Original Article

The relative importance of ethics, environmental, social and governance criteria

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ABSTRACT

Responsible investing (RI) is a growing phenomenon in the international investment arena. This article investigates the level of knowledge of members of South African pension/provident funds with regard to RI and the importance with which they view various ethical, environmental, social and governance (ESG) criteria. Respondents ($n = 281$) indicated a relatively low level of understanding of the concept of RI. Significant differences were noted in the perceptions of respondents about the relative importance of ethical and ESG criteria based on their gender and level of education. The findings could assist asset owners in reformulating their investment mandates, which in turn, will enable fund managers to invest in a more responsible manner.

Key words: Corporate governance criteria, ethical criteria, environmental criteria, pension/provident funds, responsible investing, social criteria

INTRODUCTION

Although several definitions of the concept of responsible investing (RI) exist, they generally refer to the integration of ethical principles as well as environmental, social and governance (ESG) considerations into investment decision-making and ownership practices. Although many investors still question the rationale and effectiveness of such an approach, empirical evidence shows that RI in developed economies has moved from a fringe investment strategy to a mainstream consideration (Wen, 2009; Derwall *et al*., 2011; Cadman, 2011).

Several authors acknowledge that RI is closely related to the concept of corporate social responsibility (CSR) (Syriopoulos *et al*., 2007; Hill *et al*., 2007). Both concepts support the notion that businesses should generate wealth from limited resources, and assert that this should be done within certain legal, social and environmental frameworks. According to Mill (2006:132), CSR looks at the creation of wealth from the viewpoint of companies, whereas RI considers it from the viewpoint of investors. It is argued that companies will be forced to improve their CSR efforts, should there be more pressure from shareholders to do so (Rehbein *et al*., 2006; Proffitt and Spicer, 2006; Sjöström, 2008; Klein and Zur, 2009; Huppé and Bala-Miller, 2011).

Given the fact that institutional investors own the majority of corporate securities globally (up to 70% in some countries), their role as engaged shareholders and change agents cannot be overemphasised.

In contrast to individual investors (also called private or retail investors), institutional investors manage funds on behalf of clients (or asset owners) such as pension funds, insurance companies, trade unions and religious organisations. Examples of large institutional investors (also called fund or investment managers) in South Africa include the Public Investment Corporation, Sanlam Asset Managers, Investec Asset Management, and STANLIB Asset Management. The actions of institutional investors are guided by the fund mandates of their clients. These mandates typically stipulate the types of securities and regions in which the client would like to invest, as well as performance benchmarks. As representatives of asset owners, institutional investors have a fiduciary duty to act in the best interests of their clients. The can do so by engaging with the boards of investee

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companies, filing shareholder resolutions, voting at meetings of shareholders, and divesting from companies that do not adhere to their requests for improved performance (be it financial or social performance).

Empirical evidence suggests that institutional investors globally are beginning to recognise the power they have to influence corporate decision-making (Vanderkerckhove *et al*., 2007; Becht *et al*., 2010; Poulsen *et al*., 2010). The situation is, however, very different in South Africa (Viviers *et al*., 2009:1; Winfield, 2011). According to a study by Eccles *et al.* (2009:5), the majority of institutional investors in South Africa claim that a range of ESG issues are at least somewhat material in "evaluating the likely performance of investments". The majority, however, said that they are either not concerned with, or had a limited proportion of assets in, responsible investments. At the most, 15% of pension fund assets in the mentioned study were managed under a formal RI mandate. Principal officers of pension funds argue that investing in responsible investments meant lower financial returns, this despite mounting evidence to the contrary (Bauer *et al*., 2005; Fernandez-Izquierdo and Matallin-Saez, 2008; Jones *et al*., 2008; Renneboog *et al*., 2008a; Viviers *et al*., 2008; Drut, 2010; Renneboog *et al*., 2011).

Fund managers in the study by Eccles *et al.* attributed the lack of interest in RI to a lack of demand from asset owners. Crotty (2012a) and Kirima (2012), likewise, argue that the lack of RI, in general, and shareholder engagement, in particular, in South Africa are driven by the nature of investment mandates given by institutional asset owners (particularly pension funds) to fund managers. Regulation 28 of the Pension Funds Act (No. 24 of 1956) requires of all local pension and provident funds to establish an investment strategy that:

(i) takes due account of the objectives of stakeholders, the nature and term of the liabilities, the funding methods used in the fund, including, in the case of a defined contribution fund, any smoothing of investment returns accrued to individual member accounts, and the risks to which the assets and the liabilities of the fund will be exposed;
(ii) sets out the percentages of the total fair value of the total assets of the fund that maybe invested in various classes and categories of assets, and the extent of power that the investment manager will have to diverge from these percentages, with or without the consent of the board;
(iii) should include the criteria according to which investment managers shall be selected, and the manner and frequency of the assessments of their performance.

