Responsible Investing in the times of Pandemic. Hosted by Mahesh Joshi on VoiceAmerica.com. May 20, 2020

Producer

When you think about business competition, where are you focused? Your town? Your states? Across the country? You need to be concerned with competitors around the world. Welcome to Global Business with Mahesh Joshi. Today, you'll hear about the mega trends in global business and how they affect your organization, as well as explore issues, solutions, and some amazing facts about business worldwide. Now, here is your host, Mahesh Joshi.

Mahesh Joshi:

Welcome to the global business with Mahesh Joshi. I have with me Mr. Ian Robertson from Canada, to discuss about responsible investing. Responsible investing becomes all the more an important subject in the times of pandemic. Ian is my guest today and he's the portfolio manager, director and wise president of Odlum Brown, and he is a member of the firm's executive committee. Ian has been a volunteer leader in the investment industry since late 1990s.

Mahesh Joshi:

He has volunteered extensively with CFA Institute, both locally and globally, and has been a leader within Canada as board chair of the Responsible Investment Association, or RIA. He's an enthusiastic supporter and volunteer at University of British Columbia, and has been recognized several times for these and other community contributions. Ian is pursuing his PhD, part time, at the University of Oxford focusing on corporate governance and responsible investment.

Mahesh Joshi:

He has presented on various aspects of responsible investment at industry and economic conferences, including at the University of Oxford, the University of Sheffield, Imperial College London, and St. Mary's University Halifax. His first published paper was awarded best student paper at the United Nations backed PRI's 2017 academic conference. Ian is a longstanding reviewer of both fiction and nonfiction books. His reviews have been published in the Financial Analysts Journal, the Journal of Sustainable Finance and Investment, and CFA Institute's Enterprising Investor, and can also be found online on goodreads.com and on his personal website, ianrobertsoncfa.com.

Mahesh Joshi:

He has authored a book chapter, Responsible Investment Requires a Proxy Voting System Responsive to Retail Investors. And his book reviews include: Principles of Sustainable Finance; The Power of Single Number, A Political History of GDP; Investment Risk Management; Succession Planning for Financial Advisors; Building an Enduring Business; and How to Really Ruin Your Financial Life and Portfolio. Hey Ian.

Ian Robertson:

Hey Mahesh. Thanks so much for having me on Global Business on VoiceAmerica - a pleasure to be with you.

Mahesh Joshi:

Welcome, and a very interesting topic in front of us today; very, very pertinent topic also in the current times when pandemic is around us. The responsible investment or responsible investing, just on my research on some of your papers and I found it very, very interesting how ESG investing, that's what I got out of it… how it is taking such a sound footing, how companies are taking it seriously and how the funds or the value which is being invested using these vehicles are in consideration of those factors have grown to $30.7 trillion in 2018 from $22.8 trillion in 2016.

Mahesh Joshi:

That's a tremendous growth, especially when you compare with the entire S&P 500 which is what? Almost $25 trillion. But it doesn't stop there. I believe some numbers are available that the next two decades this number may increase to almost $50 trillion, which is a pretty big amount. That means this has really taken some serious roots. Ian, I would like you to start with sharing with our listeners what is it responsible investing?

Ian Robertson:

Well, Mahesh, you asked the million dollar question there and I want to tell you what responsible investment is, and how I think about it, by going back a little bit in history. And for those listeners who are older than, say, 30 or so this will resonate with them because they will have been through this evolution in terminology from what we sometimes call socially responsible investment or ethical investing to what we now call responsible investment -and socially responsible investment and responsible investment - two of the three words are the same, but they have distinct meanings.

Ian Robertson:

And I want to go back a little bit in history just to try to characterize that, so that people get a good understanding of, "Ah, I see. This is the evolution of it and this is what the different terms mean. In investments there have been organizations and individuals that have avoided particular stocks for a long time, probably for as long as we've had stock markets. And it's religious organizations that really did this in a sort of structured way with their investment portfolios. They would avoid certain stocks that didn't resonate with their values, so the things that we would call 'sin stocks'.

Ian Robertson:

And so they would have an investment portfolio, it would generate some profits; they would take those profits and do good works with them to help their members and to help the community, but they would avoid these stocks. And individuals as well have forever invested more often with things that they know, that they're comfortable with, and have avoided stocks that they didn't know or were uncomfortable with them. It's the same logic and rationale that Warren Buffet will tell you to use if you're buying individual stocks.

