

## IRI Working Paper

# Investment Beliefs Statements

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Initiative for Responsible Investment

***Abstract:*** Investment Beliefs Statements articulate the fundamental perceptions of trustees and their institutions on the nature of financial markets and the role they play within these markets. An Investment Beliefs Statement serves as a bridge between high-level goals and practical decision-making, and help trustees, fiduciaries, and others responsible clarify their views on the nature of financial markets through which they must operate and how these markets function. This working paper emphasizes the importance of Investment Beliefs Statements, their role in the investment management process, and their usefulness in clarifying the focus and goals of institutional investors. Examples of both investment policy statements and investment beliefs statements illustrate their differences and the role that investment beliefs statements can play in integrating responsible investment and sustainability into investment practices.

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## **Investment Beliefs Statements**

### **What They Are, Why They Are Important**

#### ***Introduction***

This IRI Working Paper provides basic background on Investment Beliefs Statements and presents a series of questions that can be raised in them, emphasizing those that relate to sustainability and responsible investment. It also provides examples of Investment Beliefs Statements currently published by a range of institutional investors, particularly those that include issues of sustainability and responsible investment.

The purpose of this paper is threefold. First, it is intended to emphasize the importance of Investment Beliefs Statements, their role in the investment management process, and their usefulness in clarifying the focus and goals of institutional investors. It also illustrates potential formats that these statements can take.

This paper also underscores the importance of transparency and full disclosure of investment beliefs. Institutional investors necessarily operate in accordance with a set of investment beliefs that are at a minimum implicit in their investment practices. All too few, however, are explicit and transparent as to the nature of these beliefs—i.e., how they believe markets operate, their definition of success in investment, and their assessment of the proper role of investors in the marketplace. Fund managers and trustees have an obligation to their beneficiaries to be as clear and explicit as possible about these beliefs, to act on them coherently and consistently, and to review and update them regularly.

Third, the Working Paper highlights a variety of questions and issues relating to sustainability and responsible investment that can be considered in Investment Beliefs Statements. We believe the consideration of the role of these issues in the investment process is an important step for institutional investors. They may view them important to determining financial outcomes or aligning mission with practice, or they may decide that these factors should not be considered. Whatever their viewpoint, our objective here is not to define others' beliefs. Our aim is rather to provide a framework within which institutional investors can articulate their beliefs in the interests of transparency and clarity. Clients, participants and beneficiaries have a right to understand as completely as possible the belief systems that are guiding the deployment of their capital.

Recent academic has been done by the International Centre for Pension Management (ICPM) at the University of Toronto under the leadership of Keith Ambachtsheer. Several papers by Kees Koedijk and Alfred Slager; Roger Urwin, Claire Woods, and Gordon Clark; and Keith Johnson and Frank Jan de Graaf have argued for the importance of investment beliefs. See Recommended Readings below for a representative list of these articles.

## **Investment Beliefs, October 2011**

### ***Importance of Investment Beliefs Statements***

Investment Beliefs Statements articulate the fundamental perceptions of trustees and their institutions on the nature of financial markets and the role they play in these markets. An Investment Beliefs Statement is neither a mission statement nor an investment policy statement, however. The former sets forth the institution's fundamental goals. The latter describes the specifics of how the institution hopes to achieve those goals. An Investment Beliefs Statement serves as a bridge between high-level goals and practical decision-making. Investment Belief Statements are important because they help trustees, fiduciaries, and others responsible clarify their views on the nature of financial markets through which they must operate and how these markets function. They set forth the institution's rationales for the selection of investment styles and managers; the principles they apply in the investment process; and the strategic decisions they make and why. (Koedijk et al., 2009)

The noted pension-fund consultant, Keith Ambachtsheer includes "sensible investment beliefs" as one of five key factors in successful pension investing. The other four are aligned interests, good governance, right-scaled, and competitive compensation. (Koedijk and Slager (2011: x)

Beliefs drive practice and it is important that practice is aligned with beliefs. An Investment Beliefs Statement can help guide investors toward practical decisions about their investment style, investment managers, asset allocation, security selection, and the degree of activism they may wish to adopt with relation to their investments. A clearly formulated Investment Beliefs Statement can help avoid misunderstandings or conflicts of interests between asset owners and their service providers. It can also help lead trustees, fiduciaries and others to better understanding of investment processes, to more rigorous monitoring of external managers and other service providers, and to improvements in the governance of their funds.

Finally, investment beliefs can help investors steer a consistent course, regardless of today's investment fads and can provide a benchmark against which investment practices can be judged. They argue further that the questions that should be answered as investors clarify their will address the major issues confronting finance at any given moment. As they put it, "Investment beliefs echo the major debates in investment management."

As Koedijk et al. (2010) have noted, "[T]rustees should be in control of their investment process, and they should be aware of the choices that they face and the consequences of their decisions." An Investment Beliefs Statement will help trustees maintain that control, make clear and conscious choices about the investment process, and understand the implications of their investment practices.

Koedijk and Slager distinguish four basic sets of investment belief—those addressing financial markets; those considering the value added by the investment process; those relating to organizational skills and design; and finally those relating

## **Investment Beliefs, October 2011**

to sustainability and corporate governance. (2011: 47). The first three are those most often addressed in Investment Beliefs Statements.

We have stressed also here issues relating to sustainability and the broader purpose of finance, which are not included so frequently. However, Koedijk and Slager assert, “SRI [socially responsible investment] can be considered a true investment belief when the organization links sustainable investments with a long-term view of the capital markets and society.” (2011: 137)

Urwin and Woods in their 2009 paper “Sustainable Investing Principles: Models for Institutional Investors” have written: “Sustainable investing is an investment strategy derived predominantly from investment beliefs—investors who embrace sustainable investing believe that an investment strategy with greater breadth and depth will produce stronger investment performance both now and in the future.” They suggest that “sustainable investing is mostly about investment beliefs and contrasts with responsible investing which is more about values” and state that they “see a beliefs-based rationale as crucial to the effectiveness and longevity of any sustainable investing strategy.”

Johnson and de Graaf in their 2009 paper “Modernizing Pension Fund Legal Standards for the Twenty-First Century” include the requirement of an “annual Board affirmation of a statement of investment beliefs and mission” among their recommendations for best practices for modernizing pension fund legal standards. Clark and Urwin in their 2008 paper “Best-Practice Pension Fund Governance” similarly note that examples of pension funds with best governance practices “rely upon a process centered on strong beliefs,” observing that “Only with a clear and accepted beliefs structure can an institution sustain its competitive edge in financial markets.”

Investors may have many reasons to believe that the incorporation of social and environmental factors is an important part of the investment process for either normative or instrumental reasons. We have therefore included in this paper a number of questions that can help clarify the connection between social and environmental issues, portfolio management, market stability, and the larger economy. Less research, however, has been conducted on topics relating to the incorporation of social and environmental issues into the investment process. One particularly useful website for academic research on the financial connection between financial performance and SRI practice is [sristudies.org](http://sristudies.org).

Financial markets are social constructs that serve societal needs and are capable of abuse that can undercut their purpose, or innovation and reform that can enhance benefits. As Koedijk, Slager and Bauer have noted, investing “is not a hard science like physics or chemistry; it is primarily a social science.”