The board is obliged to consult experts with sufficient skill and experience on an appropriate investment strategy, unless the board itself includes members with sufficient skill and experience to perform this function.

At present, the investment mandates of local pension and provident funds give little consideration to ethical and ESG issues. This can be attributed, amongst others, to pension fund trustees not realising the importance of the management of ethical and ESG risk in the process of wealth creation, and not knowing which criteria to integrate into their investment strategy.

This research, which focusses on the relative importance of a range of ethical and ESG criteria, was conducted from the perspective of pension/provident fund members. This was done to address a gap in the literature, as most studies on the topic only investigate the views of institutional investors (Eccles *et al*., 2009; Herringer *et al*., 2009; Ballestero *et al*., 2012). The findings of this study will assist South African asset owners to reformulate their investment strategies according to the ethical and ESG preferences of their members.

PROBLEM STATEMENT AND RESEARCH OBJECTIVES

In addition to ranking the criteria for ethical and ESG investment in the South African context, this article also investigates the level of knowledge of the members of South African pension/provident funds with regard to RI. To give effect to the primary research objective, a number of secondary research objectives were formulated, namely:

- To conduct an in-depth review of the literature on RI in South Africa
- To construct a research instrument to obtain the views of local pension/provident fund members on RI, the relative importance of ethical and ESG criteria as well as corporate reporting of ESG issues
- To collect and analyse primary quantitative data using appropriate statistical techniques
- To provide pertinent recommendations based on the empirical findings.

REVIEW OF THE LITERATURE

A bewildering array of terms is used in the literature to describe the phenomenon of integrating ethical and ESG considerations into investment decisions and ownership practices. The most commonly used terms include ethical investing, social investing, socially responsible investing, and, more recently, sustainable and responsible investing (Eccles and Viviers, 2011:389).

What does responsible investment entail?

Ethical investing suggests that investments are based on the ethical disposition of the individual investor. Devout members of religious groups, such as Quakers and Methodists, were the first investors who screened their investments for moral acceptability (Schueth, 2003:189; Sparkes and Cowton, 2004:45).

The term 'ethical investing' has increasingly been replaced by the more contemporary term 'socially responsible investing'. Mansley (2000:5) argues that many investors feel uncomfortable using the word 'ethical' to describe investment matters, as it carries religious or moralising overtones. Sparkes and Cowton (2004:45) further argue that the word 'ethical' might imply that mainstream approaches to investment are unethical. By using the term 'socially responsible investing', it is anticipated that some of these preconceptions will be avoided, and that a broader, more positive approach to nonfinancial considerations will be adopted by investors.

Since the launch of the United Nations Principles for Responsible Investment (UNPRI) in 2006, more researchers and practitioners have been using the term 'responsible investing' (e.g., Dembinski *et al*., 2003; Thamotheram and Wildsmith, 2007; Cadman, 2011). Whereas socially responsible investing is deemed more closely linked to a values-based approach, RI is seen to be more focussed on the evaluation of the long-term financial implications of the management of ESG risk in companies (EuroSIF, 2008:6). Given the prominent role that the UNPRI play in promoting RI internationally and in South Africa, the term 'responsible investing' will be used in this article.

The European Sustainable Investment Forum (EuroSIF) (2008:54) distinguishes between eight strategies that responsible investors can employ. These include ethical exclusions, positive screening, best-in-class, RI theme funds, simple screening, norms-based screening, engagement and integration. A full discussion of these strategies, however, falls beyond the scope of this study.

Having defined RI as an investment strategy that incorporates an active consideration of ethical and ESG issues into investment decision-making and ownership, the focus will now turn to the link between RI and CSR.

The link between RI and CSR

Mill (2006:132) argues that, for many investors, RI involves the selection of financial securities from a subset of publicly listed companies that are seen as meeting the criteria for socially and environmentally responsible behaviour. RI and CSR are, thus, closely related phenomena. Mill (2006:132) even asserts that RI and CSR are mirror images of each other.

Researchers such as Solomon *et al.* (2002:3) have long argued that companies are bound to improve their CSR efforts and management of ESG risk, should there be more pressure from shareholders to do so. Shareholders and other stakeholders stand to benefit from intensified activism (Guay, Doh and Sinclair, 2004:125).

Given the fact that pension funds across the globe own the majority of corporate securities, their role in promoting both CSR and RI cannot be overemphasised. In South Africa, too, pension funds, are large and powerful asset owners, with the Government Employees Pension Fund (GEPF) owning almost half of the total retirement savings of the country (Government Employees Pension Fund, 2009; Karima, 2012:80). The GEPF and its investment manager, the Public Investment Corporation, are both signatories of the UNPRI, and are increasingly voicing their concerns about ethical and ESG considerations with the boards of investee companies (Investec's largest investor votes against resolutions, 2012; Crotty, 2012b).

