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What is so responsible about responsible investing?

Harry Hummels¹

*Corporate social responsibility has become a religion filled with priests,
in which there is no need for evidence or theory*
Michael Porter²

1. The growth of responsible investment

The characteristic of responsible or ethical shareholders is that they do not merely acquire a risk-bearing share in the financial operation of a company, but deliberately opt to invest their money in firms which, as well as having good financial prospects, also take account of social, ethical and/or environmental aspects. The commonest form of responsible investment is investment in listed companies. Non-financial considerations also apply in the selection of fixed-income securities such as government and corporate bonds. An interesting asset class that explicitly addresses social, ethical, or environmental considerations is currently emerging: targeted investments with a specific non-financial goal. Examples are: microfinance, responsible timber investments, or clean energy. This paper will address the topic of responsible investment from the viewpoint of the institutional investor. Retail investments are disregarded.

Anyone who looks at the development in the institutional markets cannot help noticing the significant growth in attention for and investments in financial products that take into account environmental, social, ethical, and governance criteria. That is particularly true if the growth of the responsible investment markets is compared with that of the markets for conventional investments. However, growth figures tell us little, when it is not certain which investments belong to the 'ethical' or 'responsible' investment category and which do not. The simple fact that a company is included in an index of ethical shares or in an ethical investment vehicle is not necessarily an indicator of the ethical quality of its activities and behaviour. The only conclusion that can be drawn is that the company apparently satisfies the eligibility criteria of the index or fund manager. In the end, the investors themselves must therefore determine the social, ethical or environmental quality of the corporate activities or conduct with which they do (not) wish to be associated. Secondly, looking at the activities of a corporation one can ask whether investments in the production of tobacco products, alcohol, nuclear energy, arms or genetically modified crops, to mention just a few examples, have anything to do with responsible or irresponsible behaviour by a company or its investors? This gives rise to a problem, which can be described as follows:

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² Interview with Michael Porter in *EBF*, Issue 15, Autumn 2003.

'If there is no clarity and unanimity on the conceptualisation of corporate responsibility how can suppliers of responsible investment solutions determine to what extent they are actually investing in responsible companies or activities?'

A second, related question is: 'What is the importance of responsible investing in terms of the fiduciary responsibility of investors, or the aim of maximising the investment return?' I shall briefly examine this issue taking a European – and more in particular a Dutch – point of view.

This paper is structured as follows. In section 2 I will outline the various meanings of CSR. Section 3 views the concept of CSR in practical terms, involving restrictions on the management's freedom to decide the course pursued by the company. In section 4 I look at the significance of this practical interpretation for institutional investors – and particularly for pensions funds.

2. The meaning of CSR

2.1 Many terms, but do they indicate the same object?

Apart from the widely used 'corporate responsibility' or 'corporate social responsibility' in the debate on the responsibilities of a corporation one also comes across such terms as 'ethical business', 'responsible business', 'sustainable business', 'corporate citizenship', or 'stakeholder management' and variations on that theme. Also terms like 'People, Planet, Profit' and the 'Triple Bottom Line' crop up with great regularity. I shall concentrate in this paper mainly on the terms 'business ethics', 'corporate responsibility' and community involvement. Any comments in this paper on the restrictions attached to these terms also apply, *mutatis mutandis*, to the other terms.

2.2 Some shortcomings

Corporate responsibility has already been around for a long time, and dates back to the late 19th century. However, the concept did not really develop until the social, organisational and academic debate of the 1970s. Experience from that period has shown that the term 'corporate (social) responsibility' raises a number of questions. Or, as Goyder remarks, "the CSR debate is bedevilled by unconvincing rhetoric". In the following six issues will be discussed: demarcation, self-interest, stakeholder congestion, restating objectives, management incompetence and fluctuating trends in society.

2.2.1 Demarcation

The demarcation issue concerns the definition of the term 'corporate (social) responsibility'. What does it cover and what is excluded? Is a company behaving responsibly if it complies with the law? It is hardly surprising that companies (ought to) abide by the law, and the question is therefore whether such legalistic actions merit additional qualification highlighting the company's responsible behaviour.

