INVESTMENT INSIGHTS

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SUSTAINABLE AND RESPONSIBLE INVESTMENT (SRI)

Sustainable and Responsible Investing (SRI) is an investment discipline that considers ethical and sustainable factors to achieve a positive impact on society. These strategies may not only have a positive impact on society broadly, but as research suggests, they may also have a positive impact on investment returns. This issue of Investment Insights looks at SRI, one of the most popular segments of the investment industry today.

BACKGROUND

While SRI has gained popularity recently, its origins date back centuries to when various cultures attempted to set guidelines for types of investments.[1] From the 1960s, the SRI strategies have continued to evolve until the 2000s, and in 2006 the United Nations created formal Principals for Responsible Investing (PRI). The PRI signatories, typically financial institutions, voluntarily incorporate socially responsible investing into their investment practices.

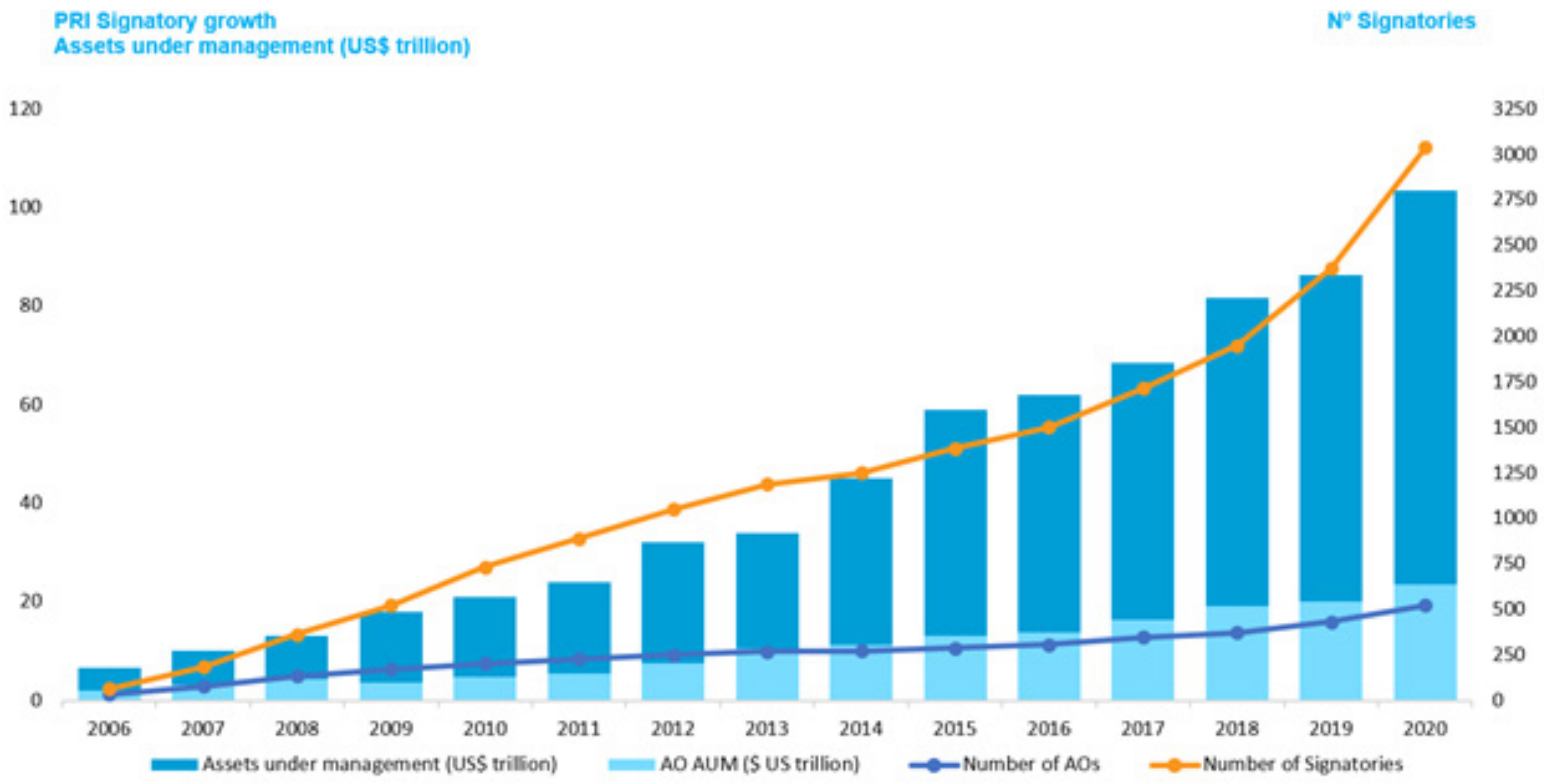
KEY POINTS

- Sustainable and Responsible Investment (SRI) an investment discipline that not only endeavors to generate competitive investment returns, but also incorporates ethical and sustainable factors into investment decisions.
- Previously known as Socially Responsible Investing, today SRI encompasses a broader focus than only social issues.
- SRI strategies are gaining popularity among investors, as they account for 1 in 4 dollars invested in the United States today.
- These strategies are especially popular among younger investors who continue to gain interest.
- A growing body of research has found a strong link between sustainable investing and financial performance.

1 "The History of Socially Responsible Investing." CNote, 15 Nov. 2019.

Cornerstone WEALTH SERVICES