Not all institutional investors in South Africa are as positive about RI as the Public Investment Corporation (Giamporcaro and Pretorius, 2012). This stems mainly from a lack of demand from pension fund trustees (Eccles *et al*., 2009:5). The lack of demand, in turn, could be as a result of pension fund trustees not seeing the link between management of ethical and ESG risk and long-term financial performance. It could also be attributed to a lack of knowledge of the relative importance of ethical and ESG investment in the South African context.

The following section presents an overview of nonfinancial criteria that can be applied when investing in a responsible manner.

Criteria for responsible investment

Over the years, a large number of criteria for RI have been developed by investors who wish to integrate ethical and ESG concerns into their financial considerations. An investigation by Viviers *et al.* (2009:3) of the investment mandates of 43 South African RI funds revealed that local RI fund managers often screen companies based on their Broad-based Black Economic Empowerment (B-BBEE) credentials and programmes to develop social infrastructure and service delivery (such as building houses, roads, schools, health-care facilities, dams, etc.,). Eccles *et al.* (2009:15) also found that local fund managers view development of infrastructure as a very important ESG consideration. As illustrated in Table 1, other material ESG issues in South Africa relate to corporate governance, sustainability, B-BBEE and gender empowerment as well as HIV and AIDS.

Ethical criteria are often based on the religious beliefs of and support for universal human rights by the investor. Table 2 provides examples of religious beliefs and universal human rights that can be used as investment screens. Table 2 also contains the main investment criteria relating to the natural environment and society.

In addition to the criteria listed in Table 2, responsible investors could also formulate criteria relating to suppliers. Three issues highlighted by Schepers and Sethi (2003) are: The promotion of B-BBEE (by purchasing products/services from designated groups), conducting business

Table 1: Perceptions of the materiality of ESG issues in South Africa

Pension funds	Asset managers	Advisory service providers
Corporate governance	Infrastructure development	Infrastructure development
Sustainability	Corporate governance	B-BBEE and gender empowerment issues
Infrastructure development	B-BBEE and gender empowerment issues	Employee relations
HIV and AIDS	Employee relations	Corporate governance
B-BBEE and gender empowerment issues	Sustainability	HIV and AIDS
Employee relations	HIV and AIDS	Sustainability
Environmental management	Environmental management	Environmental management
Human rights	Human rights	Human rights
Health issues	Climate change	Health issues
Climate change	Health issues	Climate change

Source: Eccles *et al*. (2009:15, 18, 20); ESG: Environmental, social and governance; B-BBEE: Broad-based black economic empowerment

Table 2: Criteria for ethics and ESG investment[a]

Religious beliefs and universal human rights

A responsible company should NOT

- Produce products that are harmful to society or that could lead to social ills
- Sell products/services that are in conflict with religious convictions of the investors
- Test products on animals for the development of cosmetics
- Test products on animals for the development of medicines
- Operate in countries where human rights are openly violated
- Operate in countries with oppressive political regimes
- Operate in countries where the rights of women are disregarded
- Operate in countries where minority groups are disregarded
- Operate in countries where corruption in government is rife

Environmental issues

A responsible company should

- Have good policies and practices in terms of Reduce-Reuse-Recycle
- Employ environmentally friendly (green) business practices
- Be proactive in reducing pollution
- Actively reduce the solid waste from their production processes
- Strive to reduce the packaging and waste originating from their products
- Support environmental initiatives
- Use (or be investigating the use of) renewable energy sources
- Not have been fined or prosecuted for breaching any environmental laws
- Engage in carbon-offsetting initiatives

Society in general

A responsible company should

- Promote B-BBEE in innovative ways
- Embrace employment equity practices
- Support initiatives to combat crime

Contd...

Table 2: Continued

- Demonstrate its commitment to combating the HIV/AIDS pandemic through initiatives in the workplace
- Actively engage with government to improve provision of public health care
- Actively promote creation of jobs in South Africa through the support of small and medium-sized enterprises
- Develop rural economies

Employees and trade unions

A responsible company should

- Have comprehensive HIV/AIDS policies and programmes in place for their employees
- Provide antiretroviral drugs to HIV-infected family members of their employees
- Invest heavily in the training and development of their employees
- Have a good track record in protecting the health and safety of their employees
- Have good relations with trade unions
- Not have been involved in court cases relating to unfair labour practices
- Adequately address the needs of disabled employees
- Be known as a 'caring' employer
- Not employ children in their manufacturing facilities

Customers

A responsible company should

- Have a reputation for exceeding the needs of customers
- Market products/services in an ethical manner
- Avoid misleading advertisements
- Produce safe products/services
- Not have been found guilty of unethical marketing practices