The question whether a company's actions merit the CR label also arises in connection with its charitable activities. In his famous New York Times article Milton Friedman forcefully opposes a view that corporations behave responsibly when donating money to charities and other good causes. According to Friedman, business people are spending other peoples money – either the shareholders' money or that of clients, employees or

others who are taxed without having any say in the expenditure. Porter and Kramer (2006) defend a more nuanced position, arguing that corporate philanthropy can be in the interest of the shareholders, the employees and the business in general. By aligning the objectives of a charitable cause directly to the business objectives, they argue, the interests of the stakeholders (including the shareholders) are served.

2.2.2 Self-interest

The second issue concerns the motive behind the company's actions. Even if a company is clearly respecting the law and aligns its business and charitable activities in a way that is beneficial to all stakeholders, it is still often unclear whether its behaviour can be described as 'responsible'. Is the dialogue with a stakeholder an expression of corporate responsibility if the sole object of and reason to initiate that dialogue is to protect or promote the company's reputation or the interests of the shareholders?

2.2.3 Stakeholder congestion

In many definitions, CR coincides with concern for the interests of the stakeholders. However, there is generally no limit to the number of stakeholders with whom a company maintains, or could maintain, relations. That creates the risk that companies may face an infinite number of claims. According to Freeman (1984:31), the term 'stakeholder' was meant "to generalize the notion of stockholder as the only group to whom management need to be responsive". At the end of the day, anyone who is affected by an enterprise has a (normative) claim on that enterprise entitling them to be given an answer, and sometimes actually to be heard. As a result there are so many stakeholders hammering on the corporation's door it might face serious *stakeholder congestion*.

2.2.4 Goal displacement

Various critics draw attention to the issue of goal displacement. Without exception, they point out that the company's aim is to make a profit. As Levitt says: "Welfare and society are not the corporation's business. Its business is making money, not sweet music".³ It is inappropriate for the management of the corporation to pursue social, ethical or environmental goals unless they help to boost profits. However, there can be no question of separate, stand-alone objectives.

2.2.5 Incompetence

The fifth issue concerns the incompetence of the management to take proper account of social, ethical or environmental objectives in running the business. Critics on both the stakeholder side and the shareholder side draw attention to this problem. In this connection, Freeman and Liedtka remark:

"Corporate social responsibility promotes incompetence by leading managers to involve themselves in areas beyond their expertise – that is repairing society's ills."

Friedman states that managers have no specific expertise for taking appropriate, wise decisions on social, ethical or environmental issues. They often give in to social pressure and tend to look for the easy way of pleasing stakeholders (see also Levitt, 1958; Henderson, 2001).

³ Levitt, T. 'The dangers of social responsibility'. In: Harvard Business Review, Sept./Oct. 1958, pp. 41-50

⁴ Freeman, R.E. & Liedtka, J., 'Corporate social responsibility. A critical approach'. In: *Business Horizons*, July-August 1991, pp. 92-98

2.2.6 CR comes and goes in waves

Corporate responsibility appears to be a new issue – with a history of no longer that 10 to 12 years – but it's not. Not only were terms like 'the social responsibility of business', 'corporate responsibility' and 'corporate social responsibility' already used after World War II, in essence the question of corporate responsibility is much older than that. The contribution of men like Carnegie, who described corporate responsibility in terms of *stewardship* and *charity*, is seen as the starting point of what is now known as CR.⁵ Various 'waves' of CR can be detected after World War II.⁶ For instance, in his article in the *Harvard Business Review*, published in 1958, Levitt observes that "management's social responsibility ... has become a deadly serious occupation".

