6 Socially Responsible Investment

Mohamed Elshinawy, Oluwagbenga Adamolekun, Audrey Paterson, Mohamed Sherif and Stephen Rae

Introduction

So far, we have considered various issues and aspects of social accounting and their applications such as in corporate social responsibility (CSR). We now turn our attention to another important aspect of business, which is how organisations attract and maintain financial investment to support and grow. Businesses require investment; without it, they have no financing for operations that foster growth. Some investors have their own set of priorities when committing cash to an organisation and these can encompass their personal concerns about the social responsibility activities of the prospective investment. These concerns have led to a practice known as *socially responsible investment* (SRI). This can loosely be defined as shareholders making investments with a desire for socially beneficial outcomes, in addition to the obvious desire for financial returns.

SRI can be viewed as investors responding to an organisation's CSR actions. It can act to control, or mediate, corporate behaviour. For example, investors may reward a particular behaviour, e.g. by buying shares only in organisations that have a dedicated commitment to Fair Trade sourcing. Alternatively, investors may refrain from investing in organisations that have taken actions that are not within their social preference, e.g. not investing in an organisation that is known to use sweatshop labour. By choosing where to invest their wealth, investors have the power to grant or deny funding to organisations. In turn, organisations must follow expected social standards, or face lower investment, higher capital costs and potential financial failure. However, selecting where to invest is not a straightforward matter for investors when non-financial concerns are present. For example, it leads to questions over which actions are to be rewarded or penalised and the extent to which the investor values social results over financial returns.

SRI serves as a means to find suitable investment opportunities when faced with these and similar concerns.

The concept of SRI has grown considerably in recent years, particularly in response to the media raising awareness of the ruthlessness of corporate activity and social inequality across the globe. In this chapter, we begin with a discussion of the SRI concept and provide a brief outline of its evolution and its continuing importance to the present day. Following this, we discuss the legitimacy of SRI in the 21st century and the influence of the United Nations sustainable development goals and principles on SRI and the impact of these on investors' behaviour. Approaches to SRI decision making are then introduced in the form of *environmental social governance* (ESG) a vital tool in selecting investments based on a combination of financial returns, social responsibility, and personal ethics. The importance of non-financial outcomes to investors is also discussed. This is then followed by a discussion of some investment options that are available to investors before moving on to consider the performance of SRI investments.

The socially responsible investment concept

Socially responsible investment (SRI) refers to an investment type that prioritises ethical and social concerns in addition to the traditional financial activities of selecting securities and building portfolios (Weigand *et al.*, 1996). SRI is also known as ethical investment, green investment, or sustainable investment and seeks to achieve financial returns within the context of social, environmental, and ethical considerations (Hutton *et al.*, 1998; Lowry 1993). Overall, it identifies and indicates the manner in which potential investments or organisations are either included or excluded according to an ethical screening of their activities and products. Thus, investors select investments based on values that reflect their desire for ethical action toward positive social change.

The SRI concept is not new but has been around in various forms and guises for centuries. History suggests that the Islamic, Jewish and Christian religions embraced economic actions that aligned with their beliefs. In the middle ages, the Catholic Church forbade loans that had very high rates of interest (usury). This position has also been held in other religious beliefs. Some of the first instances of social responsibility investment are argued to have been influenced by religious tenets such as the old Jewish tradition (i.e. Talmud) and the Religious Society of Friends (Quakers). Indeed, the Quakers in the US colonies became involved in the early custom of social investing by focusing on their principles. There is also evidence of socially responsible investment within the Methodist faith dating back more than 200 years. Some historians suggest the foundations of SRI can be traced back at least to the ideology of Islamic Sharia investing and perhaps even before that. Each religion developed and applied their own value principles to investment, e.g. the Muslim faith did not permit investment in banks. The

Methodists favoured investments that aligned with their faith's social principles such as the right to organise and bargain collectively, avoid discrimination (age, race, gender etc.) and be allowed human rights.

It can therefore be argued that SRI has been a part of business decisions for centuries and this tradition has continued to influence it in more modern times. In the UK, ethical funds have strong roots in Victorian social reforms and have historically tended to focus on employee welfare, or the development of a local area. In the 19th century for example, the church became very active in investing in public health and non-university education. In the 1920s churches encouraged members not to invest in organisations that made money from gambling, tobacco, and alcohol. In other parts of Europe, the emergence of specific investment funds has been more of a contemporary phenomenon. The first recognised ethical fund in continental Europe was the Ansvar Aktiefond Sverige, created by the Church of Sweden in 1965. Similar funds addressing societal needs have since appeared elsewhere.

From the above, we can see that the concepts of social accountability and responsible investment have a long tradition. However, the examples seen in Chapter 2 demonstrate that social responsibility was not a significant concern for the vast majority of businesses. Rather, their focus was on profit maximisation, in which social responsibility concerns held little or no weight. It was the reporting of large profits, executives' bonuses, evidence of environmental damage and social inequality in the mid-20th century that led to increasing attention being turned onto the activities of organisations and the impact that they have had on the natural environment and wider society. This has led to the worldwide establishment of many SRI activist groups seeking greater social and environmental responsibility from organisations and governments. Some of these and their attitudes to SRI were identified by the OECD in 2007 and are laid out in Box 6.1.

Other issues that have increased calls for more social accountability and SRI include civil unrest, political instability and war. For example, in the US, the unprecedented media coverage of the Vietnam War began to turn a large section of public opinion against armed conflict, with attendant effects on investments in the arms industry. Around the same time, the Civil Rights Movement led to wide changes in societal norms in respect of fairness, equality and human rights. Increased attention was also drawn to environmental considerations as emergent environmental science began to show the effects of unrestrained pollution and consumption of limited resources. In the early 1970s, a number of funds that focussed on socially responsible investment were launched in the US and they increased significantly after the EXXON Valdez Alaskan oil spill incident of 1989, which caused huge environmental damage (Brown and Braddock, 1990).