[a]The examples provided in this table do not represent an exhaustive list, but merely those criteria most commonly found in the literature. ESG: Environmental, social and governance; B-BBEE: Broad-based black economic empowerment. Sources: Krumsiek (1997); De Vries and De Villiers (1997); Sparkes and Cowton (1998; 2004); Cowton (1998); Johnson and Greening (1999); Schepers and Sethi (2003); Schueth (2003); Haigh and Hazelton (2004); McLachlan and Gardner (2004); Hussein and Omran (2005); Shank *et al*. (2005); Visser (2005); Gay and Klaassen (2005); Boasson, *et al*. (2006); Proffitt and Spicer (2006); Barnett and Salomon (2006); Williams (2007); Renneboog *et al*. (2008b); Statman and Glushkov (2009);

with suppliers that meet local and international labour practices and engaging in environmentally friendly practices. Responsible investors can furthermore evaluate the philanthropic activities of businesses. A number of investment criteria used to determine whether companies engage in philanthropic activities seek to evaluate whether companies:

- donate funds on a regular basis to projects that develop social infrastructure and service delivery, to individuals or organisations in an attempt to strengthen the core business of the firm, to projects that improve the standard of living in previously disadvantaged communities and to local charities;
- support the development of sporting talent on a local and national level as well as the development of the visual and performing arts (Cowton, 1998; Johnson and Greening, 1999; Sparkes and Cowton, 2004; Vermeir *et al*., 2005; Williams, 2007).

Criteria for corporate governance deal with issues such as the composition of the board of directors, accountability and transparency. Researchers such as Cowton (1998), Neubaum and Zahra (2006), and Schepers and Sethi (2003) argue that the most important criterion for governance for domestic companies relates to whether the board of directors mirrors the demographics of the country. As outlined in the three King reports on corporate governance, this issue is particularly important in the South African context. Another important element of governance relates to corporate reporting on ethical and ESG performance.

Corporate reporting on ESG performance

According to a 2005 report by the World Economic Forum (2005), one of the main barriers to the wider acceptance of RI in the global arena is the lack of reliable ESG information (Mainstreaming Responsible Investment, 2005). Hummels and Timmer (2004:73) argue that ESG information is not only important to responsible investors, but to all investors, as failure on the part of companies to manage their ethical and EGS risks could negatively impact on financial performance. Researchers and practitioners alike are thus increasingly calling on companies to expand the range of nonfinancial items on which they report, and to have their sustainability reports externally verified. Despite the fact that all companies listed on the Johannesburg Stock Exchange now have to prepare integrated reports, many responsible investors still find the information insufficient for decision-making purposes.

RESEARCH DESIGN AND METHODOLOGY

A positivistic research paradigm was adopted to determine the relative importance of a range of criteria for ethical and ESG investment in the South African context. As indicated earlier, the research also set out to investigate the level of knowledge of members of South African pension/provident funds with regard to RI.

Measuring instrument

A measuring instrument, based on an in-depth literature review, was constructed in the form of a self-administered questionnaire. Section A requested biographical details of respondents on a nominal scale. Three open-ended questions were phrased, requesting the name of the employer of the respondent, the name of the pension/provident fund to which the respondent made monthly contributions, as well as a telephone number or e-mail address of the respondent (for verification purposes only).

Section B set out to determine whether the respondents were familiar with the concept of RI, and, if so, their definition of it.

Section C consisted of 60 statements on the criteria for ethical and ESG investment. A five-point Likert-type scale ranging from "not important at all" (1) to "very important" (5) was used. Section D dealt with the importance of the reporting of ESG performance. Ten statements on a five-point Likert-type scale, ranging from "not important at all" (1) to "very important" (5) were used to measure the perceptions of the respondents. The last two questions used a nominal scale to establish whether respondents enquired, or were interested in enquiring, about the policy regarding RI of their pension/provident fund.

Population and sample

The target population of this study included the general workforce of the Nelson Mandela Metropole who had contributed to a pension/provident fund in the twelve months preceding the study (July 2009). By virtue of their employment contracts, most employees are members of pension/provident funds. In other cases, members are self-employed individuals who have realised the necessity of saving for their retirement. Members have a direct interest in how the pension/provident fund is managed (as this has a bearing on the size and sustainability of the investment that will be available to them upon retirement); yet, they hardly have any influence on the investment philosophy (mandate) of the fund. Involvement of members in the administration of the pension/provident fund is usually quite limited (they receive communiqués once or twice a year, indicating the value of their investment or changes in the management of the fund or the structure of contribution).

A nonprobability sampling method, namely judgemental sampling, was used to extract the sample. A total of 281 completed questionnaires were suitable for statistical analysis.