2.2.7 A closer examination of the six issues

The issues mentioned above create confusion and uncertainty concerning the social, ethical or environmental requirements imposed on a business and its management. Using the example of Total, the French oil company, it becomes clear that a clarification of the practical meaning of CR is desirable. What should consumers, investors, politicians, civil servants or journalists think of a company receiving high grades for its social, ethical and environmental policies, practices and performance on one hit list or index, while being excluded from another due to its presence and its activities in Burma. How does this confusion influence the decisions of interested parties? Total has improved its performance in complying with codes of conduct, engaging with interest groups and its social, ethical and environmental reporting. Clearly, the dominant interpretation among European investors is that an investment in Total is acceptable. In fact, Total is seen as 'one of the best in its class' – the class being the (European) oil sector. However, the dominance of this interpretation does not prove that it is actually correct.

2.4 Conclusion

No one seems to dispute that companies should behave responsibly within the scope permitted by the rules – rules that are regularly being revised and updated, while new rules are added to the entirety of local, national or international rules. But if so many interested parties feel drawn to spread the word, we might ask whether it is not time to save businesses and society from CR gurus and addicts. Shouldn't companies simply get 'back to business', with the management conducting the 'business of business' with due regard for the social and environmental effects of the business?

3. CR in perspective

3.1 Freedom and enterprise

Isaiah Berlin, in his famous inaugural speech dating from 1958, asserts that freedom is an immensely important asset. In *Two concepts of liberty* he discusses the concept of freedom as applied by the classical English political philosophers, such as Hobbes, Locke, Smith, Bentham and Mill. Quoting Hobbes, Berlin states that "a free man is he that ... is not hindered to do what he hath the will to do". So according to Berlin, a person is free if he or she can take decisions without interference from anyone else. The greater the area

⁵ See Mitchell, N.J., *The generous corporation*, New Haven, 1989 and Freeman, R.E., and J. Liedtka, 'Corporate social responsibility. A critical approach'. In: *Business Horizons*, July-August 1991, pp. 92-98.

⁶ To gain some insight into this development, see the various articles by William Frederick and the general article by Sandra Waddock, entitled 'Parallel Universes', *Business and Society Review*, 109, 2004.

over which a person has control – and where others must refrain from interfering – the greater that person's freedom.

Freedom is a key issue not only for individuals but also for society. Without freedom, remarks Berlin, with reference to John Stuart Mill, all human civilisation is doomed to sink into mediocrity. A society without freedom lacks spontaneity, creativity, originality and moral courage, and the truth will not be discovered. As Adam Smith observed, freedom is not only important for individuals but also for the business community. However, the freedom of the individual or company cannot be unlimited. If it were, that would create social chaos, and it would no longer be possible to meet the basic needs of the members of a society. "Liberty", as Berlin remarks, "is not the only goal of men."⁷ Not only do individuals in practice renounce some freedom in their daily lives in favour of other essentials such as well-being, security, justice or peace, it is often also possible to present reasonable arguments for doing so. As always, the question is where does the boundary lie and to what extent can human freedom be restricted without impinging on a minimum degree of freedom required for a dignified existence. Berlin criticises restrictions on the freedom of individuals and groups imposed without at least their implicit consent. Human existence requires laws that restrict freedom to some extent, but laws that individuals and groups themselves have made – or can consent to – on rational grounds. Without those self-imposed laws, there is no such thing as liberty.⁸

3.2 Social responsibility as a restriction of freedom

According to Jeremy Bentham "every law is an infraction of liberty" even if the law results in an increase in the overall liberty of a society. Laws restrict the freedom of individuals and businesses to create value without inhibition and as they see fit. The constantly recurring question is therefore: 'How far should a society go in influencing the freedom of action of individuals and organisations, or restricting that freedom?'

