

How Socially Responsible Investing is defined? Discussion over SRI as recently developed investing trend practised all over the world

Jak zní definice společensky odpovědného investování? Diskuze o SRI jako nové celosvětové investiční strategii

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Abstract

Socially responsible investing (SRI) is buying stocks of companies focused on such sectors like waste industry or alternative energy and other ecologic sectors. An average investor often understands SRI as stock funds investing in green technologies. But the rank is even wider; SRI means a support of companies who respect the environment and apart from this also respects the human rights, community development and other criteria possibly involved in corporate social responsibility (CSR) concept or, by other words, the environmental and social criteria and corporate governance (ESG). SRI funds include social and environmental factors as a part of their investing strategy. SRI has even recently developed from nonrelevant investing strategy into a worldwide practised investment trend. The article collects various definitions of socially responsible investing and explains the concept of SRI. It looks briefly at SRI development in time. Further the paper designs the SRI in practice; names some existing funds that invest in socially and environmentally responsible areas and compares these to conventional funds. The SRI is connected here together with corporate social responsibility and so called ESG criteria – all these three concepts or strategies are closely gathered and as such can definitely influence our society in future, as this article estimates.

Key words

Socially responsible investing (SRI), Corporate social responsibility (CSR), Environmental and social criteria (ESG), decision making in investment

JEL Classification: G11, G21, M14

1. Introduction

There has been a dramatic development of SRI during last three decades: a niche strategy used by few investors has become a broad investing trend practiced by many. [3]

There are more and more investors interested in the usage of their money; who are the companies they invest in? Recently it is not only the result or efficacy but also the production, their attitude towards employees and the environment and sustainable development. Important is not to use animals to testify product, keep equal rights for men and women. It is alternative

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energy production, nanotechnology, or other companies supporting the sustainable development are attractive for these. This kind of investors we can name as a social responsible investors. This kind of investing was firstly seen in the 80s. The first social responsible investors were rather considered not to smart and realistic but rather Maecenas's. Nevertheless, recently is a good valorization is evident. The oldest stock index functioning in SRI is Domini Social Equity (DSE) 400 founded in 1990 – its average return is 11.87 % (SP 500 index was increasing by 11.31 % in the same period of time. A SRI fund shouldn't invest in such industries like weapon production, or into companies that enjoy the child work, firms braking human rights, companies significantly impacting environment. So, if a company involved in SRI changes it's acting by negative way, then is excluded from SRI funds; still there is a chance to be invited again. This decision of exclusion is nothing bad for a financial health of an organization but, on the other hand, such a decision has an indispensable influence on the public meaning.

There are many live discussions about these SRI funds profitability; some financial analytics say the SRI funds are not less nor more profitable than traditional funds. Others' opinion is that SRI funds are even more rentable than ordinary funds. The reason, according to them, is better selection of stocks. According to the first opinion leaders, the most important role in this decision making process of an investor plays his good feeling. [10]

SRI funds are often represented as investing in ESG – ESG criteria mean three basic principles of SRI: environment, social responsibility and corporate governance. According to BNP Paribas Investment Partners 15 % of global investment in stimulating tools comes to the sectors like eco-energy, waste industry, renewable sources, water industry etc. In USA they even talk about “Green New Deal” paraphrasing Rooswelt's stimulating tool of the 30s. This stimulating tool is made up by 787 milliards USD and 106 of them is directed to environmental initiatives. Although in Europe socially responsible way of investing has increased more rapidly than in the rest of world, in Czech Republic there this theme evokes rather an amusement. [9]

There even arose special SRI firms dealing with creating new SRI strategies. [3]

Often there is a basic question whether it is possible to gain similar or competitive returns from SRI funds or if usually an investor must give up a certain part of returns to reach positive social influence. Next chapters might answer to these questions.

2. SRI practice vary in various countries

In Czech Republic, there is a leading financial group KBC which operates also in Belgium. They run some funds oriented on the environment; KBC Eco Fund Climate Change, or KBC Eco Fund Alternative Energy. There exist some socially or ethically oriented funds in Czech Republic but rather the environmental ones dominate. In the majority of cases these environmentally oriented responsible funds are managed by banks with foreign owner. Apart from KBC the bank company called ČSOB offers funds like Water Wealth, Climate Change or Harmonic Growth. [12]

In USA there exist so called Community Development Loan Funds (CDLFs) as nonprofits. They serve the most at-risk populations and do so in the most innovative fashion. Some examples are Boston Community Capital (in business) or Cooperative Fund of New England (in community facilities). There are also some examples in America of socially responsible corporations like McDonalds or Avon; the first one has helped significantly to Afro-Americans giving them work and there is a majority of women on top management positions in Avon corporation. [5]

