

INTRODUCTION TO RESPONSIBLE INVESTMENT

Responsible investing, also known as ethical investing or sustainable investing, is a holistic approach to investing, where social, environmental, corporate governance and ethical factors are considered alongside financial performance when making an investment.

There are many different ways to engage in responsible investment, and most investors use a combination of strategies including negative or positive screening; environmental, social and governance (ESG) integration; and impact investing.

Anyone can be a responsible investor, whether they are individuals choosing where to put their retirement savings; a trustee of a trust or foundation; or an institutional investor such as a super fund, fund manager, bank or asset manager.

What is responsible and ethical investing?

Responsible investing, also known as ethical investing or sustainable investing, describes a holistic approach to investing, where social, environmental, corporate governance and ethical factors are considered alongside financial performance, when making an investment.

Examples of responsible investing vary broadly and could include:

- divesting from a company with a poor human rights record;
- engaging with a company included in an investment portfolio around its exposure to carbon intensive industries;
- making an investment in a program or social enterprise that is focused on tackling a pressing social or environmental issue; or
- analysing and selecting a portfolio of companies to invest in based on their overall environmental, social and governance performance.

Investors engage in responsible investing for a range of reasons including: to align investments with their own or their clients' personal values and ethics; to reduce risk; and to achieve strong financial returns in the short and long term.



Why is responsible investing worthwhile and important?

All businesses, and therefore all investments, have an impact on people and the planet, both positive and negative. Responsible investing seeks to minimise the negative effects generated by business and promote positive impacts, ultimately delivering a healthier economy, society and environment alongside stronger financial returns.

Simply put, responsible investing is good for business, and investors are realising the materiality of social and environmental themes in determining the risk and return profile of an investment. Companies or assets are unlikely to thrive if they ignore environmental issues (such as pollution, climate change, water and other resources scarcity), social issues (for example, local communities, employees, health and safety), governance issues (such as prudent management, business ethics, corruption, strong boards and appropriate executive pay) or ethical issues.

Responsible investment is also increasingly being considered part of investors' fiduciary duty to their beneficiaries and clients.

What level of consumer demand is there for responsible investing?

Consumers are becoming more active in demanding their money be invested responsibly and ethically. In Australia, the overwhelming majority of Australians now expect their savings (87%) and superannuation (86%) to be invested responsibly and ethically, and 3 in 4 people would consider shifting their banking and superannuation to an alternative provider that invests responsibly and ethically. Similarly, more than three-quarters of New Zealanders (76%) expect their KiwiSaver or other investments to be invested responsibly and ethically.

How do responsible investments perform?

In Australia, responsible investments typically outperform their equivalent mainstream counterparts year on year, over 3, 5 and 10 year horizons. For example, in 2019, Australian equities responsible share funds produced an average return of 10.1% over 5 years and 9% over 10 years. This compares with returns of 7.8% and 6.8% respectively for the S&P/ASX 300 index.

What are the different types of responsible investment?

There are many different ways to engage in responsible investment, and investors often use a combination of strategies including:

ESG integration: involves the systematic and explicit inclusion of environmental, social and governance (ESG) factors into traditional financial analysis and investment decision-making by investment managers. This approach rests on the belief that these factors are a core driver of investment risk and opportunity, rather than being driven by ethical considerations.

Negative or exclusionary screening: screening that systematically excludes specific industries, sectors, companies, practices, countries or jurisdictions from funds that do not align with the responsible investment goals. This approach is also referred to as values-based or ethical screening, as well as divestment. Common criteria used in negative screening include gaming, alcohol, tobacco, fossil fuels, weapons, pornography and animal testing.

Positive screening: screening in sectors, companies or projects selected for positive ESG or sustainability performance relative to industry peers. It may also be referred to as best-in-class screening. It involves identifying companies with superior ESG performance from a variety of industries and markets.

Norms-based screening: involves the screening of investments that do not meet minimum standards of business practice, usually based on international norms and conventions such as those defined by the United Nations (UN). In practice, norms-based screening may involve the exclusion of companies that contravene the UN Convention on Cluster Munitions, as well as positive screening based on ESG criteria developed through international bodies such as the UNGC (UN Global Compact), ILO (International Labour Organisation) and UNICEF (UN Children’s Fund).

Corporate engagement and shareholder action: refers to the employment of shareholder power to influence a company’s behaviour. This may be conducted through direct corporate engagement such as communications with senior management or boards, filing and voting on shareholder proposals and proxy voting in alignment with comprehensive ESG guidelines.

Sustainability-themed investing: relates to investment in themes or assets that specifically relate to sustainability themes. This commonly involves funds that invest in clean energy, green technology, sustainable agriculture and forestry, green property or water technology where the fund has the explicit objective of driving improved sustainability outcomes alongside financial returns.

