

Briefing Paper - Ethical Investments

1. Introduction

Members have expressed an interest in investing in green and sustainable enterprises, with respect to our treasury management resources.

30th October 2017

Ethical Investment “Funds” were suggested and approved by members at the mid year treasury review.

27th March 2018

Ethical investment appendix included in the 2018/19 treasury management strategy, requiring clarification from members, before any investments can be made.

October 2019

Enquiries made to external advisors, regarding “Ethical Investment” options, as this is a new evolving area of investment, and as such new products are being introduced.

Two new products were suggested:

- Standard Chartered Green and Sustainable Product Framework
- Barclays Green Product Framework

2. Ethical Investments – What are they?

In essence ethical investment comprises **investing in companies** (UK and/or abroad).

These companies would have:

- Ethical Values
- Ethical Policies
- Operate in certain sectors

Which would need to meet Torridge District Council’s definition of “Ethical” (and/or “green”).

Torridge’s definition of “Ethical” therefore needs to be defined, in order to select suitable investments.

Ethical Categories:

Ethical investments fall in to two broad categories:

- Ethically Filtered (“do no harm”) – exclude, tobacco, armaments etc.
- Ethical Overlay (have a “specific” objective) – e.g. education, renewable energy etc.

More information is required from members to clarify the council’s objectives with regards to “ethical” investing, especially in relation to the two categories above.

These objectives should be added to the councils TMSS (treasury management strategy summary).

Ethical Investment Types:

As ethical investments, are investments in companies, there are the following options:

- Direct investment in individual **company shares** (High risk)
- Ethical **investment Funds** (groups of shares, usually with similar goals)
- Ethical (or more often “Green”) **Bonds**, lending money to individual companies. Including Ethical “Money Market” funds (shorter dated bonds).
- Ethical (or more often “Green”) **Bond funds**. Groups of bonds from companies that meet certain criteria (defined by the fund). Short term bond funds are called Money Market Funds.
- “Green/Sustainable” **Treasury deposits** – lending to a bank (e.g. Barclays or Standard Chartered), under a framework, where they use the funds to only finance suitable counterparties. These are a recent addition to the market.

Which ever investment type is selected, this should be included in an ethical statement and added to the TMSS (treasury management strategy summary).

Treasury Management impact

When considering an investment the council has to consider Security/Liquidity/Yield. Shares/Equity funds/Bond funds can be volatile, and therefore security is a concern, they should generally only be considered at lower levels of investment and for longer periods of time (i.e. 3 years +).

Green/Sustainable treasury deposits, are lower risk, however the market is small and fairly limited. Also our current counterparty policy only allows deposits with UK Fitch F1 rated banks, which means the market is relatively small to being with. Money market funds are also lower risk, and give similar returns to current treasury deposits, but are not currently authorised under our treasury management policy.

Current yields have been approx 1% in recent years; this has however reduced in the current year to around 0.3% due to Covid-19 (and the corresponding reduction in the Bank of England Base Rate)

Many ethical/green share and bond funds have produced higher rates (around 6%) over the last few years, these however are subject to the risk of the market, and can also give rise to large losses (e.g. the market dropped >20% in early 2020, though it has since largely recovered).

The current treasury management policy has strict criteria for selecting investments (treasury deposits), as there are so many different types of share and bond funds, it would not be appropriate for the treasury management officer to be selecting these. This should be done by a group/meeting made up largely of the members, this will need to be determined before these types of investments can be made.

3. Benefits vs Risks

Type	Benefits	Risks
Share / Bond Funds	Higher annual returns possible - many share funds and bond funds have produced returns of around 6% in the last few years (though past performance is not an indicator of future performance)	Potential for large losses - Value can go down as well as up. e.g. stock market dropped 20% in early 2020 (though it has since recovered most of this)
Share / Bond Funds		Cost of entry - many funds have a cost of entry and exit, making them more suitable for longer term investments
Share / Bond Funds		Lost flexibility - longer investment horizon, means money is tied up for longer, therefore not available to be utilised for local projects, such as: - New Environmental Centre - Future High Street - Homelessness Accommodation (Note: Current borrowing rates are around 2.6%)
Green Treasury Deposits / Money Market Funds	Short term investment timelines (retaining flexibility)	Possible reduction in returns compared to standard treasury deposits and standard money market funds - (council would need to define the yield it is willing to sacrifice in order to invest in ethical/green products).

4. Next Steps

Before investing in ethical investments can proceed, the council needs to:

i. **Set “ethical” objectives**

- What to exclude (tobacco, Oil, etc)
- Where to invest (UK companies only? International? Include Developing world?)
- Define specific or general goals/sectors, e.g. invest in education companies, invest in renewable energy, invest in energy efficiency etc.

ii. **Identify Ethical/Green investments** that align with these objectives.

- iii. **Set up a member group/meeting** to select specific suitable investments.
- iv. **Consider and set suitable limits**, for both the amount to invest (e.g. £100K to £5m+), and the investment duration (e.g. less than 3 months, less than 1 year, 1 to 3 years, 3 to 5 years, etc), for each type of investment:
- Individual Shares/Bonds – Value Limit? Duration?
 - Share Funds – Value Limit? Duration?
 - Bond Funds – Value Limit? Duration?
 - Green/Sustainable Treasury Deposits – Value Limit? Duration?
- v. **Propose an ethical statement for the TMSS**