Collection and analysis of data

A pilot study among several students and academics in the field of management and statistics at the Nelson Mandela Metropolitan University was conducted. Problems identified in the questionnaire were addressed to ensure face validity. To ensure the reliability of the scores, Cronbach's alpha coefficients were calculated. For scores derived from a measuring instrument to be reliable, this coefficient should be above 0.70 (Gillham, 2004). Primary data were analysed by means of the Statistica 9.0 package. Descriptive and inferential statistics were calculated.

Research hypotheses

The research hypotheses that were empirically tested will now be described.

Gender

The majority of studies on the profile of responsible investors indicate that they tend to be female (Beal and Goyen, 1998:129; Krumsiek, 1997:25). Lewis and MacKenzie (2000:197) attribute this to more women now occupying higher paying positions (and thus becoming savers and investors in ever-increasing numbers). These authors estimate that 60% of all responsible investors in the United States are women. To test whether gender influences the perceptions of pension/provident fund members regarding the relative importance of ethical and ESG criteria, the following null hypotheses were formulated:

$H_{0,1}$: There is no difference in the perceptions of male and female pension/provident fund members with regard to the relative importance of:
$H_{0,1.1}$: Religious convictions and universal rights
$H_{0,1.2}$: Environmental practices and performance of businesses
$H_{0,1.3}$: Philanthropic activities of businesses
$H_{0,1.4}$: Corporate policies and practices pertaining to society in general
$H_{0,1.5}$: Corporate policies and practices pertaining to employees and trade unions
$H_{0,1.6}$: Corporate policies and practices pertaining to customers
$H_{0,1.7}$: Corporate policies and practices pertaining to suppliers

Age

In a study by Rosen and Sandler (1991:221), the average age of responsible investors was 13 years younger than that of conventional investors (39 versus 52). In contrast, Lewis and Mackenzie (2000:179) found that responsible investors tend to be middle aged. Beal and Goyen (1998:129) also established that retired investors tend to be more interested in RI. To test whether age influences the perceptions of pension/provident fund members regarding the relative importance of ethical and ESG criteria, the following null hypotheses were formulated:

$H_{0,2}$: The age of a member of a pension/provident fund has no influence on his/her perceptions of the relative importance of:
$H_{0,2.1}$: Religious convictions and universal human rights
$H_{0,2.2}$: Environmental practices and performance of businesses
$H_{0,2.3}$: Philanthropic activities of businesses
$H_{0,2.4}$: Corporate policies and practices pertaining to society in general
$H_{0,2.5}$: Corporate policies and practices pertaining to employees and trade unions
$H_{0,2.6}$: Corporate policies and practices pertaining to customers
$H_{0,2.7}$: Corporate policies and practices pertaining to suppliers

Level of education

In line with Rosen and Sandler (1991:222), Schueth (2003:189) also established that responsible investors tend to be better educated than conventional investors, with many holding a tertiary education. Responsible investors also tend to be professionals and white-collar employees (Beal and Goyen, 1998:129; Rosen and Sandler, 1991:221).

To test whether their level of education influences the perceptions of pension/provident fund members regarding the relative importance of ethical and ESG criteria, the following null hypotheses were formulated:

$H_{0,3}$: The level of education of a member of a pension/provident fund has no influence on his/her perceptions of the relative importance of:
$H_{0,3.1}$: Religious convictions and universal human rights
$H_{0,3.2}$: Environmental practices and performance of businesses
$H_{0,3.3}$: Philanthropic activities of businesses
$H_{0,3.4}$: Corporate policies and practices pertaining to society in general
$H_{0,3.5}$: Corporate policies and practices pertaining to employees and trade unions
$H_{0,3.6}$: Corporate policies and practices pertaining to customers
$H_{0,3.7}$: Corporate policies and practices pertaining to suppliers

EMPIRICAL RESULTS

A discussion of the results of the study will now follow.

Validity and reliability

The internal validity of the scores of the measuring instrument was ensured through face validity and content validity. Cronbach's alpha coefficients [Table 3] were calculated to establish the reliability of the scores derived from the measuring instrument.

The results in Table 3 suggest that the scores derived from the instrument were all very reliable, as the Cronbach's alpha coefficients were all above 0.7, ranging between 0.86 and 0.95.

Table 3: Cronbach's alpha coefficients for ethical and ESG criteria

Criteria	Cronbach's alpha coefficients	Questionnaire statements
F1: Religious convictions and universal human rights	0.89	Q3.1-3.10
F2: Environmental practices and performance of businesses	0.95	Q3.11-3.21
F3: Philanthropic activities of businesses	0.90	Q3.22-3.27
F4: Policies and practices pertaining to society in general	0.90	Q3.28-3.35
F5: Policies and practices pertaining to employees and trade unions	0.92	Q3.36-3.45
F6: Policies and practices pertaining to customers	0.91	Q3.46-3.53
F7: Policies and practices pertaining to suppliers	0.86	Q3.54-3.60

ESG: Environmental, social and governance

Description of the sample

Table 4 summarises the biographical data of the respondents.

