

Greenwashing

Misclassification and Mis-selling
of Ethical Investments

November 2019

Time for the Regulator to step in



sc
m | **DIRECT**

**Smart Common-Sense Modern
Investing**

Executive summary

2019 is proving to be the year in which ethical investing is coming of age as investors increasingly seeking to prioritise Environmental, Social and Governance considerations, as well as outperformance; especially amongst socially conscious millennial investors.

To satisfy this investor requirement, we are witnessing a plethora of ESG (Environmental, Social and Governance), SRI (Socially Responsible Investing) and other ethically based strategies being launched; in the UK and internationally.

In the rush to satisfy this growing consumer demand, companies are launching products amidst a data fog where it is difficult to see or identify what is really being held within these funds. Whether it is deliberate or accidental, clients who wish to satisfy their twin goals of return terms as well as having regard for the planet and society, are being taken advantage of in numerous ways.

There is no denying that there is a real opportunity for investors to be prudent as well as using their money for positive change, but the ethical investment sector must be responsible and take every care to ensure their investment products are as genuine, measurable and transparent as possible. Of course, there is no perfect way to invest ethically or otherwise and naturally there will always be drawbacks to any investment or investment strategy, but clients should be able to decide fairly based on considered analysis, rather than emotive and misleading marketing.

Unfortunately, new research within this report by SCM Direct indicates widespread misclassification and mis-selling. **Based on this research, it is the view of SCM Direct that the UK regulator should conduct an urgent industry review, rather than its normal strategy of stepping in after investors have already been exploited.**

In view of the vast array of products and the difficulties in agreeing global benchmarks and best practice, SCM Direct suggests looking through the other end of the telescope as what is deemed ethical by one investor may well differ from the criteria of another investor. Rather than shoehorning products into particular product categories, investors should be given a fully transparent list of holdings, all costs and all details on ethical investment strategies so they can make fully informed decisions about where a particular product fits their individual investment parameters, rather than potentially being misled.

SCM Direct research findings

1. No rules or regulations on the calculation of ethical data.
2. Some funds appeared to be mis-classified as having an “*ethical*” investment focus.
3. Various ethical funds were found to be investing material amounts in tobacco, alcohol, gambling and defence stocks.
4. Key ethical quantitative data provided by companies are not audited and open to widespread abuse.
5. Ethical scores/ratings vary enormously between data providers in terms of individual securities. For example, Tesla is top on one provider’s scoring, bottom by another and average by another. When a company fails to disclose a piece of information to a provider, one data provider gave it a low score whilst another assumes an average score for the missing item.
6. Ethical scores/ratings vary enormously between data providers in terms of individual funds. For example, an identical search for “*socially responsible*” funds utilising two different investment platforms (powered by the same data provider) produced completely contradictory results.
7. Many ethical funds/strategies found to be investing significant amounts via plain vanilla Government Bonds e.g. one ethical portfolio invested 96% of its assets in a UK Government Bond fund, just 3% via an ethical fund and 1% in cash.
8. The average Ethical Equity mutual fund underperformed the market by 2.5% per annum over the three years to end June 2019, compared to a 0.8% per annum underperformance for the average passive ethical equities fund.

SCM Direct recommendations

1. Common data accounting standards for this product sector should be internationally agreed to include standardised data points so key data can be independently audited and signed off.
2. Industry wide collaboration so large data providers are encouraged to work with each other to discuss and resolve “*discrepancies*” in approach and results.
3. The FCA urgently starts a review of the UK ethical investment sector and considers enforcement against funds/portfolios whose marketing materials are found to be misleading clients.

4. Given the wide range of strategies and philosophies, and opposing views on individual securities, investors should be afforded 100% transparency, on a regular six-monthly basis, so they are fully aware of the full list of securities held in their investments. This would enable them to make fully informed decisions that best match their own ethical parameters.
5. Funds/portfolios should not be allowed to be marketed as “*ethical*” portfolios unless all the assets (excluding cash) are via “*ethical*” investments - rather than plain vanilla Government Bond funds or other non “*ethical*” funds.

1. Background - What is an ethical fund?

Ethical investing refers to an investor approach based on an individual's ethical principles and beliefs as the primary filter for investment selection. The producers of ethical funds market to this target market under the grouping of Socially Responsible Investing (SRI) or Environmental, Social and Governance (ESG) investing. Other common strategies include social investment, also known as sustainable, socially conscious, *"green"* or *"sustainable investing"* or *"responsible investing"*. There is also a subset of SRI known as *"impact investing"*, devoted to the conscious creation of social impact through investment.

In general, socially responsible investors prioritise and support corporate practices that they believe promote principles and practices such as environmental stewardship, consumer protection, human rights, and racial or gender diversity. Some SRIs avoid businesses in sectors perceived to have negative social effects, commonly alcohol, tobacco, fast food, gambling, pornography, weapons, contraception/abortifacients/abortion, fossil fuel production or the military. The areas of concern recognised by the SRI practitioners are sometimes summarised under the heading of ESG issues: Environment, Social, and corporate Governance, or responsible investing.

Despite significant growth in this area, regulators have been slow to provide a definition or methodology of what constitutes responsible investing; leaving it to investment managers and data providers to self-identify and define. We believe this has led to an alarming level of what is being identified as "Greenwashing" - a practice of making misleading claims about the environmental benefits of a fund / investment or company.

Some international institutions are alert to the issue, such as the European Union who passed a **Directive on Disclosure of Non-financial and Diversity Information**¹ that mandates large publicly held entities to issue sustainability information.

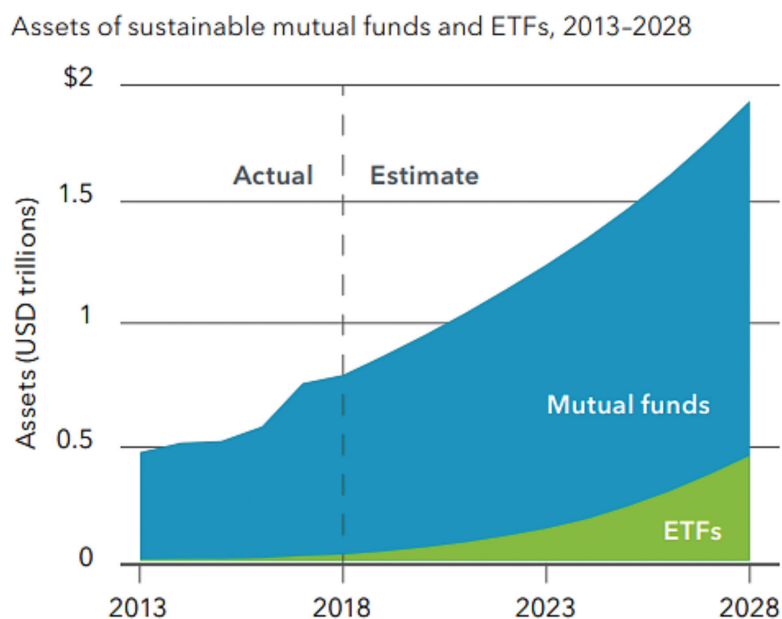
Initiatives such as United Nations Principles for Responsible Investment, UN Global Compact and the Global Reporting Initiative have emerged to make clear what constitutes responsible investment and to promote it through the support of extra-financial reporting. **However consistent, commonly agreed criteria and benchmarking remains an uphill struggle.**

¹ https://ec.europa.eu/info/business-economy-euro/company-reporting-and-auditing/company-reporting/non-financial-reporting_en

2. Growth in ethical funds

According to the UK's Investment Association, 26% of total assets under management within the UK are being managed with a responsible investment approach².

