CEO Magazine article

Eurosif, the European Sustainable and Responsible Investment Forum, is pleased to support Europe CEO's efforts in explaining Socially Responsible Investment (SRI) to an increasingly diverse audience. As SRI continues to grow and evolve, it becomes even more important to clearly explain its multiple facets across Europe.

Both retail and institutional SRI continue to move forward, yet Eurosif believes that it is the institutional side that will lead SRI further into the mainstream in the coming years. Among the many findings that Eurosif has uncovered in its recently published study, "Socially Responsible Investment among European Institutional Investors 2003 Report", one of the key points is that European institutional SRI remains a movement with various layers, differing across geographical borders. The report, which was created with the support of the EC, collates national SRI data and provides an estimate of pan-European institutional market size. Eurosif analysis also details cross-country comparisons as well as provides predictions for future SRI trends. Specifically, the study highlights the scale of European Institutional SRI across eight countries (Austria, France, Germany, Italy, the Netherlands, Spain, Switzerland and the United Kingdom).

The conclusion of the research is that presently there is a duality to European institutional SRI. It maintains a steadfast niche market, and at the same time it is gaining momentum in being accepted by the financial sector. At its 'core', institutional SRI is approximately €34 billion. This approach removes engagement practices and simple exclusions of asset managers. Using this vision, the United Kingdom is the most developed institutional SRI market in Europe. Afterwards, Germany, France, the Netherlands and Switzerland are of similar sizes. Finally, Austria, Italy and Spain close the ranks as less developed markets.

However, by enlarging the view of institutional SRI, Eurosif calculates institutional SRI among European investors as €336 billion. These figures suggest that SRI has already entered the mainstream financial markets in countries such as the UK and the Netherlands. This approach posits that engagement practices and simple exclusions are increasingly being accepted and adopted by the greater financial community. As an example, comparing Funds Under Management subject to engagement for pension funds in the UK to the total UK share ownership of their pension funds produces an SRI ratio of 24%. Similarly in the Netherlands, almost all of the pension funds surveyed for the study said they applied at least simple negative screens in their fund selection, either as a form of risk management or an ethical statement. These facts may be viewed as a good sign for the future of SRI, since the high penetration rate of these practices point to investors and asset managers viewing them as causing little or no financial risk and possibly helping build company value.

Trends in the Future

Pension Funds Driving SRI Market Growth

Growing evidence indicates that pension funds and similar retirement systems have taken a leading role in developing the European SRI market. And everything points to this influence increasing in the future. As the pension fund market continues its growth in Continental Europe, trade unions are taking an increasingly active role in institutional SRI. In many countries, unions have an important say in how pension money is managed, and their interest in this area is continuing to develop.

Another relevant element is the fact that pension funds have a long-term view for assessing their returns. This fits the argument that SRI concerns along with sound corporate governance would enhance long-term company performance. Finally, it is fairly well known that SRI has been led not by debt instruments, but through the equities markets. It is significant that the weight of equities in overall pension investment still differs greatly from country to country across Europe. SRI will move into multiple asset classes as pension funds and other institutions increasingly diversify their equity and debt ratios.

Cultural Attitudes to SRI Converging Over Time

Each nation has had a cultural starting point in SEE (social/environmental/ethical) issues. As an illustration, these were the frames of reference from where each country began to tackle SRI:

Social/Community:	France, Italy, Spain
Environment:	Germany, Netherlands
Ethics:	UK

While these tend to remain strong, market maturation, growing public awareness and, from the supply-side's point of view, the development of mainstream SRI products are coming together to broaden the scope of national concerns.

Corporate governance also is a key issue affecting all of European. Thus, SRI practitioners are increasingly tackling issues that transcend national frontiers. This results in some of the key issues helping to drive a more common perspective on SRI over time. It is foreseen that SRI and corporate governance will be linked together over time by investors.

SRI Strategies Evolving, but not Always in the Same Direction

Positive screening will increase in some countries more than others. It already plays a significant role in markets such as France and Italy. Eurosif expects its growth to continue in continental Europe. It is appealing because its approach fits into the global financial culture and encourages “sustainable” competition between corporations aiming to be among the best-in-class and thus attract investment. Many rating agencies and sustainability indexes see their future in the development of this practice. Cynics however tend to believe that positive screening is inefficient since it is for now only applied in small amounts in comparison to the overall institutional market or even to the pension funds market and the original investment universe is restricted.

Critics of positive screening find more potential in engagement practices since these strategies are not subject to such restrictions. At the current time, a key question on the engagement approach is whether it can be translated from its national base in the UK successfully into other European nations. Within Continental Europe, the Netherlands has been showing signs of using this approach successfully in some of its fund management, but the practice remains limited. Most likely, an engagement approach will be hindered in the near term by its lack of visibility and measurable results.

Finally, the debate around simple exclusions as a strategy exemplifies the debate on SRI. Many SRI practitioners discount it as “real” SRI and say that it is just the basic entry point. This may ignore the fact that simple screening is also arguably an effective entry point into the financial mainstream as it is easily defined and largely defendable. At a minimum, it is a simple tool for risk management for a broad range of institutional investors. It may also serve as a means for SRI and financial communities to create an improved understanding of each others perspectives.

Conclusions

Today the potential for market development is enormous. At the moment, core SRI is only 2.1% of total European pension fund equity holdings. The main element shaping the future of institutional SRI is how sustainability issues can successfully be integrated into long-term financial management of public funds. The strength of debates on corporate governance, transparency and disclosure suggests that to a large extent, SEE issues might become a mainstream analysis factor for the financial markets in the years to come.

About Eurosif

Eurosif (The European Sustainable and Responsible Investment Forum) is a pan-European group whose mission is to encourage and develop sustainable and responsible investment and better corporate governance. Current members of Eurosif include NGOs, financial service providers, academic institutes and research associations. The association is a not-for-profit entity that represents assets totalling over €600bn through its membership.

Eurosif was created with the ambition to help shape the SRI movement in Europe. Eurosif was launched in 2001 by five national SRI forums with support from the EC's DG of Employment and Social Affairs. Eurosif's overall aim is to aid the integration of social, environmental and ethical issues into European financial services and to provide a multi-stakeholder network to share best practices on SRI. Recent Eurosif activities in 2002-3 included calling for the inclusion of a disclosure measure in the draft Directive for Institutions for Occupational Retirement Provision (IORP Directive), launching the development of pan-European Transparency Guidelines for retail SRI funds and calling for investor representation at the EC's Multi-stakeholder Forum on CSR. Overall, Eurosif's ongoing and future efforts will help foster further exposure and clarity for the SRI sector.