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Recent Trends and Regulatory Implications of  
Social Responsibility Investment for Pension  
Funds: Some Lessons for Turkey

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# What is SRI and Why Do We Care?

- Many definitions, but **“Socially Responsible Investment (SRI) combines investors' financial objectives with their concerns about social, environmental and ethical (SEE) issues.”**

UK Social Investment Forum



**Norges Bank**

v.



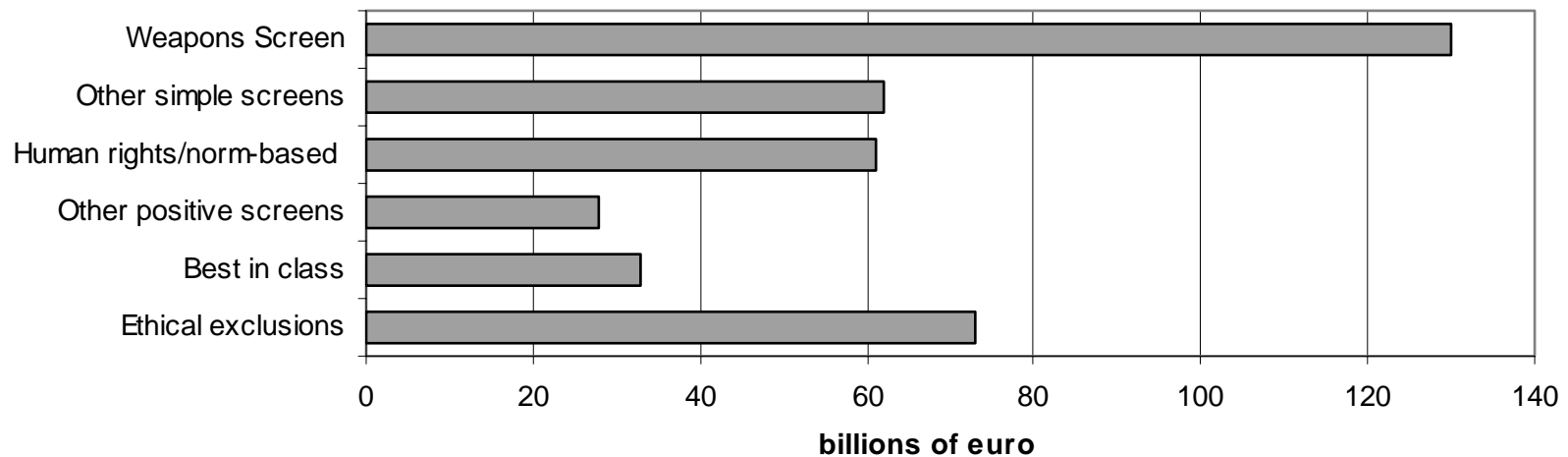
**Walmart**

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*Addresses a social (asymmetric harms), economic (externalities), and political (power) problem*

# SR I Sizes and Issues

**Figure 3: Socially Responsible Strategies practiced by European Investment Organisations  
(in billions of euro)**



Source: European Social Investment (2005)

**Social factors:** Labour's working conditions...health-impacts

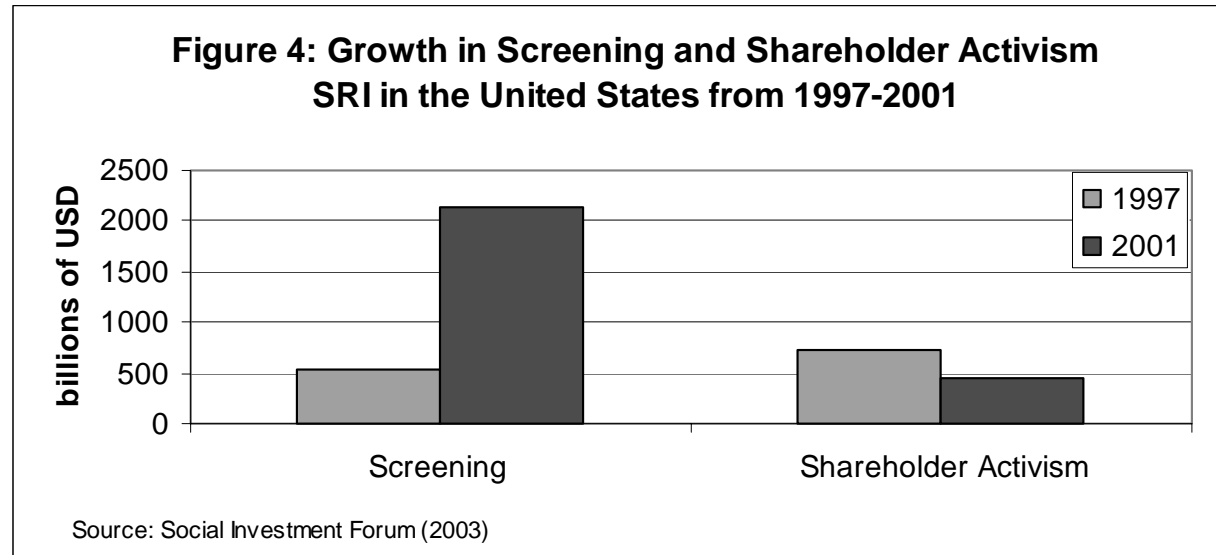
**Environmental factors:** pollution and/or climate change ... harm to forests and animals