The majority of the respondents were female (52%), older than 40 years (53%), with a tertiary qualification (77%). Of the 281 respondents, five did not indicate their employer, whereas another five indicated that they were self-employed. Employers mainly included large manufacturing companies in the Nelson Mandela Metropole. Several industries were represented in this study, such as the motor manufacturing, education, security, financial and pharmaceutical industries. The majority of respondents (82%) were able to identify the pension/provident fund to which they contributed on a monthly basis. A few provided only the names of the investment manager who administered the pension/provident fund (such as Sanlam or Old Mutual).

Table 4: Biographical data of respondents (*n*=281)

Characteristic	Category	*n*	%
Gender	Male	135	48
	Female	146	52
Age	Younger than 40 years	132	47
	40 years and older	149	53
Highest level of education	Grade 12 or lower	65	23
	Certificate/diploma/B degree	135	48
	Postgraduate studies	81	29

B degree: Bachelor degree

Respondents' understanding of what RI entails

Nearly two-thirds (62%) of the respondents indicated that they were not familiar with the concept of RI, while the rest (38%) indicated that they understood the concept. Of the latter group, only 42% could, however, define RI correctly (or at least had some idea), 36% defined it totally incorrectly and 22% did not provide any definition of their own. Only one in six respondents of the total sample (16%) could define RI correctly. Some incorrect verbatim responses included:

- "Investing in shares over a period of time or having an endowment policy over time-compounded interest."
- "Investing in a balanced portfolio."
- "A way of investing for the unknown future."

A few respondents provided correct definitions, such as:

- "Taking into consideration issues of corporate governance, environment and society through investing."
- "Investment decisions based not only on financial return but also taking into account the impact the company you are investing (in) has on the environment and other socio-economic factors."
- "Taking social, environmental, corporate governance issues into account. investors seeking not to do harm and using investment strategies to promote social good."

Descriptive statistics of the ethical and ESG factors

Table 5 summarises the descriptive statistics of the seven ethical and ESG criteria.

Table 5: Descriptive statistics for the seven ethical and ESG criteria ranked according to mean scores

Criteria	Mean	Standard deviation
F5: Policies and practices pertaining to employees and trade unions	4.24	0.84
F1: Religious convictions and universal human rights	4.03	0.85
F2: Environmental practices and performance of businesses	3.98	0.86
F6: Policies and practices pertaining to customers	3.97	0.79
F4: Policies and practices pertaining to society in general	3.97	0.89
F7: Policies and practices pertaining to suppliers	3.74	0.80
F3: Philanthropic activities of businesses	3.70	0.96

ESG: Environmental, social and governance

The evidence in Table 5 suggests that members of local pension/provident funds attach the most value to investment criteria dealing with corporate policies and practices pertaining to employees and trade unions. Comparing the criteria ranking of individual investors with those of institutional investors in South Africa [Table 1], it is evident that there is a conflict in the rankings. B-BBEE and sustainability issues were seen as the most important criteria by institutional investors, whereas these were regarded as less important by the individual investors in this study. This finding is, however, in line with that of Proffitt and Spicer (2006:165), who found that activist institutional investors in the United States focus mainly on employee- and human rights-related considerations.

The respondents attached the least value to corporate philanthropy; yet, this issue often receives a great deal of attention in sustainability reports and public relations campaigns of companies.

Table 6 provides a summary of the three highest ranking statements within each factor.

The statistics in Table 6 reveal that the respondents attach a great deal of value to the protection of human rights. This is evident from the very high mean scores (>4.2) of statements dealing with promoting the rights of women, avoiding oppressive regimes, preventing child labour, and providing safe working conditions. Although a strong emphasis has been placed on the B-BBEE credentials of South African companies in recent years, this issue is seen by respondents as having low importance (mean scores <2.6).

Table 7 shows the correlations between the seven identified factors.

Most of the factors exhibited a strong positive relationship

Table 6: Top three statements within each factor (n=281)