As the numerous financial booms, busts, unpredictable crises, and hotly contested innovations and reforms over the decades have demonstrated, financial markets are prone to extremes and abuse that can undercut their purpose and harm the broader economy. Because stable and productive financial markets depend on the quality and wisdom of the investors that make up these markets, we believe that

## **Investment Beliefs, October 2011**

Investment Beliefs Statements are crucially important. Well conceived Investment Beliefs Statements can help investors assure that financial markets are approached thoughtfully and productively by their participants.

Preparing an Investment Beliefs Statement helps investors articulate, what functions they believe these markets can optimally play in society, why they were created, and how investors should ideally act when participating in them. Investment beliefs will differ for pensions funds and asset managers. As Koedijk and Slager put it, “Asset managers use investment beliefs to demonstrate their competitive advantage, whereas pension funds use them as an effective tool for reasoned debate and decision-making.” (2011: 39)

We have designed the following set of questions primarily for pension funds, rather than asset managers and characterize these beliefs as the “why’s” and the “how’s” of investors’ decisions and the measurement of their success.

### ***The Why of Investments***

Investment Beliefs Statements may address a set of fundamental questions about why investors invest, such as:

#### *1. What makes investment successful?*

- Do you believe that investment is a zero-sum game? Do you believe that financial investment decisions can affect (positively or negatively) the economy?
- If you are a fiduciary, how do you believe investing can best serve the interests of your beneficiaries? How do you define the interests of your beneficiaries?
- Do you believe that investments have social and environmental implications for financial returns? For the health of the economy? For the interests of beneficiaries? If so, which are the factors that you believe have the most substantial implications?

#### *2. Why is the conduct of investors in financial markets important?*

Investment Beliefs Statements may address a set of fundamental questions about the conduct of investors in financial markets, such as:

- Do you believe that cumulatively investors’ policies and practices can affect the stability of the financial markets?
- Do you believe there are risks involved in the complexity of the market and the structuring of financial products offered? Do you believe there are specific risks involved in the financial markets that may negatively impact the health of the economy? Should fiduciaries attempt to monitor and manage those risks?
- Do you believe that investors should consider the particular social and/or environmental roles that asset classes can play in the economy in making their asset allocations?

## **Investment Beliefs, October 2011**

### ***The How of Investments***

#### *1. How do you believe financial markets function or should function in society?*

Investment Beliefs Statements may address a set of fundamental questions about how financial markets function, such as:

- Do you believe that markets are efficient in setting prices, and if so, how much of the time and to what degree?
- Do you believe active management can add value to the risk-adjusted returns of a portfolio? If so, under what circumstances?
- Do you believe that asset allocation plays an important role in determining overall portfolio returns? If so, to what degree relative to security selection?
- What do you believe an appropriate definition of risk in financial markets should be?
- What do you believe the benefits of diversification should be and what do you believe the appropriate role of diversification in an investment policy should be?
- Do you believe stable, honest and transparent financial markets make an important contribution to a healthy economy?
- If your investment goals require capital appreciation that keeps pace with inflation, do you believe that cost-of-living issues such as global warming, food security, access to water, efficient allocation of capital, political instability/safety, and similar issues should be considered in the investment process?
- If you are a fiduciary, how do you assure that the interests of future, as well as present, beneficiaries are served and that your decisions are impartial in their benefits to future as well as present beneficiaries?
- Do you believe that the incorporation of social and environmental factors into the investment process can shift it toward long-term horizons?

#### *2. How do you or should you as an investor interact with these markets?*

Investment Beliefs Statements may address a set of fundamental questions about how investors interact with financial markets, such as:

- Do you believe that institutional investors of a certain size are essentially “universal owners” who consequently have a particular obligation to take the broad health of the economy into account? If so, of what size?
- Do you believe that there are circumstances under which it is possible and useful for investors to positively affect the quality (financial, governance, societal, or environmental) of their investments?
- If you are an asset owner, do you believe it is important to work with asset managers whose investment beliefs correspond with yours? Do you believe that conflicts of interest between you and your asset managers are a potential danger?

## **Investment Beliefs, October 2011**

### *3. What types of information should you consider essential in your investment decisions?*

Investment Beliefs Statements may address a set of fundamental questions about the types of information that are essential for investment decisions, including questions about sustainability and responsible investment such as:

- Do you believe that investors should consider governance information in addition to financial data in making specific investment decisions?
- Do you believe that investors should consider social and environmental information in addition to financial data in making specific investment decisions?

### *4. What do you believe your obligations as an investor are to communicate and advocate?*

Investment Beliefs Statements may address a set of fundamental questions about what the obligations of investors are to communicate their investment practices, and to advocate change on the part of those in whom they have invested, such as:

- Do you believe that there may be times when as an investor your concerns about financial, governance, social or environmental issues may rise to a level of concern—either positive or negative—that communications with the purveyors of your investments become appropriate? If so, when would this be appropriate?
- Do you believe that, in such communications, it is appropriate to advocate policy changes on the part of those with whom you have made investments? If so, when would this be appropriate?
- How often and in what form do you believe it is important to communicate your investment beliefs and practices to beneficiaries, investors, or the general public.

## ***Preparing an Investment Beliefs Statement***

Developing an Investment Beliefs Statement appropriate to your institution can be a challenge and an opportunity. The process itself can be a valuable and important educational opportunity for trustees, staff, and others involved in the debates and discussions that will inevitably arise. It also has implications for the institution's definition of itself and can help focus and sharpen that definition.

Investment Beliefs Statements should be developed with due consideration for the nature, function, and mission of the organization in question. Development of an Investment Beliefs Statement is ultimately the responsibility of those entrusted with oversight of the management of investment assets. In many cases that will be the institution's board of trustees, as with large pension funds. In other cases that responsibility falls more logically on the money managers.



## **Investment Beliefs, October 2011**

There is no one set form or formula for Investment Beliefs Statements. These statements can be short or long, detailed or general, comprehensive or selective. Whatever the form, they should clearly address those issues that are the most important drivers of your investment process, the beliefs that are core to your investment practices and distinguish you most clearly from others. These beliefs should stand for the institution and be appropriate to the institution, and not simply reflect idiosyncratic personal beliefs of particular trustees or staff at any given moment. Neither, however, can they be separated entirely from, and avoid being influenced by, these personal beliefs. The challenge is to identify those beliefs that are credible and appropriate to the institution itself and likely to remain so for the indefinite future. As with other acts of self-definition, this process can be a challenging one, involving extended debate.

Not all questions that arise about the why and how of investing need to be addressed in your Investment Beliefs Statement. You should concentrate on creating a clear statement of those beliefs that are core to your approach to investment, drive your key decisions, can be easily communicated and understood, and distinguish you from other investors. You want to be certain to convey as clearly and succinctly as possible the fundamentals that you believe lie at the heart of the investment process and against which your success can be measured. The extent to which you want to go into detail will depend in part on your view of whether the role of your Investment Beliefs Statement is primarily to communicate or to educate.

Investment Beliefs Statements can be included along with Investment Policy Statements in communications with clients and beneficiaries, as well as in communications with financial consultants, outside money managers and other service providers. These communications can also include indications of how you assure that your investment beliefs are in fact aligned with your investment practices.