**Ethical factors:** violations of human rights...concerns around pornography, alcohol and gambling).

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*SRI investments roughly \$2 trillion in US and another \$1 trillion in EU.*

# Types of Screening



- **Positive screening:** Funding investments with positive social, environmental (or ethical) impacts
- **Negative screening:** Starving investments with negative SEE impacts from investment
- **Passive screening:** Relying on the SRI screening criteria of an SRI fund
- **Activism** involves “voice” instead of “exit”, encourage SRI-related change via shareholder resolutions

# Shareholder Engagement

	Conflictual	Consensual
Shareholder	<p>Norges Bank v Walmart</p>	<p>Nike v United Methodist General Board of Pensions (UMGBP)</p> <p>screening</p>
stakeholder	<p>Greenpeace</p> <p>Amnesty Intl</p>	<p>Global Reporting Initiative</p> <p>Enhanced Analytics Initiative</p>

- the process by which institutional investors and their agents seek to improve investee companies' corporate governance and/or social, environmental and ethical (SEE) performance
- Pensions exercise suasion as Both shareholder and as stakeholder
  - CalPERS decisions attract attention because of social power as well as financial power



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# SR I funds' risk and return

- **SRI portfolios have higher long-run returns**

- Good management is good management
- Builds value instead of redistributes it
- Orlitzky *et al.* (2002) -- a positive relationship between corporate responsibility and investment performance.
- Guerard (1997) -- no statistically significant differences in SRI and non-SRI samples.
- Geczy *et al.* (2005) – an SRI “constraint” can cost investors at least 30 basis points per month.

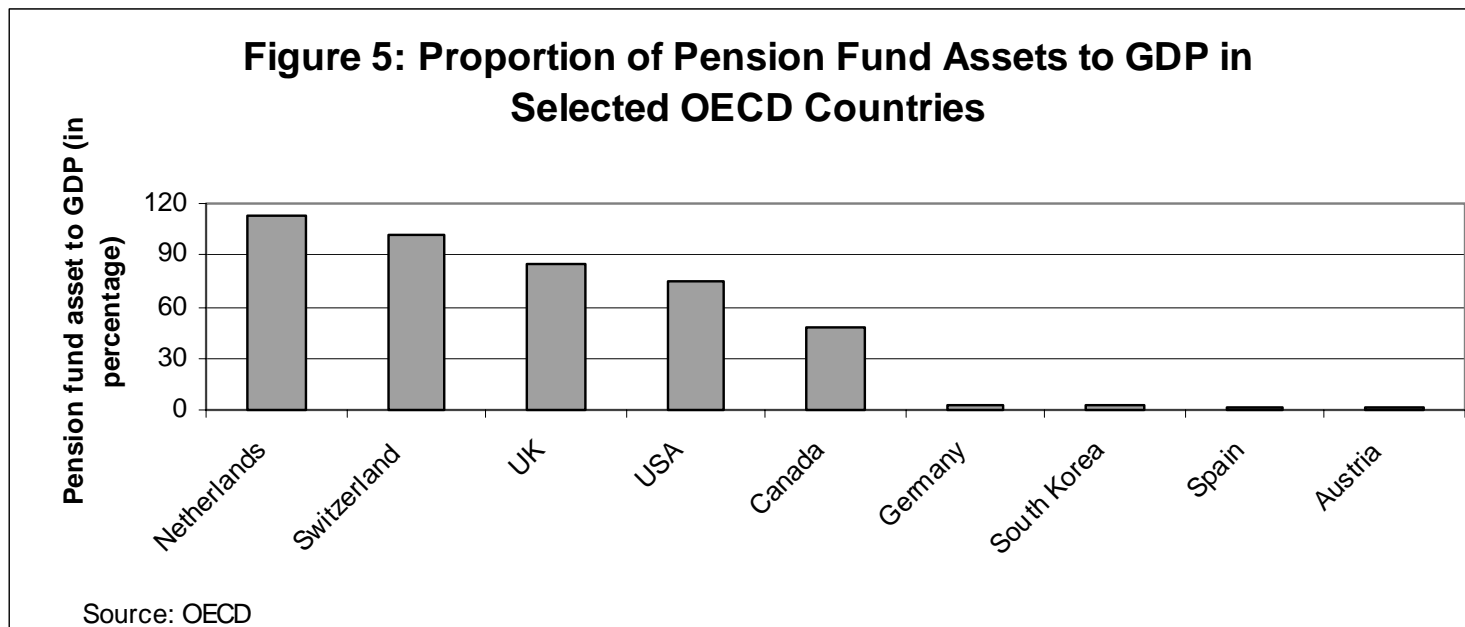
- **SRI portfolios are either less risky or price risk more fully**