Ian Robertson:

He'll say, "Stick with what you know, and invest that way." And inherently we sort of bring our morals and our values to the table in the same way that religious organizations have for more than 100 years in a more structured and sort of codified way where they screen out. Today, we would call that negative screening. And in the late 60s and 70s, we had social movements protest against the companies involved in the Vietnam War. And 10 years later we had a protest, it was when I was on campus, against the apartheid regime in South Africa and protest against companies there and the beginning of a divestiture movement.

Ian Robertson:

And today we see that with oil companies, right? That's a negative screening; get these companies out of our portfolio. But it's predicated on value system, a morals based system, that these companies are not good corporate citizens. They're sending the world a message it's not acceptable where they're involved in that, or they're supporting that, and so we should get them out of our portfolios. And, it's the integration of those social movements and the investing side that really came to be the basis of this socially responsible investment or ethical investing.

Ian Robertson:

Now, a couple of nuances that have been added to that over time, so in addition to this negative screening, the screening out of companies that are having a negative impact, there is also a movement to do positive screening. And that is to screen in any companies that are helping move the world in a better direction, that are having a positive impact. And you can implement that in a number of different ways, but that's the ethical, socially responsible investment. And in the early 2000s…

Ian Robertson:

... Investment firms have always been willing to help their clients invest in ways that they want, that are meaningful to them. But what they did in the early 2000s was come together to say we need a way to kind of codify this in an analytical way so that we can have a structured approach when we analyze these companies. And that was the origin of what we know today as the PRI, the Principles for Responsible Investment, a UN backed agency that sort of brought together other asset managers - so mutual fund companies - and asset owners - so think of them largely as pension funds and endowments - to come together to define environmental and social and governance norms and to help bring in metrics, so ways to measure these issues.

Ian Robertson:

What was a morals based approach started becoming more of an analytical tool and integrating these E, S and G factors into the analysis, the valuation of a stock. It took the values, the norms side, out of it and shifted it more to an analytical approach. And that's what we think of today as responsible investment. It's integrating those ESG factors into the analysis. It doesn't mean you can't still apply a norms based screening or a tilt towards green of some sort. But from an analytical standpoint, when these financial analysts are looking at companies and valuing them, they are going to take these ESG factors into account.

Ian Robertson:

It's kind of a long history but that's the difference between this SRI, Socially Responsible Investment, and what we term today Responsible Investment, which is the integration of ESG factors.

Mahesh Joshi:

Got it. Basically if you look at it in the past, suppose you are avoiding some companies based on some of the behavioral aspects or where they were working, what field they were in, now we have a much more structured approach where there is a positive reinforcement, which is if you are good at ESG you get selected over others and you attract more funds. Instead of the shift from the past where we can say is to avoid the companies which are into not such a desirable application of their products or services, or not taking the role of a good social citizen.

Ian Robertson:

That's exactly right, Mahesh. And, again, I want to dive one level deeper just to give listeners an idea in terms of how the mechanics work. But in general, in broad terms, that's exactly right. Let's think about a stock portfolio. Let's say you have X number of dollars] and you want to put it into stocks, and the analyst at the fund company, or your advisor, is integrating these ESG factors in the analysis. Those are often factors that are not on the balance sheet. They're not on the income statement. They're kind of additional factors.

Ian Robertson:

We already take these qualitative factors into account, right? The quality of a firm's management, their strategy, where we think their product is headed strategically versus their competitors. We've always done that, but now we're also factoring in these environmental and these social, how they treat their workers; and governance how robust is their governance structure? Is there a good diversity on their board? That kind of thing. And so if we're not taking those things into account and they're material, if they're important to that company, then we're going to be missing something.

Ian Robertson:

We're going to be missing a factor that's important to valuing the company, and where we're not going to have as robust a result in analyzing the company as we might have otherwise. Companies that are more transparent with these issues, that tell us what's happening, are more likely… studies show they're more likely to have a better valuation. They're not this black box approach you wonder what's in there. Right? If they're not being transparent with these E, S&G measures. And so they're more likely to get about a better value valuation, they'll have slightly easier access to capital.

Ian Robertson:

There are lots of studies that show this kind of thing, so you're absolutely right. These sort of 'better corporate citizens' are more likely to have all other things equal and easier time attracting capital. I do want to distinguish though the primary markets from the secondary markets. And the primary markets are where they're raising that capital, where a bank is lending them new money or whether they're issuing new stock. That's where new money is going into them, where most people are involved in when they're investing is the secondary markets - they are buying and selling - it's kind of like a merry-go-round of stocks. They are trading from one place to the other. If you have a company and you want to sell it, you sell the stock that doesn't match your values but it's going to somebody else's portfolio. And so there can be - that selling if there's enough selling pressure - it does drive down the price, the value, of that stock and you see that… If you watch the business news when you'll see that Goldman Sachs or Merrill Lynch or whomever, Bank of America or whoever it is, has put out a 'sell' recommendation or downgraded a stock you can see a drop, right?

