

The **co-operative**  
asset management

# Guide to responsible investing for investment professionals

This document is intended for investment professionals only and its content should not be relied upon by private investors when making investment decisions.

Part of The **co-operative** financial services





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## About The Co-operative Asset Management

The Co-operative Group has over 12 million customers, of whom over 292,000 are investors in our Unit Trust range, amounting to over £2.5 billion of assets under management.

The Co-operative Asset Management specialises in active UK equities. We offer a distinctive responsible investment approach which fully integrates consideration of financial as well as ESG (environmental, social and governance) issues throughout the investment process.

We are the only UK fund provider to:

- apply a common core approach to responsible investment across all the funds we manage
- apply active engagement across all the funds we manage
- feed valuable business insights gained from our engagement process back in to company analysis performed for investment purposes.

We were also the first UK investor to publish our voting record at company AGMs on our website in 2002, a practice now increasingly adopted by fund management groups offering responsible investments.

Furthermore, our flagship fund, the Sustainable Leaders Trust, became the first ethical screened fund to top the UK All Companies sector, achieved over the 12 months to 30th January 2007.



This distinctive way of investing money has been recognised in our 2007 award as the 'Best Ethical Investment Provider' from Moneyfacts, a leading industry publication.

### PRI

The Co-operative Financial Services has signed up to the internationally recognised UN Principles for Responsible Investment. They reflect the increasing relevance of environmental, social and corporate governance issues to investment practices and in signing the Principles, the organisation publicly commits to adopting and implementing them (see page 12).

## Responsible investing – the opportunity for investment professionals

According to figures from the Ethical Investment Research Service (EIRIS), ethical investment in the UK retail market hit a record £9bn as at 31 December 2007. Ten years earlier, the figure was just £1.5bn. The number of vehicles available has grown from less than 25 to almost 100 today.

People call it ‘green and ethical investment’ or ‘socially responsible investment’ or ‘social, ethical and environmental investment’.

At The Co-operative Asset Management we call it simply responsible investing. Because that’s what it is – responsible, informed, prudent.

More and more clients are concerned with what the money they invest *does*. Does it fund companies that pollute the environment? Or that profit from child labour? Or does it help make the world a better place?

The market is no longer a niche – it’s well established and it’s worldwide. So why are so few investment professionals taking up the opportunities of responsible investing?

You might feel you’ve got enough to do without taking on a new ‘specialism’ – maybe you’re thinking ‘I’m no green guru’. Perhaps you suspect that ‘green’ equals low returns, or worry it’s all a flash in the pan. Or simply that your clients are ‘normal people’ and won’t be interested.

These are common myths – myths that mean you’re missing out on the chance to:

- expand your business
- gain a competitive edge
- enhance your professional profile
- and provide a better service to your clients.

This guide will take you step by step through understanding the opportunities of responsible investing – for you, and for your clients.

- Current estimated total UK consumer spending on ethical goods is £32.3bn, this figure is up 9% in 1 year and has almost doubled over 5 years.<sup>i</sup> And these consumers, according to market research firm Superbrands, are those with the most to spend.<sup>ii</sup>

- Around 78% of the assets of the largest pension funds incorporate responsible investing principles into their investment process.<sup>iii</sup>

## Know your client's values

The motivations for responsible investing vary. For some it's concern about the environment. For others it's religious conviction. Some are simply motivated by the bottom line – and see a sound business case for responsible investing.

As you know, it's a requirement of the FSA Conduct of Business rules to know your client, in order to give the best advice possible. Until you have asked your client all their needs you can't say you know your client. Just as you'd ask a client about their risk tolerance, you should ask if they have social, ethical or environmental concerns.

In doing so, you are not only meeting your regulatory obligations, but you also open up opportunities to strengthen your client relationships and build your business. Incorporating responsible investing into your business enables you to:

- attract new clients who are concerned with what their money does
- add value for existing clients by introducing them to responsible investing.

In fact, with more and more people expressing concern with what their money does, existing clients may well expect advice on responsible investing. And if you can't provide it they'll take their business to someone who can.