Statements	Mean	Standard deviation
F5: Policies and practices pertaining to employees and trade unions		
Do not employ children in their manufacturing facilities	4.39	0.99
Have a good track record in protecting the health and safety of their employees	4.23	0.96
Invest heavily in the training and development of their employees	4.19	0.96
F1: Religious convictions and universal rights		
Do not operate in countries where the rights of women are disregarded	4.24	1.09
Do not operate in countries with oppressive regimes	4.23	1.03
Do not operate in countries where corruption in government is rife	4.23	1.08
F2: Environmental practices and performance of businesses		
Are proactive in reducing pollution	4.12	1.02
Encourage their employees to conserve natural resources	4.1	1
Encourage their employees to save electricity	4.05	1.05
F6: Policies and practices pertaining to customers		
Produce safe products/services	4.38	0.85
Have not been found guilty of unethical sales practices	4.34	0.9
Market products/services in an ethical manner	4.3	0.94
F4: Policies and practices pertaining to society in general		
Have not been fined or prosecuted for tax-related offences	4.22	1.08
Support initiatives such as Business Against Crime	4.1	1.01
Actively promote creation of jobs in South Africa through the support of small- and medium-sized enterprises	4.01	1.05
F7: Policies and practices pertaining to suppliers		
Have a clear policy on bribes and kickbacks from suppliers	4.3	0.97
Have not been fined or prosecuted for unethical dealings with suppliers	4.28	0.99
Conduct business with suppliers who meet local and international labour practices	4.1	0.99
F3: Philanthropic activities of businesses		
Donate funds to projects that improve the standard of living in previously disadvantaged communities	3.99	1.13
Donate funds to projects that develop social infrastructure	3.96	1.13
Donate funds to individuals or organisations to strengthen the core business of the firm	3.93	1.08

with the other factors. This finding points to the interrelatedness of ethics and ESG criteria. A very strong positive correlation (r = 0.832) was noted between the factor dealing with employees and trade unions (F5) and the factor dealing with corporate policies and practices pertaining to society in general (F4). In a country plagued by a high level of unemployment, respondents seem to think that companies that create jobs, train employees and treat them fairly are implicitly taking care of society.

Table 7: Correlation between the seven factors dealing with ethical and ESG criteria

Factors	F2	F3	F4	F5	F6	F7
F:1 Religious convictions and universal human rights	0.586	0.433	0.453	0.508	0.502	0.518
F2: Environmental practices and performance of businesses		0.631	0.609	0.670	0.646	0.700
F3: Philanthropic activities of businesses			0.748	0.755	0.434	0.608
F4: Policies and practices pertaining to society in general				0.832	0.539	0.709
F5: Policies and practices pertaining to employees and trade unions					0.643	0.786
F6: Policies and practices pertaining to customers						0.753
F7: Policies and practices pertaining to suppliers						

ESG: Environmental; social and governance

ANOVA and testing of the hypotheses

An analysis of variance (ANOVA) is a statistical test to establish whether the means of two or more groups are equal. To test the stated hypotheses, an ANOVA was performed. This was done on the seven ethics and ESG criteria factors (F1–F7), but not on the 60 individual statements included in the measuring instrument. Table 8 summarises the results of the ANOVA.

Gender

Based on the statistics in Table 9, six of the seven null sub-hypotheses can be rejected, as statistically significant differences were observed in the perceptions of pension/provident fund members, based on their gender. In all six cases, women attached more value to ethics and EGS criteria, compared to men. The finding that women tend to be 'greener' than men is supported in the literature. Özden (2008:40), for example, found that women have a more positive attitude towards the natural environment. Lee (2009:87), likewise, found that women scored significantly higher than men in environmental attitude, environmental concern, perceived seriousness of environmental problems and perceived environmental responsibility.

Age

No statistically significant differences were observed in the perceptions of pension/provident fund members, based on their age. As such, $H_{0,2}$ cannot be rejected. This finding

Table 8: Analysis of variance for the RI criteria factors and the independent variables

Independent variables	Dependent variables	Df	F test	*P* value
Gender	F1: Religious convictions and universal human rights	1.276	10.35	0.001*
	F2: Environmental practices and performance of businesses	1.276	3.97	0.047*
	F3: Philanthropic activities of businesses	1.276	4.84	0.029*
	F4: Policies and practices pertaining to society in general	1.276	8.17	0.005*
	F5: Policies and practices pertaining to employees and trade unions	1.276	5.20	0.023*
	F6: Policies and practices pertaining to customers	1.276	7.69	0.006*
	F7: Policies and practices pertaining to suppliers	1.276	2.93	0.088
Age	F1: Religious convictions and universal rights	1.276	1.12	0.290
	F2: Environmental practices and performance of businesses	1.276	0.34	0.559
	F3: Philanthropic activities of businesses	1.276	1.23	0.269
	F4: Policies and practices pertaining to society in general	1.276	0.09	0.763
	F5: Policies and practices pertaining to employees and trade unions	1.276	0.01	0.935
	F6: Policies and practices pertaining to customers	1.276	0.01	0.916
	F7: Policies and practices pertaining to suppliers	1.276	0.12	0.729
Level of education	F1: Religious convictions and universal rights	2.276	1.32	0.270
	F2: Environmental practices and performance of businesses	2.276	1.12	0.329
	F3: Philanthropic activities of businesses	2.276	5.45	0.005*
	F4: Policies and practices pertaining to society in general	2.276	6.45	0.002*
	F5: Policies and practices pertaining to employees and trade unions	2.276	6.18	0.002*
	F6: Policies and practices pertaining to customers	2.276	1.01	0.364
	F7: Policies and practices pertaining to suppliers	2.276	2.43	0.090