Once prepared, Investment Beliefs Statements can present a number of challenges and opportunities in their communication. An Investment Beliefs Statement needs to be clearly communicated to those who will be implementing it. For an asset owner, this means clear communications by trustees with their staff or asset managers, as well as with their financial consultants. Clear communications are necessary if internal staff and service providers are to create and execute investment practices that are aligned with these beliefs. Similarly, if trustees are acting as fiduciaries, their investment beliefs should be clearly communicated to beneficiaries so that they can correctly understand why various investment practices have been put in place.

## Recommended Readings

Among the primary readings recommended on this topic are:

- Gordon L. Clark and Roger Urwin, “Best-Practice Pension Fund Governance” *Journal of Asset Management* Vol. 9, 1: 2-21, 2008.
- Kees Koedijk and Alfred Slager, “Do Institutional Investors Have Sensible Investment Beliefs” *Rotman International Journal of Pension Management* Vol 2, 1: 12-20, Spring 2009.
- Kees Koedijk Alfred Slager and Rob Bauer. “Investment Beliefs That Matter: New Insights into the Value Drivers of Pension Funds” ICPM Sponsored Research Paper. Rotman International Centre for Pension Management: Toronto University. July 2010.
- Kees Koedijk and Alfred Slager, *Investment Beliefs: A Positive Approach to Institutional Investing*. Basingstoke, United Kingdom: Palgrave Macmillan, 2011.
- Keith L. Johnson and Frank Jan de Graaf, “Modernizing Pension Fund Legal Standards for the Twenty-First Century” *Rotman International Journal of Pension Management* Vol 2, 1: 44-51, spring 2009.
- Roger Urwin and Claire Woods, “Sustainable Investing Principles: Models for Institutional Investors” October 2009.
- Claire Woods and Roger Urwin, “Putting Sustainable Investing into Practice: A Governance Framework for Pension Funds” *Journal of Business Ethics* 92:1-19, 2010.

In addition, some consider Chapter 12 of John M. Keynes’ *The General Theory of Employment, Interest and Money* (Cambridge, United Kingdom: Macmillan Cambridge University Press, 1936) a particularly insightful background piece on the challenges of long-term investing.

## Appendix A: Examples of Conventional Investment Beliefs Statements

(All examples are excerpts, except as otherwise noted)

Appendix A includes excerpts from conventional Investment Beliefs Statements—two from pension funds, one from a money manager, and one from a university endowment. We have included them here to provide a general sense of the different types of issues and the range of approaches that institutional investors take to formulating and communicating their investment beliefs.

### ***Arizona State Retirement System<sup>1</sup>***

#### **FRAME OF REFERENCE**

The ASRS has developed the following *Investment Beliefs* in order to ensure the development of congruent and synergistic investment strategies, and to ensure the effective and efficient allocation of resources.

These *Investment Beliefs* determine the general paradigm within which investment strategies are developed, investment ideas are reviewed, and investment decisions are implemented.

Modifications to these *Investment Beliefs* will occur if expectational, academic, experiential, historic, and/or statistical perspective suggests that a superior belief system exists.

#### **INVESTMENT BELIEFS**

##### **1. Asset Class Decisions are Key**

The Investment Management Division (IMD) believes that in general, decisions with respect to what asset classes and sub-asset classes to invest in, and the allocations to these asset classes and sub-asset classes, have a greater impact on total fund investment returns than decisions in which specific securities to invest.

##### **2. Theories and Concepts should be Sound**

IMD believes that over longer periods of time, investment outcomes (rates of return) conform to logical theories and concepts. We believe that significant deviations from theoretically and conceptually sound investment constructs (such as the internet bubble or the pre-subprime erosion of risk premiums) are usually not sustainable.

##### **3. House Views should be Developed**

IMD believes that the development and articulation of sound House Views (such as perspectives on interest rates, corporate spreads, and security pricing) will ensure consistency among investment decisions, clarity of investment direction, baselines for debates, and conformity of understanding.

##### **4. Investment Strategies should be Forward Looking**

IMD believes that investment strategies should be developed based upon forward looking insights (rather than simply successful strategies of the past).

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<sup>1</sup> [https://www.azasrs.gov/content/pdf/financials/Investment\\_Policy\\_Statement.pdf](https://www.azasrs.gov/content/pdf/financials/Investment_Policy_Statement.pdf)

## **Investment Beliefs, October 2011**

### **5. Information Universes are Multiple**

IMD believes that asset class valuations and security valuations are significantly affected by endogenous outcomes (such as earnings, GDP growth rates, and competitive barriers) that are probabilistic; and that these outcomes are typically analyzed well by the investment industry.

IMD believes that asset class valuations and security valuations are also significantly affected by random outcomes (such as natural disasters, and certain supply and demand shocks) that are virtually unpredictable; and that these outcomes are typically not analyzed directly by the investment industry.

IMD believes that asset class valuations and security valuations are also significantly affected by exogenous outcomes (such as foreign policies, and global cultural interactions) that can possibly be modeled; and that these outcomes are typically not analyzed by the investment industry.

### **6. Markets are Generally Informationally Efficient Asset Class Valuations**

IMD believes that asset class valuations (for instance stock market levels versus interest rate levels) are often in equilibrium with one another, but that anomalous situations do occur which result in disequilibria between asset class valuations. These disequilibria may offer valuable investment opportunities.

### **7. Security Valuations**

IMD believes that security valuations (for instance IBM versus Cisco) are often in equilibrium with one another, but that anomalous situations do occur which result in disequilibria between security valuations. These disequilibria may offer valuable investment opportunities.

IMD believes that the extent of market informational efficiency varies across asset classes.

### **8. Market Frictions are Relevant**

IMD believes that market frictions (such as including management fees, carried interest, revenue sharing, expenses, costs, transaction spreads, market impacts, taxes, and commissions) are known with greater certainty than expected returns and are significantly detrimental to investment performance.

IMD believes that investments and/or transactions should be initiated only to the extent that there is a strong level of conviction that they will result in increased investment returns or decreased risks net of market frictions.

### **9. Internal Investment Professionals are Beneficial**

IMD believes that an in-house investment management operation that is engaged in internal portfolio management results in better investment decision making for the ASRS.

IMD believes that in-house investment personnel are more closely aligned with the purpose of the ASRS than most external parties.

## **Investment Beliefs, October 2011**

IMD believes that in-house investment personnel have a greater understanding of the risk and reward tolerance of the ASRS than most external parties.

IMD believes that at the margin in-house investment personnel can impact direct investment negotiations with vendors, as well as influence investment industry conditions (such as private deal structures and public and private fee levels).

### **9. External Investment Management is Beneficial**

IMD believes that external investment organizations can often offer greater expertise and/or greater resources and/or greater flexibility than internal personnel for various investment strategies.

### **10. Investment Consultants**

IMD believes that investment consultants can and should be effectively utilized in the following four general categories, and that utilization of consultants should be focused on situations where there is a demonstrable need in at least one of the four areas:

Independence: When ASRS' protocols or checks & balances can be enhanced

Perspective: When ASRS' comparative understanding can be enhanced

Special Skills: When IMD's skills can be enhanced

Resource Allocation: When IMD's resources can be enhanced

### **11. Trustee Expertise**

IMD believes that Trustees often have expertise in various areas of investment management and that this expertise should be utilized.