As you can see below, since 2006, the number of PRI signatories have increased from 100 to 3,000 as of January 2020, representing more than $100 trillion in assets under management worldwide.[2] In the U.S., the assets managed under a socially responsible mandate have increased 18 fold from 1995 to 2018 at an annual growth rate of 13.6%. In 2018, more than 1 out of every 4 dollars was invested using SRI strategies in the United States.[3] Despite this rapid growth, the proportion of SRI investments in the U.S. (25.7%) are roughly half as much of Europe (48.8%), Canada (50.6%), and Australia/New Zealand (63.2%).[4]



Source: PRI Association

TERMINOLOGY

One possible reason for the relatively slow adoption of SRI in the U.S. may be confusing terminology. Sustainable and Responsible Investment (SRI) is an umbrella term for a wide range of investment strategies that focus on social or environmental factors in addition to risk and return. They include community investing, ethical investing, ESG (environmental, social, and corporate governance), impact investing, and others. The original umbrella term that described these strategies was known as Socially Responsible Investing. The updated terminology reflects the fact that these investment strategies have a broader focus than just social issues.

2 "About the PRI." PRI, 1 Mar. 2020, www.unpri.org/pri/about-the-pri.
3 Note: 2018 represents the latest data available. Source: US SIF Foundation.
4 With Japan's proportion of SRI investments relative to total managed assets being 18.3%. Source: Global Sustainable Investment Alliance.

What can be confusing is that Socially Responsible Investing is still used synonymously as an umbrella term, which can lead a person who is unfamiliar with these investments to conclude that they are focused only on social issues. That is not the case, however, and the table below clarifies this common confusion. SRI is composed of 3 broad categories: ethical investing, impact investing, and sustainable investing.

	Sustainable and Responsible Investment (SRI)		
Broad Category	Ethical Investing	Sustainable Investing	Impact Investing
Examples	socially responsible investing, and values-based investing	ESG, carbon footprint, and green investing	community investing, thematic, impact-first, and venture philanthropy