The universe of dedicated sustainable investment funds in European and U.S. mutual funds and Exchange Traded Funds (ETFs) has grown from \$453 billion in 2013 to c.\$760 billion recently. This increase is predicted to rise exponentially³.



There's no guarantee that forward-looking estimates will come to pass.

Sources: BlackRock, with data from Broadridge/Simfund, June 2018.

Notes: The chart shows the total assets under management in ESG mutual funds (MFs) and ETFs globally. The 2019 to 2028 figures are based on BlackRock estimates, assuming a 5% annual growth rate in the underlying markets.

Other assumptions: MF asset growth starts at 5% in 2019 and declines by 0.5% annually throughout 2022, then at a zero-to-0.5% rate annually thereafter. ETF asset growth starts at 45% and decreases by 5% annually throughout 2022, with a zero-to-3% pace thereafter.

² <https://www.investmentassociation.m-w.site/sites/default/files/2019-09/IMS%20full%20report%202019.pdf>

³ <https://www.blackrock.com/ch/individual/en/literature/whitepaper/bii-sustainability-future-investing-jan-2019.pdf>

3. Misclassification of funds by data providers/investment platforms

Fidelity appears to misclassify many funds as being “socially responsible funds”.

When SCM searched the Fidelity platform for all funds managed by Fidelity that were deemed “socially responsible funds”⁴, the following 49 share classes appeared but SCM found only two (both of which related to the same underlying fund) that suggested such an investment focus within the KIID.

It is interesting to note that the FCA itself⁵ has stated that:

“Our Policy Statement (PS19/4), issued in February 2019, included non-handbook guidance clarifying that a fund should set out clearly in its Key Information Document if it pursues environmental, social or other non-financial objectives, and how it does so.”

Furthermore, Fidelity only manages two funds which it describes as being “specifically tailored for ESG”: the FT Sustainable Water and Waste Fund (this appears within the list of 49 funds) and the Fidelity FIRST ESG All Country World Fund⁶.

It should also be noted that Fidelity states that it has integrated ESG into their overall investment process⁷ - “ESG analysis is carried out at analyst level within the equity, fixed income, real estate and multi-asset teams and our portfolio managers are also active in analysing the potential effects of these factors when making investment decisions.” However, Fidelity also states that this leads to just 17 stocks worldwide being specifically excluded (cluster munitions and anti-personnel landmine companies).

For example, within the table on the following pages is the Fidelity European Dynamic Growth Fund⁸ which holds 6.2% in tobacco companies (3.3% BATS, 1.7% Imperial Brands and 1.2% Swedish Match) as at 30th April 2019.






























⁴ [https://www.fidelity.co.uk/planning-guidance/investment-finder/#?investmentType=funds&filtersSelectedValue=%7B%22ethicalFunds%22:%22true%22,%22fidelityFundsOnly%22:%22BN000008QX%22%7D&page=1&perPage=50&sortField=legalName&sortOrder=asc&subUniverselId=MFEI&universelId=FOGBR\\$ALL_3521](https://www.fidelity.co.uk/planning-guidance/investment-finder/#?investmentType=funds&filtersSelectedValue=%7B%22ethicalFunds%22:%22true%22,%22fidelityFundsOnly%22:%22BN000008QX%22%7D&page=1&perPage=50&sortField=legalName&sortOrder=asc&subUniverselId=MFEI&universelId=FOGBR$ALL_3521)

⁵ <https://www.fca.org.uk/publication/feedback/fs19-6.pdf>

⁶ <https://www.fidelity.co.uk/responsible-investing/>

⁷ <https://www.fidelity.co.uk/responsible-investing/>

⁸ https://www.fundslibrary.co.uk/FundsLibrary.DataRetrieval/Documents.aspx/?type=packet_fund_doc_reports_and_accounts&id=f9946b69-21c9-4e8f-9eea-3745a2479dd6&user=H%2fVZBtjpaEbpUyAtjDwYleM%2fIWQbJ7L3gZ6NdzC6Z2W-BLB6NcT3QK8MjqCP4BZTP&r=1

| Add to shortlist | Name ▲ | Negotiated discount(%) ▼ | Yield(%) ▼ | On-going charge(%) ▼ | Asset class ▼ | Morningstar rating ▼ | |
|--------------------------|---|-----------------------------|------------|-------------------------|---------------------------|-------------------------|--|
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - Asia Fund Y-ACC-GBP | – | 0.00 | 1.32 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - Emerging Markets Fund Y-ACC-GBP | – | 0.00 | 1.29 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - Europe Fund W-ACC-GBP | – | 0.00 | 1.28 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - Global Fund Y-ACC-GBP | – | 0.00 | 1.33 | – | ★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - UK Fund Y-ACC-GBP | – | 0.00 | 1.30 | UK | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Active Strategy - FAST - US Fund Y-ACC-GBP | – | 0.00 | 1.29 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - America Fund W-Acc-GBP | – | 0.00 | 1.03 | – | ★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - American Growth Fund W-Acc-GBP | – | 0.00 | 1.05 | – | ★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - American Growth Fund W-Acc-GBP-Hdg | – | – | 1.05 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Asia Focus Fund W-Acc-GBP | – | 0.00 | 1.08 | Asia and Emerging Markets | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Asian High Yield Fund W-Acc-GBP | – | 0.00 | 0.89 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Asian Smaller Companies Fund Y-Acc-GBP | – | 0.00 | 1.10 | Asia and Emerging Markets | ★★★★★ |  Deal |
| <input type="checkbox"/> |  Fidelity Funds - Asian Special Situations Fund W-DIST-GBP | 0.10 | 0.89 | 1.08 | Asia and Emerging Markets | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - China Focus Fund Y-DIST-GBP | – | 2.02 | 1.06 | Asia and Emerging Markets | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Asia Fund W-Acc-GBP | – | 0.00 | 1.09 | Asia and Emerging Markets | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Market Debt Fund W-Acc-GBP | – | 0.00 | 0.90 | Bonds | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Markets Focus Fund W-Inc-GBP | – | – | 1.10 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Markets Fund W-Acc-GBP | – | 0.00 | 1.08 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Markets Fund W-DIST-GBP | – | 0.93 | 1.08 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Emerging Markets Inflation-linked Bond Fund Y-DIST-GBP | – | 2.54 | 0.94 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Euro Blue Chip Fund W-Acc-GBP | – | 0.00 | 1.07 | – | ★★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - European Dividend Fund W-Inc-GBP | – | – | 1.09 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - European Dynamic Growth Fund W-Acc-GBP | – | 0.00 | 1.05 | Europe | ★★★★★ |  Deal |
| <input type="checkbox"/> |  Fidelity Funds - European Growth Fund W-Acc-GBP | 0.10 | 0.00 | 1.04 | Europe | ★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - European High Yield Fund Y-Acc-GBP (hedged) | – | 0.00 | 0.89 | – | – |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Flexible Bond Fund Y-DIST-GBP | – | 2.63 | 0.78 | – | ★★★★ |  Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Communications Fund W Acc GBP | – | – | 1.10 | – | – |  Deal |

continued...

