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Financial Insights

WHAT IS RESPONSIBLE INVESTING?

PURSUING A BETTER INVESTMENT EXPERIENCE

CONNECTING WITH 'YOUR FUTURE SELF'

What is Responsible Investing?

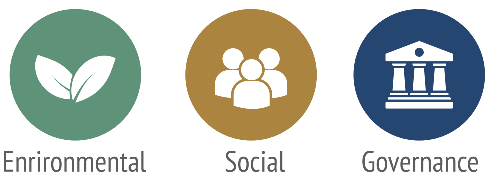
A growing focus for many investors is the area of Responsible Investing and the consideration of ESG (Environmental, Social & Governance) in their investments. Within the investment sector, there is also a clear recognition of the importance of ESG factors in terms of delivering sustainable longer term returns for investors, particularly around key macro themes such as climate change, sustainable infrastructure and natural resource conservation, which will impact on all assets into the future.

ESG investing is sometimes referred to as sustainable investing, impact investing, or socially responsible investing.

Principles for Responsible Investment (PRI)

In early 2005, the then United Nations Secretary-General Kofi Annan invited a group of the world's largest institutional investors to join a process to develop the Principles for Responsible Investment. A 20-person investor group drawn from institutions in 12 countries was supported by a 70-person group of experts from the investment industry, intergovernmental organisations, and civil society. The Principles were launched in April 2006 at the New York Stock Exchange. Since then the number of signatories has grown from 100 to over 3,000.

The PRI defines Responsible Investment as "an approach to investment that explicitly acknowledges the relevance to the investor of environmental, social and governance factors, and of the long-term health and stability of the market as a whole".



Can ESG investments deliver returns for investors?

While responsible investing is considered laudable, it is also sometimes viewed as coming at the expense of returns for investors. Nowadays, many asset managers do not think this is the case and believe that they can adopt ESG metrics and yet still maintain investment returns.

For some fund manager's, it is a strategic issue so much so that it is a core pillar of their business strategy. ESG is a set of criteria used by investors to assess the sustainability of an investment and is increasingly playing a greater part in decisions around where capital should be invested, such as in companies that can prove they have sustainable business practices, including climate-friendly practices or stronger corporate governance practices.

"Investors are increasingly at the forefront of efforts to address sustainability challenges, directing capital to projects and companies working toward a more sustainable global economy, and protecting their own portfolios from sustainability risks.

ESG from an Irish Fund Manager's Perspective:

In an Irish context, one of the largest fund manager's here operates a holistic 3 pillar approach which covers exclusion, integration and active ownership, all of which consider climate change as a key factor.

1. Exclusion: They will be excluding some companies from their investments where their conduct breaches well established globally accepted standards or where their business model centres around activities which investors feel are not consistent with a sustainable economy in the future.
2. Integration: They will include ESG factors into their investment decision making, considering them alongside other traditional factors from a risk management perspective.
3. Active Ownership: They will use their shareholding power to influence corporate behaviour to more sustainable business practices through voting and direct engagement and dialogue.

Building long-term financial security for our clients

At Heritage Wealth, we strongly believe we have a responsibility to create long-term sustainable returns for our clients and that incorporating environmental, social and governance (ESG) factors can have a positive impact on the performance of our clients' investments.

We underpin our approach with the same rigour and analysis as any other investment process and our aim is to materially improve the sustainable characteristics of our investment strategies, while maintaining the risk/return profiles within investor portfolios.

Pursuing a Better Investment Experience

History has shown that the longer you keep your money invested, the greater the chances of a positive outcome. Staying fully invested through a market cycle has, in the past, ensured investors reap greater rewards over the long-term, as rebounds after large losses are often significant.

> *"Throughout your investment journey the markets will experience highs and lows in response to social, political and economic events"*

Timing the markets involves trying to anticipate when these highs and lows will occur, with investors hoping to buy when prices have reached the bottom and sell when they have peaked.

Unfortunately, it is very hard to predict when to buy back in, and getting it wrong means you could end up locking in losses and missing out on future gains. Periods of extreme market volatility (such as that which we are currently experiencing) can heighten feelings of concern in relation to your investments, but staying the course and following our five key investment principles outlined below may help you to increase your chances of a positive outcome.

1. Stay disciplined

Although it may be uncomfortable at times, staying the course and sticking to your strategic financial plan could better serve you in achieving your long-term financial goals.

- By missing just the best 10 days in the market from 2003 to 2017, your investment returns would have been 48% lower.
- Half of the top 10% of days for market gains historically have happened in Bear Markets – so switching your funds after they fall could lead to you missing these upswings.

