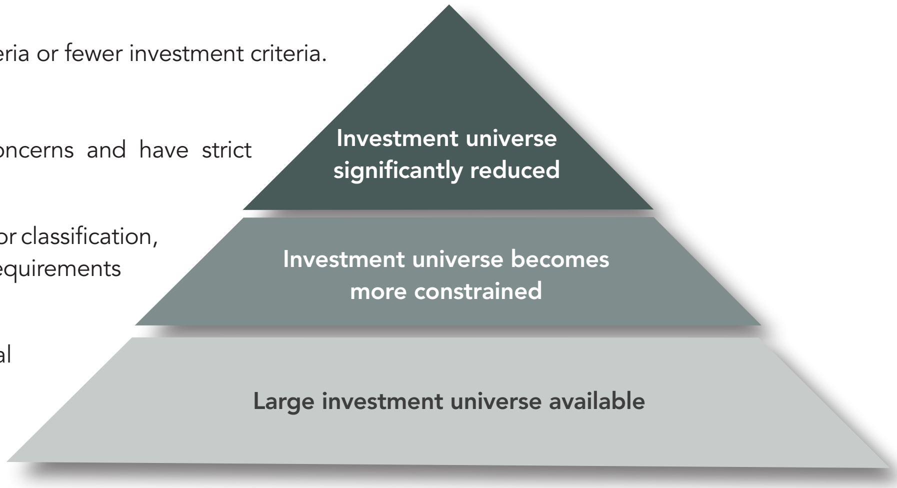
Will normally have more relaxed investment criteria or fewer investment criteria.

Dark green funds

Take into account a wide range of ethical concerns and have strict standards for implementation.

Whilst this may seem a relatively simple method for classification, finding funds which meet all of an investor's requirements can at times be tricky.

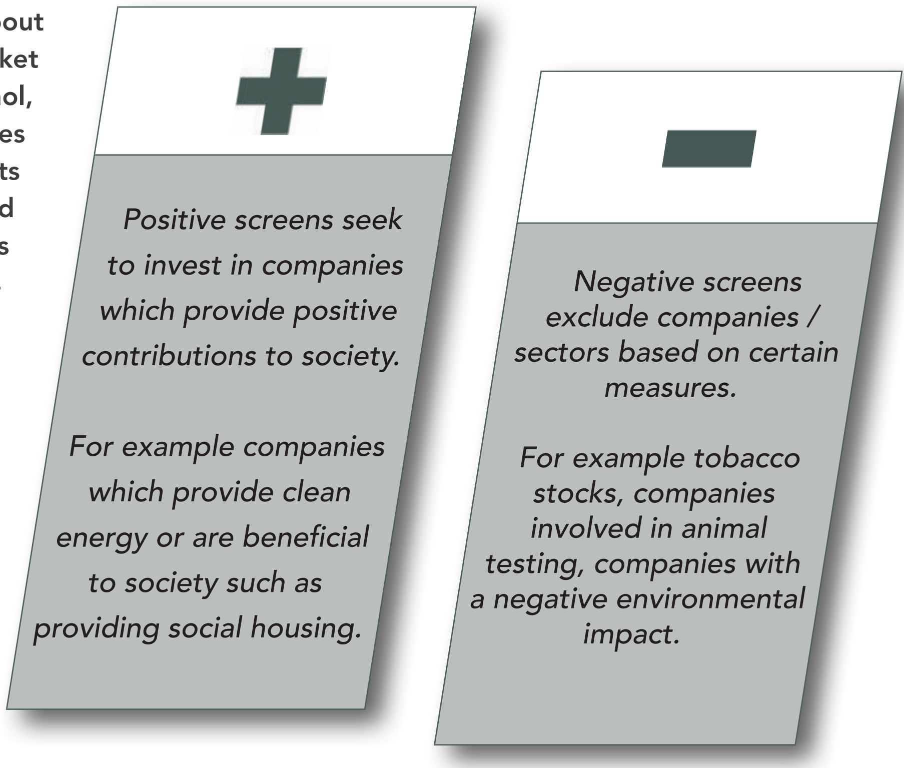
It should also be considered that the more ethical requirements a person has the harder it will be to find investments. Also, risk and volatility can increase due to lack of diversity within the investment universe.