- Social and systemic risks not accounted for in present risk-adj. returns.
- New risks of consumer activism and regulatory risk make SRI-related risks larger
- Schroder (2005) – fewer SRI funds have had poor performance (good maximin investment strategy)
- Who says you can't “push the efficient frontier?”

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*At economic heart of SRI is the pricing of social/systemic risk*

# Why Should Private Pension Funds Care About SRI?

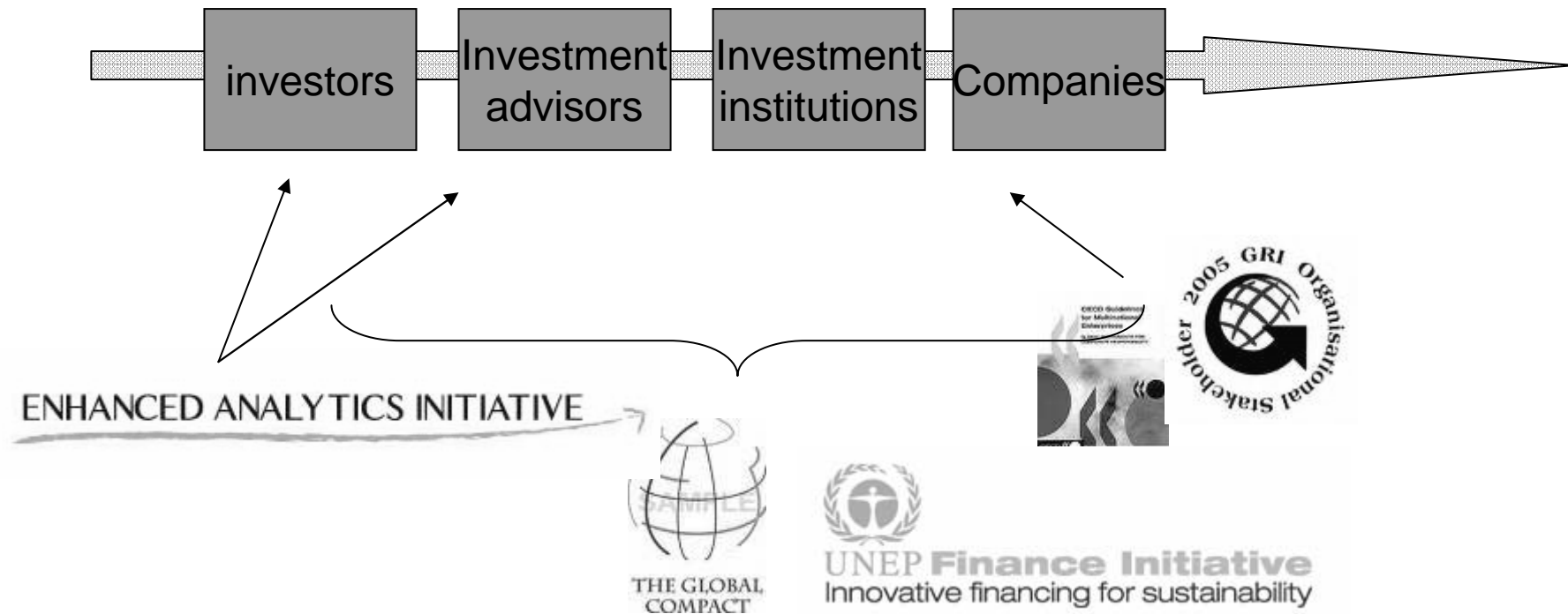


## Three camps:

1. They should not (Arrow-Debreu/Friedman view): max returns help all
2. They can help overcome externalities
3. They have a fiduciary responsibility (political SRI as embodied in international Work and SRI Fora)