The fact that social behaviour is made up of a continuous and never ending flow of interactions defining the limits of its members' freedom means that the answer to the question: 'What is socially responsible?' is constantly challenged. As a result the answer is also constantly changing. In this connection, I use the phrase *interactive restriction of liberty*. Interactions in this area are aimed at the free exchange of views on the economy and society, specific interests and political pressure to persuade corporations to take account of the social effects of their actions. Restrictions in this domain are taken up either voluntarily or as a result of the interactions with NGOs, consumers, investors, representatives of government or other stakeholders. Sometimes, however, it cannot be left up to the parties involved to regulate and restrict their behaviour. Even the most libertarian thinkers hold the view that the freedom of individuals and organisations may be restricted in order to safeguard the liberty of others. However, that should be done on the basis of laws that can carry at least the implicit consent of the persons who are impacted by those laws. Interactive restrictions on freedom with the force of law contribute to a *regulated restriction of freedom*. The regulated restriction of freedom is a specific form or sub-category, of the interactive restriction of freedom.

⁷ Isaiah Berlin, "Two concepts of liberty", in *Four essays on liberty*, Oxford University Press, Oxford, 1969

⁸ Berlin finds a similar insight in Locke, who comments that "where there is no law, there is no freedom". See Isaiah Berlin, "Two concepts of liberty", in *Four essays on liberty*, Oxford University Press, Oxford, 1969.

Nowadays we are encountering a third form of interactive restriction on liberty in society. Although it does not have the status of law, it is certainly influential, thereby differing from the routine struggle over restrictions on entrepreneurial freedom. It concerns agreements reached by the international community on the way society should be organised and its members should behave. Examples are the Universal Declaration on Human Rights, ILO conventions and recommendations, the Rio protocol. Those agreements are the outcome of consultation and negotiation. These agreements provide *authoritative restrictions of freedom*. However, as for instance the Kyoto Protocol shows, these agreements are only authoritative for those who actually commit themselves to comply with the agreement. I shall now look at these restrictions on corporate freedom, starting with the regulated restriction of freedom.

3.2.1 Regulated restriction of freedom

It is often said that a business requires a 'licence to operate'. A firm that cannot give a prompt and satisfactory justification for its activities may provoke a counter-reaction from society. A very common reaction is regulation. Not only does society believe that business should respect a number of basic rules of the game, corporations themselves tend to feel the same way. This is evident, for instance, from their statements of corporate values, business principles and codes of conduct. One of those general rules is that a corporation should respect the law. The simple fact that compliance with the law is often not enforced does not in itself provide justification for a company to ignore the rule.

3.2.2 Authoritative restriction of freedom

Sometimes questions arise relating to issues that are the subject of guidelines of influential bodies such as the Organisation for Economic Cooperation and Development, the United Nations, the International Labour Organisation, or the World Trade Organization. They are not only concerned with the conduct of corporations but also – or even primarily – with the behaviour governmental organisations, NGOs, or multilateral organisations. The guidelines do not have the status and authority of a law, but of soft laws, international treaties and ethical codes relating to issues like human rights, the control of corruption, child labour, cartels and the protection of the natural world can be highly influential. Although national governments are primarily responsible for ensuring that rights are respected and promoted, the rights are not concerned purely with government activities. The fact that the UDHR speaks of "every organ" of society entails that it also addresses corporate behaviour. Much the same applies to the core ILO conventions, such as conventions 138 and 182, concerning the prevention of child labour.

3.2.3 Interactive restriction of freedom

In the field of bribery and corruption, it is clear that laws and treaties are not sufficient to prevent all undesirable practices and risks. In real life, relationship management, gifts and 'facilitation payments' occur in a variety of forms. Those forms cannot all be regulated in detail by law. Nor do they need to be, since not everything in facilitating the relationship between a business and its stakeholders is considered socially unacceptable. An entrepreneur who wants to make a gift to a customer as a token of appreciation generally meets little resistance. However, the question is where the boundary lies between the acceptable forms of managing a relationship and the unacceptable bribing of a customer. That boundary cannot always be clearly defined, although it is sometimes clear if the boundary has been (grossly) exceeded.