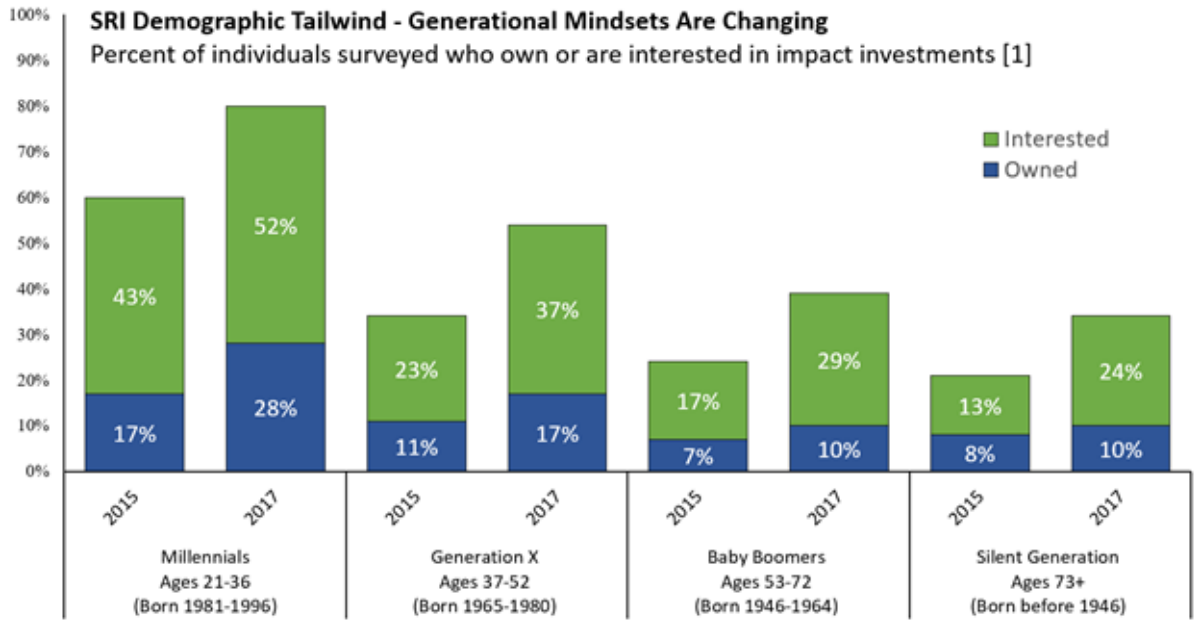
Ethical investing uses guidelines based on an investor's values (such as social, moral or religious) to exclude investments that derive their revenues from things deemed harmful. Ethical guidelines vary greatly by investors. Industries like weapons manufacturing, tobacco, gambling, and stem cell research are some common examples of issues that investors aim to exclude (screen negatively) under this approach.

While ethical investing overall aims to minimize harm by using negative screens, sustainable investing uses a broad set of long-term sustainability factors to include in investments. Some examples of these factors include good cooperate governance, labor rights, human rights, and pollution control.

Finally, impact investing aims to facilitate a positive change in a targeted manner. These strategies intend to directly allocate capital to things like renewable energy, affordable housing, microfinance, and sustainable agriculture.

TRENDS

While the adoption of SRI strategies in the U.S. appears to be slow on a relative basis (compared to the rest of the developed economies), overall, they are still gaining traction among U.S. investors. These trends are, in large part, driven by demographics with younger individuals taking more interest in these strategies. These demographic tailwinds can be seen in the graph below.