Nowadays there is a thousand of corporations in Czech Republic involved in a project called “Green corporation”. This project enables to employees to bring and collect electronic waste in special boxes. By this way almost 800 tons of electronic waste was collected during 2010 – while the previous year it was one hundred tons less. Just during one year this project saves seven tons of copper or nine kilos of gold. The most successful of all Czech corporations referring to the amount of waste recollected was Telefónica O2. [15]

Despite global spread of SRI movement worldwide, research has indicated different practices and principles in different countries and continents. [2]

3. Examples of socially responsible investing practice

Budde doesn't confirm the theory that an investor should give up some returns to reach socially positive impact nor the opinion that SRI strategies would achieve better results than market average. Nevertheless there exist some investment logic which investors can rely on: companies using sustainable business models, companies which are better governed, companies who issue their CSR reports, companies producing certain products like renewable energy; all these might be better financial investment than others. [3]

Hamilton et al. investigates the performance of the SRI mutual funds from 1981 till 1990 using Jensen's alpha: The results do not show that SRI earn no statistically significant excess returns and there are no statistically significant differences between the performance of SRI funds and conventional funds. [8]

Risk-adjusted returns of SRI funds in USA and UK are not significantly different from those of conventional funds, whereas SRI funds in Continental Europe and Asia-Pacific strongly underperform benchmark portfolios. The volatility was lower there (in Continental Europe and Asia-Pacific) of SRI funds than the volatility of conventional funds. [13]

SRI, or funds which are interested in environmental and social aspects have risen significantly during the recent decades. [7]

The share of SRI funds on the total mutual funds' assets is in Germany only 0,04 % and in France 0,01 %. Worldwide there was 12,2 % of total assets under management involved in some strategy of SRI in 2010, where in 2007 it was 10 %, according to the Social Investment Forum (2010). [1]

There is a Governmental pensions fund in Norway which is socially responsible and is one of the greatest sovereign funds in Europe. Its income is made by the national budget surplus, where a majority of these are represented by incomes of large petroleum companies. In 2009 the value of the Norway national pension fund was six times higher than the national budget of Czech Republic.

Apart from Domini Social Equity (DSE) (see above in the introduction chapter) there are various other funds aimed at so called ESG criteria. We can number Credit Suisse Equity Fund (Lux) Global Sustainability, Global Ethical Equity by Pioneer Funds or Sustainability Leaders Funds by HSBC. In Czech Republic there the socially responsible investors can choose of around nineteen SRI funds. Two of theme is possible to buy in Czech Crowns. These are “ČP Invest Živé planet” and “ČSOB Fond Vodního bohatství”. Other funds are offered by Fortis group, HSBC or KBC. [10]

In practice, SRI can be performed by three basic strategies which serve to investors to express their values and priorities for society in their investments. Screen means to filter large amount of information to find exactly what an investor is looking for. In investments area these information consist in ways of investing. The strategies, which are screening, positive or negative screening, refer to his concrete role in the investing activities – less or more active. [11]

Another three main strategies are called like Social Screening, Community and Proactive Investing and Shareholder Activism. Let us explain the basic characteristics of them: Social Screening bases on the environmental, social or governance (ESG) criteria of the issuer of stock considered to buy like selling tobacco or leaving important environmental footprint. Second named strategy would invest in companies supporting affordable housing or energy-saving technologies and so on. Last of the strategies targets the corporate behaviour. [3]

There has been observed a neutral performance in relation to conventional and socially responsible benchmarks. But the performance of funds evaluated in relation to socially responsible indices showed to be slightly higher. [4]

4. SRI definitions

SRI can be defined as a trend in investment services relatively to rising new needs of investors; for them, the so called ESG criteria (include Governance matters, Environmental matters and social ones) seem attractive. Also we can talk about SEE criteria: non-financial criteria: social, environmental and ethical. SEE or ESG criteria are more and more often considered by investors – both the institutional and the individuals. Both of the concepts, SEE and ESG, comes along with corporate social responsibility. Respectively, CSR and SRI are encouraging each other.

Despite of the growing interest in CSR and SRI there has not been one united definition for these two approaches. SRI can be defined as such a special market segment of assets management industry or the special segment in the investment services; as dynamic and fast growing one. [7]

There are several definitions:

SRI is a generic term covering any type of investment process that combines investors' financial objectives with their concerns about ESG issues. SRI is a tool, which describes any area of the financial sector where the social, environmental and ethical principles of the investor (whether the institutional or individual) influence which organization or venture they choose to lace their money with. It also encompasses how investors might use their power as a shareholder to encourage better environmental and social behaviour from the companies they invest in. [6]

Sharpio consideres SRI as the practice of making investment decisions based on both financial and financial performance. [14]

A socially responsible fund includes only such stock into its portfolio which respects certain criteria. [12]

The Principles for Responsible Investment were presented by the former United Nations Secretary-General Kofi Annan in 2005 – since then the SRI has become more visible. He said: “By acting collectively on the basis of these principles for responsible investment, we can help protect all the world's precious assets”. [16]

