

Ethical Investment: guiding the recovery

By Mark Mansley

Conventional wisdom has it that environmental and social concerns are unaffordable luxuries when the economic going gets tough – and that of course is bad news for ethical investors. That’s always been nonsense but the current crisis exposes the futility of the argument more starkly than before.

The near collapse of the global financial system, after all – precipitating deep recession, falling house prices and rising unemployment – represents as much as anything a collective failure to develop the world economy and the wider social and environmental system in a sustainable manner. Reversing this must be policymakers’ priority everywhere and inspiration is at hand in the values and ideals of ethical and responsible investors.

In this article I will examine four key ethical and responsible investment principles that need to be reasserted in the wake of the current crisis. I will contend, moreover, that between them they represent a real opportunity, not just for individuals keen to invest in line with their consciences, but for everyone seeking a rapid return to balanced and profitable economic growth.

The ethics of debt

The credit crunch has vividly highlighted the dangers of large scale debt and its accompanying interest burden.

No one suggests that borrowing should be banned but ethical investors have long been uncomfortable about the extremes of money lending – and should be vigilant when they see signs of a return to the excesses of the past. However, too many ‘responsible’ investors overlooked the evidence of debt addiction – high and unsustainable borrowings – and the role of companies in fostering that habit, as they simultaneously applauded and supported the same companies for their charity donations or policies on paper recycling.

There is now a clear case for regulating debt more rigorously. In the UK, it is ironic that if you have a few thousand pounds to *invest* you have the protection of a vast array of financial services regulation, including powerful principles such as suitability and fairness. Yet the protection for those who seek to *borrow* a few thousand pounds is scant.

Recall the purpose investment

In recent years, the rise of complex financial products, such as securitised mortgages, has meant investors have lost sight of what they are investing in, what the risks really are, and fundamentally what purpose their investments are serving. Crucially, such complexity played a key role in disguising and multiplying the accumulation of debt. For the finance industry generally, the obvious lesson is that investment needs to get

back to basics: i.e. taking money from those with surpluses and investing it in well managed entities that can put it to productive use.

Ethical investors have generally liked simplicity and shunned complex instruments in the past. Backing well managed forward thinking business, or tangible projects that contribute to society has been the heart of ethical investment. Indeed, for many the current crisis will strengthen their interest in investing directly in social enterprises – such as microfinance, community owned wind projects, organic food businesses and sustainable transport projects – where returns may be reasonable rather than spectacular, but where they understand the purpose of investing and the risks involved.

Real needs not consumption

Conventional economics must take much of the blame for the credit crunch – with its focus on material consumption as the measure of success. Crucially, economics needs to recognise that once basic needs are satisfied further gains in happiness do not necessarily come from material possessions. Given the choice, most people prefer safe streets, vibrant communities and a healthy environment rather than the latest plasma screen TV. Now is the time for politicians, business leaders and investors to embrace the growing body of research by organisations like the new economics foundation (nef) and the Worldwatch Institute in the US that underpins this more qualitative approach. Economic growth may be slower and less exciting as a result – but it will be more stable, sustainable and rewarding than the mirage that passes for consumption driven growth.

Ethical and responsible investors can help this refocus – by looking at the core values of companies – revealed in the way companies market themselves and how they invest. They should be cautious when companies indulge in advertising and marketing that feeds the cult of the consumer, nourishes false expectations of what a person ‘deserves’ and encourages excess borrowing. Companies that ‘innovate’ by focusing on evolutionary products no different to those they replace (the five-blade rather than four-blade razor, for example) should also be given a wide berth. Ethical investors are more than willing to support innovation but only if it addresses real needs rather than fuelling unwanted consumption or the latest ephemera. We must all ensure that resources are allocated to bigger challenges.

Risk is universal

Few economies, sectors or businesses have escaped the turmoil of the credit crunch. What we should have learnt, indeed, is that we are all connected to the wider economic system. The risk that arises from this, contrary to the pervasive teaching of the modern risk management gurus, cannot easily be diversified.

Although these macro risks cannot be managed by clever financial engineering, they can be managed, as ethical and responsible investors have long understood, by promoting well run companies in a well run economy.

So investors of tomorrow need to engage companies more fully on their core business strategy and financial structure, encouraging a conservative yet forward thinking approach. (“Activists”, by contrast, have been calling for companies to increase leverage and focus on the short term). If shareholders do not take the lead in this respect, pressure for a stakeholder model of the corporation will intensify – bring back the building societies, many would say.

Responsible investors must also increasingly make their voices heard in the policy debate too – responsible companies can only go so far without supportive policies. It’s encouraging, for example, to see a large group of investors that includes large banks and mainstream pension funds calling on governments to agree long term action on climate change. Similarly, ethical investors need to get behind ideas such as spending on sensible environmental measures (“the Green New Deal”), which will help address the challenge of sustainability, whilst boosting economic activity and jobs, and create interesting investment opportunities.

Seizing the opportunity

Credit, not religion, has been the opiate of the masses in the early 21st century, allowing those with limited incomes to feel in touch with the rich and to enjoy the illusion that they are full participants in the economic system. Now that this false promise has been exposed, the great increase in inequality over the last 25 years is set to become far more evident and politically charged. The credibility of ‘trickle down’ economics has been exposed as never before, and addressing inequality directly will be a key challenge in building a more sustainable economy.

For all the chaos it has left, the credit crunch in this and other respects can yet be a trigger for fundamental change. The signs are already evident – politicians sensing the anger of ordinary people, banking reputations in tatters – but the arguments are far from won. Ethical investors – by making it clear where they want to put their money, backing those businesses and opportunities that are part of the solution, and supporting a responsible approach to investment – can not only claim the high ground but bring others with them.

Mark Mansley, investment director, is responsible for the ethical investment strategy at Rathbone Greenbank Investments.*

*Rathbone Greenbank Investments provides personalised and professional investment management services for those who wish to ensure that their investments take account of their environmental, social and ethical concerns. It works with over 500 clients across the UK and manages over £350 million in assets (as at 5 April 2008). Its team has been at the forefront of ethical and responsible investment since 1992, and launched one of the UK’s first tailored ethical portfolio services.

Rathbone Greenbank Investments is a trading name of Rathbone Investment Management Limited, which is authorised and regulated by the Financial Services Authority. Registered office: Port of Liverpool Building, Pier Head, Liverpool L3 1NW. Registered in England No. 1448919.