RESPONSIBLE INVESTING:
A THREE PART SERIES

PART II: Approaches to Responsible Investing

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Responsible Investing is a rapidly growing movement and each investor has unique priorities and values that affect how they approach this movement. In Part 1 of our 3 Part Series on Responsible Investing, we discussed the establishment of the movement, starting with its roots in biblical times, and evolving to modern times. Responsible Investing is continually fueled by emerging data and involves investment themes based on the social and political issues of the time. So how does a financial professional or investor approach Responsible Investing? Currently, there are four main avenues for expressing this growing movement.

A. Socially Responsible Investing — Avoidance

Approach	Description	Motive(s) Addressed
Socially Responsible Investing - Avoidance	Avoiding investments in companies whose products, services and/or behaviors are harmful or deemed controversial	Personal Values/Mission

Key Points:

- Driven by personal values, religious doctrine or corporate mission.
- Criteria generally norms-based or product-based.
- Does not actively seek environmental or social impact.

Strategies for Socially Responsible Investing allow investors to exclude investments that do not align with their personal values, religious doctrine or corporate mission. BONUS – it is probably the easiest concept to communicate to investors.

Though most think of screening in terms of excluding companies, this approach may also be applied to specific regions or even entire countries. The breadth of exclusionary criteria predominantly falls into one of two camps: norms-based or product-based. Norms-based criteria screens investments according to their compliance with, or violation of, international principles and standards (“norms”), such as those defined by the United Nations (UN) or the International Labour Organization (ILO). One should think of norms-based in terms of corporate behavior: working conditions, child labor, employee safety discrimination, or environmental protection. Companies incorporated outside the United States may be affected more as the U.S. has laws and regulations for many norms that other countries lack.

Product-based screening criteria can affect individual companies or entire sectors. Companies are screened out for the products and/or services they provide, whether easily defined: including alcohol, tobacco, and gambling, to the relatively complex: including life ethics and most recently, fossil fuels.

Fossil fuel divestment emerged in recent years as institutional investors are increasingly under pressure from college campuses and non-government organizations (NGOs) to divest from fossil fuel holdings. Divestment criteria varies from excluding companies with the largest fossil fuel reserves to divesting based on revenue and/or power generation. Institutional investors including the California Public Employees Retirement Systems (CalPERS), Stanford University and Norway’s Sovereign Wealth Fund have implemented some form of this approach.

B. Shareholder Advocacy

Approach	Description	Motive(s) Addressed
Shareholder Advocacy	Investors leveraging power of active ownership to influence positive changes to corporate policies and behavior.	Personal Values/Mission Environmental or Social Benefit (Making a Difference)

Key Points:

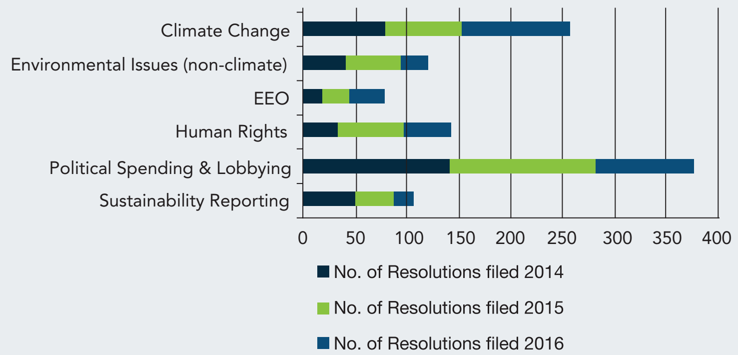
- Active ownership.
- Provides investors with a voice to effect change.
- Outsourcing and engagement companies can pool efforts and resources.

Shareholder advocacy involves the proactive execution of owner rights and responsibilities. Efforts typically seek to influence companies to make positive changes to their corporate policies and behavior through proxy voting, filing shareholder resolutions and/or engagement efforts.

Proxy voting is one way investors can influence change to a company's policies and corporate governance. Shareholders of publicly traded companies are entitled to vote their shares on issues presented for a vote at the company's annual meeting. Issues may be presented by either management or shareholders.

*Qualified shareholders may file proposals or resolutions to company management to be voted on at the next annual meeting. Typically, shareholder resolutions are opposed by the company's management, hence the need for a vote. Shareholder resolutions are a significant part of advocacy campaigns, bringing important issues to the attention of company management, board members, other shareholders, and sometimes even the media.[1]

Leading Environmental and Social Issues, by Number of Proposals 2014–2016



SOURCE: Sustainable Investments Institute, US SIF Foundation.