## ***Australia Futures Fund<sup>2</sup>***

### **MISSION BELIEFS**

#### ***The Board believes:***

(i) that the single measure embodying the goal of the Future Fund and Nation-building Funds is achieving the mandated returns over rolling 10 year and 12 month periods respectively. For the Future Fund, while the amount of risk taken cannot be captured in one figure, it is best assessed by reference to downside outcomes over rolling three year and 10 year periods;

(ii) that peer group risk should not be used to shape strategy. The Future Fund Investment Mandate provides an unusually long-term investment horizon and this presents a competitive opportunity to add value;

(iii) that while quantitative measurement of risk is important, so is building qualitative views of risk through understanding the environment and its potential impact on the portfolio. In addition, operational, counterparty and reputational risk need assessment and management;

(iv) that the amount of risk taken should be conditioned by what strategy is most likely to meet the investment goals given current conditions.

### **GOVERNANCE BELIEFS**

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[http://www.futurefund.gov.au/data/assets/pdf\\_file/0015/4119/15943\\_FF\\_AR\\_2010\\_WEB\\_V2.pdf](http://www.futurefund.gov.au/data/assets/pdf_file/0015/4119/15943_FF_AR_2010_WEB_V2.pdf)

## **Investment Beliefs, October 2011**

### ***The Board believes:***

- (i) that high quality governance of the investment process is critical to success. The likelihood of meeting investment goals is directly related to the time, expertise and organisational effectiveness applied to decisions by the Board and management. Within this, the clear identification and separation of the Board's and management's responsibilities is particularly important;
- (ii) that it should ultimately be responsible for all investment decisions. This leads to decisions being tiered with the Board retaining control over top tier decisions, passing over responsibility below this tier to management subject to the Board's oversight;
- (iii) that its role is to act as a principal, acting in complete alignment with the Fund's mission. It has a critical role in managing agency issues, including those of management, and influence over compensation levels and incentives are critical to achieving success in this regard;
- (iv) that there is value in ensuring adequate time, diversity of view and specialist advice are applied to its deliberations.

### **INVESTMENT STRATEGY BELIEFS**

#### *The Board believes:*

- (i) that its focus should be on the effective management of beta (market related risk) because it is a stronger driver of long-term returns than alpha (skills related risk);
- (ii) that markets can be inefficient and skilful managers can add value after fees (albeit that the degree of inefficiency varies across markets and over time) and that this return is, in general, lowly correlated with market returns;
- (iii) that a flexible approach to asset allocation exposures is appropriate;
- (iv) that a higher expected return per unit risk (investment efficiency) can be obtained from a broadly diversified allocation across asset classes. In addition, the long time horizon supports a tolerance for illiquid assets;
- (v) that while the quantification of returns, risks and correlations are necessary inputs in the design and review of investment strategy, the difficulty and limitation of these assumptions means qualitative considerations are also important.

## ***Pictet<sup>3</sup>***

Our underlying investment philosophy reflects our beliefs with respect to the basic mechanism and functioning of financial markets. It underpins our approach to analyzing markets and to the way we evaluate the economic environment or individual companies.

Thus, in guiding our investment decisions and allowing us to define what we are looking for in precise detail, it forms the basis for all processes within Pictet North America Advisors. This philosophy is founded upon the following principles:

- The price of a financial asset should reflect the current value of its future cash flows.
- In reality, the prices of financial assets deviate from their level of equilibrium, sometimes over an extended period of time.

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[http://www.pictet.com/en/home/pictet\\_north\\_america/investment\\_expertise/investment\\_philosophy.html](http://www.pictet.com/en/home/pictet_north_america/investment_expertise/investment_philosophy.html)

## **Investment Beliefs, October 2011**

- In the long term, the price should return to its level of equilibrium.
- The nature of market inefficiencies varies over time, but there are always some opportunities worth seizing.
- The valuation level at any given time is no indication of a financial asset's immediate return but is significant in the long-term (five years or more).
- A stock's equilibrium level depends on the relationship between the returns and the cost of capital of the company in question.
- Inflation and interest rates lie at the heart of market mechanisms.
- In the short to medium term, there is greater certainty in anticipating economic trends on the basis of financial market developments than vice versa.

### ***Yale University<sup>4</sup>***

Policy asset allocation targets provide the foundation for the investment process, as no other aspect of portfolio management plays as great a role in determining a fund's ultimate performance. Yale derives its target allocation using a combination of quantitative and qualitative analysis. By employing the quantitative tool of mean-variance optimization, the Investments Office identifies efficient portfolios with expected returns that surpass those of all other portfolios for the same level of risk. Inputs to the process include estimated return, risk, and correlation measures for different asset classes. Important qualitative considerations include the nature of active management opportunities, the degree of asset class illiquidity, and Yale's comparative advantages as an investor and active manager.

In producing portfolio recommendations, the Investments Office complements top-down mean-variance optimization with bottom-up assessment of market conditions. By evaluating the absolute and relative attractiveness of investment opportunities uncovered by Yale's far-ranging roster of external investment managers, the Investments Office directs funds toward more attractive opportunities and away from less compelling situations. That said, given the long-term nature of policy targets, bottom-up considerations play a secondary part in the asset allocation process relative to the lead role of mean-variance optimization.

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Market return studies indicate that high levels of equity market exposure benefit long-term investors. However, the associated risks come through less clearly. Significant concentration in a single asset class poses extraordinary risk to portfolio assets. Fortunately, diversification provides investors with a powerful risk management tool. By combining assets that vary in response to forces that drive markets, investors create more efficient portfolios. At a given risk level, properly diversified portfolios provide higher returns than less diversified portfolios. Conversely, through appropriate diversification, a given level of returns can be achieved at lower risk. Harry Markowitz, known as the father of modern portfolio theory, maintains that portfolio diversification provides investors with a "free lunch," since risk can be reduced without sacrificing expected return.

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<sup>4</sup> [http://www.yale.edu/investments/Yale\\_Endowment\\_10.pdf](http://www.yale.edu/investments/Yale_Endowment_10.pdf)

## **Appendix B: Examples of Investment Beliefs Statements and Related Statements Addressing Sustainability and Responsible Investment**

(All examples are excerpts, except as otherwise noted)

Appendix B includes excerpts from the Investment Beliefs Statements and Investment Policy Statements of various institutional investors and asset managers, which address issues of sustainability and responsible investment.

The line between Investment Beliefs Statements and Investment Policy Statements can be indistinctly drawn at times. In the interests of completeness we have included examples of investment policy statements addressing social and environmental issues—such as policies stating that institutions will not invest in tobacco companies or companies with a record of employment discrimination. We have included these because they imply a belief—for example, that these practices are unsustainable, unjust, unprofitable in the long run, or in need of public debate that can be prompted by strong statements of concern. The policy is clearly stated. The reason for the policy—the investment belief—is only implicit.

We have also included beliefs about social and environmental records of companies that may be debatable—for example, that companies with strong environmental and social records will outperform their peers in the long run. As with certain assertions in more conventional Investment Beliefs Statements—for example, that markets are efficient and accurately price securities—ongoing debate backed by data and research is to be expected. For a variety of reasons it is healthy for financial markets, as well as society more generally, when a diversity of opinions on issues that are publicly debated exists within the money management world.

