

## **Socially Responsible Investments: An Ethics Based Approach**

**Dr. Noor Basha Abdul**

Principal , University College of Arts, Commerce & Law, Acharya Nagarjuna University, Guntur

**K. Sarvani**

Assistant Professor, Maris Stella College, Vijayawada

### **ABSTRACT**

*The socially responsible investing (SRI) is a young phenomenon in Indian financial sector. The SRI concept entails investing in companies without compromising on values. Mutual Funds that follow SRI principles look at financial parameters and key ratios before investing in companies, but also consider their values and morals. Ethical investing is Shariah investing guided by Islamic laws. There are two inherent goals of socially responsible investing: social impact and financial gain. This paper mainly focused on the portfolio composition of the select mutual fund schemes and also the financial performance of the select schemes. From the study, it is found that the fund managers are more concerned in diversifying the portfolios by not investing in controversial industries such as tobacco, firearms, alcohol or gambling.*

**Keywords:** *Socially Responsible Investing, Portfolio composition , Financial gain*

### **Introduction**

The socially responsible investing is a young phenomenon in Indian financial sector. Socially responsible investing has come a long way from the days when it mostly meant not buying the shares of companies in controversial industries such as tobacco, firearms, alcohol or gambling. “Socially conscious” investing is growing into a widely-followed practice, as there are dozens of new funds and pooled investment vehicles available for retail investors across the world . Mutual funds and ETFs provide an added advantage to the investors who can gain exposure to multiple companies across many sectors with a single investment. And also the investors are asked to read carefully the prospectuses to determine the exact philosophies being employed by fund managers. There are two inherent goals of socially responsible investing: social impact and financial gain. These two do not necessarily go hand in hand; just because an investment touts itself as socially responsible doesn’t mean that it will provide investors with a good return. An investor must still assess the financial outlook of the investment. As awareness has grown in recent years over global warming and climate change, socially responsible investing has trended toward companies that positively impact the environment by reducing emissions or investing in sustainable or clean energy sources. Consequently, these investments avoid industries such as coal mining due to the negative environmental impact of their business practices.

## **SRI IN INDIA**

For common equity investors in India who wants to invest on SRI theme, availability of readily available investment opportunities (mutual fund or ETF) is scarce. However, S&P and CRISIL had launched an index based on environmental, social and governance (ESG) theme few years back and the index is known as S&P ESG India. The S&P ESG India is an index that provides investors exposure to 50 of the best performing stocks in the Indian equity market as measured by environmental, social, and governance parameters. The index represents the first of its kind to measure environmental, social, and corporate governing practices based on quantitative rather than subjective factors with the implementation of a unique and innovative methodology. The top 10 constituents include Mahindra & Mahindra, Wipro, Infosys, HCL Technologies, ITC, TCS, Tata Chemicals, Dr. Reddy's Laboratories, L&T and ACC. The industries actively traded in this exchange are Software, Banking, Automobiles (4 wheelers), Pharmaceuticals, Power, Cement, Refineries and Steel industry have more than 4% weight-age in the index. The Bombay Stock Exchange, in collaboration with the Taqwaa Advisory and Shariah Investment Solutions — Tasis — has launched an Islamic index in a bid to woo more investors from India and overseas. The new index — BSE Tasis Shariah 50 — was formed using the guidelines of the Islamic investment code and upon the advice of a Shariah advisory board. The index allows investors to trade in the stock markets without violating the Islamic code on investment and finance. The National Stock Exchange already has an Islamic index that is linked to Standard and Poor's Shariah-compliant index. The BSE Tasis Shariah 50 index consists of the 50 largest and most liquid Shariah compliant stocks within the BSE 500. Some of the major stocks that are part of the BSE Tasis Shariah 50 include Tata Consultancy Services, Maruti Suzuki, Bharti Airtel, Reliance Industries Ltd, etc. Two mutual fund schemes are actively traded in this index. They are Tarus Ethical Fund and Tata Ethical Fund. The present study is about these funds

