SRI, ESG and Ethical Investing
What's the difference?

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There are an increasing number of reports in the financial press on SRI investment and a question we are frequently asked is what is the difference between SRI, ESG and Ethical investing?
As more and more funds come to market with Sustainable, SRI or Ethical in their titles, it is becoming a minefield for advisers and investors alike to understand what they are invested in and if the money they have invested is working in the way they wanted.

Breaking Down The Terminology

Ethical Investment: The origins of ethical investing lie in faith-based investing which in the West stem from ideologies such as the Methodists, who looked to exclude gambling and alcohol production, and the Quaker movement, who looked to exclude arms manufacturing.

Traditionally ethical restrictions have usually applied when working with charities or trusts or portfolios managed for religious establishments. Over time, the idea of ethical investing has expanded as environmental and civil rights movements have grown and individuals started boycotting companies which did not match their values. The idea has evolved from one which focused on avoiding controversial activities to one which emphasises positive values as well and now encompasses areas such as Climate Change, Human rights, Fairtrade and conflict avoidance.

Ethical investing is subjective and can be as narrow or broad as one sees fit but the term is used universally to identify the theme and is used interchangeably with SRI and ESG.

SRI – Sustainable and Responsible Investment: SRI is a broad term that covers investment that takes environmental, social, ethical or governance issues into account to a reasonable extent. Investments will not necessarily exclude any given sector or company and can include thematic funds such as Impax Environmental Assets or Jupiter Ecology which focus on investing in companies offering environmental solutions or those with market leading environmental practices.

Funds with sustainable and responsible in the title are often those seeking out companies aiming to make positive impacts such as providing healthcare or environmental solutions or those seeking to improve social wellbeing. Due to this investment stance they will often avoid companies in areas usually shunned by traditional ethical funds such as Gambling and Tobacco and will exclude such areas in their mandate.

ESG – Environmental, Social and Corporate Governance: ESG is another term which is often heard in this arena with many managers now analysing a company's ESG policy and performance when considering investment. It seeks to analyse the behaviour of companies on a number of metrics related to the companies Environmental, Social and Corporate Governance policies to identify those who are well governed or are improving their governance.

Companies with favourable ESG characteristics have tended to outperform companies with negative characteristics and are less likely to be open to risk of fines or legal action due to poor behaviour. However as with the term SRI, companies using ESG methods may be invested in any area. Indeed, the investment pool is even wider as they are not necessarily seeking out companies deemed to be making a positive impact. However for investors which are keen to influence companies and support positive change it allows them to invest in companies where the fund manager may be using their position as asset owners to influence companies through voting and dialogue.

The Whitechurch Way

The Whitechurch portfolios are designed as Ethical portfolios which could raise the question: is this an old fashioned approach?

Our answer is, no, we don't believe so. The term Ethical is used because this is what the majority of retail investors (your clients) understand. These clients generally do not want to be exposed to certain areas of the market (key areas of concern are tobacco, pornography, arms, high environmental impact and animal cruelty) but they wish to be invested in companies having a positive impact on society.

This is why our portfolios are built using a range of funds which employ a negative screen to take out key areas of concern but include funds which have a positive criteria overlay - seeking out companies providing solutions for a changing world.

Whitechurch Investment Team, February 2017

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1503b. 23.02.17