



PRATO CAPITAL



Prato Capital Newsletter |

**OCTOBER** 2019

## **DOING WELL BY DOING RIGHT FOR OUR PLANET**

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Many investors want the world to be a better place, but do they have to sacrifice their values for financial security?



Several of our clients have asked how they can integrate their social and environmental concerns into their investment portfolios and financial plans. Many have stated that they would like their investments to align more closely with their values.

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## Sustainable Investing

*Sustainable Investing* is the process of incorporating Environmental, Social and Governance (ESG) issues into ones investments. Individuals who invest sustainably choose to invest in companies, organizations and funds with the purpose of generating social and environmental impact that align with their values. Impacts are spread across various sectors, from renewable energy and climate change, to health and safety issues; as well as responsible corporate governance and community development. **Exhibit 1** below shows some examples of issues raised with the ESG concerns.

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**Exhibit 1:**  
Some examples of Environmental, Social and Governance Issues

ENVIRONMENTAL	SOCIAL	GOVERNANCE
<ul style="list-style-type: none"> <li>• waste and pollution</li> <li>• resource depletion</li> <li>• greenhouse gas emission</li> <li>• deforestation</li> <li>• climate change</li> </ul>	<ul style="list-style-type: none"> <li>• employee relations &amp; diversity</li> <li>• working conditions, including child labor and slavery</li> <li>• local communities</li> <li>• health and safety at the workplace</li> <li>• conflict</li> </ul>	<ul style="list-style-type: none"> <li>• tax strategy</li> <li>• executive pay</li> <li>• donations and political lobbying</li> <li>• corruption and bribery</li> <li>• board diversity and structure</li> </ul>

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Until recently, this type of investing usually meant a sacrifice in portfolio returns, no long-term history of returns or a combination of both. There are now several hundred *Sustainable Investing* options, with some well-established mutual funds claiming ESG criteria.

*How do we choose appropriate investments when there are so many choices?*

At **Prato Capital**, we believe the best choices for investments provide a history of returns, offer a broad-based portfolio and still are consistent with the ESG framework. It should also focus on a set of sustainability issues whose impact can be readily measured and reported. The criteria for *Sustainable Investing* should be the same as any other investment: using factors of investing that academic research has shown provide meaningful returns over the long-term. The goal is to pursue higher expected returns while upholding environmental values.

Over the past few years, JP Morgan Chase, Bank of America Merrill Lynch, MSCI, Deutsche Bank Group, Morningstar, UBS and the United Nations have all released studies showing that ESG indexes have performed either the same or better than the traditional benchmarks they are compared to. This proves that it does not need to be a sacrifice to invest with consciously.

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## What This Is and What This Is Not

There are many terms and acronyms thrown around when the subject of **ESG investing** comes up. *Sustainable Investing* (sometimes called Responsible Investing) is most often the term people mean when talking about the ESG factors. Again, this incorporates the framework of Environmental, Social, and Governance issues into investments. At **Prato Capital**, this is the group that we are discussing with clients when they ask about incorporating *their values into their investment process*. Everybody wants to do their part to make this a better world. This is one way that we can put those values to good use.

It's worth mentioning other "categories" of investing such as *Socially Responsible Investing* (SRI), *Ethical Investing* and *Impact Investing*. These terms are often grouped together when certain investors want their ethical and religious choices to be reflected in their investments. However, investing in this group presents many issues when it comes to Financial Life Plans (FLP). As just one example, *Impact Investing* is investing with the intent of actively changing corporate behavior through shareholder and proxy voting. The primary intent of Impact Investing is *not building wealth*. Rather, it is using shareholder power to force changes onto corporations and their leaders. This makes portfolios much less diversified. When it comes to *Socially Responsible Investing* and *Ethical Investing*, the challenge here is the difference of ethical and moral ideals between us all. Many of these investment choices and funds are a one size fits all approach and this makes it difficult to find and address investors concerns equally and personally.

It is for these reasons that we focus on **ESG investing**, as this area has a longer history, is truer to its core beliefs and readily integrates into our diversified planning process.

For all of us at Prato Capital, *Sustainable Investing* is not a political statement. We believe that the companies that are pure of heart and truly care about the bigger picture are better positioned to out-perform over the long-term.

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## Conclusion

At Prato Capital, investing well and incorporating values around sustainability does not need to be mutually exclusive. We believe that over the long term,

better business practices make better companies, better investments and a better world. This should be part of everyone's financial life plan.

Do you have a plan?

*"Sustainable investing strategies work together to encourage responsible business practices and to allocate capital for social and environmental benefit across the economy."*

– From the **The Forum for Sustainable and Responsible Investment (US SIF)**

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