| | | | | | | | | |
|--------------------------|---|---|------|------|------------------------|-------|--|------|
| <input type="checkbox"/> | Fidelity Funds - Global Consumer Industries Fund W-Acc-GBP | - | 0.00 | 1.06 | Global | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Demographics Fund Y-Acc-GBP | - | 0.00 | 1.09 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Dividend Fund W-Acc-GBP | - | 0.00 | 1.04 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Dividend Fund W-QINCOME(G)-GBP | - | 2.55 | 1.04 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Dividend Fund W-QINCOME(G)-GBP (hedged) | - | 2.56 | 1.04 | - | - | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Financial Services Fund W-Acc-GBP | - | 0.00 | 1.06 | Global | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Focus Fund W-Acc-GBP | - | 0.00 | 1.08 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Health Care Fund W-Acc-GBP | - | 0.00 | 1.06 | Global | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Industrials Fund W-Acc-GBP | - | 0.00 | 1.10 | Global | ★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Low Volatility Equity Fund W GBP Inc | - | - | 0.93 | - | - | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Property Fund W-Acc-GBP | - | 0.00 | 1.09 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Global Technology Fund W-Acc-GBP | - | 0.00 | 1.04 | Alternatives and Other | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - India Focus Fund Y-GBP | - | 0.00 | 1.09 | Alternatives and Other | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - International Fund W-Acc-GBP | - | 0.00 | 1.05 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Latin America Fund W-Acc-GBP | - | 0.00 | 1.08 | Alternatives and Other | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Pacific Fund W-Acc-GBP | - | 0.00 | 1.08 | - | ★★★★★ | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Sterling Cash Fund W-Acc-GBP | - | 0.00 | 0.41 | - | - | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Sustainable Water & Waste Fund W Acc GBP | - | - | 1.10 | Global | - | | Deal |
| <input type="checkbox"/> | Fidelity Funds - Sustainable Water & Waste Fund W Inc GBP | - | - | 1.10 | Global | - | | Deal |
| <input type="checkbox"/> | Fidelity Funds - United Kingdom Fund Y-Acc-GBP | - | 0.00 | 1.09 | - | ★★ | | Deal |

Important Note

This report and links found within the report were updated during October 2019. It should be noted that as a result of being contacted by The Sunday Times in connection with an article detailing this report, Fidelity has amended its platform website to remove the ability to search for “socially responsible” funds.

SCM Direct believes that whilst such action is welcomed, it should not be necessary for SCM to continually have to highlight poor practice in the industry. If we had a regulator that was fit for purpose in protecting consumers interests, research reports such as this Greenwashing Report would not be required.

Fidelity Funds on the Willis Owen

SCM conducted the same search as they did on Fidelity's own platform, searching for Fidelity managed "socially responsible funds"⁹ available on the Willis Owen platform (as at October 2019) – both platforms are powered by Morningstar, but just five funds appeared on the Willis Owen platform compared to 49 on Fidelity's platform, none of which had a KIID document referring to an ethical related strategy:

| <input type="checkbox"/> Name | Last Close Price | Yield(%) | Ongoing Charge(%) | IA Sector | Morningstar Analyst Rating™ | Morningstar Rating™ | Morningstar Sustainability Rating™ |
|--|------------------|----------|-------------------|-----------------------------------|--|---------------------|---|
| <input type="checkbox"/> Fidelity Funds - China Focus Fund Y-DIST-GBP | 2.02 GBP | 2.02 | 1.06 | China/Greater China |  Silver | ★★★★★ |  |
| <input type="checkbox"/> Fidelity Funds - Global Dividend Fund W-QINCOME(G)-GBP (hedged) | 1.23 GBP | 2.56 | 1.04 | – | – | – |  |
| <input type="checkbox"/> Fidelity Funds - Global Health Care Fund W-Acc-GBP TRE | 2.00 GBP | 0.00 | 1.07 | Global | – | ★★★★★ |  |
| <input type="checkbox"/> Fidelity Funds - Global Technology Fund W-Acc-GBP TRE | 3.37 GBP | 0.00 | 1.04 | Technology and Telecommunications | – | ★★★★★ |  |
| <input type="checkbox"/> Fidelity Funds - India Focus Fund Y-GBP | 2.59 GBP | 0.00 | 1.09 | Specialist |  Bronze | ★★★★★ |  |

Many of the Fidelity funds e.g. the Fidelity European Opportunities Fund were not classified as "socially responsible funds" on the Willis Owen screening mechanism, but were classified as "socially responsible funds" on the Fidelity screening mechanism (both investments platforms are powered by Morningstar).

IWeb¹⁰

A search for funds according to their "Morningstar sustainability rating type" found several funds which were classified as having a low sustainability rating, even though the fund name and attributes would suggest the opposite. For example, the Kames Global Sustainable Equity fund¹¹ is managed with pre-defined sustainability criteria¹² e.g. not investing in companies involved in adult entertainment, animal testing, gambling, genetic modification, tobacco, weapons and nuclear power and furthermore applying "multiple data sources including data from ESG (environment, social & governance) rating agencies, broker research and primary research" but this received a low Morningstar sustainability rating of 1¹³ (the maximum being 5) as at October 2019.

⁹ [https://www.willisowen.co.uk/explore/explore-funds#?filtersSelectedValue=%7B%22brandingCompany-Id%22:%7B%22id%22:%22BN000008QX%22%7D,%22ethicalFunds%22:%7B%22id%22:%22true%22%7D%7D&page=1&perPage=10&sortField=legalName&sortOrder=asc&universeId=FOGBR\\$ALL_4586](https://www.willisowen.co.uk/explore/explore-funds#?filtersSelectedValue=%7B%22brandingCompany-Id%22:%7B%22id%22:%22BN000008QX%22%7D,%22ethicalFunds%22:%7B%22id%22:%22true%22%7D%7D&page=1&perPage=10&sortField=legalName&sortOrder=asc&universeId=FOGBR$ALL_4586)

¹⁰ <https://www.markets.iweb-shared dealing.co.uk/funds-centre/fund-supermarket/>

¹¹ <https://www.markets.iweb-shared dealing.co.uk/funds-centre/fund-supermarket/detail/IE00BYZJ3441>

¹² <https://www.aegonassetmanagement.com/globalassets/asset-management/netherlands/strategies/documents/ucits/kames-funds/gsef/prospectus-kames-global-sustainable-equity-fund.pdf>