Ian Robertson:

It's because there are some people rushing to the exits and they going to sell it. In the long run those kinds of things, those dips down from 'sell' recommendations or bumps up from 'buy' recommendations, kind of even out over time. Ultimately in the long run, the stocks find their level based on their earnings stream and all the other ESG issues. But when you sell it, you may drive down the price a little bit but eventually the stock will settle into a proper level. They go too high, they go too low, but if you look at a long-term trend they should track what their earnings are.

Mahesh Joshi:

Oh, perfect. Ian, we'll take a short break and we will continue our discussion after the break.

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Mahesh Joshi:

Welcome back. You're listening to Global Business with Mahesh Joshi, and I have with me Ian. And we are talking about responsible investing in the times of pandemic. Thank you Ian, very insightful first session on what is responsible investing. And you talked about ESG and some other parameters, how the positive reinforcement is being pulled in to reward the companies who are doing good for society, environment and who are governed very well. Let's continue from what we were discussing earlier. What is ESG? And you explained very well what's its role and how it is so important?

Ian Robertson:

It's a good question because this origin that I went back to, with religious organizations and divesting from or screening out certain stocks, we bring those morals, our own individual morals, with us. It's a type of behavioral finance except instead of a subconscious one, which is what most behavioral economists or behavioral finance folks study, these subconscious actions that we can't get away from that are sometimes surprised to learn of. But our values are front and center, right? It's not really a surprise to us what those are, but it is a type of behavioral finance.

Ian Robertson:

And so when we look at companies and we ascribe some sort of moral characteristic or values based characteristic to them, this is what company has worked so hard to cultivate. Right? Their brand image, and how we feel about them. But when we get down to that analytical part, that ESG integration, that sort of basis that I described that started with that UN backed agency, the PRI, the analyst's use, they are going to look at these environmental and these social and these governance factors with a lens that, first and foremost asks, “Is this issue material to this company and to this sector?”

Ian Robertson:

To give you an example, if you look at a banking stock or a financial services company and you're thinking about carbon footprint, it's not that they don't have any carbon footprint, but in terms of the grand scheme of their operations and where the risks are and how they impact society - they should work to reduce their carbon footprint as much as possible - but from a financial standpoint, it's probably not a material factor; so, again, they should do all they can.

Ian Robertson:

But if we look at a utility, a company that's providing energy to us, the carbon footprint for that type of company ... or for an oil and gas company or an extractive company or a mining company ... the carbon footprint to those companies is really a big deal. And so if you think of, for example where I live in British Columbia, we've had a carbon tax here for something like a dozen years, and now we have one nationally as well in Canada. And so if you think about carbon footprint and you think about financial risks, we clearly want the carbon footprint of the world to go down, and if we look at the risk, the materiality to a company, it's going to be much more important to the bottom line to the earnings for an oil and gas company or to utility if, for example, carbon taxes come in. We've seen versions of carbon taxes, or CAP and Trade in a few parts of the world, and it may be that we may get more of those. When you're analyzing the company and you're trying to look out what are their earnings going to be like in five years or in 10 years, and if you're a pension fund, for example, that has a 50 or more year time horizon… Right? ... because as long as they have people that they are paying a pension to, that's how long they're going to invest for, those issues become really material. And so it is different. The materiality of environmental issues, and social issues, and governance issues is going to be slightly different for different companies and different sectors. And so, well, our morals will naturally lead us to think, or our values… I mean, there's kind of a heuristic that we use to say 'oh, yeah, oil companies that that's the source of the carbon', but we may not actually think about it in terms of utilities where we get they're the ones burning the fossil fuels to produce power. And so sometimes our morals will lead us in a good… we can't change them .... they're going to lead us in a good direction, but we want to also bring in what the analysts are saying, to say, "Is this important or not?" And this is where it gets kind of interesting, the analysts have this neoclassical economics or financial training. Right? It's a sort of mathematical output trying to get the best risk-adjusted return, and our values come from this behavioral side of things.

Ian Robertson:

But there's an economist in… I think he's at Santa Clara, maybe Santa Barbara ... anyway, California ... Meir Statman ... and what he says is we've had these epochs, these waves of theoretical underpinnings. At first, it was the neoclassical that just drove us to this optimized risk-adjusted return and to buy all the stocks and keep them at as low a price as possible. And that's where Vanguard and BlackRock and others get their theoretical roots from. And then we had the behavioral finance folks come in, and what Meir Statman and others say is that it's actually a combination.