Included here are examples from statements from pension funds (seven), asset managers (six), US foundations (two) and others (two). For the most part these are included in larger statements of investment beliefs or investment policies. We have excerpted them here to provide a general sense of the different types of issues and the range of approaches that institutional investors take to formulating and communicating their investment beliefs on sustainability and responsible investment.

### **Pension Funds**

#### ***Australian Christian Superannuation Fund***

##### **3.5 Responsible Investment is consistent with fiduciary duty**

Ultimately, the ability of investments to deliver return to investors depends on their long-term ability to generate positive earnings. Companies that operate in a responsible and sustainable manner are better placed to continue operation well into the future. Companies that take excessive social or environmental risk are likely to exhibit volatile



## **Investment Beliefs, October 2011**

performance when those risks eventuate. The Fund believes that, all other things being equal, a company that is operating in a sustainable and responsible manner will be better positioned to deliver long term return on investment. The Fund believes this to be true, regardless of the moral imperative from the Fund's members to invest in accordance with biblical values.

### ***British Columbia Teachers' Pension Plan<sup>5</sup>***

4.8 The Board believes that the best performing and most profitable companies in the Canadian and world economies maintain high ethical standards, comply with environmental regulations, have a track record of progressive labour relations, do not have business dealings with countries where human rights are violated, and do not have the production of armaments as their primary activity.

### ***Fonds de Reserve Pour les Retraites***

3.4 For a public investor with a long term perspective such as the FRR, it is essential to take into account environmental, social and good governance criteria in its investment policies in order to fully understand the risks and opportunities associated with the corporations in which the FRR is or may be invested. These criteria may in fact have a significant effect on their valuations. Analyzing the social environmental sustainability and of these corporations' strategies, their overall positive or negative consequences and the risks that they can entail for the reputation of the FRR are also necessary. Observations made about the effect of environmental problems on the investment policies of the FRR, and particularly on its long-term benefits, will be followed up on.

### ***New Zealand Superannuation Fund<sup>6</sup>***

#### **Our Beliefs About Investment**

Our long investment horizon and limited need for liquidity put us in an excellent position to make and benefit from investment decisions not available to many, while having an ability to deal with harsher market and economic conditions without having to revert to forced sales. Our sovereign status confers some benefits in terms of lower tax payable to foreign jurisdictions.

The combination of these factors optimises our chances of long-term investment success.

Our investment beliefs complement and underpin our endowments and are set out below.

Our beliefs are important because, together with the statutory duties set out in our mandate, they fundamentally drive the investment decisions that we make. Other investors will have different externally and internally sourced parameters and this will inform their investment choices.

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<sup>5</sup>[http://www.pensionsbc.ca/portal/page/portal/pencorcontent/tpppage/publications/teachers\\_investment/tpp\\_sipp.pdf](http://www.pensionsbc.ca/portal/page/portal/pencorcontent/tpppage/publications/teachers_investment/tpp_sipp.pdf)

<sup>6</sup> <http://www.nzsuperfund.co.nz/index.asp?pageID=2145879228>

## Investment Beliefs, October 2011

<b>Investment Decision</b>	<b>Investment Beliefs</b>	<b>Investment Facts</b>
<b>Governance and investment objectives</b>	Clear governance and decision-making structures that promote decisiveness, efficiency and accountability are effective and add value to the Fund.	It is important to be clear about investment objectives for the Fund, risk tolerance, and the timeframe over which results are measured
<b>Manager and investment selection</b>	<p>True skill in generating excess returns versus a manager's benchmark (i.e. pure alpha) is very rare. This makes it hard to identify and capture consistently. Some markets or strategies have characteristics that are conducive to a manager's ability to generate excess return. These characteristics tend to evolve slowly over time, although the shorter-term opportunity set that may be available in any market/strategy can vary through the cycle. We believe most excess return is driven by a combination of the research signals the manager is using, the conduciveness of their market to generating excess returns, beta factors and luck. <b>Responsible asset owners who exercise best-practice portfolio management should have concern for environmental, social, and governance (ESG) issues of companies</b></p> <p><b>Improving ESG factors can improve the long-term financial performance of a company</b></p>	<p>The more efficient a market is, the more difficult it is for a manager to generate excess return. Research signals and methods used by managers tend to commoditise over time through market forces. In some cases synthetic exposure to a market or factor can provide a guaranteed excess return to the Fund, and this represents an additional hurdle that an active manager must surpass.</p>

### ***Ontario Municipal Employees Retirement System (OMERS)<sup>7</sup>***

#### **15. Socially Responsible Investing**

The OAC believes that well-managed companies are those that demonstrate high ethical and environmental standards and respect for their employees, human rights, and the communities in which they do business, and that these actions contribute to long-term financial performance.

<sup>7</sup> <http://www.omers.com/pdf/SIPandP.pdf>

## **Investment Beliefs, October 2011**

Corporations should account for their behaviour and its implications for the creation of value. The OAC supports the view that companies should maintain policies and procedures with respect to environmental, social and governance issues that materially affect long-term shareholder value.

The OAC encourages the adoption of high standards of behaviour as a means to maximize long-term shareholder value. As part of its due diligence in researching investments and monitoring performance, the OAC incorporates environmental, social and governance factors into its decision-making processes.

The OAC participates in various investment initiatives through its Investment Entities that provide broader benefits to our economy while generating the returns necessary to meet the obligations to the Primary Plan members. When bidding for or making investments in physical assets in Canada, full consideration will be given to the consequences in respect to the outsourcing or delivery of core government services related to those assets.

### ***U.K. Environment Agency Active Pension Fund<sup>8</sup>***

#### **Investment strategy**

Our investment strategy will seek to take account of the relationship between good environmental management and long-term sustainable business profitability. We will seek to overlay this environmental strategy across our investment portfolio. We recognise that when the strategy is applied to investments in equities, bonds, gilts, property and private equity, this will involve considering different approaches, constraints, risks, opportunities and potential benefits. Our main influence will be through our strategic asset allocation, manager structure, manager election, performance benchmarks, monitoring, and reporting – and not by getting involved in the day-today investment decisions, which is the role of our asset managers. We will encourage our fund managers to use research on various environmental risk and/or “green” performance rating/ranking tools to identify and avoid financial risks attributable to environmental issues, such as climate change, that could impact negatively on investment returns. We will, through monitoring their performance, ask our fund managers to explain and justify financially any investment decisions, for example on stock selection, which in our view are environmentally controversial. We will favour investing on a positive “best in class” selection basis, and encourage the use of engagement rather than negative screening.

### ***Universities Superannuation Scheme<sup>9</sup>***

#### **Responsible investment**

6.1 As an institutional investor that takes its fiduciary obligations to its members seriously, the trustee company aims to be an active and responsible long-term

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<sup>8</sup> [http://www.environment-agency.gov.uk/static/documents/Active\\_pension\\_fund\\_statement\\_of\\_investment\\_principles.pdf](http://www.environment-agency.gov.uk/static/documents/Active_pension_fund_statement_of_investment_principles.pdf)

<sup>9</sup> <http://www.uss.co.uk/UssInvestments/Responsibleinvestment/RIObjectivesStrategy/Pages/default.aspx>

## **Investment Beliefs, October 2011**

investor in the assets and markets in which it invests. By encouraging responsible corporate behaviour, the trustee company expects to protect and enhance the value of the fund's investments in the long-term.