Just as it is not possible to specify clearly what is acceptable and what is not, we can see the limits to the potential influence over business activities exerted by laws, treaties or authoritative pronouncements. In such cases, a democratically elected political executive can (and should) use the other policy and management instruments available to it. Examples include engaging with companies, conducting research, facilitating the social debate, promoting transparency, or encouraging self-regulation. The government is not the only player here that can influence corporations. NGOs can also contribute towards the interactive redefinition of corporate freedom of action.

In the end, the effectiveness of such initiatives depends on management accepting the sense of restricting its freedom. In other words, the interactive restriction of freedom is a form of voluntary restriction in terms of self-restraint or of positive commitment. This voluntary commitment often takes the form of a covenant, a code of conduct or a statement of values. Managers who are not willing to discuss non-financial issues are not, however, in themselves acting socially irresponsible. Management's actions are only irresponsible if they are contrary to laws, treaties, conventions, covenants or agreements that the management has accepted either implicitly (regulated or authority-led restrictions on freedom) or explicitly (interactive restriction of freedom). And although the corporation's stakeholders may claim that management is acting irresponsible in externalising cost, it is only society by way of legislation, covenants or codes that ultimately draws the line between responsible and irresponsible behaviour or between responsible and irresponsible business activities.

The conceptualisation of corporate responsibility as offered in this paper has consequences for the way institutional responsible investors can operationalise responsible investment. In the following paragraph I will outline three types of strategies of responsible investment and highlight the implications of the operationalisation of corporate responsibility provided in this paper.

4. Institutional investors and corporate responsibility

At the beginning of this paper it was mentioned that a lack of clarity and unanimity on the operationalisation of corporate responsibility impacts the responsible investment industry. In this paper I will concentrate on pension funds as one of the leading parties in the investment community. Pension funds like CalPERS and NYCERS in the USA, ABP and PGGM in the Netherlands, USS and Hermes in the UK, FRR in France, or AP 7 in Sweden, have taken steps to further the development and implementation of responsible investing.

4.1 Fiduciary responsibility as an ethical responsibility

First and foremost pension funds have a fiduciary responsibility to act in the best interest of their beneficiaries. American trust law provides a lead for putting that fiduciary responsibility into practice. The relevant laws state that pension fund trustees have to manage the fund's assets in accordance with the principles of 'loyalty' and 'care'. The principle of loyalty states that an institutional investor's policy-makers must be loyal to the financial interests of the beneficiaries. The principle of care requires an investor to act prudently. This means according to the American Department of Labor ('DOL') that a trustee is allowed to take non-financial goals in his investment decisions into account, if

the resulting investment portfolio is equal to a 'conventional' portfolio to which no investment restrictions apply.

At the end of 2005, this view got an important addition with the publication of the report *A legal framework for the integration of environmental, social and governance issues into institutional investment*. This report was drawn up by law firm Freshfields Bruckhaus Deringer. It describes how in 'common law traditions' and in 'civil law traditions' is looked at the fiduciary responsibility of institutional investors. In both traditions the legislation and the case law leave institutional owners and asset managers space to apply ESG criteria.

4.2 Responsible investments and corporate responsibility

In a recently published study with the title '*The future has arrived*' the joint Dutch pension funds define responsible investing as investments "*based on financial, social, governance and environmental considerations and/or influencing companies, governments and other relevant players, based on these considerations*"⁹. In this paper three strategies are examined from the viewpoint of restricting the freedom of corporations. In order to do justice to the idea of responsible investments, one also needs to assess the financial performance of the portfolio management. This is particularly true for pension funds with a responsibility to act in the best interests of their beneficiaries¹⁰.

4.2.1 Exclusion

The exclusionary strategy is affected by the operationalisation of corporate responsibility given in this paper. It is proposed to screen investment portfolios on the basis of a limited number of criteria based on international treaties, codes, and conventions. Examples of such codes and conventions are: the Universal Declaration of Human Rights, the ILO key principles, the OECD guidelines on bribery and corruption and international treaties on the non-proliferation of weaponry including landmines, atomic, biological and chemical weapons. The financial effect of an exclusionary policy can be quite radical, while at the same time it can be no more than a ripple. It all depends on the strictness with which the investor applies the criteria to the investment process.