Impact investing: targeted investments made into organisations, projects or funds with the intention of generating positive, measurable social and environmental outcomes, alongside a financial return.

RIAA's responsible investment spectrum

APPROACH	TRADITIONAL INVESTMENT	RESPONSIBLE & ETHICAL INVESTMENT						PHILANTHROPY	
		ESG Integration	Exclusionary/negative screening	Norms-based screening	Corporate engagement and shareholder action	Positive / best-in-class screening	Sustainability-themed investing	Impact investing	
METHOD	Providing limited or no regard for environmental, social, governance and ethical factors in investment decision making	Explicitly including ESG risks and opportunities into financial analysis and investment decisions based on a systematic process and appropriate research sources	Excluding certain sectors, companies, countries or issuers based on activities considered not investable due principally to unacceptable downside risk or values misalignment	Screening of companies and issuers that do not meet minimum standards of business practice based on international norms and conventions; can include screening for involvement in controversies	Executing shareholder rights and fulfilling fiduciary duties to signal desired corporate behaviours - includes corporate engagement and filing or co-filing shareholder proposals, and proxy voting guided by comprehensive ESG guidelines	Intentionally tilting a proportion of a portfolio towards solutions; or targeting companies or industries assessed to have better ESG performance relative to benchmarks or peers	Specifically targeting investment themes e.g. sustainable agriculture, green property, 'low carbon', Paris or SDG-aligned	Investing to achieve positive social and environmental impacts - requires measuring and reporting against these, demonstrating the intentionality of investor and underlying asset/ investee and (ideally) the investor contribution	Using grants to target positive social and environmental outcomes with no direct financial return
INTENTION		Avoids harm							
				Benefits stakeholders					
					Contributes to solutions				
FEATURES AND OUTCOMES		Delivers competitive financial returns							
		Manages ESG risks							
			Contributes to better system stability and economic sustainability						
					Pursues opportunities and creates real - economy outcomes				

* This spectrum has been adapted from frameworks developed by Bridges Fund Management, Sonen Capital and the Impact Management Project

Who can make responsible investments?

Anyone can be a responsible investor, whether they are individuals choosing where to bank or put their retirement savings; a trustee of a trust or foundation; or an institutional investor such as a superannuation or Kiwisaver fund, bank or an asset manager.

How do I know whether something is a responsible investment?

Responsible investment is not a 'one-size fits all' approach. Each responsible investment product or opportunity differs depending on the strategy or methods being used, as well as the particular features of companies or enterprises being invested in. For example, one product's responsible investment credentials may lie in it not investing in tobacco or ammunitions, while another product may be labelled a responsible investment because it solely invests in projects that deliver renewable energy.

The Responsible Investment Association Australasia's [Responsible Returns](#) online tool is designed to help consumers find, compare and choose responsible and ethical superannuation, banking and investment products that best match their values and interests. Each product listed on Responsible Returns has been certified in accordance with RIAA's [Responsible Investment Certification Program](#), indicating that a responsible investment product has been independently verified as true to label. Investment advisers are also able to filter products by product type, investment approach, inclusions, exclusions, geography and asset class, in order to identify products right for their clients.

How big is the market for responsible investing?

Assets managed in accordance with responsible investment principles now represent 37% (\$1,149 billion) of Australia's total \$3.14 trillion assets under management (AUM). This compares with the \$178 billion invested in responsible funds at the end of 2013, which at the time, represented just 17% of the total AUM.

In New Zealand, assets managed in accordance with responsible investment principles now represent 52% – or \$153.5 billion – of New Zealand's total NZ\$296.3 billion AUM. This represents a threefold increase over five years.

The growth in responsible investment in Australasia reflects broader trends, with global responsible investment assets reaching \$US30.7 trillion at the start of 2018 (a 43% increase from 2016), according to data from the Global Sustainable Investment Alliance.

Further reading

[RIAA Responsible Investment Benchmark Report Australia 2020](#)

[RIAA Responsible Investment Super Study 2019](#)

[RIAA Responsible Investment Benchmark Report New Zealand 2020](#)

[RIAA impact investment research - various](#)

[Global Sustainable Investment Alliance Global Sustainable Investment Review 2018](#)

ABOUT RIAA

The Responsible Investment Association Australasia (RIAA) champions responsible investing and a sustainable financial system in Australia and New Zealand. RIAA is dedicated to ensuring capital is aligned with achieving a healthy society, environment and economy.

With over 300 members managing more than \$9 trillion in assets globally, RIAA is the largest and most active network of people and organisations engaged in responsible, ethical and impact investing across Australia and New Zealand.

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