Socially Responsible Investing in Canada

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Buoyed by climate change and other issues, the socially responsible investment (SRI) industry in Canada has grown significantly in the last few years. New companies have entered the market launching new funds and other products and grabbing attention from the media, policymakers and financial heavyweights.

Yet-in spite of the accolades – there is a sense that the industry is not meeting its own very high expectations or the expectations of Canadians as a whole. While there has been growth, there is still a long way to go before the industry gets close to the level of potential demand.

SRI in Canada got its official start in 1986 when the Vancouver City Savings Credit Union launched The Ethical Growth Fund, the first Canadian mutual fund to screen investments according to social and environmental guidelines. The industry grew in fits and starts since then, but has recently hit a period of unprecedented media and financial industry attention.

A measure of this is the significant role played by SRI in recent reports on national environmental policy and resource industry policy. For the first time, SRI has played a major role in national debates about the environment and capital markets and the corporate social responsibility of the extractive industry.

"While SRI is yet to become a mainstream practice in the capital markets, its influence in the marketplace is growing rapidly, particularly in relation to investments in high social and/or environmental impact sectors," stated the Report of the National Roundtables on CSR and the Canadian Extractive Sector in Developing Countries. The report, the result of months of consultations between government, industry, non-government organisations (NGOs) and investor representatives, drew heavily on recommendations from the SRI Industry.

This followed on the heels of a two-year consultation by the National Roundtable on the Environment and Economy, an influential government advisory council, which called for a host of capital market reforms to encourage incorporation of environmental, social and governance factors in investment.

The growing clout of the SRI industry among policymakers has also been reflected by investment industry interest. Numerous asset managers and fund companies have launched SRI products recently, including many of the chartered banks, the pillar of Canada's financial system. In the last 12 months, the Royal Bank of Canada (RBC), Toronto-Dominion Bank and Scotiabank have launched SRI mutual funds. SRI managed accounts have also been introduced at the Bank of Montreal and the National Bank.

"The mood has changed almost 180 degrees," Michael Jantzi, president of Jantzi Research Inc, told the Canadian Responsible Investment Conference in 2007, after announcing the RBC-Jantzi Mutual Funds. "RBC has been tracking our industry for a long time. They believe now is the opportunity to come into the market."

Social Investment Organization's (SIO) own statistics, as compiled in the 2006 Canadian SRI Review, illustrate the level of growth in the last few years. The report, similar to the Social Investment Forum's Trends Report in the US, found that assets managed under SRI guidelines jumped from C$65 billion in 2004 to an astounding C$503 billion in 2006. This represents nearly 20% of the Canadian institutional and mutual fund market.

The jump was due primarily to the inclusion of assets from some of Canada's major pension funds, such as the Canada Pension Plan Investment Board, the Caisse de depot et placement du Quebec and the British Columbia Investment Management Corp, all of which adopted SRI policies in 2005 or 2006. The policies direct the funds to vote their shares according to environmental, social and governance criteria and, in some cases, to actively engage with companies on these issues.

Yet, in spite of this good news, mutual fund assets remain aggravatingly low. Total assets of SRI mutual funds and retail venture capital funds to the end of March 2008 were C$12.8 billion, less than 2% of the total mutual fund market of C$688 billion, as estimated by the Investment Funds Institute of Canada.

So while the concept of SRI is certainly attracting attention from Canadian institutional investors and fund companies, it is clear that SRI is failing to engage with the majority of Canadian investors. This is even more disappointing given that research shows that Canadians are supportive of the concept of SRI. Recent investor surveys by GlobeScan, a major opinion research company, have found:

- Nearly nine out of ten investors believe the financial community should pay more attention to social and environmental performance when valuing companies.
- More than nine out of ten investors agree that corporate CEOs and Boards should monitor the performance of their companies on corporate social responsibility.
- More than three-quarters of investors are interested in learning more about the social performance of companies in their portfolios.
- More than three-quarters of investors believe that corporate social responsibility reporting is an important factor when making an investment decision.

So with the majority of Canadians reporting interest in the social and environmental performance of the investments in their portfolios, there is obviously a huge gulf between what Canadians want from their investments and the assets pledged in SRI accounts.

Plugging the Gap

In response to this gap between actual and potential demand, SIO Board and staff have prepared a Three Year Growth Plan for the SIO, focusing on new strategic initiatives to use the modest staff and budget resources of the trade association to help the industry to develop. We believe the plan represents the best thinking of the industry's leaders in determining what can be done to address the barriers to growth. The Growth Plan also recognises that recent industry expansion has given SIO more tools to work with. The SIO hopes to use these tools to help plug the gap between potential demand for SRI and actual assets.