2018 Proxy Resolutions and Voting Guide, Interfaith Center on Corporate Responsibility

Submitted resolutions generally address financial, corporate policy/governance, environmental, and social issues. Resolutions can still be effective even if not presented at an annual meeting.

[1] **US SIF website: In the United States, the regulations and bulletins that the Securities and Exchange Commission (SEC) has issued under Section 14a-8 of the Securities Exchange Act of 1934 govern the inclusion of shareholder proposals in proxy statements. This shareholder proposal rule permits shareholders to file a proposal at a company if they own at least $2,000 or 1% of the company's shares and have held the shares continuously for the year prior to the company's annual submission deadline.*

Simply filing a resolution gets people talking, often initiating conversations between shareholders and management to find common ground.

Current events can often shape the topics of resolutions. The Interfaith Center on Corporate Responsibility, "a coalition of faith and values-driven organizations who view the management of their investments as a powerful catalyst for social change," notes the following new resolution topics for 2018:

New Topics This Year

- Gun Safety
- Paid Family Leave
- Political Contributions – Cost Benefit Analysis
- Risk of Lending, Underwriting Tar Sands Production
- Senior Executive Incentives – Integrate Cyber Security Risks
- Report on Board Oversight of Consumer Data Breach
- Risk Oversight Committee (social media)
- Responsible Tax Principles
- Create Board Committee on Human Rights (glyphosate)
- Supply Chain Policy on Prison Labor

Engagement, whether initiated by a shareholder filing or through direct engagement campaigns (and sheer perseverance), facilitates constructive dialogues between companies and their shareholders. Tactics can include face-to-face meetings, social-media campaigns, telephone calls or joining investor networks, which bring investors together to advance efforts (power in numbers).

C. Environmental, Social, and Governance (ESG) Integration

Approach	Description	Motive(s) Addressed
ESG Integration	Evaluates environmental, social and governance (ESG) performance factors to assess risk and incorporate into investment analysis and portfolio construction.	Personal Values/Mission Managing Risk

Key Points:

- Aims to improve risk/return.
- Relies on relevant and timely information.
- ESG is hard to measure in monetary terms.

"There is growing realization that whether motivated by economic value or moral values, ESG issues are relevant for all long term investors" – CFA Institute

ESG Integration (ESG) expands the spectrum of investment analysis from purely financial metrics to include sustainability elements into portfolio construction. Investors theorize that companies with strong ESG practices will enhance financial performance, while those with poor ESG practices are more susceptible to financial risk. The issues that fall under E, S and G are many and often intertwined.

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Examples of ESG Issues:

Environment Issues	Social Issues	Governance Issues
Climate Change	Human Rights	Executive Pay
Biodiversity	Child Labor	Bribery & Fraud
Carbon Emissions	Repressive Regimes	Board Structure
Air and Water Pollution	Employee Health Safety	Lending Practices
Water Stress	Diversity	Political Lobbying

Poor attention to corporate practices can affect the bottom line and often lead to media worthy events. Remember Enron or the BP Deepwater Horizon accident?

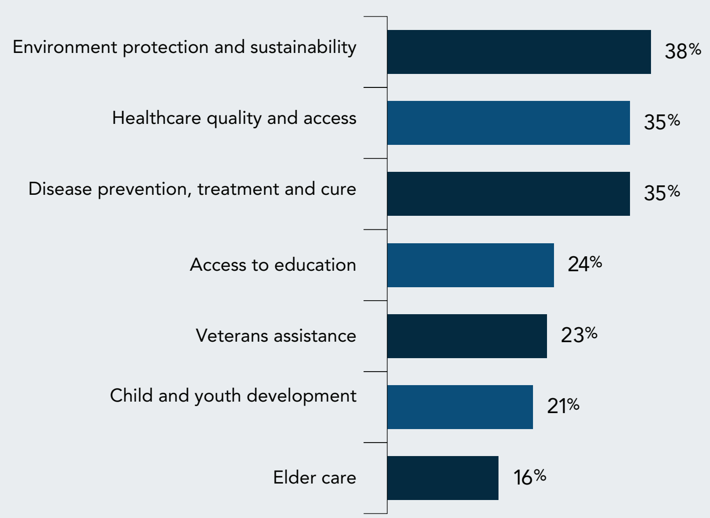
Companies are now promoting their good/sustainable corporate practices in order to bolster reputational risk.

