Socially Responsible Investing – SRI or ESG – What are they?

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Socially Responsible Investing (often referred to as SRI) has been a part of investing for a long time. Initially, it was intended to promote particular religious or social values (such as temperance, anti-tobacco or anti-gambling preferences). Eventually it grew to include pacifist values, human rights, health and (the latest a focus) a green environment. On the face of it SRI sounds great, but *analytically speaking* SRI performance has always left me questioning its role in our portfolio. SRI is only workable within a plan if the client understands and accepts the likelihood of lower returns (as opposed to being fully invested in the market and investing those gains in carefully chosen socially responsible ventures). In 2008 SRI investors lost more than the domestic market (around 40% on average), but some have now evolved into ESG or environmental, social and governance (ESG) investments. ESG appears to show much more promise than SRI, but is a much newer strategy and therefore offers us less data upon which to base our performance and risk measurements.

What is currently included in SRI versus ESG investment products? SRI is investing with one's values, screening out or not investing in certain companies or industries, or only investing in particular companies. On the other hand, ESG looks to invest in companies based on environmental, social and governance factors. In the beginning, SRI performed poorly as people selected out (often lucrative) sectors and businesses based on perceived moral or social values. Now the claim is that SRI focuses on broader areas of sustainability but with an eye to the long term potential, shifting it closer to the realm of ESG. The implication is that this type of selection leads to investment in a set of companies that are better run, whose business models offer less risk and deliver better financial performance in the long run. Unfortunately, ESG is less well know and seldom used by non-institutional advisors.

Most clients want to invest in SRI or ESG as long as it does not cost them. Others are willing to pay a premium for this type of investment. There are times when ESG investments can be made and still retain equivalent returns. As stated, the performance and risk is generally less clear when working with ESG since they are newer. Time will tell and we will keep evaluating this strategy. I find clients inevitably begin to understand that by selecting a subpopulation from the entire investment world they are less diversified and may take a potential performance and volatility hit.

Frankly, clients deserve a globally diversified portfolio. Moreover, it is easier to attain looked-for returns by employing well-established low-cost investment vehicles. Nevertheless, when clients chose to support SRI or ESG with some of their investments we can accommodate this request IF they have the capacity to absorb the potentially lower returns and potentially higher volatility.

In the future we will continue to evaluate ESG products and will use them to supplement components in our diversified global portfolio.

==== ONLINE RESOURCES ===

www.socialinvest.org

www.ceres.org

www.csrwire.com

www.greenmoney.com

www.socialfunds.com

www.srinews.com

www.aikapa.com