6.2 The trustee company therefore requires its fund managers to pay appropriate regard to relevant extra-financial factors including corporate governance, social, ethical and environmental considerations in the selection, retention and realisation of all fund investments. The trustee company expects this to be done in a manner which is consistent with the trustee company's investment objectives and legal duties.

6.3 Specifically, the trustee company has instructed its internal fund managers and called on its external managers to use influence as major institutional investors to promote good practice by investee companies and by markets to which the fund is particularly exposed.

6.4 The trustee company also expects the scheme's fund managers, both internal and external, to undertake appropriate monitoring of the policies and practices on material corporate governance and social, ethical and environmental issues of current and potential investee companies so that these extra-financial factors can, where material, be taken into account when making investment decisions.

6.5 The aim of such monitoring should be to identify problems at an early stage, and enable engagement with management to seek appropriate resolution of such problems. The trustee company uses voting rights as part of its engagement work to ensure that voting is undertaken in a prioritised, value-adding and informed manner. Where collaboration is likely to be the most effective mechanism for encouraging company management to address these issues appropriately, the trustee company expects its fund managers to participate in joint action with other institutional investors as permitted by relevant legal and regulatory codes.

6.6 The investment committee monitors this engagement on an on-going basis with the aim of maximising its impact and effectiveness. The trustee company's governance, social, ethical and environmental policies are also reviewed regularly by the board and updated as appropriate to ensure that they are in line with good practice.

## **Asset Managers**

### ***Aviva<sup>10</sup>***

We place great store on both the role and importance of effective corporate governance and sustainable business practices in safeguarding the capital we commit to a business and in the promotion of good practice in these areas. To that end we retain two of the UK's leading corporate governance and SRI investment teams, who work with and support all our fund managers, monitoring company practice in these areas and

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<sup>10</sup>[http://www.avivainvestors.com/internet/groups/internet/documents/salessupportmaterial/pdf\\_024453.pdf](http://www.avivainvestors.com/internet/groups/internet/documents/salessupportmaterial/pdf_024453.pdf)

## **Investment Beliefs, October 2011**

extending our scope and ability to engage with companies.

### ***F&C Investments<sup>11</sup>***

F&C strongly believes that the prudent management of environmental, social and governance (ESG) issues is fundamental to creating value for investors. Companies that are successful in avoiding ESG risks, and also at identifying and capitalising on the opportunities, will outperform over the longer term.

### ***Generation Investment Management<sup>12</sup>***

Generation's investment philosophy integrates sustainability research into a rigorous traditional investment process in order to deliver superior long-term results.

#### **Investing for the Long-Term**

Numerous studies show that most of a company's value is determined by its long-run performance, and in our view a short-term orientation has significant negative repercussions for businesses and the global economy. If businesses are forgoing value-creating investments to manage short-term earnings, this will damage their long-term prospects. A short-term perspective hinders innovation and research and development, diminishes investment in human capital, encourages financial gymnastics and discourages leadership. We believe outperformance requires a long-term outlook.

#### **Sustainability as Material to Business and Markets**

Central to our investment philosophy is the explicit recognition that sustainability factors directly affect long-term business profitability. The interests of shareholders, over time, will be best served by companies that maximize their financial performance by strategically managing their economic, social and environmental performance.

#### **A Systemic View of Global Challenges**

When considering sustainability, Generation focuses on the entire spectrum of interrelated factors. This means judging solutions on a life-cycle basis and considering the complete set of inputs, costs and externalities. Sustainability challenges are increasingly interconnected: the climate crisis and poverty, pandemics and demographics, water scarcity and migration/urbanization. We never consider sustainability challenges in isolation.

#### **Sustainable Development as Economically Transformative**

Today, the global context for business is clearly changing—capital markets and capitalism are at a critical juncture. We are convinced that the transition from a high-carbon to low-carbon economy will be the most significant process in modern economic history—matching the Industrial Revolution in scale, and the technological revolution in pace. We believe investors are increasingly aware of the materiality of this transition for business, and we think financial markets have a significant opportunity to chart the way forward. In fact, we believe sustainable solutions will be the primary driver of industrial and economic development for the coming decades.

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<sup>11</sup> <http://www.fandc.com/new/Institutional/Default.aspx?ID=80513>

<sup>12</sup> <http://www.generationim.com/strategy/philosophy.html>

***Portfolio 21<sup>13</sup>***

The business and investment case for environmental sustainability has become increasingly clear and the corporations that are embracing it are strategically positioned to prosper in the 21st Century.

The investment strategy behind Portfolio 21 is an understanding that adaptation to changing global environmental investment risks is inevitable. The earlier this thinking is integrated into business practices, the more natural capital we'll be able to retain for future generations, and the greater the economic stability we will be able to achieve.

We believe companies that prove this understanding by innovating with environmental sustainability strategies have a real competitive advantage today and are poised for further leadership and innovation in the future.

***Trillium Asset Management<sup>14</sup>***

We believe companies with strong environmental, social, and governance (ESG) profiles are better managed for the long term, have lower risk profiles, and are positioned to outperform their peers. We engage directly, through shareholder engagement and advocacy, and indirectly, through allocating capital to companies and sectors with positive economic, ecological, and social impact.

***Walden Asset Management<sup>15</sup>***

The primary tools of the social investor are sustainability research and portfolio screening, corporate dialogue, conscientious proxy voting, sponsorship of shareholder resolutions and public policy advocacy. Grounded in our commitment to meet clients' investment objectives and our shared vision for a healthy and just society, Walden works to strengthen corporate responsibility and accountability by being active in each of these strategies.

Through dialogue with company decision-makers and sponsorship of shareholder resolutions, we build awareness among corporate directors and managers that investors are about more than just financial returns.

**Foundations**

***Hazen Foundation<sup>16</sup>***

We wish to avoid investing in companies whose internal policies, conduct, and services and products are harmful to the communities and young people we support the society as a whole. We seek to invest in companies whose conduct, products and services have a

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<sup>13</sup> [http://www.portfolio21.com/why\\_p21\\_valu.php](http://www.portfolio21.com/why_p21_valu.php)

<sup>14</sup> <http://trilliuminvest.com/about/>

<sup>15</sup> <http://www.waldenassetmgmt.com/social/strategies.html>

<sup>16</sup> [http://www.moreformission.org/assets/files/Hazen\\_Social\\_Screening\\_Policy\\_2\\_12\\_2007\\_v3.pdf](http://www.moreformission.org/assets/files/Hazen_Social_Screening_Policy_2_12_2007_v3.pdf)

## **Investment Beliefs, October 2011**

positive impact. For these reasons the investment portfolio of the foundation will have the following screens:

**1. Diversity.** We will avoid companies that have a pattern of discrimination based on race, gender, age, sexual orientation or disability. We will seek companies that foster workplace and board diversity including: representation of women, people of color, and the disabled on boards of directors, and in top management; commitment to corporate diversity, including the establishment of programs that support a more diverse workplace; and recruitment, advancement and training programs for women, people of color and the disabled.