¹³ <https://www.markets.iweb-shared dealing.co.uk/funds-centre/fund-supermarket/detail/IE00BYZJ3441>

Kames Global Sustainable Equity fund ¹⁴

| Top 10 Holdings | | Sectors | | World regions | |
|---|--------|--------------------|--------|---------------|--------|
| Security | Weight | Sector | Weight | Country | Weight |
| Amplifon SpA | 4.42% | Technology | 27.03% | USA | 55.85% |
| Keyence Corp | 4.29% | Healthcare | 25.88% | ITA | 10.13% |
| Insulet Corp | 3.92% | Consumer Cyclical | 19.21% | JPN | 9.60% |
| Everbridge Inc | 3.41% | Industrials | 14.40% | GBR | 6.26% |
| Technogym SpA | 3.35% | Financial Services | 5.20% | AUS | 3.18% |
| Icon PLC | 3.22% | Basic Materials | 4.70% | ESP | 3.01% |
| First Republic Bank | 3.12% | Consumer Defensive | 3.58% | BEL | 2.59% |
| Tesla Inc | 3.05% | | | CAN | 2.50% |
| Albemarle Corp | 3.04% | | | CHN | 2.25% |
| Fidelity National Information Servic... | 2.96% | | | NOR | 2.10% |

| Investment style | Unit type | Morningstar analyst rating™ | Morningstar sustainability rating™ | Eligibility |
|------------------|--------------|-----------------------------|---|--|
| Active | Accumulation | N/A |  | <input checked="" type="checkbox"/> Share dealing <input checked="" type="checkbox"/> SIPP <input checked="" type="checkbox"/> ISA |

Similarly, the SVM All Europe SRI fund received the same low Morningstar sustainability score ¹⁵ (as at October 2019) even though the fund “adopts a positive engagement approach toward investment and enters into meaningful dialogue with companies regarding social and environmental issues.” ¹⁶

| Top 10 Holdings | | Sectors | | World regions | |
|-------------------------|--------|------------------------|--------|---------------|--------|
| Security | Weight | Sector | Weight | Country | Weight |
| Prudential PLC | 6.99% | Financial Services | 24.72% | GBR | 64.68% |
| Norcross PLC | 6.08% | Industrials | 19.53% | FRA | 17.17% |
| DCC PLC | 5.08% | Basic Materials | 16.99% | DEU | 9.80% |
| AXA SA | 4.64% | Consumer Cyclical | 10.49% | NLD | 3.29% |
| Smurfit Kappa Group PLC | 4.33% | Technology | 7.53% | CHE | 2.57% |
| Synthomer PLC | 4.06% | Consumer Defensive | 7.15% | IRL | 2.49% |
| Danone SA | 3.85% | Energy | 5.09% | | |
| Forterra PLC | 3.72% | Healthcare | 4.75% | | |
| Cargill SE | 3.64% | Communication Services | 3.44% | | |
| Informa PLC | 3.43% | Utilities | 0.31% | | |

| Investment style | Unit type | Morningstar analyst rating™ | Morningstar sustainability rating™ | Eligibility |
|------------------|--------------|-----------------------------|--|--|
| Active | Accumulation | N/A |  | <input checked="" type="checkbox"/> Share dealing <input checked="" type="checkbox"/> SIPP <input checked="" type="checkbox"/> ISA |

¹⁴ <https://www.markets.iweb-sharedealing.co.uk/funds-centre/fund-supermarket/detail/IE00BYZJ3441>

¹⁵ <https://www.markets.iweb-sharedealing.co.uk/funds-centre/fund-supermarket/detail/GB00B1FL7V46>

¹⁶ https://www.fundslibrary.co.uk/FundsLibrary.DataRetrieval/Documents.aspx/?type=packet_fund_class_doc_factsheet_private&id=51484fa4-dabe-4475-9be0-48317bbfb32c&user=Z4ZHs%2bjzLBcHQva4YDrMJ36mxxVcPZpwzTLqNT9fpdrIs-DjMaQw7IMixey%2fwGRyD&r=1

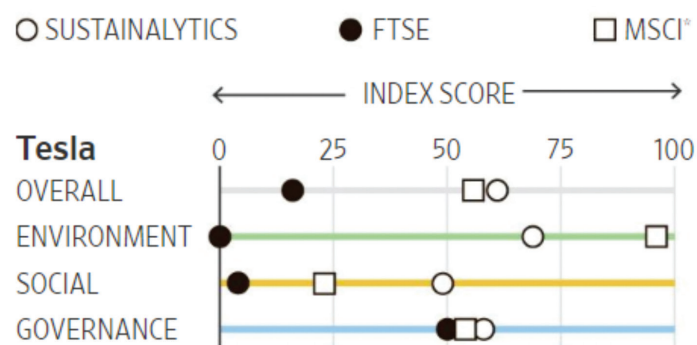
4. Ethical scores and ratings vary enormously between data providers

There is very low correlation between ESG scores for companies according to two leading data providers – FTSE and MSCI.

A big brand example of the variance is Tesla¹⁷ which is ranked by MSCI at the top of the industry, and by FTSE as the worst carmaker globally on ESG issues. Whilst Sustainalytics put them in the middle.

MSCI gave Tesla a near-perfect score for environment, due to its emphasis on the low carbon produced and its clean technology whilst FTSE gave it a “zero” on environment as it only rates the emissions from its factories.

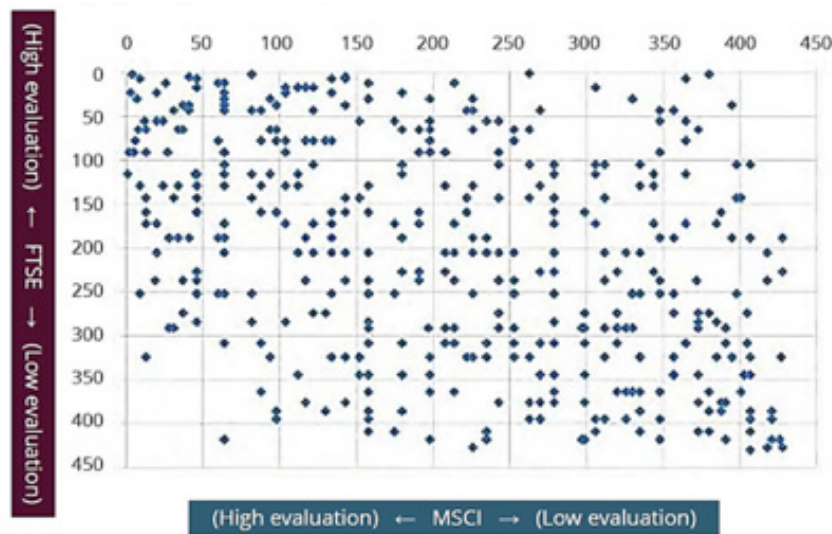
FTSE also assumes a company not disclosing a piece of information receives a low score for the missing item whilst MSCI assumes an average score.



Source: The Wall Street Journal

Investment group, CLSA, analysed 400 ratings from FTSE and MSCI and plotted each company and their evaluation score. You would expect them to be similar, as both index providers ranking companies similarly.