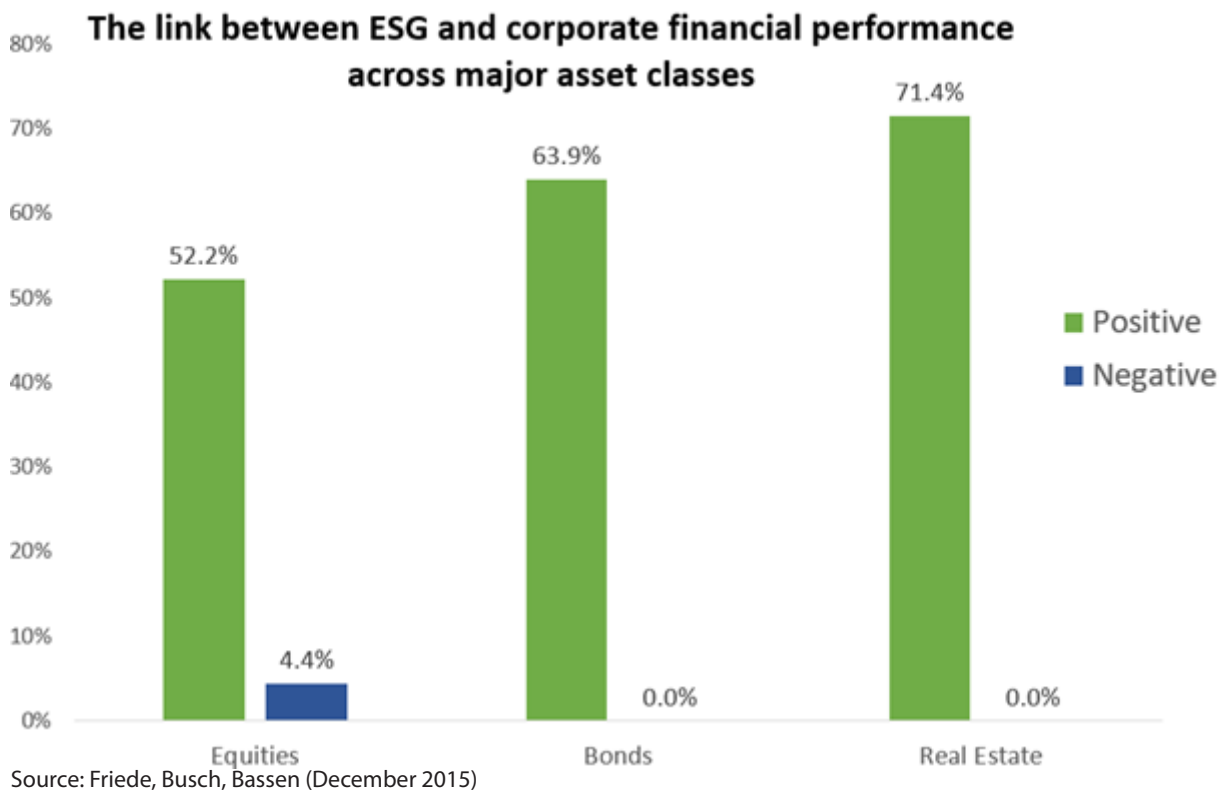
Sources: Olivia Albrecht and Nathan Chiaverini from 2020 ETF Summit by PIMCO; and, Credit Suisse, Data from various third party surveys.
[1] U.S. survey of 808 investors with at least $3M in investible assets.

According to a survey of investors, the majority of individuals under age 52 owned or were interested in owning SRI strategies in 2017 (the latest survey available). This represents a 58% increase in just two years from 2015 to 2017. Among millennials, the preference for SRI strategies is even stronger. More than 80% of respondents between the age of 21-36 already owned or had an interest in SRI strategies as of 2017. Given the increase in investor demand, the number of investment managers that focus SRI strategies has grown substantially over recent years. In the early days of SRI investing, only a small number of investment managers specialized in SRI strategies. Today that is not the case. According to the US SIF Foundation's report on Sustainable, Responsible And Impact Investing Trends in the U.S., there were more than 365 SRI money managers and 1,145 community investment institutions in the U.S. as of 2018.

PERFORMANCE

With continued rising investor demand and more SRI strategies to meet the demand, it appears that the SRI is here to stay for the long term. SRI investors, however, like all other investors, look for competitive returns. Many SRI investors feel that it is not necessary to forgo competitive investment returns when investing responsibly.

One of the largest studies on SRI performance was done by Deutsche Asset & Wealth Management and Hamburg University in 2015.[5] This meta-study (a combination of multiple studies) examined more than 2000 empirical studies since the 1970s, making it one of the most comprehensive academic reports on this topic. The study found that since the 1970s, the vast majority of research has found a positive relationship between a company's SRI and corporate financial performance. The graph below shows the findings across 3 different major asset classes.[6]



Source: Friede, Busch, Bassen (December 2015)

5 Friede, Gunnar, et al. "ESG and Financial Performance: Aggregated Evidence from More than 2000 Empirical Studies." SSRN, 19 Dec. 2015.
6 Ibid.

Since 2015, a number of other prominent studies have found similar results across asset classes.[7] Overall these studies have not found evidence of the relative negative performance of SRI strategies when compared with traditional investment strategies. Or to put simply, SRI strategies aim to "do well by doing good."[8]

If you have any questions about SRI or would like to know more about SRI, please contact your financial advisor.

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7 Desclée, Albert, et al. Sustainable Investing and Bond Returns - Research Study into the Impact of ESG on Credit Portfolio Performance. BARCLAYS, 2016; Matthews, Jessica, et al. "The Financial Performance of Real Assets Impact Investments." The GIIN, Cambridge Associates & Global Impact Investing Network, 2017; and, O'Brien, Amy, et al. Responsible Investing - Delivering competitive performance. TIAA. 2017.

8 This quote is often attributed to Benjamin Franklin.