- Responsible investing is included in the new best practice standards in financial planning (ISO 22222) and the new financial adviser exams (FSSC, CII & IFS).
- Both Pension Funds and Child Trust Funds are now required to have disclosure regarding social and ethical issues.

## Approaches to responsible investing

There are dozens of product providers in the market and no two have exactly the same approach to responsible investing.

We believe that the most important feature of responsible investing is a process called engagement, in which fund management groups, as shareholders, use their influence over companies to encourage them to adopt higher standards of governance and corporate responsibility.

Engagement is important because it proactively facilitates positive and significant changes in businesses that would otherwise not occur. You can read more about engagement in the section 'A closer look at engagement' on page 12.

In addition, there are two common approaches to responsible investment funds:

- positive selection – investing in companies because the fund supports their sector (such as clean energy), policies (such as fair trade) or products and services (such as social housing)
- negative screening – avoiding investing in companies because of their sector (such as the arms trade), policies (such as sweat shop labour) or products and services (such as pornography).

### Our approach

Our flagship fund, the Sustainable Leaders Trust, integrates the strongest elements of all these methods, as well as employing a 'best-in-sector' approach. First we assess how well a particular sector meshes with our values.

For example, the beverages industry may offer handsome returns – but the business can have negative social and environmental impacts that need to be factored into the investment case.

Then, we look for evidence of companies that are genuinely addressing those impacts and we will seek to invest in the very best in the sector.

In addition, we look for crossovers between sectors that express our clients' values and sectors benefiting from changes in society (such as clean energy).

Occasionally, companies still have room for improvement, although their potential positive contribution is clear. Our pragmatic approach allows us to identify and invest in exceptional cases – and actively engage with the company to improve their performance.

From this carefully constructed universe, the fund manager selects investments on the basis of future growth prospects of a company.

## Ethical issues at a glance

Some clients have strong views on a particular issue, such as gambling, or are passionate about a particular area – such as animal rights. Others just want to know their money is working to make a better world.

No list will be exhaustive, but the issues below are those most frequently raised by investors and covered by responsible investment funds.

Environment	People	Animals	Governance	Values
Climate change	Human rights	Animal testing	Board structure	Arms trade
Habitat loss & biodiversity	Workers' rights	Fur	Excessive executive pay	Tobacco
Genetic engineering	Equal opportunities	Factory farming	Political donations & lobbying	Alcohol
Pollution & toxics	Access to medicine		Bribery and corruption	Pornography
Nuclear power	Health & safety			Gambling

These issues are often described by the umbrella term ESG (environmental, social and governance).

### Our Ethical Engagement Policy

The Co-operative Asset Management is the only UK fund management group to apply a customer-driven engagement policy across all its funds. In 2005 we gave our customers the chance to tell us what issues they cared most about. The results were used to create our Ethical Engagement Policy. Our customers know we are engaging companies with their concerns.

### Engagement in action

During 2007, The Co-operative Asset Management challenged advertising, marketing and Public Relations company WPP Plc regarding irresponsible lobbying activities of some of its subsidiaries. We argued that responsible representation should be prioritised over carbon emissions. In August 2008, the company informed us of a raft of reforms that met our recommendations including embedding ethical training for employees, strengthening its Code of Conduct to address client choice and enhance the systems that ensure this Code is being observed.

## Common concerns

### Isn't all this 'green' and 'ethical' business a fad?

All the indicators demonstrate otherwise. The recent battle between the supermarkets for green credentials shows which way the wind's blowing:

- growing consumer and regulatory pressure on social, ethical and environmental issues increasingly benefits responsible investing
- corporate social responsibility is now seen in many sectors as crucial to brand value
- companies that contribute, and adapt, to emerging social and environmental challenges may offer superior long-term performance
- climate change will keep the environment top of the agenda.

We have joined more than 280 top investment houses, with assets totalling £41 trillion, in supporting the Carbon Disclosure Project – a scheme that seeks information from companies on their exposure to climate change risks.<sup>iv</sup>

### Aren't responsible investment funds exposed to greater risk?

An estimated 70% of the value of top companies relates to 'intangible assets' such as 'goodwill' and 'brand reputation'<sup>v</sup>. That's value exposed to social, ethical and environmental risks. Analysis of these risks can put responsible investment funds ahead of the game, by helping them identify companies that the market may have mis-priced.