Ian Robertson:

When you and I go to invest, we want the financial rewards. Or if we're leading an organization's investments, we want the best possible return that we can, but we also want it to resonate with our values. And they're not mutually exclusive, but they're coming from different directions. And we just have to recognize that sometimes they're going to produce results that are exactly what we want. But other times there may be a little tension between an analyst saying, "No, this is actually a really good investment," and our values saying, "Oh but… I get that and I want the best risk-adjusted return, but it really bugs me." You know?

Ian Robertson:

And if you think about if you had a portfolio of stocks and your advisor or you decide that a tobacco stock is the best, it's going to produce a really good return in there, for a lot of people it would just bothered them to know it was in there. I mean, pick your stock. It could be any - tobacco's an easy one to pick on - and so there's this combination of things that we're after. And so the ESG comes from this analytical basis and the socially responsible investment, that ethical part of the investing, comes from a different angle and when oil companies are overpriced or the risk isn't factored in them properly, or when you get a collapse in the oil prices, it looks so easy to say, "Well, look, we made ourselves feel good by not having oil companies in our portfolio," and then the price of oil goes way down and the stocks go way down and you say, "Well, it's kind of validation." But, at some point, the opposite will probably be true. Right? At some point they'll be undervalued and they'll go up better than the market and… You just want to think about the different types of investment theory that are going into this, those behavioral roots that we all come with and this analytical part that's really amoral.

Ian Robertson:

It's not immoral, it's just amoral. They're just looking at trying to figure out what the profits are going to be, and what the risk to the company is, and how it fits into our portfolio. And then we can all feel free to screen it out. We don't have to include any stocks we don't like in a portfolio, but we have to recognize we're doing that for a different reasons than what the analyst is coming at it from.

Mahesh Joshi:

Perfect. What it looks like, what you explained, although this ESG thing or all the social and moral values they started taking roots maybe two decades ago or maybe 10 years, 15 years ago when these storms came up, the ESG and all that. But now with this signing of this… United Nations backed what you were talking about, Principles of Responsible Investment. That was signed by… I was looking at to a data on it that more than 2000 money managers signed up for that. They have signed onto this United Nations backed Principles of Responsible Investment. Those guys are all seeing almost… What? $80 trillion worth of assets. If this is a kind of awareness that is already available, that means there is a big push coming in this direction. And the other point which you mentioned very well that suppose I am a naive investor, for me my return is very important because I'm putting in my hard earned money. The question would come to my mind, “Am I sacrificing a return by focusing my moral compass on ESG and doing all the good things for society, for the environment, for governance?” But it appears that this size of money managers and the asset class recognizing it should not be much of a risk on sacrificing a part of your return. What do you think about that?

Ian Robertson:

There's been a long debate, and I want to say 'yes' and then explain why.

Mahesh Joshi:

Sure.

Ian Robertson:

In theory by investing using you your moral compass, your values, either as the guide or as part of the guide to how you invest, in theory you are going to have a suboptimal risk-adjusted return. But I say that theory. But I would say in practice you'd be hard pressed to notice the difference. And in fact, what I was talking about with this economist in California, Meir Statman he's saying we had the neoclassical, then we had the behavioral, and now we have this sort of mixture of the two of them. We have to recognize that people are getting both things out of their investments. They want to be able to go to a cocktail party and say, “I have this new wind farm stock” or, “I don't have a tobacco stock.” It's important to them. It's fulfilling a need. Let me go back to this difference between in theory, 'yeah maybe', but in practice, 'no, probably not'. And in fact you may be getting more from the other side of things than you're even giving up in theory. In theory, the best risk-adjusted return… This is this neoclassical finance that goes back to Harry Markowitz in the 50s and, Fama and this Efficient Frontier / Modern Portfolio Theory.

Ian Robertson:

And so you want to hold, essentially, the basket of all of the stocks together and then you adjust your risk by that complete basket of stocks. And you just change the percentage you have in a treasury bill, for example. Right? If you want to be all growth, it's 100% that complete basket of stocks; and if you want to be all safety, then it's 100% treasury bill. And most people are somewhere in between. It's just a straight line sliding scale and most people have probably seen that straight line. If you want a higher return, you have to take more risk.