Positive and Negative Screening

Historically, ethical investing has been about excluding stocks or sectors of the market perceived to be unethical such as alcohol, tobacco, gambling, defence or companies with poor environmental or human rights records. This exclusion has, in the past, led to underperformance of such funds versus the wider market when areas such as tobacco or mining outperformed.

As the market has developed, many funds now look to seek out companies they consider are providing a positive contribution to society, such as those providing social funds or clean energy. In many cases a fund will combine a combination of the two approaches starting with a negative screen to exclude certain areas and then applying a positive screen to help identify the most attractive companies.



Investing in a Changing World

The world is changing rapidly; climate change is a key concern with many countries committing to meet goals set at the Paris Climate Conference. An increasing global population is increasing demands on healthcare; and water and food shortages are placing new demands on infrastructure and agriculture.

New technologies are being developed to cope with these changes we are facing and this is opening up new investment opportunities. For instance:

- Cyber-crime - companies providing security against online fraud
- Renewable energy - companies producing efficient and environmentally friendly energy alternatives
- Health foods - companies developing cost efficient natural foods to combat obesity and diabetes

The changing face of business

The way many businesses are run is also changing, increased global news coverage and use of social media highlights business practices that many find unacceptable and many companies are now making changes to address this. *The Rana Plaza disaster in Bangladesh in 2013 was a wake up call for many companies in the fashion industry to look more carefully at the rights and safety of workers employed throughout their supply chain, whilst the BP Deepwater oil spill created huge fines and court costs for BP.

*As an example.

Simply translated disasters such as Rana Plaza, Barclays Libor Rate rigging scandal, the BP Macondo Oil Spill or the BHP Brazil Dam burst all have a negative impact on companies share prices. In the latter two cases the incidents led to significant fines and court costs which have had a longer term impact on share price. In the case of Barclays the scandal impacted on the value of the overall brand. By applying a high level of screening for Environmental, Social and Corporate Governance, many funds in the ethical space seek to mitigate exposure to companies which may have left themselves open to such issues.

Energy

If we take the area of energy as an example, in the past many mining and oil stocks would have been excluded on the grounds of environmental concerns, and in many cases, poor human rights records. This led to ethical investors being excluded from a large area of the market which could negatively affect returns. Renewable energy started to become an area for investment many years ago but the industry was in its fledgling phase and the technologies were new and untested making the returns from this alternative area of the market risky and volatile. The industry has however matured and is now a credible and profitable alternative to the traditional areas of energy investment.

Thematic Investing

Many managers take a thematic approach when it comes to positive screening and investing, identifying key trends such as clean water and sanitation, sustainable food production and carbon reduction as areas of growth as companies seek to find solutions to these issues.

This thematic approach is then used either as a basis for the fund or a selection of themes are implemented throughout the fund.

An example of a thematic fund would be one focused on reducing environmental impact. The managers would look for companies which provide products or services which focus on reducing other companies environmental impact, for example they could provide recycling services, filters to reduce air pollution or solutions to reduce consumption of a resource in the manufacturing process such as water.

Or a fund may have a social or positive impact theme by investing in socially beneficial activities and areas such as affordable housing, education and community services.

A manager may run a more general fund such as one invested in global equities and use a positive overlay to invest across a broad range of themes.

So what is the benefit of this?

The use of thematic investing is twofold:

- It allows fund managers to invest for positive change by investing in companies which are providing solutions to global issues
- In cases such as social themes, where the positive impact is easily measurable, it allows fund managers to identify areas of future growth as the companies providing the solutions are operating in the areas where there is visible growing demand

Is Ethical Investing for Me?

Ethical investing is not for everyone; peoples values vary widely and what one person views as a cause for concern may be disputed by others or they will just not consider such issues when it comes to investing.