### Doesn't a restricted investment universe lead to under performance?

All active managers filter stocks on different grounds. And recent studies have shown a link between companies' social & environmental management and financial performance<sup>vi</sup>.

It pays to be responsible and, increasingly, those who aren't – pay.

## Performance with responsibility

With some product providers you hear a lot about 'socially responsible' but not enough about 'investing'. Make sure that the providers you recommend have strong investment credentials, as well as claiming socially responsible expertise.

The Co-operative Asset Management's Sustainable Leaders Trust was the first ethical screened fund to top the UK All

Companies sector, beating over 320 funds including mainstream blue chip equity funds. And that's been achieved while excluding the Oil & Gas and Mining sectors – both strong performers over the period (i.e. 12 months to January 2007). This achievement is testimony to the sound investment fundamentals of the fund.

## How to evaluate funds

No two funds are the same – so here are the key issues you’ll want to take into account when assessing responsible investment funds for your clients.

### Performance

As with any investment, the track record of the Fund Manager – especially over the long-term, is paramount.

### Values

Do the values, approaches and any no-go areas of the fund match your clients’?

### Transparency

Ensuring that you and your client can understand exactly what the fund *does* is crucial. It ensures the client understands what they are buying. And it helps you compare products. It may be wise to avoid funds whose investment and stock selection processes seem complicated, confusing or riddled with ethical jargon.

### Experience

Embedding ethical issues into the investment process is notoriously difficult. Does the organisation have the necessary experience and resources? How does the Fund Manager come up with a rounded view of a company based on a balance of financial and ESG considerations?

“Responsible investing should never be an excuse for under performance.”

**Mike Fox, CIS Sustainable Leaders Trust’s Fund Manager**

## Our commitment to transparency

At The Co-operative Asset Management, we aim to make our investment approach and fund range clear and easy to understand. The purpose and strategy of our funds are very straight-forward. Our own commitment to corporate transparency is demonstrated by our being the first UK institutional investor to publish online a record of how we voted at company AGMs.

## Research and risk

Investment decisions are only as good as the quality of research they're based on. How does research integrate financial considerations (eg balance sheets, business strategy, competitive position) and ESG issues (i.e. governance risk, impact on the environment, employee policies)? How do the research outcomes feed into stock selection? How does the fund manager construct a diversified portfolio and mitigate risk.

## Engagement

Your client wants a fund that reflects their values. How are those values applied when selecting companies for investment?

“Responsible investing is not something we apply to a few isolated funds, it's integral to our whole investment process. Corporate social responsibility is what our organisation was built on. In 2007, we were ranked in the highest category of the UK's leading benchmark – the Corporate Responsibility Index.”

**Ian Jones, Head of The Co-operative Asset Management's Responsible Investment Team**

How does the fund engage with the companies it invests in to put your clients' values into practice? Can it demonstrate success in improving companies' performance?

## Leadership

Does the fund provider itself show leadership in corporate social responsibility? It's as simple as putting your money where your mouth is. Research shows that ethical consumers are wary of companies jumping on the green bandwagon<sup>vii</sup>. For some clients how the fund provider behaves is as important as financial returns.

## Leadership at The Co-operative Asset Management

- The Co-operative Group is considered to be Britain's most ethical brand<sup>viii</sup>.
- We are one of the world's largest purchasers of renewable electricity. – 98% of the electricity we use comes from green sources<sup>ix</sup>.
- Our Solar Tower head office in Manchester (pictured right) is the largest solar power project in the UK<sup>x</sup> – and we've brought together 40 of the UK's biggest Plcs to share our expertise in powering business with wind power<sup>xi</sup>.

Read more about how we 'walk the talk' at our website.

**[co-operativeassetmanagement.co.uk](http://co-operativeassetmanagement.co.uk)**

## A closer look at engagement

You'll hear a lot about engagement from ethical investment product providers. Engagement is an important part of responsible investing as it involves not just evaluating companies' responsible business practices, but also actively facilitating their improvement.