Of course, an investment firm is free to offer investment products that go beyond these basic criteria and include in its investment screening other social, ethical or environmental issues that it considers relevant for the profile of the fund or mandate. However, these additional features are not required from a generic or broadly accepted corporate responsibility view. Corporations that are excluded on the basis of arguments that stretch beyond these minimum requirements are not necessarily irresponsible. They only do not meet the investors' criteria.

⁹ Joint Dutch Pension Funds, *The future has arrived*, The Hague, February 2008

¹⁰ The literature presents mixed results on the financial value of responsible investments. See for example Moskowitz, M.R., "Choosing socially responsible stocks". In: *Business and Society Review*, Vol 1, 1972, pp. 71-75; Vance, S.C., "Are socially responsible corporations good investment risk?" In: *The Management Review*, Vol. 64, no. 8, 1975, pp. 18-24; Alexander, G.J., and Buchholz, R.A., "Research notes: CSR and Stock Market Performance". In: *Academy of Management Journal*, September 1978, pp. 479-486; Hamilton, S., Jo, H., and Statman, M., "Doing well while doing good?". In: *Financial Analysts Journal*, November 1993, pp. 62-66; Reyes, M.G., and Grieb, T., "The external performance of socially responsible mutual funds". In: *American Business Review*, Vol. 16, January 1998, pp. 1-7; Statman, M., *Socially Responsible Mutual Funds*, Association for Investment Management and Research, October 2000.

When it comes to excluding companies – or entire sectors of industry – some investors take far-reaching decisions like the exclusion of the oil and gas sector, nuclear power, the financial industry (due to its inherent lack of transparency), the airline industry, the aircraft industry, the tobacco industry, the alcohol industry, the gambling industry, et cetera. Here ethics might come at a price. If one is so principled not to invest in these industries, this attitude might ultimately raise the risk profile of the portfolio, which in turn might lead to a breach of fiduciary responsibility.

4.2.2 Inclusion¹¹

The inclusion strategy can be subdivided in:

- a) *Positive selection* – of which the best-in-class approach is the most common form;
- b) *A comprehensive values assessment*; this approach focuses on uncovering hidden financial value through the analysis of a corporation's social, ethical, environmental and governance values and performance;
- c) *Targeted investments*. Examples of the latter subcategory are investments in clean energy, sustainable timber, microfinance, clean tech, and the like.

Ad a) Best-in-class approach

A best-in-class approach means investing in equity of companies that come on top of responsible investment compared to their competitors. Assets are being invested based on a 'responsible universe' or a 'responsible index'. The index often does not take the financial performance of the corporation into account. Characteristic for a best-in-class approach is usually that it aggregates all scores and then compares the scores with the corporation's competitors in the same sector or industry. So the final assessment is always a relative judgement.

Ad b) A comprehensive values assessment

Institutional investors select investments on the basis of relevant information providing insight in the (hidden) value of the entity in which they invest or want to invest. In the recent past investors have also integrated governance considerations since academics studies demonstrated that well-governed companies financially outperformed poorly governed competitors¹². What counts for governance as a relevant non-financial aspect of business also seems to be the case for eco-efficiency but not necessarily for other ESG-issues.

Ad c) Targeted investments

Institutional investors can target specific investments in alternative asset classes like microfinance, climate change, sustainable forestry or alternative energy. These

¹¹ For this paragraph I am indebted to my colleague Prof. Dr. Rob Bauer. This contribution was published as part of the study of the Joint Dutch Pension Funds, called *The future has arrived* and was released on 14 November 2007 (English translation February 2008). The study can be downloaded via www.vb.nl

