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Socially responsible investing (SRI): From mainstream to margin?

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ABSTRACT

This article discusses the place of ethics within socially responsible investing (SRI) and tries to understand whether the debate about the spread of SRI strategies for all asset management practices (SRI mainstreaming) is necessary for SRI development. We conclude that the mainstreaming of SRI in global investment funds has transformed the original goal of "making good" into a quest for profitability. We also add that SRI must place ethics at the center of the debate in order to regain the primary virtuous logic it had when it was still part of a "margin" or niche market.

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1. Introduction

In 1999, Cowton entitled his research "Accounting and Financial Ethics: From Margin to Mainstream" with the aim of understanding whether ethical investment could move from a niche (margin) market to a mainstream or global market. A few years later, Dunfee (2003) entitled his research "Social Investing: Mainstream or Backwater" and sought to determine whether socially responsible investing (SRI) had the potential to converge across traditional asset management practices. Since then, the research community has tried to understand how to promote SRI practices in mainstream asset management (Arjaliès, 2010; Crifo and Mottis, 2013).

Meanwhile, SRI financial performance has grown and enabled SRI to become *financialized*, which means financial goals are the main objective of the portfolio managers, rather than achieving ethical goals, and that financial strategies of conventional funds are applied to SRI funds. The major focus of research in the SRI field has been to understand whether SRI was bankable and if it could be green and profitable. Indeed, since the 1990s, researchers, who have taken advantage of the emergence of nonfinancial or ESG (environment, social, and governance) data, have been able to regress and compare the performance and risk of ethical funds and conventional funds alike. Ultimately, ethics can be diluted in funds or investments that can generate similar performances compared to traditional projects (Revelli and Viviani, 2015), which brings up a concern about the real ethicality of SRI funds (Hellsten and Mallin, 2006).

Beyond the research, performance-based SRI has become anchored in a kind of asset management strategy called *ESG integration*, which has been defined by Novethic[1] as "less restrictive" SRI and "involves consideration by conventional

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[1] Novethic is a media and a research center based in Paris. It is considered to be one of the most influential media in France and Europe concerning all corporate social responsibility (CSR) and SRI issues. Novethic launched in 2009 "the Novethic SRI label", the "first European certification awarded

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management (also called mainstream) of some environmental, social and governance (ESG) key criteria or to make ESG analysis available to all management teams, or to encourage joint work between financial and extra-financial analysts".

This article first considers whether SRI has lost its original ethical values, which are derived from the Quakers and acted out in exclusive and activist funds,[2] and then guides the discussion on whether SRI should return to being a niche market instead of a mainstream market. It is important to ensure that SRI is rooted in strong ethical values and based on results, not just talk, and to determine if going beyond its niche to please everyone has been at the risk of having its principles swayed by the need to prove itself financially. The aim of this article is to explain how mainstream SRI has promoted SRI financialization and to propose ways to rebuild financial aspects within ethics, thus prioritizing individual ethics of the investor and identifying the impact of ESG criteria.

2. The logic of SRI performance

2.1. Convergence of SRI and traditional asset management: should we leave SRI as a niche market?

For years now, many researchers have tried to understand how SRI could affect or blend into traditional asset management practices (Arjaliès, 2010; Cowton, 1999; Dunfee, 2003; Sparkes and Cowton, 2004). The first step is to distinguish between the challenges of the SRI niche and mainstream SRI. SRI niche investing uses dedicated products for which the socially responsible dimension or ESG results in management constraint (Azoulay and Zeller, 2006). Mainstream SRI, however, seeks to integrate ESG dimensions into conventional management. The challenge is thus to compare an SRI that can clearly express its values and ethical convictions (SRI niche) with an SRI that focuses on material ESG issues, reflecting a fundamental analysis of business performance (SRI mainstream).

The problem is to identify whether SRI has to come out of a closed market of militant individual investors and join a more traditional market (including major institutional players such as pension funds). In 2003, Dunfee said that ethical investment had "the potential to become a mainstream phenomenon practiced by ordinary investors and reflected in the investment policies of retirement plans and mutual funds" (p. 252), provided that extra-financial information is accurate and comparable for all investors and portfolio managers. Sparkes and Cowton (2004) stated that the adoption of SRI policies by pension funds and insurance companies generated a very significant increase in assets in countries such as the United States, United Kingdom, Canada, and Australia. The authors point out that the Global Reporting Initiative (GRI) in 1999 and Principles for Responsible Investment (PRI) in 2006 played a major role in the development of SRI in all management practices, as much as the creation of ethical and SRI indices such as the FTSE4Good and Dow Jones Sustainability have done. In this sense, the growth of the SRI market has been exponential since the mid-2000s. According to the Global Sustainable Investment Alliance (GSIA, 2014), the European and US SRI markets represent 95% of the global SRI market in 2014. These two markets have, respectively, increased from US$336 billion in 2003 to US$13,608 billion in 2014 (+3950%) and from US$2164 billion to US$6572 billion in 2014 (+204%).[3]. The spectacular growth of the European SRI market could be explained by the explosion of the amounts invested into ESG integration and less restrictive SRI strategies, called *broad SRI* by Eurosif. The real issues concerning ESG stakes developed when pension funds and institutional investors began to understand that integrating socially responsible issues into their management process would not penalize the financial performance of their investments. Through a survey of SRI asset managers and institutional investors in the French market, Crifo and Mottis (2011, p. 18) point out that "for nearly three quarters of respondents, the main added value of SRI lies in better management of risk investments," adding that "it refers to a classic setting of financial performance: any information that reduces the risk of a portfolio helps to increase its value".

According to Arjaliès (2010, p. 69), the "mainstreaming era" for SRI in the French market was between 2006 and 2009 when Novethic used the term *SRI integration* for the first time and indicated that a new form of SRI emerged from investors who integrated nonfinancial criteria into a conventional financial analysis process. As for the Anglo-Saxon countries, institutional investor integration of ESG criteria into management strategies helps to institutionalize these practices in markets and within teams of financial analysts and managers. Arjaliès (2010) also points out the decision of the French pension reserve fund (FRR) in 2008 to adopt SRI screening of all its investments as an example of mainstreaming.

The actual trigger for the integration of SRI into the mainstream market occurred during the postfinancial crisis period (after 2009). Since then, ESG-integration processes have considerably accelerated, especially in asset management companies and among brokers, because of the negative image created by financial actors during the 2008–2009 crisis. Today, mainstream analysts and fund managers tend to incorporate ESG information into their investment strategies to restore a highly contested social legitimacy and to expand the scope of the opportunities and risks included in traditional financial analysis. Beyond the desire for rehabilitating legitimacy, institutional actors using SRI thus see a diversification opportunity to generate

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to Socially Responsible Investment funds that systematically integrate environmental, social and governance (ESG) criteria in their management". The definition proposed for *ESG Integration* could be seen at http://www.novethic.fr/lexique/detail/integration-esg.html.

[2] Exclusive funds remove from their investment universe entire sectors that are considered as unethical (alcohol, gambling, tobacco, etc.). Activist funds use their voting rights in corporations to put public pressure on their management concerning their Corporate Social Responsibility (CSR) strategies.

[3] According to European Social Investment Forum (Eurosif) for the European market and US Social Investment Forum (US SIF) for the US market. Eurosif and US SIF are networks that aim to promote the integration of ESG criteria in financial management through lobbying institutions, publishing research reports, and organizing events to raise awareness of ESG investors.

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