2. Volatility is part of investing

Markets rise and fall daily, weekly, monthly – it is part of the natural cycle of investing. But historically, each significant market downturn has been followed by an eventual upswing.

- In the U.S., Monday March 23rd 2020 saw the third-best one-day gain for equities since 1945 for the S&P 500, after the two-day rebounds that followed the Black Monday Crash of 1987, and the Lehman Brothers bankruptcy in 2008.
- Despite the infamous 'Black Monday' of 1987, it was still a positive year for equities.
- Despite the last Bull Market being one of the longest on record, we still saw double digit falls in 8 of the 11 years.
- Since 1980, European equities have finished the year in positive territory on 31 of 40 years, yet in each of those years, the market suffered an average intra-year decline of 15.2%.

3. Keeping your money in cash is not the long-term answer

Investors often think of cash as a safe haven in volatile times, or even as a source of income. But the ongoing era of ultra-low interest rates has depressed the return available on cash to near zero, leaving cash savings vulnerable to erosion by inflation over time.

With interest rates expected to remain low, investors should be sure an allocation to cash does not undermine their long-term investment objectives.

- Cash returns remain at record lows.

4. Over the long-term, holding money in 'riskier assets' is rewarded

Short-term market movements are often the result of changes in valuation and sentiment, and how investors feel about the stock market. This contrasts with long-term market movements, which are the result of changes to companies' fundamental worth.

- In any ten-year period, the odds of equities posting positive returns is 96%.
- In any ten-year period, multi-asset funds (mixture of equities, bonds, cash, property and alternatives) have never made a loss.

5. Diversify, Diversify, Diversify

A basic tenet of investing is diversification.

Diversification means spreading risk by mixing a range of asset classes within your portfolio. A well-diversified portfolio might include equities, bonds, alternatives, property, and cash and helps smooth the return over the long run.

- While there is no such thing as a 100% risk-free investment, diversification can mitigate the inherent risk of investing, helping you to reach your long-term financial goals.
- Achieving your long-term goals requires balancing risk and reward. Choosing the right mix of investments and then periodically re-balancing and monitoring your choices can make a big difference in your outcome.

Connecting with 'Your Future Self'

In one of his famous fables, Aesop told us of the grasshopper who spent his Summer singing in the long grasses and generally having a wonderful time, whilst his neighbour the Ant spent that same summer industriously storing up food for winter. As with most fables, the end of the tale came with a clear moral message as the ant enjoyed his food throughout the long harsh winter, whilst the grasshopper wasted away with hunger.

Fast-forward 14 centuries, and what have we learned from this cautionary tale? Reports such as Ireland's national risk assessment (August 2019) which indicated that just 35% of private sector workers have their own pension; and the CFSI pulse report (Nov 2018) stating that up to 42% of adults in the US may not he saving for retirement at all, would suggest that many of us are still opting to live for today, like our friend the grasshopper.

Current Pain for Future Gain?

Behavioural research proposes that one of the reasons many people fail to prioritise their future needs is that they just do not connect with their future selves. In fact, neurological studies have found that our brain activity when thinking about our older selves closely resembles the thought patterns which our brains conjure when thinking about other people.

Our uncertainties as to what will unfold in the future, as well as our tendency to underestimate the pace at which time passes, creates a cognitive dissonance. This disconnection could help explain why many of us are unwilling to sacrifice what we want today, for the sake of what will be good for us in the future.

Building a Connection

Hal Hershfield, a psychologist at the University of California, Los Angeles, has been studying the concept of the 'future self' for over a decade. He proposes writing letters to our future selves as a way of building a connection to the needs and desires of who we will become. Hershfield's research also suggests that seeing digitally aged images of ourselves can encourage this connection even fruther. His research has shown that building this connection can have positive impacts with regards to more than just saving for retirement, with other benefits including exercise and overall lifestyle choices.

"Really taking the time to think about what we want to see, do, feel and experience, will encourage us to move away from the vague and abstract picture of our retirement and take the time to evaluate our current priorities. "

Another recommendation comes from Duke University's professor of psychology and behavioural economics, Dan Ariely. Ariely suggests taking the time to ask a series of questions which engage the imagination and encourage us to really think about the way we want to live in the future. Questions which require specific answers rather than vague assumptions - for example thinking of a specific retirement date in the future - will help forge a stronger connection with our future needs.

One thing is certain - our future selves will look back and thank us!

This article was published in the Voyant 'Voyage' international financial planning magazine in January 2020.

Get In Touch

We want to thank you for taking the time to read our newsletter. If you would like to find out more on any of the items discussed in this edition, feel free to contact us, we are happy to help.

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