*Their size ensures their SRI decisions (or lack of) will impact on capital markets*

# What Guidance Exists So Far?



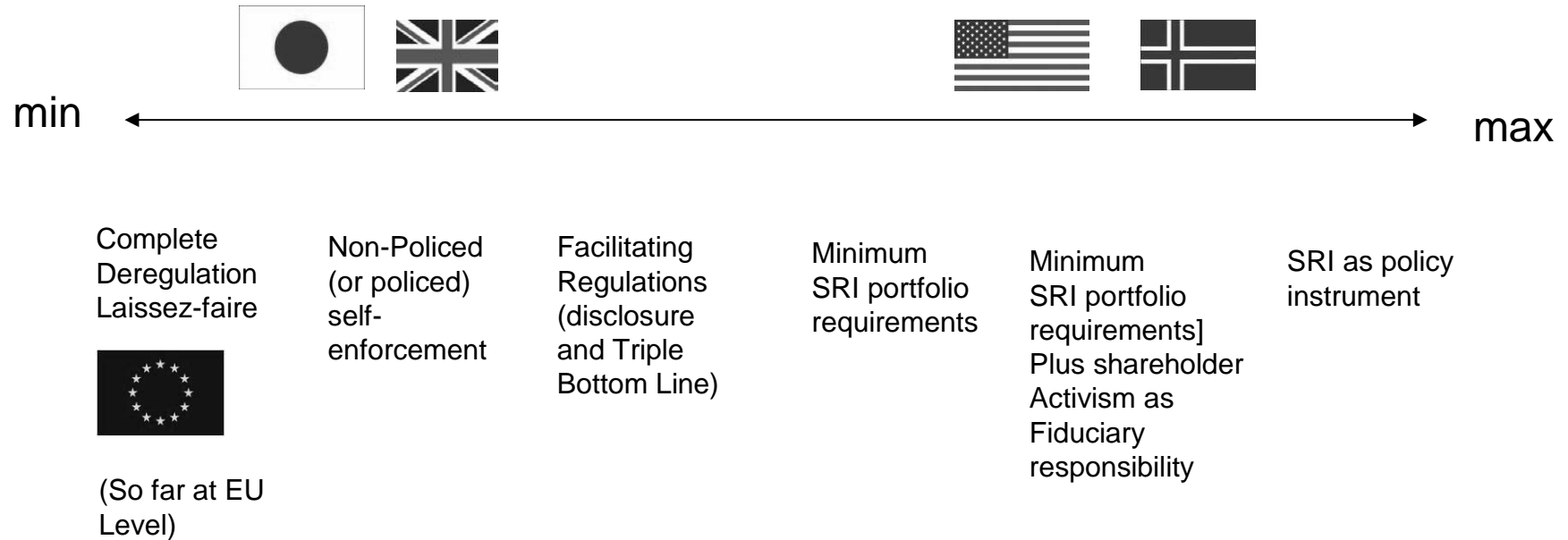
## Possible Critiques

1. vague language and their lack of enforcement mechanisms
2. weaknesses of self-regulation (insufficient and profit max regulation, self-enforcement)
3. Problems of incentive compatibility

*Profit max, duty of care, and politics are real drivers?*



# Possible and current regulatory responses to SRI



*Further OECD work will usefully poll regulators using standard criteria*

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# Regulatory Options

- Should companies/investors or intermediaries be regulated?
    - Savers/investors: They know best their own risk profiles
    - Intermediaries: can be contributors to systemic/social risks
  - Do what extent is SRI a policy tool for addressing market failures?
    - Private pension funds' investment decisions may help address externalities in social and environmental "markets" (MBprivate → MBpublic)
    - A Pigouvian tax in disguise
  - Dead weight loss and a harm shared is a harm squared
  - Regulation or moral suasion directed toward company pension trusts instead of funds themselves
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# Options for Turkish Policymakers?

- **Should ESG regulation be applied in Turkey's present environment?**
  - Distortion vs. investment promotion
- ***Avropalilastiramadiklaramizdanmisiniz?***
  - Need to conform with international norms versus capacity to set those norms
- **Low hanging fruit**
  - Educating investment professional
  - Use of trade associations
  - CSR!
- **Differences in Turkey's economic structure** and government capacity may make an interventionist policy welfare-improving (though more data needed!)