The first strategic initiative involves the advisor community. Research shows most advisors fail to inquire into their clients' social and environmental concerns, the first step needed to build an SRI portfolio. According to the GlobeScan research, 66% of investors have not considered or had a discussion with their financial advisor about the corporate social responsibility performance of companies in their portfolios. A further 11% have considered the issue, but not brought it up with their advisors.

Thirteen percent have brought the issue up with their advisors, and 1% said both they and their advisors have brought it up. Only 8% of advisors have brought it up with their clients.

The SIO Growth Plan targets the advisor community as one of the barriers to growth. SIO is planning to develop an advisor course on SRI for use with Advocis, the Canadian association of financial advisors, delivering the course to thousands of advisors across the country in the next three years. SIO is also working with regulators to mandate advisors to ask about social and environmental issues, and to include this information in their "know your client" reports and investment suitability assessments. In this way, SIO hopes to develop higher levels of education and awareness, and overcome the barriers that advisors have in asking clients about their social and environmental concerns.

The second strategic initiative that SIO plans to work on in the next few years is in the area of foundations and endowments. Foundation trustees in Canada are becoming increasingly interested in SRI. Attendance at SRI workshops for foundations is growing, and the foundation umbrella organisations tell us that they are receiving more requests for information. Yet, this has not translated into significantly higher numbers of manager searches or investment policy reviews with SRI mandates. With recent growth in the philanthropic sector, foundation staff members are under increasing pressure to deliver a growing range of complex services. It's simply not realistic to ask these already-stretched staff members to take on additional duties to investigate foundation SRI options.

Yet the recent controversy in the US involving newspaper coverage of Darfur investments by the Gates Foundation has sparked increased interest in SRI as a risk management tool for foundations. Foundations appear to be increasingly sensitive to donors who could be turned off by investments in companies that have poor CSR records on issues of vital importance to the donors and their foundations.

At the SIO, we believe this represents a strategic opportunity to engage with the foundation sector. Like our plan for an advisor course, we plan to develop a course for trustees on the basics of SRI, and the steps needed to develop an SRI investment policy, and SRI capability in dealing with investment managers. And similar to our plan with Advocis, we will approach the foundation umbrella organisations to determine their interest in partnering with us on the course.

The third and final strategic initiative in which SIO plans to work is in the area of pensions. As noted earlier, some of Canada's largest pension funds have adopted SRI policies, focused on proxy voting, corporate engagement and investor collaborations. Yet none of these pensions have incorporated ESG analysis into their stock research, security selection and portfolio management. As well, the pensions with SRI policies are large in assets, but small in number. They represent some of the very largest public pensions in the country. There are fewer SRI policies at small and mid-size public pensions, and SRI policies at private corporate pensions are virtually non-existent (with the exception of some SRI defined contribution mandates).

Until just a few months ago, SIO did not actively invite pensions to become members. Our past thinking was that SIO was a trade association for companies with a commercial interest in SRI, and there wouldn't be a place for pensions without a for-profit interest in SRI. But in the consultations for the Three Year Growth Plan, it became apparent that any organisation with an interest in SRI-private or non-profit should be welcomed into the SIO. SIO has often been called a "big tent," where all organisations with an interest in SRI are welcome. Now that principle applies to pensions.

Our planned strategic initiative in this area is a Pension Sector Roundtable, made up of pensions with SRI policies that have become associate members of the organisation. The Roundtable will form a confidential forum for pensions to discuss SRI issues among themselves, and to hear from the perspectives of SIO's other members. In this way, SIO can assist in helping to increase SRI capabilities of Canadian pensions.

Along with these strategic initiatives are other on-going projects to support the SRI industry. These include SIO's national conference, which is moving to an annual from a biennial conference (which will be held in June 2009); the biennial SRI Review; participation in an academic cluster to encourage university research into SRI; fundraising for increased public policy capacity, and ongoing work on public policy, including mandated advisor inquiry and pension disclosure.

The Three Year Growth Plan is no magic bullet for the industry. The SIO's resources are not sufficient to bring about the "turning point" in the SRI industry in Canada. However, by encouraging greater industry collaboration, the Growth Plan will pool the collective resources of the industry in a strategic approach to some of the industry's most vexing issues.

Social Investment Organization is Canada's national association for socially responsible investment. For more information, please visit http://www.socialinvestment.ca.

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