**2. Products and Services.** We will avoid investing in companies that:

- Have a pattern of producing harmful products;
- Are subject to significant fines, lawsuits or controversies with regards to price fixing, anti-trust violations, and consumer fraud;
- Poor community relations relating to discrimination or exploitation of the poor such as redlining and predatory lending.

We will seek companies that make positive products and/or services that improve the health and environment of our communities.

**3. Environment.** We will avoid companies that are major polluters of the air, water, and land. We will avoid companies with poor performance in the areas of:

- hazardous waste
- environmental regulatory problems
- toxic emissions

We will seek companies that are positively addressing environmental issues including reducing their negative environmental impact by eliminating or reducing the use of toxic and hazardous materials, using recycled materials, and developing innovative products that help the environment.

**4. Tobacco.** We will avoid investing in companies that derive revenues from the manufacture of tobacco and tobacco related products.

**5. Alcohol.** We will avoid investing in companies that derive revenue from the manufacture of alcoholic beverages.

**5. Workplace Policies.** We will avoid companies that have a pattern of workplace and human rights abuses including:

- Use of child or forced labor;
- Violation of minimum wage and working hour standards;
- Discrimination in hiring and promotion;
- Violating principles of freedom of association and collective bargaining;
- Employee harassment and abuse;
- Poor workplace safety and health.

For companies that use overseas suppliers and vendors, they should have codes of conduct in place and ensure the implementation of them. Companies will be favored that have inclusive diversity policies; comprehensive employee benefits, training and development opportunities; a positive workplace health and safety record and that pay a livable wage.

## **Investment Beliefs, October 2011**

**7. Firearms and Weapons.** We will avoid investing in companies that manufacture firearms and/or derive significant revenue from the sales of firearms. We will avoid companies that derive revenues from the manufacture of conventional and or/nuclear weapons.

**8. Human Rights.** We will avoid investing in companies that have serious human rights issues or support governments with significant human rights abuses. We will favor companies that have policies and take a leadership role in protecting and ensuring human rights and worker rights. We will take a favorable view of companies that implement codes of conducts and actively address human rights abuses.

**9. Corporate Governance.** We will avoid companies with poor governance structures or that have a record of illegal or questionable activities and whose corporate governance practices compromise stakeholder interests. These practices include:

- Lack of oversight of the preparation of the entity's financial statements;
- Poor internal controls and the independence of the entity's auditors;
- Excess compensation arrangements for the chief executive officer and other senior executives;
- Lack of independent board members;
- Securities fraud;
- Insider loans.

### ***Needmor Fund<sup>17</sup>***

#### **XI. Mission Related and Social Goals and Restrictions**

In keeping with its mission of seeking to empower traditionally disadvantaged populations, the Needmor Fund believes it has a responsibility to use its resources to promote health and human dignity and to give special attention to the needs of the poor. Therefore, the Needmor Fund will include in its investment decisions a consideration of the social impact of corporate behavior. In deciding where to invest its resources, the Needmor Fund will seek to promote social justice and world peace. We encourage transparency and accountability of corporations and encourage disclosure to affected stakeholders. We support corporate cooperation with efforts to require higher standards of public disclosure and to cooperate with independent monitoring and social auditing.

##### **A. Human Rights**

The Needmor Fund wishes to avoid companies implementing regressive practices, or which support the maintenance of particularly oppressive governments like Burma, Indonesia, Nigeria and China. In general, fund managers will avoid investments in emerging markets. Exceptions may be discussed and approved by the Finance Committee.

##### **B. Weapons Production**

To express its opposition to the arms race and its belief that a substantial amount of public funds should be shifted from military expenditures to social services, the Needmor Fund will not invest in companies which are major defense contractors or have any involvement in the production of nuclear weapons systems or agents of chemical or biological warfare. Major defense contractors are defined as those that have defense

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<sup>17</sup> <http://www.needmorfund.org/InvPol.pdf>



## **Investment Beliefs, October 2011**

contracts making up at least 5% of their total sales or are among the U.S. government's top 100 defense contractors. Nonweapons support contracts (such as food and clothing sales to the Department of Defense) will not be counted as defense contracts.

### **C. Energy**

The Needmor Fund believes that energy should be produced in a safe, clean and efficient manner and that energy conservation should be encouraged. In a growing world with shrinking natural resources, well-conceived energy policies and practices are increasingly important for the economic health and safety of local communities. Until nuclear energy can be produced safely and cost effectively with adequate provisions for long-term waste disposal and plant decommissioning, the Fund regards nuclear power generation as a substantial social and financial risk. Therefore, The Fund will avoid investment in all firms involved in the production and sale of nuclear energy. (This does not include firms whose products, while utilized in nuclear power plants, are not designed specifically for nuclear power reactors.)

The Fund is interested in supporting alternative energy development, the potentially safe use of nuclear energy, and energy conservation.

### **D. Product Quality**

The products and marketing practices of U.S. corporations exert an immense influence on the quality of our lives. In support of its goal of building healthier communities, the Needmor Fund will not invest in companies that derive more than 5% of their sales from the tobacco, gambling, or pornography industries. The Fund will also avoid investment in those companies that have knowingly sold harmful products, fixed prices, billed fraudulently or engaged in other questionable business practices. The Fund prefers to invest in companies whose products are reasonably priced, of high quality, and are socially useful. We are particularly concerned about predatory pricing in the health care industry.

### **E. Environment**

The Needmor Fund wishes to support efforts to produce a cleaner environment. Given that corporations play a substantial role in environmental issues, the Fund wishes to encourage improvements in this area by investing in those firms whose environmental records are average or better for their industry, and avoid investment in those firms that have below average environmental records. We like to invest in companies with Board and management commitment to environmental issues, including an environmental policy statement, incentive packages that reflect positive and negative environmental performance, and demonstrated support for strong public environmental policies.

### **F. Employee Relations**

The Needmor Fund believes that a key factor in the long-term health of a community is the presence of fair employment and promotion opportunities. As a result, it wishes to invest in those firms with strong employee relations practices and to avoid those with below-average practices. The Fund believes in workers' rights to organize labor unions, therefore the Fund will not invest in companies that are on the AFL-CIO boycott list. We encourage investments in companies that practice neutrality in elections where its employees are voting on union representation. A diverse array of concerns enter into the make-up of a company's overall relationship with its workforce. We encourage companies that we invest in to pay fair wages (as measured by the communities in which they operate), support human and worker rights, and protect the environment wherever

## **Investment Beliefs, October 2011**

they operate. We seek companies with a record of maintaining a healthy and safe workplace, a record of regulatory compliance and an on-going audit process that goes beyond regulatory requirements. We expect corporations to have and enforce codes of conduct for suppliers and to work to eliminate sweatshop or equivalent conditions, child labor and other exploitative practices. The Fund believes that characteristics of positive relations include a proportional representation of women and minorities in positions of influence, innovative benefits such as childcare; meaningful profit sharing; and competitive compensation. The Fund is also concerned about excessive executive compensation and endorses proposals to link executive compensation to financial, social, and environmental performance. There should be nondiscrimination in employment and advancement on the basis of race, ethnicity, gender, sexual orientation and disability.