We encourage investment professionals to closely examine the way in which engagement is undertaken, as it can take many forms. Some product providers call research or gathering information 'engagement'. But this has no direct bearing on a company's direction or practices.

At The Co-operative Asset Management, when we say 'engagement' we mean tackling companies over issues of concern and championing best practice. For all our funds engagement is rigorous, ongoing and designed to add value to decision-making in the investment process. The impact of our engagement is independently audited to ensure that it continues to set the industry standard.



### Engagement in action

In 2006-7, we engaged with Weir Group which had supplied equipment to Sudan, an oppressive regime, for oil exploration and production. In light of the risks this presented, we asked the company to justify its continued involvement and to halt operations in Sudan until a robust peacekeeping force was in place. Soon after, it embarked on a programme of "controlled withdrawal" from the region.

### Performance and (UN) Principles

In the 2007 survey of signatories to the UNPRI (see page 4), we scored in the top 10% of all signatories on integrating ESG issues into investment analysis and decision-making processes and being active owners who incorporate ESG issues into ownership policies and practices<sup>vii</sup>.

## A closer look at integration

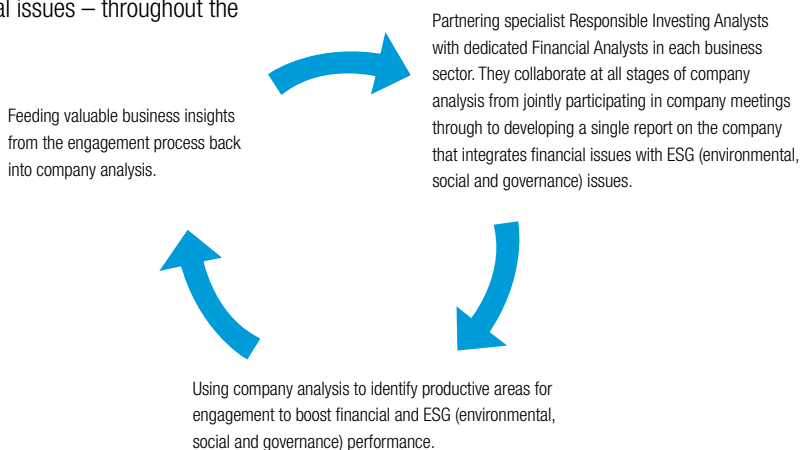
Increasingly, responsible investment providers seek to distinguish themselves by advocating an ‘integrated’ approach. We urge investment professionals to look closely at how this is done. For example, investment managers might influence the engagement process, but without using engagement feedback in making their investment decisions.

Genuinely integrating financial analysis, engagement, and social, ethical and environmental issues – throughout the

investment process – leads to a more robust, informed view of a company. And ultimately, we believe, to superior investment decision-making.

At The Co-operative Asset Management, we see this approach as a one-way street.

For us, integration means creating a virtuous circle:



## Engagement In action

In 2007, Co-operative Asset Management published a report examining the social and environmental impacts and risks associated with the current growth in the biofuels industry, covering issues such as emissions, land use and labour rights. It made recommendations on how different companies can manage these risks. Copies were sent to a range of stakeholders, including to 66

investee companies in the oil, food, waste, chemical and transport sectors. We received responses from 15 investee companies and held face-to-face meetings with a further 9. We found that respondents were making some progress towards a sustainable model. But we must also infer that the ‘silent majority’ have a lot of catching up to do.

## How The Co-operative Asset Management can help you

The Co-operative Asset Management combines bottom-up stock selection with the application of carefully developed themes to construct detailed investment cases on undervalued companies.

In advocating The Co-operative Asset Management to clients, advisers can be assured that they are recommending:

- Britain's most ethical brand, The Co-operative Group<sup>x</sup>
- a responsible investment approach which fully integrates financial and ESG criteria in stock selection
- an investment process characterised by clear and informed views on why companies are undervalued and offer good long-term prospects
- an investment resource comprising experienced and committed individuals working to deliver out-performance while effecting positive change in the companies they invest in.

In early 2007, our flagship fund, the Sustainable Leaders Trust, became the first ethical screened fund to top the UK All Companies sector.