ESG still needs work. Currently there is no global reporting framework, which can hinder company comparisons. Though initiatives to standardize corporate disclosure are in progress and more companies are reporting ESG metrics, it is largely self-reported so data may be limited and unverified.

D. Impact Investing

Approach	Description	Motive(s) Addressed
Impact Investing	Intentionally seeks to deliver measured, positive environmental and social impacts alongside financial returns.	Personal Values/Mission Environmental or Social Benefit (Making a Difference)

Top Impact Investment Interests



U.S. Trust Insights on Wealth and Worth 2016, Aligning Investments with Values.

Key Points:

- Positive social or environmental impact is paramount intention of investors.
- Rising demand from millennial and women investors.
- Financial return expectations can vary.

The Global Impact Investing Network defines impact investing as "investments made into companies, organizations and funds with the intention to generate measurable social and environmental impact alongside a financial return."

This approach seeks to deliver measured, positive environmental and social impacts alongside financial returns. It is harnessing the financial markets in a way that not only produces income for investors, but also provides targeted funding to make effective, positive environmental or social change in the world.

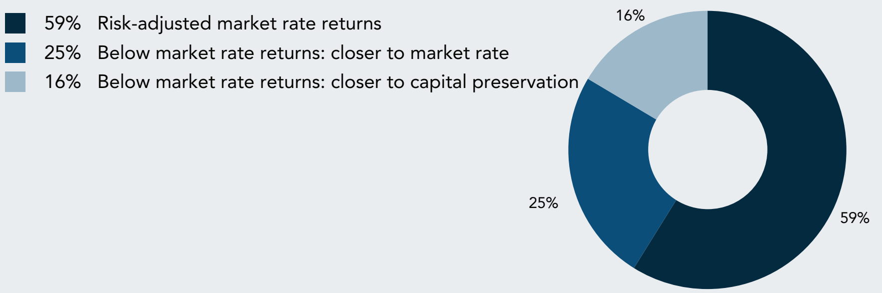
According to The U.S. Trust, Insights on Wealth and Worth 2016 Survey, "Millennials, women and those with the greatest level of wealth are most interested in social impact investments." Impact investors believe in walking the talk for themselves as well as the companies and issues they invest in.

Impact investors have differing financial return expectations. Some investors pursue competitive or market-rate returns, while others are willing to accept lesser financial returns to maximize their objectives. The Global Impact Investing Network reports "...that portfolio performance overwhelmingly meets or exceeds investor expectations for both social and environmental impact and financial return..."

As the needs of investors evolve and new and emerging preferences take form, the Responsible Investing landscape will continue to expand. In increasing numbers, investors are measuring value by both financial and social return. As of January 2017, $22.9 trillion globally managed assets are using sustainable investments strategies.[2] Financial professionals who implement Responsible Investing strategies will be able to continually address the needs of this growing market of values-based investors.

Target financial returns principally sought by number of respondents

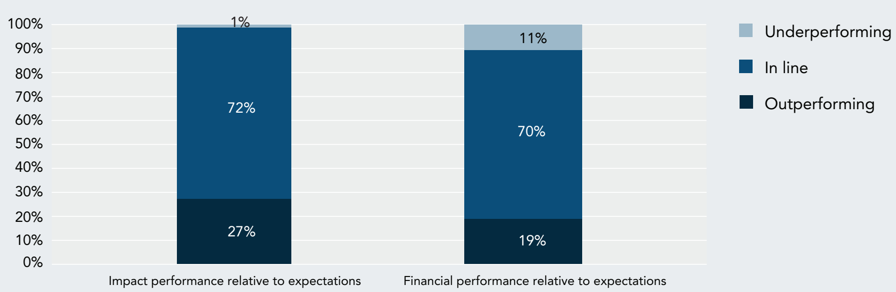
n = 158



Source: GIIN

Figure vii: Performance relative to expectations

n = 151; Some respondents chose 'not sure,' and their responses are not included here.



Source: GIIN

[2] US SIF Report http://www.ussif.org/blog_home.asp?Display=85

To learn how to incorporate responsible investing into your business model, see Part III of Responsible Investing: A Three Part Series.

Our Firm

Crossmark Global Investments is an innovative investment management firm. We provide a full suite of investment management solutions to institutional investors, financial advisors and the clients they serve. We have a multi-decade legacy of specializing in values based investment strategies for clients. Founded in 1987, the firm is headquartered in Houston, Texas.

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