CONSIDERATIONS REGARDING THE SOCIAL RESPONSIBLE INVESTMENTS ON CAPITAL MARKET

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ABSTRACT

The social responsibility concept has a dramatic dynamics in the last decades taking in account typology of economic agents involved: transnational corporations, small and medium enterprises and portfolio investors. In this paper, we analyze the development of environment, social and governance (ESG) practices on the European capital market and the active implication of investment consultants and stock exchanges in this field. Taking in account the conclusions of this article, some legal measures could be set up in Romania in order to promote the concept of social responsible investment (SRI) on the local capital market.

KEYWORDS: *investments, social responsibility, capital market, social governance*

The corporate social responsibility –dimensions and functions

The transnational corporations have multiple effects on the host economies and on the entire world economy. Along time, the transnational corporations have been implicated in different social responsibility (SR) programs, and many benefits are registered for local economies and transnational corporations. The social responsibility of transnational corporations gets very specific meanings and characteristics taking into account the fact that they are part of a global economic and social environment, at confluence of levels of rights and obligations determined by the economic and social medium of the home and the host countries.

The first and most important promoters of the SR programs are transnational companies, and the number of signatories of the United Nations Global Compact demonstrates an increased interest for such activities. Thus, [1, 5, 8] in Europe, more than half of the signatories are small and medium enterprises (SMEs), this situation being found in countries such France and Spain. This is understandable given the fact that 90% of European companies are SMEs, and two thirds of the private sector workforce is employed by SMEs.

Beside the social activism of companies, we remark the preoccupations of public authorities and international institutions for the running of SR programs. Growing interest of authorities for social responsibility practices is due because the public policy is not a substitute for SR, but it can contribute to achievement of the public authorities` objectives in certain areas because companies can promote various programs:

- to recruit more people from disadvantaged groups, thus achieving a better integration on labor market and increase social inclusion;
- to prepare the workforce, that remains so competitive in a global economy, and in this way the employment of the population is increasing;
- to promote certain food and non-toxic chemicals or public awareness on the prevention of certain diseases, and this contributes to improvement of public health;
- environmental protection and investment in eco-innovation, thus contributing to a more rigorous use of natural resources and protection.

Some specialists have drawn the attention that companies have an important dilemma regarding the promotion of SR programs. The SR programs bring a competitive advantage to the promoters, but if we take in account the cost of these programs, the positive effect is hard to be measure and the SR friendly companies could being, in the end, less competitive than their less responsible competitors [9]. In addition, the non-SR friendly companies could face with SR risks that may have negative influence on the corporate value and the cost of the capital [2].

The social responsible investment and capital market's actors

The transnational corporations and the small and medium enterprises are not the only economic agents with preoccupations regarding their social responsibility. On the capital market, many investors construct their portfolios and make decisions taking in account environmental, social and governance (ESG) issues like climate change, human rights, labor standards, product safety, poverty reduction or human capital. The result is the launch of new concepts: social responsible investment and sustainable investment. This trend is sustained [11, 14] not only by institutional investors like pensions funds or financial consultants, but also by

- ✓ publicly listed companies that run different social responsible programs,
- ✓ policy makers and regulators that want to offer some legal directions in this fields;
- ✓ accounting and auditing standards boards that offer standards to evaluate social responsible investment (SRI);
- ✓ stock exchanges that impose listing conditions and disclosure guidance, establish specialized trading platforms and launch EGS related traded products, sustainability indices and
- ✓ multilateral bodies like World Federation of Exchanges (WFE) that support the efforts made in this field by exchanges, investors and listed companies.

On the capital market, many investors take into consideration in the portfolio constructions and decision-making process the influence of extra-financial factors like environmental, social and governance issues. The investors that integrate ESG issues into portfolio activity and investment activity are considered *responsible investors*. Therefore, the responsible investors are aware of the extra-financial risks like cohesion risk, reputation risk and embezzlement risk (internal fraud, corruption, forgery and unfair competition) that cause the decrease of the company's value and, in this way, the profits are affected.

The importance of the ESG issues is demonstrated by the official figures regarding the extension of the sustainable investment market. According to professional bodies [14], in USA, around 11% of the assets under professional management are involved in socially responsible investments [6, 10, 13] and in Europe, the share is 17% (Eurosif). In addition, many institutional investors like pensions funds (over 170 pension's funds that manage over $18 trillion) have signed the United Nations Principle for Responsible Investment.

Many exchanges from developed and even developing countries have taken initiatives in order to promote ESG principles among the listing companies; and in this way, the individual and institutional investors have the possibility to make social responsible investment in a facile manner. These initiatives can be divided in three sections.[2, 4, 8, 9]

1. *The exchanges promote ESG standards for the listing companies*. For example, in Malaysia, the listing companies must include in their Annual Report a description of their corporate social responsible investment activities and practices. In China, the most important exchanges – Shenzen Stock Exchange and Shanghai Stock Exchange issued a SR guidance. These initiatives are supported by public authorities – Ministry of Environmental Protections and China Securities Regulatory Commissions have launched a „Green Securities" policy and the listed companies must disclosure more information about their environmental record. Other exchanges have been revised their Corporate Governance Principles or Codes in order to raise ESG awareness among the listed companies.