The Fund Manager, Mike Fox, won the 'UK Growth Fund Manager of the Year 2007' award from Citywire, and is 'A' rated as at 30/06/2008.



The Co-operative Asset Management's Sustainable Leaders Trust, UK Growth Trust and UK Income with Growth Trust, are available through Cofunds, Fidelity FundsNetwork and Hargreaves Lansdown Vantage platforms.

## Your next step...

**Contact broker services**

**0845 603 9986**

**co-operativeassetmanagement.co.uk**

responsibleshareholding@cfs.coop

- i [www.eiris.org](http://www.eiris.org)
- ii 'Business embraces its ethical future' BBC New 1 Nov 2006 <http://news.bbc.co.uk/2/hi/business/6102450.stm>
- iii 'Your money your choice: A guide to Ethical Investment' Ethical Investment Association & UK Social Investment Forum 2005 <http://www.ethicalinvestment.org.uk/uploads/YourMoneyYourChoice.pdf>
- iv <http://www.cdproject.net/aboutus.asp>
- v 'Bringing "Accountability for Brands" to the Boardroom: Is that my job too?' Paper No. 20040101 - By Michele Levine, Chief Executive, Roy Morgan Research. January/ February 2004 edition of The New Investor: February 12, 2004 <http://www.roymorgan.com/news/papers/2004/20040101/> see also: "Brand Valuation: The financial value of brands" By Interbrand <http://www.research.commissionedbythenationalconsumerCouncilandAccountAbility> (a charity committed to improving businesses' social and ethical performance) found that The Co-operative Group was the most trusted business in the UK, with key differentiation in the areas of honesty, the environment and the treatment of employees (SR2005 p6, survey undertaken by Globescan in May 2006). [channel.com/papers\\_review.asp?sp\\_id=357](http://channel.com/papers_review.asp?sp_id=357)
- vi For example: Orlitzky, M, Schmidt, F & Rynes, S 2003, 'Corporate social and financial performance: A meta analysis', Organization Studies, vol 24, no. 3, pp 403-11. <http://oss.sagepub.com/cgi/content/abstract/24/3/403> and "A study into the influence of Environmental Governance and Financial Performance" Prepared by Innovest Strategic Value Advisor/Advisers November 2004 [http://www.innovestgroup.com/images/uk\\_ea\\_corp\\_gov.pdf](http://www.innovestgroup.com/images/uk_ea_corp_gov.pdf)
- vii Stephen Cheliotis, Superbrands: quoted <http://news.bbc.co.uk/1/hi/business/6102450.stm>
- viii An independent consumer survey carried out in 2007 and 2008 found that for both years The Co-operative was Britain's most ethical brand. The Co-operative Group (including the Co-operative Bank) was ranked number one for 2007 and 2008 with Body Shop and Marks and Spencers ranking second and third respectively. The GFK NOP Ethics brand Survey was conducted in the US, UK, France, Germany and Spain amongst 5000 individuals in total. The study found that consumers are increasingly choosing to buy brands which they believe to be ethical, with many willing to pay a premium for an "ethical guarantee" (GFK NOP Press Releases 2007 & 2008).
- ix The Co-operative Group Sustainability Report 2005 p23
- x [www.cis.co.uk/servlet/Satellite?cid=1116834043935&pagename=CoopBank/Page/tpiBlank&c=Page](http://www.cis.co.uk/servlet/Satellite?cid=1116834043935&pagename=CoopBank/Page/tpiBlank&c=Page)
- xi [http://www.goodwithmoney.co.uk/cfscombi/pdf/Responsible\\_Shareholding.pdf](http://www.goodwithmoney.co.uk/cfscombi/pdf/Responsible_Shareholding.pdf)
- xii Scores have been calculated based on signatories' self assessment and using the scoring methodology approved by the PRI Assessment Group. Not all responses have been independently verified by the PRI Secretariat, PRI Assessment Group, or any other third party. Individual results including comparisons to the overall results (quartiles) are indicative and do not imply an endorsement of signatory activity. While this information is believed to be reliable, no representations or warranties are made as to the accuracy of information presented, and no responsibility or liability can be accepted for any error, omission or inaccuracy in this information.

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