### **Review of literature**

1. Ronald Paul Hill, Thomas Aincough, et al (2006) examined the relationship between corporate social responsibility (CSR) and company stock valuation across three regions of the world. They represented the potential impact of corporate social performance on firm financial performance considering the investor characteristics,
2. Alexander Kempf & Peer Osthoff (2007) investigated the effect of socially responsible investing on portfolio performance. From the study, they found that more and more investors apply socially responsible screens when building their stock portfolios. This raises the question whether these investors can increase their performance by incorporating such screens into their investment process. Based on the above review of literature, the following objectives are framed:

## **PORTFOLIO COMPOSITION OF THE FUNDS:**

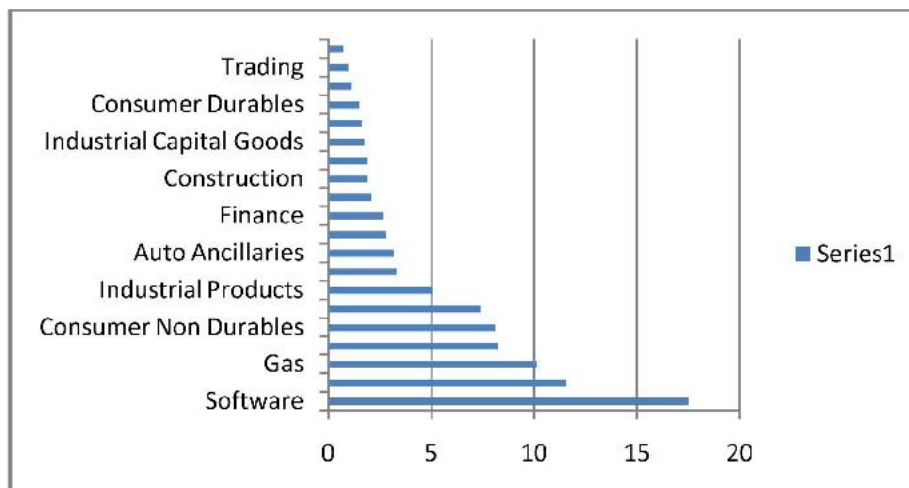
### **1. Taurus Ethical Fund (An Open-Ended Equity Oriented Scheme)**

Taurus Ethical Fund from Taurus Mutual Fund is India's First Actively Managed Equity Oriented Shariah Compliant Diversified Fund. The investments in this fund are based on the fundamentals of Shariah or Shariat, which are guided by the Islamic investment philosophy which invests in companies based on certain screening norms. This fund is managed by seasoned Investment Professionals from Taurus Mutual Fund. The investment objective of this fund is to provide capital appreciation and income distribution to unit holders through investment in a diversified portfolio of equities, which are based on the principles of Shariah.

#### **Features of Taurus Ethical Fund**

- o 1st Actively Managed Shariah Compliant Fund in India Will invest only in Listed Indian Stocks
- o Uses S&P BSE 500 Shariah Index Index as the Benchmark Index
- o The Fund allows a socially responsible form of investing and offers adequate diversification
- o The Fund follows diligent and disciplined investment process with adequate risk controls

**Graph No:1 Representing Portfolio Composition of Tarus Ethical Fund.**



Portfolio composition has decisively moved towards absolute ideas with growth tailwinds. This is despite heavy composition of defensives in benchmark Index. This has caused increase of portfolio beta. Portfolio is underweight in FMCG, Pharma and IT sector while being overweight in Oil and Gas and Capital Goods. Re-alignment in the portfolio has been due to potential broad based recovery in the economy and consequent benefit to Industrial companies in the economy.

## **2. Tata Ethical Fund: (An Open-Ended Equity Oriented Scheme)**

Tata Ethical Fund is an open ended equity fund which invests in a diversified equity portfolio based on principles of Shariah. The investment objective of the scheme is to provide medium to long-term capital gains by investing in Shariah compliant equity and equity-related instruments of well researched value and growth-oriented companies. The asset allocation is 100% investment in equity Shariah Compliant listed, to be listed and unlisted securities of companies and other instruments; if allowed under Shariah principles.