Ian Robertson:

But that is the lowest amount of risk for the optimal return, it's by buying all of the stocks in the universe. If you work backwards and you screen something out, let's say it's a tobacco stock or a coal stock… Those are two popular ones; I'm going to get the oil in a second ... but, they're really small parts of the economy. And if you screen them out and you hold the rest of the basket, you'd be hard pressed to measure what the difference is in the returns. It's there. But when you look at your statement at the end of the month, it's unlikely that there's any measurable difference in the return and the volatility, the risk in the portfolio.

Ian Robertson:

In theory, this 1950s, ‘60s, ‘70s theory, or Modern Portfolio Theory there was a difference and the math shows it. But in practice not. Plus you get the benefit of saying, “Those stocks, those sectors, those companies drive me crazy,” and you don't have to put up with them in your portfolio. There's a benefit there, but we're just sort of recognizing that you're still getting, essentially, the best risk adjusted return and you're fulfilling this other need, which is not having these stocks that drive you crazy. But I have to say, the bigger the thing that you screen out, the more likely it is to have an impact ... and so oil is actually a much bigger sector, or if you screen out countries - if you screen out Europe, let's say - that's a big thing to give up. Right? And we all know this, that all of our advisors are trying to get us to invest globally because we have this propensity to invest where we live, our home country bias as we call it. And so that's kind of a long answer to your question. Do you get the best returns? Well, if you screen out maybe in theory you're getting something up; in practice probably not.

Ian Robertson:

But it is also good to remind listeners that by integrating these ESG factors into the analysis you are doing a much more comprehensive… or the analyst is doing a much more comprehensive valuation of the company and they're more likely to come out with a better answer, a better portfolio.

Mahesh Joshi:

Perfect. Perfect. Ian, very interesting and very enlightening discussion. This is very good piece of information. We'll take a short break and we'll continue our discussions on the subject after the break.

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Mahesh Joshi:

Welcome back. You're listening to Global Business with Mahesh Joshi. We are having very intriguing discussions with Ian. He's in Canada. I'm sitting in Houston. Interestingly, technology makes us talk a lot of good, nice things you can share across any platforms Ian. Very good explanation, very good learning, on how you're using your moral compass on your investing decisions, whether it is the max return you're getting or you're getting suboptimal, or the combination of what you think you're getting is bigger than the total value of just pure return.

Mahesh Joshi:

I just want to share a few things that our listeners, some of the quotes which I've seen from some of the companies. It is definitely… There are many different ways to approach responsible investing. That's what I understood from discussion with you in the last two sessions. But that ESG, which has been widely used, is a part of responsible investing. Definitely it has taken roots over the past few years, and if the indication is the… the funds allocated there or to such companies are clearly saying that; and all those money managers becoming part of that.

Mahesh Joshi:

And I read out from what Credit Suisse says in a recent report, that ESG looks to dominate investors' agendas in the years ahead. Bank of America mentions that 70% of U.S. assets can be analyzed without using ESG. And from Goldman Sachs one of the analysts said, last year, as ESG issues become increasingly material across many industries our, which means Goldman Sachs, analyst teams have taken pen to paper to address the impact on corporates.

Mahesh Joshi:

And on similar lines, JP Morgan have also mentioned that the demand for sustainable investing has been clearly growing over the past year. It looks like there are a lot of new vehicles which are coming in to invest in this direction and also the focus is increasing. But one piece which came very strikingly obvious to me is there are certain geographies who are very deeply in growth now and they have contributed a lot. It looks like almost 93% of sustainable investing, part of that $30 trillion number which I talked about 2018, 93% came from Europe, United States and Canada.

Mahesh Joshi:

If you see the two largest continents with North America and Europe but developed economies, most of them, they are very cautious about it. And next in the sequence of investment comes Australia and New Zealand combined together and then Japan. There is a geographical hint also here where it has taken roots. And also these are the geographies, especially if you look at North America, where the intensity and the focus is quite a bit a return on investment and what kind of return you're getting.

Mahesh Joshi:

Definitely there is some balance coming up where people are keeping their modern values ahead and along with the returns, so their moral compass is also positioning them in the right direction along with the returns. And combination of two could be coming very well. In earlier session you described very well where is analytics, where is the moral or values, and how they're getting aligned. In this session, Ian, can you talk about how to have a combination of both moral values and analytics, and also how can individual investors, like me or our listeners, can also participate in it, influencing the decisions with the companies or wherever they have invested.

Ian Robertson:

It's a very good question about the influence on companies. We started off our discussion talking about 'does that divestiture or that ESG integration, the analysis, affect the cost of capital for companies?' And there is some evidence to say that it does, but we have to be thoughtful about how much it impacts them and whether the cost of capital is going to just go to a certain level regardless of whether we sell the stock. Because somebody else buys it and maybe it goes back up to a normal price or a proper valuation over time, so maybe there's a short term impact. Good question as to whether there's a longer term impact on the cost of capital.

