GEORGE LATHAM, WHEB, MONDAY 30 OCTOBER 2017

Impact investing and intentionality: a holistic response

What is the purpose of finance? What should our investments achieve? These are questions that we would do well to hold on to as we consider how to develop approaches to responsible investing. It may sound obvious, but I worry that much of the responsible investment industry has forgotten this basic challenge as different strategies have developed over the past 30 or 40 years. Asset owners have asked a series of narrow questions and fund managers have responded in kind, answering specific questions, without any real thought to the underlying nature of the challenge. We are now at a crossroads, where the growing interest in Impact Investing is a real opportunity for the industry to form a more holistic and complete response. But we can only really seize this chance if we first understand where and how previous answers have fallen short.

A wide variety of methods characterise the industry collectively known as responsible investing. The first approach involved screening companies out on ethical grounds. From here we have seen the evolution of Corporate Social Responsibility, Socially Responsible Investing, Environmental, Social and Governance analysis, of Stewardship and Engagement. Typically, these strategies are used independently of each other and are not joined up. For example, many best-in-class ESG strategies reject the notion of ethical screens to focus on corporate behaviour as a means of differentiating good and bad, instead of the impact of a company's product. Most of these strategies have been developed in response to clients' demands.

The industry has developed a response not a solution; typically, ABC Fund Management has its flagship global equity strategy, which is the approach that it believes is the best way to invest… and then a church group or a foundation client comes along and says we want to invest in global equities but we cannot invest in armaments, tobacco, alcohol and gambling. ABCfm responds by creating an 'ethical' version of its investment strategy, which screens out these sectors. I've seen similar conversations when clients tell fund managers that they must integrate ESG analysis, become UN PRI signatories, or vote all of their shareholding. What results is a sub-optimal version of ABCfm's preferred investment strategy, or a module bolted on to the side which is extraneous to the actual process of selecting investments and building a portfolio.

More importantly, does screening out a few "sin" stocks really achieve the purpose that the church group or foundation client is asking at its core? If it is simply to protect the asset owner from reputational damage or an uncomfortable headline then perhaps, although ethical screens have to be drawn tightly in order to cover all eventualities – as the Church of England found out in the Wonga affair not so long ago. Asset owners have tried to communicate their mission by defining the **inputs** into an investment strategy, but in the process have lost focus on the output or Impact. This is consistent with the reductionist way in which the financial services industry operates, looking to make sense of a complex system by reducing it down to a few simple, measurable building blocks.

Over the past 30 years the finance industry has ballooned in scale as it has become servant unto itself, losing sight of its wider social utility. The increasing 'financialisation' of investment through benchmarking, quantitative and short-term trading strategies and other abstract approaches has made money ever more separated from its end purpose – or work – within the real economy. In the end investment should surely be about putting savers' money to work in the service of the economy in order to create outcomes that support higher standards of living and welfare throughout our society.

The notion of impact investing has the potential to reconnect investments with this purpose precisely because it switches focus away from inputs and onto the end output, or impact of the portfolio. The question we need to ask at the outset is what do we hope to achieve, what is our mission? At WHEB we have defined this through our corporate purpose – our mission is to advance sustainability and create prosperity through positive impact investments.

By starting out with a stated intentionality in such a way, the conditions are created by which sustainability, responsibility and purpose can become something more than a bolted on optional extra or, as I have heard it described, the icing on the cake. Instead it should become the foundation ingredient of the cake itself, built into an investment strategy and taking a more holistic view of the challenge sustainable investing.

Businesses which create positive social and environmental impact through their products and services are underpinned by long-term secular change and have structural growth characteristics that are superior to the rest of the economy. This framework can therefore be a powerful source of investment value.

Secondly, our analysis of 'ESG' issues is driven by our desire to understand the fundamental quality of the businesses and other investment opportunities that we are researching. We have strong conviction in the impact of ESG issues on company performance either in their own right, or as a wider proxy for the quality of a business franchise, especially over a multi-year investment horizon. Our engagement activity with companies is driven fundamentally by a desire to understand them better, and to advocate for practices that we believe will help secure the company's long-term success. The investment team scrutinises governance as a core part of our investment process and uses voting powers to push for better practices. These are tools that make us better investors in the pursuit of positive impact, rather than boxes to tick to comply with a set of criteria.

To develop a truly holistic strategy, intentionality and purpose must reach beyond the narrow confines of the investment product, and be embedded in the business which sits behind it. This we have sought to do at WHEB, for example by becoming a certified Benefit Corporation.

The intentionality of generating positive impact sits at the core of everything that we do. I believe that this has enabled us to consider our investment strategy in a more holistic context, and in so doing to create a more complete response to the challenges of mission alignment and purpose which lay behind those early requests to screen sin stocks out of portfolios.

George Latham, WHEB

George Latham is responsible for management of WHEB's Listed Equity business. As Chief Investment Officer he is responsible for overseeing the investment process and chairing the Investment and Risk Committee. He also plays an active role in business development and oversees institutional client relationships. Prior to joining WHEB, he led the award-winning SRI team at Henderson Global Investors. During his fifteen years managing UK and pan-European equity and managed funds, he has been awarded 'A' and 'AA' Citywire ratings, nominated for Investment Week's Fund Manager of the year and named in Citywire's top 100 managers in the UK. He was responsible for designing and launching Threadneedle Asset Management's sustainable and responsible investment strategy. He has a degree in Geography from Oxford University, and served as a British Army Infantry Officer. He holds UKSIP qualifications. (UK)