SRI growth is the fastest in Italy (v databázi mám i článek k SRI in Italy) – page 136. A je zde popsán typický investor. [5]

The simplest and most accurate definition of SRI is an approach to investing where an investor includes personal, religious, moral, or ethical values in investment decisions. SRI is about reflecting values that are personally meaningful to the investor and applying these values into investment decisions. Socially responsible investors may avoid certain companies because of the products or services they make or sell. Once companies make the SRI cut, they are subjected to the same analysis used by traditional investors. The basic difference between socially responsible investing and traditional investing consists in rejecting or, in the opposite way, in accepting potential investment candidates. But, of course, if a company doesn't sell

tobacco or alcohol or if it is not included in weapon industry or behaves responsible towards the environment, it doesn't necessarily need to be a good investment candidate. A potential investor must consider not only the ESG criteria but also whether the company is viable, has growth potential and all the other characteristics of a good investment beyond SRI features. Some investors prefer owning individual stocks to so called mutual funds because the potential for gain can be higher, with a corresponding increase of risk. Mutual fund is a pool of investor money managed by professionals with stated investment goals, who decide about selling and buying. Other SR investment options apart from mutual funds are individual stocks, bonds, community investments or hybrid investments. [11]

A commonly accepted definition of Socially responsible investing is that SRI includes those investment strategies that consistently and explicitly consider social factors as part of the investment process. [3]

Summarizing the existing definitions, SRI is a special approach to investment, where not only financial criteria are taken into account but the special extra-investment or non-financial criteria are considerate in the investment process as well. [7]

5. Discussion

Let's have a question: What about the next development of socially responsible investing? There are some options we can design; one of them, for Czech Republic for example, is the attractiveness of SRI for national pension retirement fund. In case that the new reforming proposal is accepted, there will arise a need to valorize the relatively high amount of money collected by these funds as pension payments. Socially responsible investing may be an optimal opportunity for this valorization because of its relatively low risk. This kind of system is observable in Norway. In recent political and economic situation, in addition, might increase the SRI's popularity; the confidence of investors in national stocks seem rather grow week in conditions of the actual events; some examples we can find in Greece, Italy, Spain or even USA, where the Standards and Poor Agency decreased the evaluation by one degree. The nations, thus, become no more attractive as investing aim for being deep in debt and unprofitable. So, SRI, as another option of its future development, may become a relatively stable way of appraisalment for various kinds of investors' substances.

6. Conclusion

The world has become too small to think in terms of national boundaries either when buying products or when buying stocks. [5]

Why is SRI so important? Socially responsible investors can make a certain kind of pressure on corporations to behave more responsibly; to change policies and advocating better labour and environmental policies. The success is when SRI results in debates in corporation's top management which reflects in pollution, climate change, corporate governance etc. [11]

There is no need to worry about conventional investing; even though the social screening, for example, would gain high popularity, these strategies would not beat the conventional ones because SRI strategies are more about aligning investors' values with their investments goals. [3]

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Summary

Článek pojednává o společensky odpovědném investování (Socially Responsible Investment, SRI) jako o relativně novém fenoménu v oblasti finančnictví. Zajímavé je ale i pro jeho prolínání do odlišných rovin; do společensky odpovědného chování (firem) i do oblasti životního prostředí. SRI je tak úzce spjato se společenskou odpovědností firem (CSR) a také ESG kritérii, tj. firemní politikou s ohledem na otázky životního prostředí a otázky společenské. Běžně se pod pojmem SRI rozumí investice do zelených technologií, ale jeho dosah je mnohem širší. Společensky odpovědné investování znamená investování do společností zaměřených například na odpadové hospodářství (nebo je samy mají nastavené s ohledem na životní prostředí), obnovitelné zdroje energií (nebo je používají). SRI podporuje firmy, které provádějí svou činnost v souladu s koncepty trvale udržitelného rozvoje, tedy s ohledem na životní prostředí, společnost, komunitu, lidská práva, apod. Obecně lze tato hlediska shrnout pod pojem společenské odpovědnosti firem. SRI fondy zahrnují právě environmentální a společenská hlediska do svých investičních strategií. SRI se za poslední dekády rozvinulo z nevýznamného způsobu investování, které zpočátku spíše vyvolávalo úsměv vzhledem k rentabilitě, ve světově rozšířený trend v investování. Článek jmenuje některé definice SRI, nastiňuje jeho rozvoj v čase a vysvětluje jeho podstatu také na praktických příkladech. Uvádí některé existující fondy hodnocené jako fondy SRI a porovnává je s těmi běžnými konvenčními investičními fondy. Spojuje SRI se společenskou odpovědností firem a odhaduje, jaký by mohlo mít SRI další vliv na budoucí rozvoj ve finanční oblasti a ve společnosti všeobecně.