



VALUES-ALIGNED INVESTING 101: THE QUESTIONS WE HEAR MOST OFTEN FROM FAMILIES

WE HEAR A LOT ABOUT ESG AND IMPACT INVESTING – WHAT IS THE DIFFERENCE BETWEEN THE TWO?

There are many terms that are being used interchangeably to describe this type of investing: SRI, ESG, impact investing and others. Each term has a different meaning with different implications and can achieve different results for an investor. We learned that calling it “values-aligned investing” made sense for the families with whom we work as it achieved what they ultimately were trying to do: align their portfolios with their values.

Investing in managers or companies that align with investor values isn't anything new; what is new is the attention it has received from the industry and investors in recent years. Originally, this type of investing was referred to as socially responsible investing (SRI) and it was primarily about excluding certain investments from a portfolio (ex: weapons, tobacco, etc.). Over time, investor interest shifted to be more intentional and proactive, and ESG investing (Environmental, Social, and Governance) was born. ESG investing goes a step further than SRI and allocates investment dollars to companies whose business and policies are positively affecting the environment and society, and companies that have good governance practices (fair treatment of employees, concern for the communities in which they operate, the environment and consumers).

Impact Investing as we know it emerged around 2007, initially directed toward private market investments that were generally focused on solving specific problems in the environment and society with measurable outcomes.

The challenge with using all these terms interchangeably is that investors are left trying to assess which make sense for them and their investment portfolios.

The good news is that the industry is paying attention to what investors are demanding and is now bringing to market investment solutions that give investors the power to choose the type of values-aligned solution that works best for them. We believe that a combination of SRI, ESG, and impact investing solutions are needed to build an optimal values-aligned portfolio.

WITH SO MANY GLOBAL CHALLENGES, HOW DO WE PICK A CAUSE TO INVEST IN?

For an investor passionate about bringing positive change, it can be difficult to choose one specific cause. A good way to start is through a discovery process about your family's values. This process can help a family identify the values that most inspire and bring them together with purpose as a family. Families can also use the Sustainable Development Goals (a 2015 initiative by the United Nations) to decide which goals resonate with their own values, for example, poverty, hunger, health and wellbeing, education, gender equality, economic growth, climate change, clean and affordable energy, etc.

The second part to identifying the values that are important to a family is to decide which of these values can be “translated into investment themes.” In general, the themes we think about include:

1. Place – directing capital to a certain geographic area (e.g. the U.S., a local economy, or an international developing nation)
2. Groups – directing capital to support diversity or marginalized populations; this can include investments based on gender, minorities, or small or medium businesses (vs. larger institutions)
3. Environment – directing capital to focus on renewables, pollution, energy efficiencies, water and the like
4. Society – allocating capital to address hunger, poverty, health and wellbeing; economic development; education; affordable housing; financial inclusion

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5. Governance – families can choose to invest in companies that are better governed; this could be defined as having a diverse board and work force, fair pay, better work force treatment within the company and supply chain, transparent reporting methods, sustainable sourcing and product integrity

These priorities and focus areas can be included into the family's investment policy statement and reviewed periodically, just as one would review financial objectives.

DO WE HAVE TO GIVE UP RETURNS TO INVEST ALONGSIDE OUR VALUES?

This is perhaps the most frequently asked question from families and historically the biggest hurdle to allocating funds to ESG or impact investments. Numerous studies now exist that show investors do not sacrifice returns when investing in socially responsible, ESG, and/or impact investments.

In fact, some traditional managers are starting to incorporate ESG factors as part of their investment process as it can help uncover and manage risks not exposed by financial analysis as well as point out better run companies overall.

HOW DOES IMPACT FIT INTO MY OVERALL PORTFOLIO? DOES MY WHOLE PORTFOLIO HAVE TO BE IMPACT?

The market has evolved sufficiently that we are now able to source SRI, ESG, or impact investments for almost every asset class, so it is possible to have your entire portfolio aligned with your values. Some families, however, have identified very specific areas in which they would like to make an impact, and in those instances, a thematic investment approach is used.

Some examples of values-aligned investing solutions in various asset classes include:

- Fixed Income: Micro-finance and taxable and tax-exempt bond managers that analyze credits for financial and ESG characteristics and that invest in scenarios such as health care, education, and renewable infrastructure

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- Equity: Top-rated stock managers (either index or active investing) that have the highest rating in ESG characteristics and returns. Also, equities that are focused on certain themes such as water, environmental services, or gender equality
 - Real Assets: Renewable energy, affordable housing or sustainable agriculture
 - Private Markets: Private equity and venture capital funds that are focused on clean technology, education, sustainable food, healthcare and education

HOW CAN WE TELL IF AN INVESTMENT IS A SOUND IDEA?

It is important to remember that these are investments, and as such, must undergo the same level of due diligence and financial analysis as any investment you would consider adding to your portfolio. To determine whether an investment is a sound idea from a values-aligned perspective, it is important to understand the intentionality of the manager - how they incorporate ESG metrics into their investment process and how they report on these metrics. Extensive research and due diligence (both qualitative and quantitative) are needed in order to ensure each investment decision aligns not only with your values, but also with your overall investment goals.

To learn how you can begin aligning your investment portfolio with your values, please call or email WE Family Offices at any time.

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