¹⁷ <https://www.wsj.com/articles/is-tesla-or-exxon-more-sustainable-it-depends-whom-you-ask-1537199931>



Source: CLSA, GPIF

The SCM team decided to look at other well-known companies that investors might expect to have a poor ESG rating to see how they fared.

For example:

- Boeing (major defence and aerospace operations)
- BAE Systems (major defence contractor)
- BAT (major tobacco company)
- Exxon Mobil (major oil and gas company).

All these companies received an average ESG rating according to Sustainalytics – where a score of 1 is the worst and 100 is the best.

Boeing¹⁸

Environment, Social and Governance (ESG) Ratings ⓘ

| Total ESG score | Environment | Social | Governance |
|--|-----------------------------|-----------------------------|-----------------------------|
| 52 24th percentile Average Performer | 54 39th percentile | 43 10th percentile | 61 39th percentile |

BAE Systems¹⁹

Environment, Social and Governance (ESG) Ratings ⓘ

| Total ESG score | Environment | Social | Governance |
|--|-----------------------------|-----------------------------|-----------------------------|
| 62 54th percentile Average Performer | 58 46th percentile | 59 54th percentile | 70 79th percentile |

¹⁸ <https://finance.yahoo.com/quote/BA/sustainability?p=BA&tsrc=fin-srch>

¹⁹ <https://finance.yahoo.com/quote/BA.L/sustainability?p=BA.L&tsrc=fin-srch>

British American Tobacco²⁰

Environment, Social and Governance (ESG) Ratings ⓘ

| Total ESG score | Environment | Social | Governance |
|--|-----------------------------|-----------------------------|-----------------------------|
| 65 77th percentile Average Performer | 76 93rd percentile | 60 70th percentile | 57 36th percentile |

EXXON Mobil²¹

Environment, Social and Governance (ESG) Ratings ⓘ

| Total ESG score | Environment | Social | Governance |
|--|-----------------------------|-----------------------------|-----------------------------|
| 64 63rd percentile Average Performer | 55 46th percentile | 75 79th percentile | 58 24th percentile |

(As at october 2019)

It could be argued that with more than 125 ESG data providers in the market since 2016 with no agreed common criteria or benchmarks, according to the Global Initiative for Sustainability Ratings, it is hardly surprising that there is no consensus.

State Street recently found that typically only half of companies analysed had a consistent score between four well known providers²² and that “Most data providers treat their methodologies as proprietary information. By relying on an ESG data provider’s score, asset owners are taking on the perspectives of that provider without a full understanding of how the provider arrived at those conclusions.”

ESG Scores are Different Across Providers
(Cross Sectional Correlation for Constituents of the MSCI World Index, June 30, 2017)

| | Sustainalytics | MSCI | RobecoSAM | Bloomberg ESG |
|----------------|----------------|------|-----------|---------------|
| Sustainalytics | 1 | 0.53 | 0.76 | 0.66 |
| MSCI | | 1 | 0.48 | 0.47 |
| RobecoSAM | | | 1 | 0.68 |
| Bloomberg ESG | | | | 1 |

4.1 No rules or regulations on how ESG data is calculated

According to Bloomberg,²³ “The ESG ratings industry is...much less regulated than the world of credit ratings, with no official standards and qualifications.”

There are no laws or regulations, only guidance from national regulators which has led to different interpretations and standards in different countries.

²⁰ <https://finance.yahoo.com/quote/BATS.L/sustainability?p=BATS.L&tsrc=fin-srch>

²¹ <https://finance.yahoo.com/quote/XOM/sustainability?p=XOM&tsrc=fin-srch>

²² <https://www.ssga.com/investment-topics/environmental-social-governance/2019/03/esg-data-challenge.pdf>

²³ <https://www.bloomberg.com/news/articles/2019-08-11/how-to-tell-if-your-investment-is-really-responsible-quicktake>

This has allowed ‘greenwashing’ to flourish, where funds make an unsubstantiated or misleading claim about the environmental benefits of a product, service, technology or company practice.

Even the FCA has spotted this²⁴:

“There are currently no universally agreed common, minimum standards and guiding principles for measuring the performance and impact of green finance products.” ...

“Issuers do not have a consistent approach to disclosing climate-related risks and it is not clear whether the currently available data are helping investors make informed assessments, or if they may be causing confusion or even distorting markets.”

Recently, the FCA²⁵ stated that:

*“We have carried out some initial diagnostic work on firms’ sustainable product offerings, to gauge whether there is evidence of potential greenwashing. Early indications from this work are that the ‘sustainable’ label is applied to a very wide range of products. **On the face of it, some of these do not appear to have materially different exposures to products that do not have such a label.**”“We will challenge firms where we see potential greenwashing and take appropriate action to prevent consumers being misled.”*

In April 2019²⁶ the head of the International Accounting Standards Body (IASB), which sets the accounting rules followed by 144 countries, admitted that greater reporting on companies’ sustainability is unlikely to make them behave better and that “Greenwashing is rampant.”

He also stated that the IASB had no plans to create its own sustainability reporting standards: *“Setting sustainability reporting standards requires expertise that we simply do not have”.*

This begs the question, who is going to do this work or has the expertise?

4.2 Many ethical funds and strategies found to be investing significant amounts via plain vanilla Government Bonds

Government Bonds are being included in ethical funds or portfolios, and are effectively being classed as “green” by many managers, even though the various governments would

²⁴ <https://www.fca.org.uk/publication/discussion/dp18-08.pdf>

²⁵ <https://www.fca.org.uk/publication/feedback/fs19-6.pdf>

²⁶ <https://www.ft.com/content/fbc6e4f7-bd89-3971-af89-7c007cb57e8c>

not appear to meet the typical constraints set by the same managers for their ethical corporate bonds or equity investments that typically screen out 'sin stocks' including tobacco, gambling, weapons, adult entertainment and nuclear power.

SCM also found that various managers invest via UK and US Government Bonds despite the following facts:

- I. UK Government received taxes from the tobacco industry of £8.8 Bn pa²⁷ during 2017/2018
- II. UK Government received taxes from the gaming industry of £2.86 Bn pa²⁸ from betting and gaming tax receipts during 2017/2018
- III. UK Government has exposure to the nuclear weapons via its Trident nuclear programme²⁹
- IV. UK Government has exposure to the nuclear industry given it has *"been supportive of new nuclear plants"* with 15 Nuclear Power generators in existence³⁰.