¹² For example, Gompers, Ishii and Metrick have analysed the impact of 24 possible protection constructions on equity returns. After correction for risk, the portfolios of well-managed companies appeared to generate no less than 8.5% higher returns than portfolios of badly managed firms in the period 1990-1999. Moreover, well-managed companies are usually higher valued on the stock exchange, and have larger profit margins and returns on own assets as well. (Gompers, P., Ishii, J.L. en Metrick, A., *Corporate Governance and Equity Prices*, uit: Quarterly Journal of Economics, Vol. 188:1, 2003, pp. 107-155). However, recent research by Core, Guay and Rusticus shows that information relating to good corporate governance seems to be largely incorporated in the market value. Moreover, a large part of the forecasted returns by Gompers, et al. can be explained by the ICT-hype at the end of the past millennium. Leaving out technology shares the outperformance is much smaller and statistically insignificant. (Core, J., W. Guay en T. Rusticus, *Does Weak Governance Cause Weak Stock Returns? An Examination of Firm Operating Performance and Investors' Expectations*, uit: The Journal of Finance, 61, 2006, pp. 655-687)

investments combine the objective of returns with socially desirable outcomes. The relevance to the ESG domain is usually immediately clear, while such investments also contribute to the desired spread of risks in the portfolio.

Evaluation

Although it might be a good thing to look for hidden financial value – or financial risk – in the social, ethical and environmental characteristics of a corporation, investors using an inclusion strategy do not necessarily respect laws nor international codes, conventions or principles. From the corporate responsibility point of view put forward in this paper the best-in-class approach, for instance, has little credibility. The inclusive strategies do not have an ethical or corporate responsibility bottom line. This was particularly confronting in the case of Total's presence and activities in Burma. Although a wide variety of rating agencies – providing the rough data that constitute ESG building blocks for the institutional portfolio managers - consider Total to be among the best performing companies in the ESG areas, the corporation indirectly contributes to the violation of human rights by the country's ruling military coalition. This means that a company can be both best-in-class and contributing to violations of international standards, principles, codes, and conventions at the same time.

4.2.3 Engagement

Engagement and proxy voting to affect the management of a corporation are relatively new strategies available to investors. Only limited research has been carried out into the effects of both strategies on the risks and returns of companies as well as on the risk return profile of investments in those firms. This applies in particular to longitudinal research, which is simply not available. Nevertheless, an appealing example is the so-called CalPERS effect. For years, the large US pension scheme CalPERS has been publishing a black list of companies that, according to the pension fund, perform badly on corporate governance: the so-called focus list of corporate laggards. Before they figured on the list, these companies were performing far below the average valuation. After they were black-listed by CalPERS the firms achieved considerably above average. From a viewpoint of promoting corporate responsibility as proposed in this paper an engagement strategy appears to be very promising although, as was mentioned already, the efficacy of the strategy is still highly unproven.

5. Conclusion

This paper interprets corporate responsibility (CR) in terms of generally accepted or self-imposed restrictions on corporate freedom. The paper distinguishes between three types of restrictions of corporate freedom that together define the 'corporate responsibility arena':

- regulated restrictions on freedom causing firms to respect the law,
- authoritative restrictions on freedom causing businesses to adhere to international agreements, conventions and treaties, and
- interactive restrictions on freedom in the form of covenants, codes, self-restraint or positive commitments to corporate responsibility in so far as these are explicitly endorsed by the top management.

Beyond these restrictions the corporation is free to pursue its interests. This means that the management is free, within the limits specified, to carry out its mandate and fulfil its *ethical* obligation to exercise its fiduciary responsibility to act in the interests of the stakeholders while being accountable to the shareholder.

For the financial world, putting corporate responsibility into practice in terms of generally accepted or self-imposed restrictions on corporate freedom offers a clear and useful approach. It means that investors do not bear the entire moral burden of society on their shoulders, but contribute to the implementation of the rules, conventions, covenants and agreements that are broadly accepted in society.

For institutional investors there seem to be very few financial obstacles preventing the implementation of responsible investing along the lines described in this paper. And there are no operational impediments either. This means that responsible investment may become an important development if investors can be persuaded of their capabilities here, and of the compatibility of ethical and fiduciary responsibilities.