Ian Robertson:

But taking account of ESG, as banks will do when they're lending money they may raise or lower their cost of capital. And I've spoken to the heads of capital markets at some Canadian banks and they're starting to do that when they are making loans, to for example the extractive industry, to say, "Well, we need to factor in these issues." What about the carbon tax? What about the issue of stranded assets? Is the asset valuation of the company really…? Are we going to be able to take, or are they going to be able to take, all of that oil and gas out of the ground or is some of it going to be stranded as we shift to other technologies?

Ian Robertson:

It's a very complex weaving of issues, but I think it's fair to say that it does affect the cost of capital. But there is another very direct way that investors, when you're investing your money, can have an impact on the company. And that is through proxy voting. Proxy voting, so if I can go back that 100 years or more when companies were first forming, the public companies, that was in the Victorian era that our modern conception of the limited liability companies sort of came into view. There had certainly been corporations earlier than that, but they were sort of more family business, community businesses, or the mercantilists that were tied up with trade and colonialism.

Ian Robertson:

But the modern corporation with limited liability goes back to the Victorian era. And originally they would be coffeehouse types of… you would see who the other shareholders were ... but as companies got bigger, as they got more geographically dispersed, as the shareholders started to exchange… they used to have standardized accounting ... and then shareholders start to exchange shares anonymously, right? You'd sell to somebody not at the coffeehouse, not the person you know, but somebody who maybe in another part of the country, and then you get more and more shareholders.

Ian Robertson:

This issue of how you hold management, how you hold companies to account, becomes a very important theoretical consideration. And so what we have is elected boards of directors to represent the shareholders and other stakeholders as well. And it's important how we elect those boards of directors and then you appoint the auditors and they do their job every year. And so those are proposals every year to shareholders and we vote on them; and we say, "Yes, we'll elect that director." Maybe there's somebody who we don't like, and we vote against that director, and we approve the auditors.

Ian Robertson:

Where companies are not behaving as well as they could be on environmental, or social, or governance issues, ESG issues, shareholders have a right… especially in the States, they have to meet certain standards, certain thresholds; it has to be a material issue and kind of a policy-related issue ... but they can put a proposal on that annual ballot as well. It might say, for example, "We would like you to have a policy on board diversity." Maybe it's a board that is typically… They would often in the past have been all middle-aged or older white guys, right? You'd have this…

Ian Robertson:

You'd say, “We want you to have a written board diversity policy about how you attract and assess directors and their skill sets.” But it could be an environmental issue, it could be how you treat workers, worker conditions, any number of material ESG things. And so then that shareholder proposal could go on the ballot. And those are really important issues. They tend to be filed with the larger more iconic companies, so the Dow Jones 30 would… I've looked at this number and I think at somewhere close to a half… a third to a half ... of all of the proposals filed in the States that go on the ballot are filed with these larger companies, with the idea that you get the biggest ones, the McDonalds or the Coca-Colas or the Apples or the Googles or the whomever, to implement a policy and others will eventually follow suit. They just tend to attract a larger number of proposals. But those proxy votes are actually really important ways for investors to know that their voice is being heard, because for every share you hold there's a vote going either for that proposal or against that proposal.

Ian Robertson:

Remember the director elections and the auditor elections are important. They tend to be a little less contentious. But these shareholder proposals, by definition are things that management is not doing that some group of shareholders, maybe a large group of shareholders, thinks is important to move the company in a better direction; and, usually, to have a more profitable outcome. Usually they're trying to be a win-win situation or reduce risks, right? Increase transparency.

Ian Robertson:

And so one of the things that investors should look at is if they're investing through a mutual fund or an index, an exchange traded fund, or with an advisor directly is to say, “How is my vote being cast?” Is it being cast, and if so is it being done with any thought about the issues? Or is it a default, “I'm just voting with management. We like the management. We wouldn't have invested in it if we didn't think it was doing a good job, so just vote yes, yes, yes with management.” And on the face of it there's a logic to that, but if you think about it it's assuming that management is always doing the right thing and that there's nothing they could do better.

