How Long Is a Piece of String?

The definition of what it means to be ‘responsible’ or ‘sustainable’ is always changing. Today, the main focus is on sustainable, responsible supply chains. But the corporate social responsibility (CSR) agenda may be on the move again. How responsible is your company’s investment strategy?

Over recent years, institutional investors, such as insurance companies, foundations, endowments, sovereign wealth funds and public and private pension funds have devoted more attention to CSR-related issues when investing into corporates’ (corporations not including financial services providers such as insurance companies and banks) equities or bonds through primary or secondary capital markets based on their socially responsible investments (SRI) activities.

Institutional investors can play a decisive role in driving corporate social responsibility by offering carrots and sticks to the companies whose equity or debt they hold. They either exclude companies in certain sectors (Negative Criteria) such as tobacco or pornography or only invest in certain industries (Positive Criteria) such as renewable energy or clean technologies. Furthermore, by focusing their investments on those companies with the highest CSR scores in a specific sector (Best in Class) or by investing only in the leading company in the chosen area (Best of Class), they can encourage competition around best practice. In addition, institutional investors can also enter into a dialogue.
with corporates, influencing them through “engagement activities”. For example, they might use their right to vote in general assemblies on relevant issues.

Upon closer investigation, however, the apparently clear distinction between investors and the companies they invest in does not hold true. A company may attract institutional investors’ investments. At the same time, however, it may also be an institutional investor in its own right. For example, the pension assets of corporates in Germany, Switzerland and Austria alone are well over €1 trillion. But there may be a disparity between what a company does to attract institutional investors and what it does as an institutional investor. So, for example, a company might work hard to be perceived as sustainable in order to be selected for investment by rating, research, and index companies or consultants focusing on SRI. But when it comes to choosing their own investments, they might not use sustainability as a criterion.

We wanted to find out if such a disparity exists.

Using a unique, proprietary database of 13,000 institutional investors across Europe and the Gulf Region provided by a leading strategy consultant for the investment industry, we focused on the datasets of investors in Germany, Austria and Switzerland and screened over 1,000 institutional investors, including, among others, corporates and their investment vehicles, public and private pension funds, foundations, endowments and major single family offices, for their SRI-related activities. We also screened their portfolio investments, annual reports, press releases and any other available data to see if socially responsible investments were actively pursued.

We also screened over 500 specialists providing indexes or rating research or consulting services who manage SRI-related funds or portfolios for institutional investors. Whenever a link to an institutional investor was visible, we included the investor in our “sustainable investor universe”. So if one company managed, for example, a SRI portfolio for a specific institutional investor and communicated it to the public, this was also considered. Whenever there was a link to an investor, the institutional investor mentioned was added to our universe. In line with the snow ball method, we continued screening until no further investors could be added to the universe.

This triangulation of different information sources provided us with a solid “sustainable investor universe” of 159 institutional investors. This was our first finding – that only a small minority of around 16% of 1,000 institutional investors actively follow an SRI approach when investing their assets. We then sought interviews with these investors, focusing on three core questions:

- Which approach do you use in investing sustainably (e.g., best-in-class, positive or negative criteria, overlay)?
- Do you pursue this approach yourself and/or do you work together with service providers supporting you? Could you name these service providers?
- Which standards do you adhere to (possibly your own standards)?

Using the interview material, we excluded two further groups from our universe: those organizations that were distributing sustainable products but not investing sustainably themselves as part of their own portfolio investments and those institutional investors (particularly corporates) who promoted sustainability (for instance, in order to be included in a sustainable index) but so far have not pursued sustainable strategies when investing their own portfolios.

Corporates formed a clear majority of our initial ‘sustainable investor’ universe.

Many companies that work hard to be perceived as sustainable fail to apply the same criteria to their own financial investments. In fact, only a tiny minority of companies ‘walk their talk’ when it comes to their own investing activities.