2. In order to facilitate the investors' selection of social responsible investment, *the exchanges have launched many sustainability indices*. The pioneers and the leaders in the field of indices` constructions are the main securities exchanges: London Stock Exchange Group, NASDAQ OMX and NYSE Euronext. There are also new entrants in this field [12, 13]: the exchanges from countries like China, India, Brazil, Korea, and South Africa. These sustainability indices are set up on the shares issued by listed companies that meet certain ESG criteria. Taking in account the way of construction, these indices are *broad based indices* of stocks from all industry sector (like FTSE KLD Global Sustainability Index, Korean SRI Index or Wiener Borse VÖNIX Sustainability Index), *sector indices* (like NASDAQ OMX Clean Edge Global Wind Energy Index or Deutsche Börse's DAXglobal Alternative Energy Index) and *broad based indices focused on specific ESG issues* (like NYSE Euronext Low Carbon 100 Europe Index).

3. *Some exchanges have been set up specialized markets for specific social responsible investment or there are specialized exchanges where ESG related products are traded.* **O**n BlueNext, carbon another related products like Certified Emission Reduction (CER) credits under the Kyoto Protocol's Clean Development Mechanism and European Union Allowances (EUAs) under the European Emissions Trading Scheme (ETS) are traded on the spot and futures markets. Other exchanges like European Climate Exchange (ECX) and Intercontinental Exchange (ICE) have launched carbon derivatives on EU allowances (EUAs) and certificated emissions reductions (CERs). We remark also the cooperation between Eurex, an important derivatives exchange and a specialized exchange – European Energy Exchange (EEX) in order to advance the ESG goals. The result is the trading of derivatives on the emission rights: CER futures, EUA futures and options on EUA futures.

In this world of sustainable investors, there is an important actor that can promote the integration of ESG issues in investment strategies of institutional investors: the consulting firm. In fact, the consultants are seen as „gatekeepers" taking in account their role in advising individual investors and investment managers of institutional investors. [10]. At international and regional levels, many surveys were conducted in order to observe the implications of consultants in ESG integration in investment strategies, and the results are similar, even the locations are different. According to UNEPI, the consulting firms "observed a growing interest in ESG investment advice among their client base" [13]. Event the interest for ESG integration is growing; many steps must be done in order of further educations of trustees and managers of institutional investors. Some trustees are not conscientious of the importance of selecting managers with ESG expertise and some managers are not interested in promoting ESG integration in investment strategies.

The surveys conducted in USA and Europe revealed that investors are the most important promoters of ESG integration because they make request in this respect to consultant firms. In other cases, the investors are incorporating ESG criteria in the investment strategies because of the existence of regulations and law's provisions [10]. Therefore, until now, the most consultants have a passive role in promoting ESG criteria. In order to improve the institutionalizing of ESG issues in the consultant industry, some world leading consultants have set up teams with full time consultants focused on social responsible investment.

Conclusions

The SRI universe is expanding due to some factors like: the increase of inflows into existing SRI products, the adoption of SRI strategies by managers and investors not previously involved in this field, the development of new SRI products, the effort of consultants in order to provide ESG expertise to their clients, the measures took by stock exchanges that promote ESG principles and offer appropriated products and indices; the promotion of ESG related disclosure laws.

So, there are many implicated parts on the SRI market, but the policymakers play the crucial role because they must ensure the regulatory framework for promotion and disclosure of ESG practices. But, the public authorities must not to be the single promoters of ESG principles. All financial actors (individual and institutional investors, stock exchanges and consultants firms) have to try to implement the ESG strategies in their activities. Even this implementation is not an easy or costless process, the financial actors are aware of the benefits of sustainable investment. [3]. So, they are engages in changes process regarding the management and organization, the investment and financial strategies, the innovation strategies, the advisory process, the personnel selection etc.

The importance of social investment for world economy is demonstrated by the set up of *the Principles of Responsible Investment Initiative* as a voluntary framework supported by UNEP Finance Initiative and UN Global Compact. In present, there are over 830 of signatories of these principles, divided in three categories: asset owners, investment managers and professional service partners. The survey conducted by PRI Imitative in 2010 reveals the implication of investment institutions in ESG integration: over 95% of asset owners and 87% of investment managers promote an investment policy that incorporates the ESG issues; and around 50% of respondents have a dedicated ESG specialist in their organizations. [13]

The stock exchanges are important players on SRI markets because they have the power to established different ESG criteria for listed companies through corporate governance codes and listing regimes and to promote sustainable investment through their ESG related traded products or markets.

In conclusion, the social responsibility programs and initiatives are, in a large extend, voluntary, but public authorities must take certain steps to making the most positive effects on society For example, in Romania, with regard to European experience, some measures could be adopted in order to support the economic agents in promoting social responsibility. The Government may amend regulations regarding the private pension funds in order to obligate them to disclosure information regarding the promotion ESG issues in the investment process (the case of Great Britain since 1996). In addition, the Company Law could be amended so that companies to be required to report how they take in account the interest of stakeholders such as employees, community or the environment (the case of Great Britain since 2002). The Capital Market Law may change and the companies should be obligated to publish annual reports on their social involvement (the case of France since 2001).

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