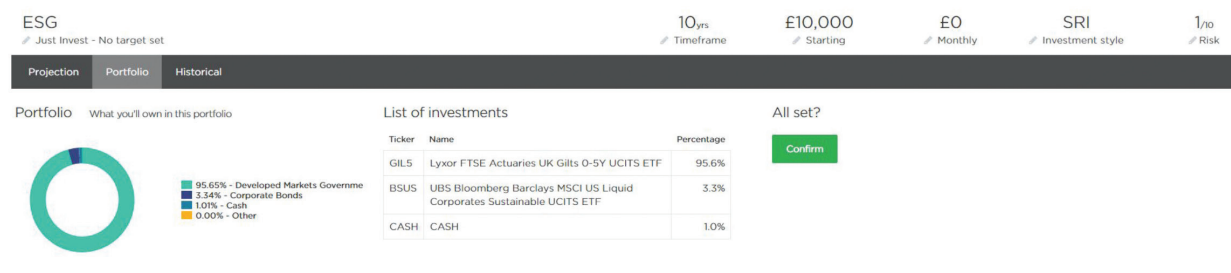
Similar, if not more worrying question marks apply to US Government Bonds, as the U.S. recently announced it would cease all participation in the 2015 Paris Agreement which aimed to reduce the emission of gases that contribute to global warming.

It would appear logical to conclude that if UK and US Government Bonds are deemed to be appropriate for an ethical fund, then every UK or US Government Bond fund should be marketed as an ethical fund, which is plainly nonsensical.

Examples of ethically based portfolios or funds with significant holdings in Government Bonds:

Nutmeg

A client choosing to invest in the lowest risk Nutmeg SRI portfolio would have **95.6%** of their money invested in a plain vanilla UK Government Bond fund and just 3.3% in a specific SRI fund (investing in bonds) as at October 2019:



²⁷ <https://obr.uk/forecasts-in-depth/tax-by-tax-spend-by-spend/tobacco-duties/>

²⁸ <https://www.statista.com/statistics/284338/betting-and-gaming-united-kingdom-hmrc-tax-receipts/>

²⁹ [https://en.wikipedia.org/wiki/Trident_\(UK_nuclear_programme\)](https://en.wikipedia.org/wiki/Trident_(UK_nuclear_programme))

³⁰ <https://www.world-nuclear.org/information-library/country-profiles/countries-t-z/united-kingdom.aspx>

Wealthsimple

Wealthsimple offers a conservative SRI portfolio in which **76%** (as at October 2019) is invested in UK Government Bonds even though its website³¹ states:

"We invest your money across the entire stock market using a range of global SRI funds that are carefully screened and weighted for environmental, social and governance factors, as well as for performance."

| Asset name | Description | Weight |
|--|-------------------------------|--------|
| UBS ETF MSCI UK IMI SRI GBP A dis | UK Equities | 8.04% |
| iShares MSCI USA SRI ETF USD Acc | US Equities | 6.96% |
| iShares MSCI Europe SRI ETF EUR Acc | Europe Equities | 2.11% |
| UBS ETF MSCI Pacific SRI USD A dis | Pacific Equities | 0% |
| iShares MSCI Japan SRI EURH ETF Acc | Japanese Equities | 0% |
| iShares MSCI EM SRI UCITS ETF | EM Equities | 1.78% |
| iShares Global Clean Energy ETF | Global Clean Tech | 1.11% |
| iShares Core UK Gilts UCITS ETF | UK Govt Bonds | 28% |
| UBS Bloomberg Barclays MSCI US Liquid Corporates Sustainable UCITS ETF | US Sustainable Corporate Bond | 4% |
| Lyxor FTSE Actuaries UK Gilts 0-5Y (DR) UCITS ETF | UK Short-term Gilt | 48% |

iFunds

Within its Ethical Cautious Portfolio³², **74%** is invested in Government Bonds, with 25% in UK Government Bonds, 26% in US Government Bonds and 10% in Japanese Government Bonds.

Portfolio allocations - 30th September 2019

| Asset class | Fund (may vary from platform to platform) | % |
|---------------------------|---|-------|
| Global Equities | UBS MSCI ACWI SRI ETF | 17.0% |
| UK Equities | UBS MSCI UK IMI SRI ETF | 8.0% |
| Euro Government Bonds | Vanguard Euro Gov Bond Index Fund | 13.0% |
| US Government Bonds | Vanguard US Gov Bond Index Fund | 26.0% |
| Japanese Government Bonds | Vanguard Japan Gov Bond Index Fund | 10.0% |
| UK Government Bonds | iShares Core UK Gilts ETF | 20.0% |
| UK Inflation Linked Gilts | iShares Index-Linked Gilts ETF | 5.0% |
| Cash | Cash | 1.0% |

³¹ <https://www.wealthsimple.com/en-gb/feature/socially-responsible-investing/>

³² <https://storage.googleapis.com/wzukusers/user-19038165/documents/e4af80e3051744b8b465e81e1d3a2782/iFunds%20Ethical%20Cautious%20factsheet%20Q3%2019.pdf>

Moola

In the Moola Cautious Portfolio³³, investors can expect a **59%** allocation to UK Government Bonds (as at October 2019). Their website states:³⁴

“Only the leading companies are included in your portfolio. Industries considered harmful are excluded from portfolios such as weapons manufacturers, nuclear energy providers, companies involved in gambling or pornography and manufacturers of cigarettes, alcohol or GMOs.”

This statement only refers to holding investments in companies rather than Government bonds.

| MOOLA | | | Exit to main site | Save your progress |
|---------|---|-----------|-------------------|--------------------|
| Ticker | Name | % of fund | | |
| GIL5 LN | Lyxor FTSE Actuaries UK Gilts 0-5 Year UCITS ETF | 53 | | |
| AWSG LN | UBS MSCI World Socially Responsible With Developed Markets GBP Hedged UCITS ETF | 23 | | |
| SUUS LN | iShares MSCI USA Socially Responsible UCITS ETF | 8 | | |
| GILS LN | Lyxor FTSE Actuaries UK Gilts UCITS ETF | 4 | | |
| SDUE LN | iShares MSCI Europe ESG Screened UCITS ETF | 4 | | |
| UKSR LN | UBS MSCI UK IMI Socially Responsible UCITS ETF | 3 | | |
| GILI LN | Lyxor FTSE Actuaries UK Gilts Inflation-Linked UCITS ETF | 2 | | |
| CLIM LN | Lyxor Green Bond UCITS ETF | 1 | | |
| SUSS LN | iShares EUR Corporate Bond Socially Responsible 0-3 Year UCITS ETF | 1 | | |

Wealthify (majority owned by Aviva)

Within the Wealthify Cautious Ethical Portfolio³⁵, investors currently have **52%** invested via UK, US and European Government Bonds (as at October 2019).

³³ <https://moo.la/explore/dash>

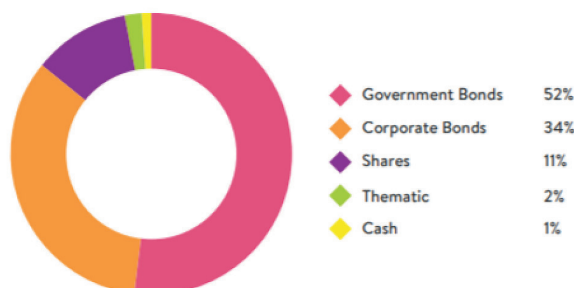
³⁴ <https://moo.la/ethical>

³⁵ <https://invest.wealthify.com/CreatePlan/FactSheet/c07b871c-1735-4f52-a032-7ccae4463cf5?file=pdf>

| Investment | Type | % of Plan |
|---|-----------------|-----------|
| iShares US Short-term Government Bonds Hedged | Government Bond | 25% |
| Royal London Short Duration Government Bonds | Government Bond | 24% |
| Vanguard Euro Government Bonds | Government Bond | 3% |
| Royal London Ethical Bond | Corporate Bond | 8% |
| Rathbone Ethical Bond | Corporate Bond | 8% |
| Royal London Sustainable Managed | Corporate Bond | 8% |
| Edentree Amity Short Duration Bonds | Corporate Bond | 3% |

Investment Mix

This is a typical example of the mix of investments in an Ethical Cautious Plan.