Ian Robertson:

And so it's really important to look at that proxy voting record. And in the background… You can see how the votes are cast. In the background a lot of the larger firms and these leading ESG firms and responsible investment firms are engaging with the companies behind the scenes. That's a part we can't see but they're often in dialogue to say, “Could you disclose your carbon footprint? Could you develop and publish a board diversity policy?” You know, any number of issues. And if they're getting some traction on that and the company…

Ian Robertson:

Often these are new issues to companies, especially smaller ones, and so you may be getting very positive results without actually having to go filing a shareholder proposal and voting publicly against what management is doing. You want to know whether the investment firms are engaging with the companies and you want to know how those votes are going. And so that's a really important part. And just to circle it back to what we were talking about earlier, this analytical-based ESG integration versus the values approach where we want to screen out the companies that drive us crazy, let's take a look at an oil and gas company for example.

Ian Robertson:

If we're concerned about the climate crisis and just don't want any part of the oil companies whose products are at the root of this, then we may not want those in our portfolio. And that's sort of the heart of this divestiture movement, right? That we see on lots of campuses and for lots of larger portfolios pensions and others campaigns against that, to the best out of those stocks. But if you think about what we were just talking about, the engagement and the voting of proxies, if you own the stock you get some votes.

Ian Robertson:

You get to vote in trying to get them to change their behavior, so to lower their carbon footprint, to tie executive pay to reducing carbon emissions in their production of these products. And so it's not an easy answer to say, “How am I going to make the biggest difference?” How much does it drive me crazy to have it in my portfolio versus, yeah but my vote can count and if I invest it this way. That's the heart of the debate.

Mahesh Joshi:

Yeah, and this is a very critical point. You hit a very good point here, that how do you influence that decision? It depends on how you invested. What we're going to do is we'll take a short break and we'll continue our discussion after the break.

Producer:

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For the past two years, Global Business with Mahesh Joshi has been a top rated program on the VoiceAmerica business channel. Now, with its popularity growing, he has converted many of the concepts discussed on the show into an easy-to-read book from Oxford University Press, one of the top publishers in the world. Place your order for the book globalbusiness@mkjgb.com. Act now and as a special offer you'll receive a signed copy of the book by the author, Mahesh Joshi. Order today at mkjgb.com.

Producer:

This is global business with Mahesh Joshi. To reach the program, please call in to +1 866-472-5790. That's worldwide access to +1 866-472-5790. You may also send an email to maheshjoshi.82@gmail.com. Now back to the program.

Mahesh Joshi:

Welcome back. You are listening to Global Business with Mahesh Joshi and we are having very interesting discussions with Ian about responsible investing, especially in the times of pandemic. But we are understanding from Ian what exactly it is and how does it influence our decision making, and how our decision to having invested in that gives us certain rights. Ian you talked about certain rights you have in terms of proxy voting. Now, there could be various varieties of proxy voting depending on what have you bought, a stock or something else. Can you share with us how does it differ and how an investor can execute his right… his or her rights?

Ian Robertson:

Yeah. It's not easy, but let me outline three different ways. Way back when stock started trading on the exchange, you got mailed a physical certificate. Right?

Mahesh Joshi:

Very true.

Ian Robertson:

It was like a giant piece of money.

Mahesh Joshi:

I had to get rid of them.

Ian Robertson:

There you go. Yeah, yeah. Those of us who were old enough to remember those, but today people don't really know what they… because it's electronic, right? It's on your phone, your list of stocks. But I say that because all also four times a year they would mail you, or if it paid a dividend they would mail you a dividend check, right? They'd mail you the share certificates, you put it under your bed or you got a check in the mail four times a year you put it in the bank. And once a year they mailed you that proxy that said, "Elect our directors and approve the auditors," and you mailed it back. People really did.

Ian Robertson:

70% to 90% of investors mailed that proxy back and it worked like a charm. But the problem was more and more trades started happening and they couldn't create the share certificates fast enough. Right? If you sold your stock, you had to take your old one in and they destroyed it and they issued a new one with the new person's name on it. Today, the… The trading became electronic and really efficient and we see that, right? I mean, you watch the stocks flip over on the screen if you watched the business channel and it's amazing how much gets traded.

Ian Robertson:

The proxy system, that once a year form that used to come to you, is still a once a year form and the whole investment industry has become much more complex with the rise of mutual funds, exchange traded funds, advisors and sub-advisors. And it's a very complex web. If you own stocks directly today through a broker, a brokerage firm, you will probably still get those proxies and those annual reports in the mail. The challenge for you, as a brokerage investor, is that the issues are really complex. 40, 50 years ago you were probably okay actually just ticking the box 'yes' with management: 'Here are the directors; approve the auditors'.