### ***Fundamental principles of the fund***

- o Investments in well-researched value and growth oriented companies from Shariah compliant sectors
- o Avoids investments in companies involved in activities like alcoholic beverages, gaming/ casinos, non halal food products and conventional financial institutional based on Riba (interest)
- o Avoids companies with higher debt to equity ratios and thereby invests in low leverage companies
- o Purification of any prohibited income on yearly basis as advised by Shariah advisor
- o This is more suitable to the investor who are willing to gain long term capital appreciation
- o The investment objective of the Scheme is to provide medium to long-term capital gains by investing in Shariah compliant equity and equity related instruments of well researched value and growth-oriented companies.

Portfolio composition of the Tata Ethical fund has determinedly moved towards categorical thoughts with growth perspective. This is despite heavy composition of defensives in benchmark Index. Portfolio is underweight in Technology, Diversified ,Metals and Consumer Durables sector while being overweight in Automobile ,Engineering ,Health care ,Energy and FMCG sectors . Realignment in the portfolio has been due to potential broad based recovery in the economy and consequent benefit to Industrial companies in the economy.

## ANALYSIS AND DISCUSSION

The comparison between the select mutual fund schemes and benchmark is done to analyse the financial performance of the select mutual fund schemes. This study provides an outlook to the investors who are willing to invest in values added advantage. The study is done on the two following points:

1. Comparing the performance of SRI indices with traditional indices;
2. Comparing the performance of SRI funds with traditional investment funds/indices;

The traditional indices of Taurus Ethical Fund is S&P BSE 200 and SRI indices is S&P BSE 500 Shariah. The mean specifies the average performance of the Fund. Beta signifies the risk profile of the fund. Alpha denotes the market independent return. The traditional indices of Tata Ethical Fund is Nifty 500 Shariah and SRI indices is Nifty 50.

**Table:1 Comparison of Taurus Ethical Fund Vs Equity Benchmark Performance**

Particulars	Taurus Ethical Fund	S&P BSE 500 Shariah	S&P BSE 200
Mean	14.12	13.45	15.66
Standard Deviation	13.79	12.58	14.65
Sharpe Ratio	0.68	0.7	0.75
Beta	0.85	-	-
Alpha	2.74	-	-

Source: Value research online

From the above table, it is clear that the Taurus Ethical fund is performing in a remarkable way when compared to the S&P BSE 500 Shariah market performance as the mean value is more for the fund i.e mean of the Taurus Ethical fund is 14.12 where as mean of the benchmark S&P BSE 500 Shariah is 13.45. The beta value of the scheme is 0.85 which is less than 1 which means that the fund carries only moderate risk. The value of Alpha, the market independent factor of the fund is 2.74 which signifies the fund performance is mostly influenced by the internal factors. Therefore, the SRI funds are attractive to the investors who desire to reap the advantage of investment with added ethics.

**Table:2 Comparison of Tata Ethical Fund Vs Equity Market Performance:**

Particulars	Tata Ethical Fund	Nifty 500 Shariah	Nifty 50
Mean	14.5	16.77	12.59
Standard Deviation	12.79	12.87	14.21
Sharpe Ratio	0.77	0.94	0.56
Beta	0.72	-	-
Alpha	4.09	-	-

Source: Value research online

From the above table, it is evident that the Tata Ethical Fund is performing equivalent good to the performance of Nifty 50 (Equity Market) as the mean value of the fund 14.5 % is more than the equity performance of 12.59%. And also when we considered the risk parameters, the Tata Ethical fund is found comparatively less risky than the equity market risk as the standard deviation of Tata Ethical fund is 12.79 where as the Equity market- Nifty 50 standard deviation is 14.21. The Beta value is 0.72 which is less than 1. It signifies the moderate risk undertaken by the fund. The Alpha value is 4.09, which states the fund financial performance dependency on the fund's internal factors.

### **CONCLUSION**

The chief finding of this research is that socially responsible investing does not result in lower investment returns. This is an important finding because it provides support to individual investors and trustees of institutional funds that they can pursue a program of socially responsible investing with the expectation that investment returns will be similar to traditional investment options.

This seems to be an interesting area of research emerging that indicates that CSR factors are beginning to be incorporated into the markets. It is also being increasingly successful in convincing that investments placed within an SRI portfolio not only support a cause in which the investors believe but also offer prospects of a very good financial return.

### **References**

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