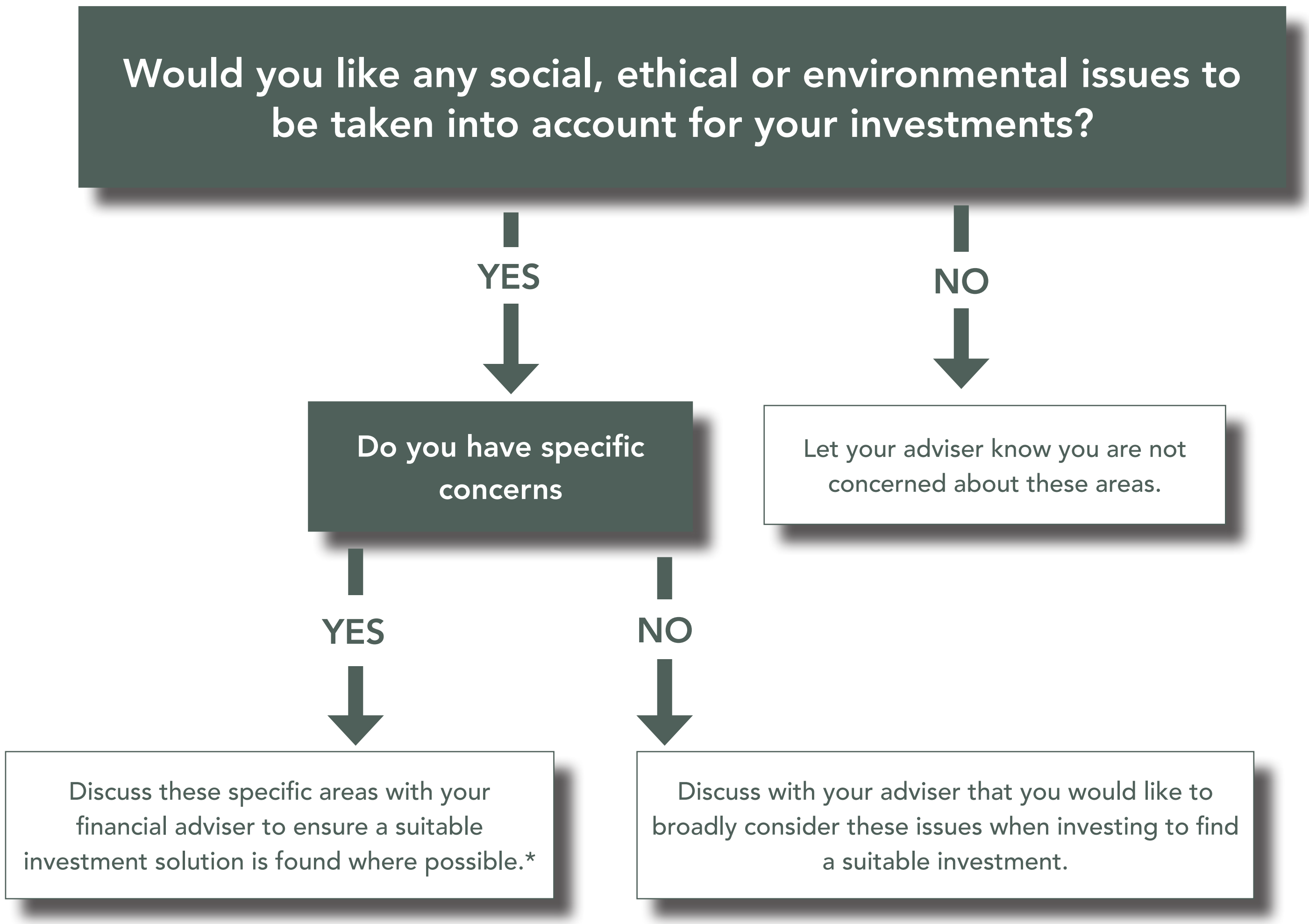
After reading this guide you may have a clearer idea about this area of investment and you can consider if:

There are specific areas you do not want to be invested in
Being mindful that the more areas you want to exclude will reduce the investment universe and increase risk and volatility due to lack of diversity.

Or

There aren't any specific areas you wish to be excluded from...
However, you would like to invest in companies that consider their environmental and social impact and in many cases look to provide solutions to problems such as healthcare, clean water and carbon emissions.

Many companies do take this into consideration whether or not they are included in an SRI fund. However, an SRI fund should ensure that ONLY companies which act in this manner are invested in.



* It should be noted if you have a large number of restrictions or very esoteric restrictions it may not be possible to find suitable solutions.

Jargon Buster

Corporate Governance: A set of processes rules or practices by which a company is directly controlled by balancing all the stakeholders' interests. It provides the framework for attaining a company's objectives. Stakeholders encompass everyone involved from the CEO, board and management through to staff, customers, suppliers and shareholders. It essentially governs how a company behaves.

Corporate Responsibility/Corporate Social Responsibility (CSR): This describes a company's initiatives to assess and take responsibility for its effects on environmental and social wellbeing. Or how their operations may impact customers, employees, communities and the environment. The term generally applies to positive efforts which go beyond that required by the regulators.

