

*In this edition of The Private Investor we are delighted to include an article by Dr Quintin Rayer, who is Head of Research and Ethical Investing at P1 Investment Management. We are keen to boost our coverage of ethical and sustainability issues, so hope to include more contributions from Quintin in the future.*

## Introducing Ethical Investing

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### Biography

Quintin has worked for actuarial and investment consultancy firms and a multi-national European bank, including wide experience in quantitative fund and risk analysis. He is a Fellow of the Institute of Physics, a Chartered Fellow of the CISI and a Chartered Wealth Manager. Quintin has applied skills gained from his Oxford University Physics Doctorate and while working in engineering to finance. He is the second UK graduate from the Sustainable Investment Professional Certification (SIPC) programme and joined P1 in January 2017, founding their ethical and sustainable investing proposition.

### Introduction

Ethical investing has become a growing area of interest in recent years, with terms like ‘sustainable’ or ‘responsible’ investing also common. While the terminology can seem confusing, behind it lies a straightforward idea; money can be invested both to generate returns and do good (or at least minimise harm).

Ethical investment may be seen as falling into the ‘nice-to-have’ but non-essential category but is actually crucially important. It permits anyone with savings, including in pensions, to contribute to the betterment of society or to help with environmental issues including global warming. This becomes clear by exploring the relationship between sustainability and finance, which, in turn, sets the background for ethical investing.

Unsustainable human activities have generated threats including climate change (associated with rising sea levels, extreme weather and flooding, for example) resulting in damage, loss of life, and disruption to food and fresh water supplies. Lengthening life-span means demographics will have an impact on healthcare and pension costs. More of a growing world population will demand improved living standards as less developed countries modernise. Responsible investors argue that behaving unsustainably will cease to be an option.

### The Role of Companies

Corporations are ubiquitous and powerful, with a truly international presence. Humanity needs them to end unsustainable behaviours and tackle future challenges. These may include environmental problems, climate change and social issues. Regrettably, part of industry’s dynamism comprises the externalisation of costs on to the environment, communities, employees or future generations [1].

Financial markets play a role in helping to both support and control corporate behaviour. Markets reward ingenuity, efficiency, talent and productivity through the ability to raise funds from share and bond issuance, as well as by valuing companies through share pricing. Companies making far-sighted investments tackling these problems will benefit in either the short or longer term, making them valuable investments.

Since corporate activity is an essential part of human activity and development, sustainable investment also requires that companies generate economically sustainable long and short-term returns. This counters short-termism, in which immediate profits are made at the expense of damaging longer-term profitability.

## The Modern Business Environment

In today's environmentally and socially aware business environment, there is an appreciation that:

- Companies taking environmental risks have historically caused disasters (e.g. oil spills, deforestation, mining pollution).
- The social costs of business practices can no longer be ignored, as in previous eras (for example, the slave trade). Public tolerance of unacceptable worker conditions has diminished (e.g., mining and child labour).
- Companies require effective governance to confidently develop, meet legal and ethical requirements, and be accountable to stakeholders, including owners and shareholders. Corruption facilitates losses and sub-optimal decision-making. Poor oversight encourages high-risk behaviours and damaging scandals; potentially undermining reputations of entire industry sectors. For example, the banking and finance LIBOR scandal [2].

In the modern technologically-enabled world, environmental, social and governance failures are readily exposed, rapidly achieving global media coverage. Failures can result in financial losses, adverse litigation, reputational damage and clients taking business elsewhere. This can cause enormous damage to companies' values, share prices and even long-term survival.

Thus, ethically and sustainably orientated companies can target higher long-term profits by addressing pressing challenges while avoiding failures. At the same time, they accumulate marketing advantages and loyal customers as a result of their ethical behaviour.

### Why this Matters

Many individuals are motivated by recognising the challenges facing humanity (and other species) as a result of threats such as climate change, as well as many social issues. Global awareness of corruption also raises recognition of the importance of good governance.

Individuals understand the importance of ethical issues and extend these considerations into ever-increasing aspects of their lives. Beyond retail consumer decisions, more people are using ethical considerations to guide their investments as well. In January 2019, according to the Investment Association, there were £16.8 billion of assets in the UK ethical funds sector, an increase of £0.7 billion since January 2018 [3].

Ethical investors select companies that help tackle the challenges of environmental, social and other problems while avoiding companies that engage in unsustainable or harmful behaviours. They use the influence of financial markets to reward companies with positive behaviours while reducing capital available to those participating in unacceptable activities. Selection of individual companies to support can be targeted in line with specific ethical objectives. Individuals can direct their savings into ethical investment funds, and can often make decisions regarding pensions savings so that these are also invested ethically. In short, ethical investors seek to "do well, while doing good".

### Footnotes

[1]

J. Porritt, "The world in context: beyond the business case for sustainable development," Cambridge: HRH The Prince of Wales' Business and the Environment Programme, Cambridge Programme for Industry, 2001.

[2]

BBC News, "Libor scandal timeline", 2013. [Online]. Available at: <http://www.bbc.co.uk/news/business-18671255>. [Accessed 19 July 2017].

[3]

Investment Association, "PDF ARCHIVE OF STATISTICS," January 2019. [Online]. Available at: <https://www.theinvestmentassociation.org/fund-statistics/full-figures/>. [Accessed 25 March 2019].