M&G

M&G's Sustainable Multi Asset fund³⁶ states that its "Assets are selected that meet the fund manager's ESG (using an ESG-screening approach) or impact criteria" but SCM could not find within M&G's marketing materials as to how such principles were applied to Government Bonds.

As at the end of April 2019 it held c. **31%** in Government Bonds:

- 6% in European Government Bonds
- 15% in US Government Bonds
- 10% in other Government Bonds.

³⁶ <https://www.mandg.co.uk/investor/funds/sustainable-multi-asset-fund/gb00bhr41h73/>

| Classification of investments | |
|--|-----------------------------|
| The table below shows the percentage holding per sector. | |
| | % of fund as at 30.04.19 |
| EQUITIES | |
| United Kingdom | |
| UK equities | 3.47 |
| Europe | |
| European equities | 16.92 |
| North America | |
| North American equities | 9.51 |
| Japan | |
| Japan equities | 12.23 |
| Asia pacific (ex Japan) | |
| Asia Pacific equities | 7.51 |
| Other | |
| Other equities | 2.46 |
| FIXED INCOME | |
| Europe | |
| European Government bonds | 5.75 |
| Europe investment grade corporate bonds | 0.91 |
| North America | |
| North American Government bonds | 15.30 |
| North America investment grade corporate bonds | 4.14 |
| Global | |
| Global fixed income funds | 1.91 |
| Other | |
| Other Government bonds | 10.45 |
| Other investment grade corporate bonds | 0.46 |
| Other Interest rate futures | (0.13) |
| CURRENCY | |
| Forward currency contracts | 1.09 |

Asset Class Allocation

| | % |
|---------------------------|-------|
| Sterling Equities | 57.32 |
| Sterling Index-Linked | 37.20 |
| Sterling Government Bonds | 3.80 |
| Cash | 1.68 |

AXA

AXA's Ethical Distribution Fund³⁷ held nearly 42% of its fund in UK Government Bonds (including index-linked bonds) in October 2019. AXA states³⁸ that it:

"adheres to a strict ethical investment methodology, screening companies on a range of criteria, in order to determine their suitability for investment" and "also invests in bonds issued by the UK government (gilts), including index-linked gilts, and cash. The screening process only applies to equity holdings (companies) in the portfolio, not to government bonds."

³⁷ https://retail.axa-im.co.uk/document-viewer/-/documents/download/axa_b2c_9161_en

³⁸ <https://retail.axa-im.co.uk/documents/26049/3050092/AXA+Ethical+Distribution+Fund+-+Ethical+Principles+document+update+-+Jun....pdf/5d212b70-5a22-c9d7-8943-e19d7a87268b>

5. Various funds, classified as being “ethical”, found to be investing significant amounts in tobacco, alcohol, gaming and defence stocks

SCM recognises that it is not uncommon to have small exposures to stocks within the tobacco, alcohol, gaming and defence sectors within ESG/SRI funds but was surprised to find several funds in which the total amount invested in such activities amounted to 5% or more of the fund.

L&G Future World ESG UK Index³⁹

“Invests in shares of UK companies as represented by the Index, which is alternatively weighted to give greater weight to companies that score well against environmental, social and governance criteria. This means the Fund will invest more in companies that score well against these criteria, and less in companies that do not.”

The fund as at 31st August 2019, according to Bloomberg, 11.4% of the fund was invested in tobacco, alcohol, gaming and defence stocks.

| Legal & General Future World ESG UK Index fund | %Weight |
|--|--------------|
| Gambling (Non-Hotel Casinos) | |
| WILLIAM HILL PLC | 0.08 |
| Internet Gambling | |
| GVC HOLDINGS PLC | 0.12 |
| 888 HOLDINGS PLC | 0.01 |
| Beverages - Wines/Spirits | |
| DIAGEO PLC | 5.25 |
| Brewery | |
| MARSTON'S PLC | 0.03 |
| Aerospace/Defence | |
| BAE SYSTEMS | 0.64 |
| MEGGITT PLC | 0.17 |
| ROLLS-ROYCE HOLDINGS PLC | 0.68 |
| Aerospace/Defence - Equipment | |
| COBHAM PLC | 0.18 |
| Tobacco | |
| BRITISH AMERICAN TOBACCO PLC | 3.05 |
| IMPERIAL BRANDS PLC | 1.16 |
| Electronics - Military | |
| ULTRA ELECTRONICS HOLDINGS | 0.06 |
| TOTAL | 11.43 |

³⁹ <https://www.legalandgeneral.com/investments/funds/full-fund-range/future-world/future-world-esg-uk-index-fund.html>

Vanguard SRI European Stock Fund⁴⁰

"The Fund employs a passive management or indexing investment strategy designed to achieve the performance of the index, by investing in all, or a representative sample of, index securities that satisfy the application of a screening process for socially responsible investing. The Fund will not hold stocks of companies in the index that do not meet specific "socially responsible" criteria."

According to Bloomberg, this fund as at 31st August 2019, had 5.7% of the fund invested in alcohol, gaming and defence stocks.

| VANGUARD INV SERIES PLC SRI EUROPEAN STOCK | %Weight |
|--|-------------|
| Gambling (Non-Hotel Casinos) | |
| FLUTTER ENTERTAINMENT PLC | 0.03 |
| Internet Gambling | |
| GVC HOLDINGS PLC | 0.04 |
| Beverages - Wines/Spirits | |
| DAVIDE CAMPARI-MILANO SPA | 0.04 |
| DIAGEO PLC | 1.42 |
| PERNOD RICARD SA | 0.61 |
| REMY COINTREAU | 0.06 |
| Brewery | |
| ANHEUSER-BUSCH INBEV SA/NV | 0.86 |
| CARLSBERG AS-B | 0.14 |
| HEINEKEN HOLDING NV | 0.14 |
| HEINEKEN NV | 0.35 |
| Aerospace/Defence | |
| MEGGITT PLC | 0.43 |
| MTU AERO ENGINES AG | 0.53 |
| ROLLS-ROYCE HOLDINGS PLC | 0.40 |
| SAAB AB-B | 0.17 |
| Aerospace/Defence - Equipment | |
| COBHAM PLC | 0.45 |
| TOTAL | 5.67 |

⁴⁰ <https://www.vanguardinvestor.co.uk/investments/vanguard-sri-european-stock-fund-accumulation-shares/portfolio-data>

Morgan Stanley Global Brands Fund⁴¹

The Morgan Stanley investment policy seeks

“to engage with management teams to assess relevant factors material to long term sustainable returns including environmental, social and governance (ESG) factors. The Investment Manager will retain discretion over which investments are selected and ESG factors may not be the sole determinant for selecting an investment.”