Ian Robertson:

But not all shareholder proposals are worded well, or actually in your interest; they could be niche interests. I mean, generally, they're well-worded and well-meaning but you need to think about it and you may need to research the issues. And if you have a… again, 50 years ago people might've had five or 10 stocks and today you've probably got a portfolio of 20 or 30 ... and so you've got more complex issues and you've got more of them coming at you, and they all come in a season, right? Right about now actually. And so it's tough.

Ian Robertson:

And so your broker may be able to give some guidance on how to vote that, but I have to say that's not a part of the system that's built up. Mutual funds, some of them will just follow along with management. They couldn't be… They're not that interested. I was going to say couldn't be bothered but there's a resource issue here. They may not actually take the time to research and vote thoughtfully on the shareholder proposals, and they may just default to voting with management. But there are some out there that really go to task and they're going to be engaging with companies, and so if you want your vote to make a difference, you need to look for those types of companies. And on the exchange traded funds I have to say that their record on voting, this is what I research at school in my PhD, the exchange traded funds don't have a really good record of voting in favor of the shareholder proposals historically. That may be changing, but what's hard to tell is how much they're engaging with companies in the background. I don't want to take them to task unnecessarily because they could be doing some very good.

Ian Robertson:

And there was actually a recent example this year just a month or two ago, and I think it was BlackRock but I can't remember, where it appears that there was a very successful engagement outcome. And so they're so big - they're five, six trillion dollars… so big - and they have to be careful how they tread. But anyway, from that voting, to make your vote count it is most likely going to happen [a] if do it yourself, the research, and make sure your shares get voted. But that's a lot of effort. Or you're using some kind of intermediary, a fund for example, that's doing it. And if you're part of a pension plan, chances are really high that your pension plan is taking this seriously, and thoughtfully, and voting them well.

Mahesh Joshi:

It looks like ESG are the responsible investing we talk about. There are a lot of funds. There are almost more… I believe that more than 10,000 funds, that means that there are so many funds. That is not risky, first of all. Second, in the returns, so returns could be either they're the highest or a certain level. But if the company or the investment that you're making, those guys are focused on these issues, maybe the business would be more sustainable for a longer period of time. Because they're just not in terms of monetary benefit they're looking, they're looking at a holistic picture; because a business or an investment has a lot of rules to play in the society.

Mahesh Joshi:

You can see that that investment of yours that you put, if it's a kind of responsible investment those companies are; or the vehicles you have invested are taking care of the society which supports it. And what I also saw somewhere more than 60% of these funds, they're ranking in the top half of the Morningstar category and almost close to half of the large-cap blend sustainable funds were beating the

S&P 500. Well, that is for last year 2019. And if you compare that with the large-cap funds total, only 26% of them were beating it.

Mahesh Joshi:

There are some signs which are kind of evident and that it is good to invest into such vehicles or such companies or such opportunities because the return, it looks like, they are coming close to if not equal to the traditional funds. And there may not be a very huge downside risk or something. Is that safe to say that? Because if somebody is taking things holistically, basically it's working towards making the business work; or wherever you're invested, to make it work and you're not talking only one piece you're looking at everything around it. Ian, great discussing with you. We are running out of time now.

Mahesh Joshi:

And unbelievable that the time just flew by our very interesting subject, and we will talk to you about this subject at another future opportunity. But thank you for highlighting what is responsible investing, why it is becoming so popular and how individual investors can use the vehicle of proxy voting and all to influence the company that they've invested in their own reality. Or it could be a limited way, but there is a way to influence that. I'll let you give a closing comment and then we'll close the program today.

Ian Robertson:

Mahesh, thanks so much for having me on today. It's been a real pleasure spending some time with you. And if I could give people one take away, it is that you can invest in ways that make you feel comfortable with your investments. And that integrating ESG issues into the analysis part is essential. It's essential to making sure that all of the issues are taken account of; and that by analysts taking account of those issues, to the extent they're material, that they're telling companies what's important and companies pay attention to them and then it improves their behavior.

Ian Robertson:

On the one hand you, you've got your vote back to reflect back to companies through your vote, what's important, and you've got these analysts also asking the companies about environmental and social and governance factors and the companies pay attention. Taking into account the ESG factors is the core of responsible investment, but we should also feel very comfortable tilting portfolios in ways that also help us sleep at night and feel more comfortable with what we're holding, whether that's done directly through direct stocks or through mutual funds for ETFs.

Mahesh Joshi:

Very well said, Ian. Ian, thank you so much. It was a real pleasure discussing this important subject today.

Producer:

You've been listening to Global Business with Mahesh Joshi. We hope you'll tune in for another edition of the program next Wednesday at 9:00 AM Pacific Time and 12 noon Eastern Time on the VoiceAmerica Business Channel. Have a good week.