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Well to be honest, the phrase ‘beauty is in the eye of the beholder’ is key here. What’s ethical for one person may not be for another and there are many different approaches to making values led and ethical decisions about investing.

When ethical investment is mentioned, most people will think of what we refer to as traditional ethical screening, such as avoiding businesses that sell weapons and instead investing in a green friendly, wind farm. Whilst this is not necessarily inaccurate, as seen below, techniques and processes have evolved a great deal and, over the last few decades to provide many different styles and options.

So how do you know if an investment is ethical or not?

At Ethical Futures we use our experience of screening processes to determine whether or not an investment fits your ethical criteria. Our job is as facilitators not moral arbiters. So we work with you to explain how screening works and where it invests – so that you can make an informed decision as to what is right for you. That decision is not just down to ethics, but also considers what your tolerance of risk is and how certain types of investments sit with your investment objectives.
What is ethical screening?

Screening is a process to determine if a company will be considered for investment based upon a benchmark of certain criteria. Those criteria can relate to avoiding something (referred to as negative screening), such as investment in firms producing weapons, alcohol or pornography. **Negative screening** is the most simple and most common method used, but now it’s often seen as a starting point onto which other styles are then added. The alternative to negative is positive and focuses on what a company’s does, such as renewable energy, education or simply having a good employment policy. **Positive screening** is used to identify good reasons to invest instead of choosing things to avoid; it is asking “why?” instead of “why not?”

One of the most common additional investment approaches is ‘engagement’. This is a very practical and measured form of shareholder activism, where investors, using the power of their share ownership, enter into dialogue with firms to try and encourage behavioural change.

The combined approach of using both negative and positive screening, perhaps incorporating some engagement, is often referred to as ‘socially responsible investment’. It’s a balanced and pragmatic approach. A further extension of this is to focus on issues of sustainability and themes such as ‘climate change. Thus over the last 5 - 10 years we have seen increasing evidence of funds that may not necessarily be defined as ‘ethical’ but are, to a degree, allied to the same agenda.

Generally speaking **thematic investment** is considered a means of top-down investment with a focus on broader macroeconomic themes. These tend to be funds that take a central issue and then use that as criteria to invest across a broad range of businesses. For example a client may be passionate about the impacts of climate change. A thematic fund could take this into account and invest in active sectors where positive action could have a real effect such as environmental technology, energy efficiency, water and waste management. Due to the highly specific nature of these funds they may not always require standard negative ethical screening.

A broader approach that can yield positive ethical results is **responsible governance**. Also known as engagement, it is an approach that uses communication and your power as an investor to encourage ethical practice. Engagement does not actively screen companies it instead looks to have a positive impact by incentivising companies to adhere to better standards such as implementing environmentally conscious measures. A fund manager will effectively lobby the company over issues with the goal to encourage ethical business practice and engagement can be implemented alone or as part of a larger procedure.

The final investment approach is the **social impact** strategy. It is a relatively recent development in ethical investment and has a core focus on the contribution the clients money will have on society. It provides the opportunity for a client to make a tangible difference alongside profit. This is another opportunity for a client to find an investment whose ethical goals align with their own. This could include investing in a fund that offers loans in the form of microfinance to people who would otherwise have no access due to the high-risk nature of their country or lack of collateral.

Social investing tends to put the emphasis on the social or environmental impact, rather than financial return. Therefore, although they are investment led the monetary return may be a secondary consideration.
Our aim is to select investments relevant to issues that are important to the client. The way we do this is consistent for all clients but the outcomes will vary for client to client, dependant on issues such as capital available to invest investment term, ethical values, investment objectives and tolerance of risk.

As you will see from our investment philosophy, we generally suggest the use of collective investment funds for clients (as opposed to direct investment) unless you have significant capital assets. The use of a fund automatically means that you have to accept the ethical policy or criteria established by the fund. Our job in this instance is to pick a ‘basket of funds’ with similar or complementary ethical styles – which will sit comfortably with both your investment and ethical objectives.

If you are fortunate enough to have substantial (in excess of £250,000) capital available, then you will be able to create a far more bespoke approach that may well include the direct investment into individual business and assets.
### Approaches to Ethical Screening

#### Negative screening

Means avoiding the types of businesses or industries that we don’t want our money involved with. This could include arms manufacturers, tobacco companies and known environmental polluters. Involvement in these kinds of activities will exclude a company from an investment fund.

#### Positive screening

Finds good reasons to invest. There are businesses out there that do some good in the world, such as creating renewable energy, helping to look after our health, adopting sustainable environmental principles or just being exemplary employers. Companies meeting any of a range of positive criteria might be selected for investment.

#### Engagement

Is simply talking to business. As an investor, you own a bit of the business, so why not engage with the management board to lobby for an improvement in standards? Fund managers give regular feedback on what they talk about. And if companies renege, then the fund manager might well disinvest.

#### Thematic investment

Is a new strand of investment approach, often used in environmental or ‘sustainability’ funds. These funds will look across sectors and geographic regions to invest in businesses that fit under a common theme such as ‘industries of the future’ or ‘climate change’. Funds will tend to have an environmental focus and may not always be subject to a traditional negative ethical screen.

#### Governance (ESG)

– Responsible governance funds may not adopt a form negative or avoidance screening approach. Their main concern is that the businesses that they invest in are responsible corporate citizens. By this we mean that there will be a lot of attention paid to what are referred to as ESG (environmental, social & governance) factors. This would include areas such as the quality of environment reporting, employee relations and executive remuneration policies. There are widely established metrics available in this area and detailed analysis and monitoring is undertaken to identify companies with potential reputational risk. Essentially, the theory being that a well run company will be less at risk of being the next VW or BP.

#### Social Impact

– Social impact is focussed on effecting change. This is one of the main purposes of a social impact investment and may outweigh the actual investment return. As such they fall into a space between traditional investment and philanthropy. Social impact investments, they can be very impactful, but might only be recommended as a small part of a portfolio designed to achieve a specific financial objective.

By their nature, the structure and regulation of social impact investments are very diverse; suitability will therefore depend on far more than just social purpose or an ethical screen.