The fund’s third largest holding as at the end of September 2019⁴² was the tobacco company, Philip Morris:

| Top Holdings (% of Total Net Assets) ⁴ | FUND | INDEX |
|---|------|-------|
| Microsoft Corp | 8.06 | 2.45 |
| Reckitt Benckiser plc | 7.61 | 0.13 |
| Philip Morris Inc | 6.83 | 0.29 |

5.1 Examples of unusual filters being used for ‘ethical’ funds

Example 1 - Timothy Plan Fund⁴³

- **Marriage** – This screen filters to recognize companies that affirm the marriage covenant – ‘a sacred bond between a man and a woman instituted by and publicly entered into before God.’
- **Life** – This screen seeks to protect the life of the unborn by screening out companies involved in the abortion industry, including foetal tissue research and the manufacturing and distribution of abortifacients.

⁴¹ http://docs.publifund.com/kiid/GB0032482498/en_GB

⁴² https://www.morganstanley.com/im/publication/msfundsuk/factsheet/fs_msfundsuk_globalbrands_iacc_en.pdf?1568301159889

⁴³ https://timothyplan.com/download/eVALUEator_Moral-Audit_Sample-Report-Popular-Mutual-Fund.pdf

Violation Overview

hide

Microsoft Corp.

MSFT *NASDAQ |

One Microsoft Way Redmond, WA, U.S.A. 98052-6399
4258828080 | www.microsoft.com

ABORTION | Philanthropy

Providing charitable aid or donations to non-profit organizations which include foundations that pay for abortions, provide emergency contraception pills, birth control pills and/or pursue "reproductive freedom", like Planned Parenthood, to everyone, regardless of age.

ENTERTAINMENT | Advertiser

Sponsors contribute to the culture of television, either positively or negatively by choosing which programs they support with their advertising dollars. In choosing to spend money on some of the most egregious content on broadcast television, they are supporting shows containing sexually graphic, violent or profane material and ultimately undermine the positive values parents are trying to instill in their young ones.

ENTERTAINMENT | Games

Publishes physical games and/or computer/video games that are sometimes considered controversial, due to the depiction of graphic violence, sexual themes, adver-gaming (a form of advertising in games), simulated gambling, consumption of drugs, consumption of alcohol or tobacco, profanity, propaganda (including same sex encounters), satanic, witchcraft, or anti-Christian themes.

LIFESTYLE | Legislation

Supports federal legislation that affects the lives of lesbian, gay, bisexual and transgender Americans.

LIFESTYLE | Philanthropy

Providing charitable aid or donations to non-profit organizations that include foundations actively pursuing and advancing the alternative lifestyle movement.

LIFESTYLE | Promote

Uses one or more methods to promote gay, lesbian, bisexual, transgender/transsexual, or questioning lifestyles (GLBTQ). This may include advertisements or marketing campaigns targeted to those who choose alternative lifestyles, proudly display or boast being "gay-friendly", and/or provide resources for the advancement of GLBTQ groups (meeting places, materials, etc).

LIFESTYLE | Sponsor

Has formed a business relationship with GLBTQ (gay, lesbian, bisexual, transgender/transsexual, and/or questioning) organization(s) or events. In an attempt to gain marketing and community relations opportunities, money, products or services are exchanged for corporate recognition for their involvement.

PORNOGRAPHY | Games

Publishes computer and/or video games that contain graphic sex or nudity.

Example 2 - SUNARES - Sustainable Natural Resources⁴⁴

Following the ancient Chinese concepts, SUNARES has divided the world of investment into two parts: Yin and Yang, which are binary reciprocal actions for all life on Earth. The 'yin' symbolises the shady side of the mountain and is associated with the basic elements of earth and water, along with the 'female' principle. Conversely, 'yang' stands for the sunny side of the mountain, which is connected to the elements of fire and air (the 'male principle').

The central thesis and basis of SUNARES is the belief that this natural balance of the four basic earthly elements has very much lost its balance due to a disproportionate increase in the 'yang' sector (this concerns all the industries associated with fire and air).

⁴⁴ <https://sunares.com/document/356>

6. Research found significant underperformance against the average actively managed ethical equities fund

SCM analysed 530 ethical mutual funds with a combined total asset of \$207 Bn* and 57 ethical ETFs with a combined total asset of \$34 Bn*, defined by Bloomberg as ethical mutual funds, with an inception date prior to 30/06/2016.

Only primary share class were selected and funds that had no comparable market cap index (such as Gender equality funds) were removed.

The closest available MSCI Index was used as a market cap proxy, save in the following:

- a) US Small Cap - Russel 2000 Index used
- b) US Mid Cap - Russel Mid Cap Index used
- c) US Large Cap - S&P 500 Index used
- d) US Broad - Russel 3000 Index used
- e) UK Broad Market - FTSE UK All Share Index used
- f) Japan 400 (if stated) - JPX Nikkei 400

* As at 02/09/19

SCM Direct found that the average Ethical Equity mutual fund underperformed the market by 2.5% per annum over the three years to end June 2019, compared to 0.8% per annum for the average passive ethical equities fund.

Our view is that the extra underperformance is largely attributable to the significantly higher charges levied by a typical actively managed ethical fund.

| | 30.06.16 - 30.06.17 | 30.06.17 - 30.06.18 | 30.06.18 - 30.06.19 | Annualised |
|-------------------------------|------------------------|------------------------|------------------------|--------------|
| Ethical Equity Mutual Funds | 18.1% | 8.6% | 2.0% | 9.3% |
| Equivalent Market Cap Indices | 20.0% | 11.1% | 4.9% | 11.8% |
| Difference | -1.9% | -2.5% | -2.9% | -2.5% |
| Ethical Equity ETFs | 20.1% | 8.7% | 0.9% | 9.5% |
| Equivalent Market Cap Indices | 20.5% | 10.0% | 1.5% | 10.3% |
| Difference | -0.4% | -1.3% | -0.6% | -0.8% |

Conclusion

The ethical fund industry is a fast-growing both in terms of the amounts invested and the number of funds available.

The FCA recently said⁴⁵ that:

“We will challenge firms where we see potential greenwashing and take appropriate action to prevent consumers being misled.”

Given that investors have chosen to invest their money with extra ethical considerations, it is shameful that the investment industry is prepared to pay lip service to such considerations to gain assets and fees, and even more shameful that the UK regulator⁴⁶ does not appear to have taken any action against firms greenwashing and thereby meet its strategic objective to ensure that markets function well and its operational objective to protect consumers.

Investors deserve better from the industry and regulator alike.

⁴⁵ <https://www.fca.org.uk/publication/feedback/fs19-6.pdf>

⁴⁶ <https://www.handbook.fca.org.uk/handbook/glossary/G2976.html>

IMPORTANT

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