A history of ethical investment

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From its roots in the religious movements which inspired Victorians concerned with issues such as temperance and fair employment conditions, ethical investment has rapidly grown in recent decades to become a powerful force for social change and is now entering the investment mainstream.

When the first UK ethical trust was launched in 1984, informed City observers estimated that the ethical investment market in the UK would eventually reach a maximum size of around £2 million. Yet by the end of 2000 it had grown in value to reach some £3.7 billion - nearly 2,000 times the original estimate - and the growth shows no signs of slowing.

The rise of ethical investment is closely linked to major changes in society in the last third of the century. It follows the growth of key social movements for the environment, human rights and animal rights. Major economic trends such as the increasing financial independence of women and young people, the growth of employment in the voluntary sector, the emerging power of multinationals, the reducing power of democratic governments and the massive increase in share ownership by unit trusts, pension funds and insurance companies have all helped to drive ethical investment forward. Taken together, these make it a rapidly expanding movement with a powerful future.

Compared with conventional investors, ethical investors are more likely to be female and younger, to work in a caring profession and to belong to at least one major organisation promoting conservation, environmental protection or social change. The combined UK membership of Greenpeace and Friends of the Earth grew from 50,000 in 1981 to over 550,000 by 1993. It is therefore not surprising that ethical investment took off over this period and outpaced total investment in unit trusts and investment trusts every year except two in the 1990s.

But ethical investment is not just a phenomenon of the last few years. It builds on Victorian social concerns such as temperance and just employment conditions. The modern roots of socially responsible investment can be traced back to the 1920s when the Methodist Church wished to start investing in the stockmarket while avoiding companies involved in alcohol and gambling. The Quakers soon followed, avoiding weapons manufacture. Churches have been avoiding tobacco, alcohol, armaments and gambling investments for years. The Church Investors Group, which shares experience among those managing ethical investments for a range of denominations, celebrated its 25th anniversary in 1998.

The first American ethically screened unit trust (or mutual fund) predated the launch of ethical unit trusts in the UK by more than a decade. In 1971, the Pax World Fund was set up in response to the demand for investments which did not benefit from the Vietnam

War. In the 1980s, opposition to South African apartheid fuelled the ethical investment movement both here and in the US.

Initiatives for a UK ethical unit trust started in the 1970s and finally reached fruition in 1984, with the launch of the Friends Provident Stewardship fund. The Ethical Investment Research Service had been set up the previous year by ethical investment enthusiasts wanting a common source of research on company activities.

Responding to increasing concern about environmental issues and sustainable development, "green" unit trusts arrived in 1988 with the launch of the Merlin Ecology Fund (now the Jupiter Ecology Fund). For the first time ever, investors were able to put their money into companies likely to benefit from the transition to a sustainable future. Other environmental funds soon followed.

Meanwhile other vehicles for socially responsible investment were starting. Mercury Provident (now Triodos Bank) was set up in 1974 to lend to projects with a social benefit. Seven years later, the Ecology Building Society began financing the purchase of properties with an ecological payback. The trade union-backed Unity Trust Bank arrived in 1984, and ethical banking received an important boost in 1992 when the Co-operative Bank introduced its highly successful ethical policy. Specialist community development finance organisations such as Industrial Common Ownership Finance began to seek "socially directed investments", offering a high social return with zero or low interest. By Autumn 2000, Shared Interest, the most successful such specialist, held nearly £20 million to finance fair trade.

The formation of the UK Social Investment Forum in 1991 brought together key figures across the full range of ethical and socially responsible investment to co-operate in sharing knowledge and advancing the agenda. Ultimately this helped to stimulate interest among pension funds, which now own more than a third of all UK shares; in 1963, they owned just 7%.

Local authority pension funds led the way in considering the social consequences of this type of investment. In the 1980s, councils sought particularly to avoid investment in South Africa and some of them later began to invest small amounts in ethical investment funds.

Following court cases in the same decade, the Goode Committee on Pension Law Reform highlighted the legality of ethical investment for pension funds. The committee's report declared that trustees are "perfectly entitled to have a policy on ethical investment and to pursue that policy, so long as they treat the interests of the beneficiaries as paramount and the investment policy is consistent with the standards of care and prudence required by law". In 1997, a group of university lecturers launched the Ethics for USS campaign for the ethical and environmental investment of their pension fund, the Universities Superannuation Scheme (USS). In 2000, USS announced its new policy on Sustainable and Responsible Investment.

Ethical investment received a further boost in 1998, when Pensions Minister John Denham announced that he was "minded to require trustees to disclose to what extent, if any, they have taken account of social responsibility considerations in their investment strategy". He won early support from the pension fund of the Sainsbury supermarket chain, which stated that it wanted to improve the environmental behaviour of companies. Since these proposals became law on 3 July 2000, all occupational pension funds have to consider formally whether or not to develop policies on social, ethical and environmental issues. A UK Social Investment Forum survey published in October 2000 found that 59% of the largest pension funds, representing over £230 billion of assets, had incorporated social responsibility issues into their investment strategies.

Changing company behaviour by shareholder influence is likely to be a key future trend within ethical investment. One turning point was the resolution on social and environmental policy proposed at the 1997 Shell AGM by corporate governance specialists Pensions and Investment Research Consultants and the church-based Ecumenical Council for Corporate Responsibility. Shareholders representing 17% of Shell's share capital withheld their support from the company on the resolution. In 2001, shareholder resolutions were tabled at the BP Amoco and Balfour Beatty AGMs.

Another key development may be the launch of Social Indexes, baskets of shares in companies selected as leaders in social and environmental performance. These indexes enable investors to compare the performance of these shares with the performance of the stockmarket as a whole. It is also a means for investors to combine ethical investment with tracking an index. The announcement of the FTSE4GOOD family of social indexes in 2001 followed the earlier introduction of the Dow Jones Sustainability Group Indexes.

Ethical investment in the UK has a long way to go to match the size of the market in the US, where the Social Investment Forum estimates that nearly one in eight dollars held with investment institutions are either in ethically screened portfolios, or subject to share voting policies which incorporate social responsibility criteria. This helps to explain why UK industry commentators now expect funds in ethically screened portfolios to grow as much as five-fold in the next few years.

A growing number of people are now investing both for financial return and to promote positive change in the world. This vital force for social change is coming of age.

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