### **G. Community Relations**

Needmor believes in organizations being accountable to those affected by their actions. Therefore we prefer to invest in companies that are accountable to all stakeholders, including employees, consumers and the communities in which they are located. This is exhibited by responsiveness to the various stakeholders and a willingness to report on practices. Needmor is concerned about predatory lending practices in poor communities.

### **Other**

#### ***Norges Bank and the Government Pension Fund<sup>18</sup>***

Section 1. Norges Bank's work on responsible management

(2) The Bank shall integrate considerations of good corporate governance and environmental and social issues in its investment activities, in line with internationally-recognised principles for responsible investment. Integration of these considerations shall occur in respect of the Fund's investment strategy and role as financial manager. In executing its management assignment, the Bank shall give priority to the Fund's long-term horizon for investments and that these are broadly placed within the markets included in the investment universe.

(3) The Bank shall develop internal guidelines that indicate how the considerations expressed in paragraph two are integrated into the investment activities of the various asset classes, for both the internally and the externally managed parts of the portfolio. In its management of the real estate portfolio, with regard to environmental protection the Bank shall give priority to considerations of energy efficiency, water consumption and waste management.

### ***RENGO<sup>19</sup>***

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<sup>18</sup> <http://www.regjeringen.no/en/dep/fin/Selected-topics/the-government-pension-fund/responsible-investments/Guidelines-for-Norges-Banks-work-on-responsible-management-and-active-ownership-of-the-Government-Pension-Fund-Global-GPFG.html?id=594253>

<sup>19</sup> RENGO is the largest trade union confederation in Japan with approximately 6.8 million members as of March 2011. The following is from "A RENGO Perspective on the Corporate Legal Framework and Investment-Fund Regulations" adopted 22 January 2009 and available at <http://www.jtuc-rengo.org/specialtopics/20090122.html>.

## **Investment Beliefs, October 2011**

Investing bodies of public pensions and corporate pensions shall incorporate Environmental, Social (Labor), and Corporate Governance (ESG) issues into their investment policies, based on the United Nations Principles for Responsible Investment (PRI), in order to promote social responsibility of companies and protect workers at acquired companies.

The investing bodies of public pensions and corporate pensions shall sign the United Nations Principles for Responsible Investment (PRI), which calls for socially responsible investment on the part of institutional investors, etc. and incorporate the following items into their investment policies:

- In regard to the shareholders' right to vote and sales of stocks, consider the state of adherence to the core labor standards (freedom of association and right to collective bargaining; the elimination of forced and compulsory labor; the abolition of child labor; and the elimination of discrimination in the workplace) of the companies where investments have been made.
- Ensure that the trustees (institutions), etc. understand the concept of protecting the workers of acquired companies and not changing working conditions, etc., to the detriment of the workers there.
- In order to guarantee that problems do not arise in socially responsible investment from the viewpoint of fiduciary responsibility, enact a Pension Basic Law which regulates the management of pensions comprehensively, referring to the UK Pension Act.
- Change the composition of the committee which sets the organization and investment policy for investing bodies of public pensions, etc. to a structure where the views of the insured can be directly represented.
- Concerning corporate pension funds, ensure that trustees representing workers understand investment issues. RENGO will issue "pension funds SRI guidelines" (tentative name) to workers' trustee of corporate pension boards

## Appendix C: Principles for Responsible Investment<sup>20</sup>

Appendix C includes the six principles that the Principles for Responsible Investment has developed and which over 200 institutional investors and asset managers around the world have endorsed. Endorsers of the PRI have not necessarily included these principles in a formal Investment Beliefs Statement. However, their endorsement of the PRI principles implies that they are committed to incorporating ESG policies and considerations into their investment practices on some basic level.

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The Principles for Responsible Investment were developed by an international group of institutional investors reflecting the increasing relevance of environmental, social and corporate governance issues to investment practices. The process was convened by the United Nations Secretary-General.

In signing the Principles, we as investors publicly commit to adopt and implement them, where consistent with our fiduciary responsibilities. We also commit to evaluate the effectiveness and improve the content of the Principles over time. We believe this will improve our ability to meet commitments to beneficiaries as well as better align our investment activities with the broader interests of society.

We encourage other investors to adopt the Principles.

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

### **1 We will incorporate ESG issues into investment analysis and decision-making processes.**

Possible actions:

- Address ESG issues in investment policy statements
- Support development of ESG-related tools, metrics, and analyses
- Assess the capabilities of internal investment managers to incorporate ESG issues
- Assess the capabilities of external investment managers to incorporate ESG issues
- Ask investment service providers (such as financial analysts, consultants, brokers, research firms, or rating companies) to integrate ESG factors into evolving research and analysis
- Encourage academic and other research on this theme
- Advocate ESG training for investment professionals

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<sup>20</sup> <http://www.unpri.org/principles/>

## **Investment Beliefs, October 2011**

### **2 We will be active owners and incorporate ESG issues into our ownership policies and practices.**

Possible actions:

- Develop and disclose an active ownership policy consistent with the Principles
- Exercise voting rights or monitor compliance with voting policy (if outsourced)
- Develop an engagement capability (either directly or through outsourcing)
- Participate in the development of policy, regulation, and standard setting (such as promoting and protecting shareholder rights)
- File shareholder resolutions consistent with long-term ESG considerations
- Engage with companies on ESG issues
- Participate in collaborative engagement initiatives
- Ask investment managers to undertake and report on ESG-related engagement

### **3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.**

Possible actions:

- Ask for standardised reporting on ESG issues (using tools such as the Global Reporting Initiative)
- Ask for ESG issues to be integrated within annual financial reports
- Ask for information from companies regarding adoption of/adherence to relevant norms, standards, codes of conduct or international initiatives (such as the UN Global Compact)
- Support shareholder initiatives and resolutions promoting ESG disclosure

### **4 We will promote acceptance and implementation of the Principles within the investment industry.**

Possible actions:

- Include Principles-related requirements in requests for proposals (RFPs)
- Align investment mandates, monitoring procedures, performance indicators and incentive structures accordingly (for example, ensure investment management processes reflect long-term time horizons when appropriate)
- Communicate ESG expectations to investment service providers
- Revisit relationships with service providers that fail to meet ESG expectations
- Support the development of tools for benchmarking ESG integration
- Support regulatory or policy developments that enable implementation of the Principles

### **5 We will work together to enhance our effectiveness in implementing the Principles.**

Possible actions:

- Support/participate in networks and information platforms to share tools, pool resources, and make use of investor reporting as a source of learning

## **Investment Beliefs, October 2011**

- Collectively address relevant emerging issues
- Develop or support appropriate collaborative initiatives

### **6 We will each report on our activities and progress towards implementing the Principles.**

Possible actions:

- Disclose how ESG issues are integrated within investment practices
- Disclose active ownership activities (voting, engagement, and/or policy dialogue)
- Disclose what is required from service providers in relation to the Principles
- Communicate with beneficiaries about ESG issues and the Principles
- Report on progress and/or achievements relating to the Principles using a 'Comply or Explain' approach
- Seek to determine the impact of the Principles
- Make use of reporting to raise awareness among a broader group of stakeholders