Divestment: Green and ethical funds may divest or sell stocks when they feel that a company no longer meets their investment criteria. The funds may reinvest in that same company, if and when they feel that it is again suitable. *Engagement* is often a precursor to divestment in an attempt to encourage companies to improve their ESG performance. The term is regularly being seen at the moment in relation to Fossil Fuel related stocks, as pressure over reducing carbon emissions is leading people to move away from investment in this area.

Engagement: Engagement is the process by which investors or fund managers seek to maintain or improve the corporate social, environmental, ethical (SEE) or governance policy, the management or performance of companies through dialogue and voting practices.

Investors can engage with companies to:

- Encourage more responsible business practices
- Encourage greater transparency and disclosure
- Improve investment returns by encouraging companies to manage SEE risks or to address new social or environmental business opportunities.

Ethical Investments: Normally refers to investments which have been screened to fit certain criteria and often includes a negative screen to remove 'sin stocks' such as tobacco and arms as well as positive screen criteria.

Environmental and Social Governance (ESG): Environmental, and Social Governance criteria are used as a measure by investors of a company's approach to dealing with these issues. Environmental criteria look at how a company performs as a steward of the natural environment. Social criteria examines how a company manages relationships with employees, customers, suppliers and the communities where it operates. Governance addresses the company's management and internal controls; the overall management and behaviour of the company. The theory is that companies with good ESG policies should perform better, however, it should be noted that most companies including Oil and Mining companies will have an ESG policy now and investing into funds defined as ESG may result in investment in areas you do not wish to be exposed to.

Green Investments: A term used to describe investments which focus on environmental issues.

Greenwashing: This is when a company or group promotes itself or its products or services as environmentally or eco-friendly without following through with action. Or they promote a general service, as eco-friendly when it is actually an industry standard.

Impact Investing: Investments that measure both financial returns and their benefit to society, aiming to achieve a balance between the two. Often the investment is made directly into a specific project where returns can be seen and measured. Such investments can be of a higher risk and potentially only appropriate for wealthier and more experienced investors.

Social, Environmental and Ethical Factors (SEE): Commonly referred to as SEE, this covers the entire range of issues in SRI and is often used in discussions on risk. Social factors refer to how a company performs within communities and whether it provides needed services or charitable donations as well as whether it minimises its impact on the areas in which it operates. Environmental factors refer to company policy on the environment or an environment management system to set targets for the continued improvement of its performance in areas like energy efficiency and waste management. Ethical factors covers a broad range of other areas including involvement in animal testing, alcohol, tobacco, gambling, genetic engineering, arms or the military and human rights.

Socially Responsible Investing (SRI): Also known as sustainable investment, responsible investment, socially responsible investment (SRI) and ethical investment. It refers to any area of the financial sector where the environmental, social governance and ethical principles of the investor (whether an individual or institution) influence which organisation or venture they choose to place their money with. It also encompasses how an investor might use their power as a shareholder to encourage better environmental and social behaviour from the companies they invest in.

Sustainability: Sustainable development can be described as development which meets the needs of the present without compromising the ability of future generations to meet their own needs. It is about balancing three goals or 'pillars' - environment, society and economy - to enable communities throughout the world to satisfy basic needs and enjoy a better quality of life, without compromising the quality of life for future generations.

Thematic Investing: Investments which follow a particular theme which may be socially driven, environmentally orientated or a combination of both, for example a clean energy fund.

Some Frequently Asked Questions

How does the performance compare?

Historically 'Ethical Investments' were known to underperform as they were based on mainly exclusionary criteria. However, this has now evolved and whilst it should be considered that there will be times when performance will be 'out of sync 'with the market if an area where there is no exposure such as mining or oils does well, over the long term performance is proving to be comparable, and at times better.

Can investors be 'a bit ethical'?

Some investors, for a variety reasons, do not want to invest all their money into SRI funds. They should speak to an adviser to discuss a solution that meets their needs.

If a fund has 'sustainable' in the title will it meet my requirement?

Not necessarily. You always need to look carefully at the underlying criteria and discuss with your financial adviser to ensure it meets your requirements.

If you would like further information about ethical investments, please contact our **Business Development Team** at **dfm@whitechurch.co.uk** or call **0117 9166175.**

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