*Statistically significant at the 95% confidence level; RI: Responsible investing; Df: Degree of freedom; As illustrated in Table 8, a number of significant differences exist

Table 9: Results of null hypotheses testing with regard to gender

Null hypothesis: $H_{0,1}$: There is no difference in the perceptions of male and female pension/provident fund members with regard to the relative importance of

Subhypotheses	Outcome of test[a]	Significant differences	Cohen's d[b]
$H_{0,1,1}$: Religious convictions and universal rights	Can be rejected	Females> Males	0.38#
$H_{0,1,2}$: Environmental practices and performance of businesses	Can be rejected	Females> Males	0.27#
$H_{0,1,3}$: Philanthropic activities of businesses	Can be rejected	Females> Males	0.33#
$H_{0,1,4}$: Corporate policies and practices pertaining to society in general	Can be rejected	Females> Males	0.39#
$H_{0,1,5}$: Corporate policies and practices pertaining to employees and trade unions	Can be rejected	Females> Males	0.32#
$H_{0,1,6}$: Corporate policies and practices pertaining to customers	Can be rejected	Females> Males	0.33#
$H_{0,1,7}$: Corporate policies and practices pertaining to suppliers	Cannotbe rejected	Not significant	n/a

[a]See Table 8 for the respective *P* values. [b]Small (0.20<Cohen's d<0.5) and moderate (0.50<Cohen's d<0.80) practical significant differences are indicated by# and *respectively

contradicts existing literature on the topic (Beal and Goyen, 1998:129; Lewis and Mackensie, 2000:179), and might be ascribed to the fact that only two age categories were evaluated in the present study (younger than 40, and 40 years and older). By adding a category for 55 years and older (i.e., members who are closer to retirement), a different picture might have emerged.

Level of education

As indicated in Table 10, three of the seven null subhypotheses can be rejected, as statistically significant differences exist in the perceptions of pension/provident fund members, based on their level of education.

In all three cases, respondents with a higher level of education attached more value to ethics and ESG criteria. This finding corresponds to the literature indicating that more educated individuals tend to be more discerning investors (Rosen and Sandler, 1991:222; Schueth, 2003:189).

Importance of the reporting of ESG performance

Table 11 shows the importance that respondents attach to reporting of ESG performance by local companies. Statements are ranked from the highest to the lowest mean score.

The high mean scores (>3.4) for all ten statements imply that respondents view the reporting of ESG performance by companies as very important. Respondents were particularly concerned about whether companies are members of the Proudly South African campaign. To qualify as a member of this campaign, the products of the companies must have at least 50% local content and be of a high quality, and the companies must engage in fair labour practices and uphold high environmental standards (Proudly South African, 2010). As respondents attached the most value to corporate policies and practices relating to employees and trade unions (F5), it comes as no surprise that investors would like to invest in companies that engage in fair labour practices and are recognised for doing so.

Finally, two open-ended questions were posed on the level

Table 10: Results of null hypotheses testing with regard to level of education

Null hypothesis: $H_{0,3}$: The level of education of a member of a pension/provident fund has no influence on his/her perceptions of the relative importance of

Subhypotheses	Outcome of test[a]	Significant differences	Cohen's d[b]
$H_{0,3.1}$: Religious convictions and universal human rights	Cannot be rejected	Not significant	n/a
$H_{0,3.2}$: Environmental practices and performance of businesses	Cannot be rejected	Not significant	n/a
$H_{0,3.3}$: Philanthropic activities of businesses	Can be rejected	Grade 12 or lower and Cert./Dipl./B degree: Not Grade 12 or lower < postgraduate Cert./Dipl./B degree < postgraduate	0.09 0.54* 0.47#
$H_{0,3.4}$: Corporate policies and practices pertaining to society in general	Can be rejected	Grade 12 or lower and Cert./Dipl./B degree: Not Grade 12 or lower < postgraduate Cert./Dipl./B degree < postgraduate	0.06 0.47# 0.55*
$H_{0,3.5}$: Corporate policies and practices pertaining to employees and trade unions	Can be rejected	Grade 12 or lower and Cert./Dipl./B degree: Not Grade 12 or lower < postgraduate Cert./Dipl./B degree < postgraduate	0.10 0.41# 0.54*
$H_{0,3.6}$: Corporate policies and practices pertaining to customers	Cannot be rejected	Not significant	n/a
$H_{0,3.7}$: Corporate policies and practices pertaining to suppliers	Cannot be rejected	Not significant	n/a

a = See Table 8 for the respective *P* values; b = Small (0.20<Cohen's d<0.5) and moderate (0.50<Cohen's d<0.80) practical significant differences are indicated by # and * respectively.

Table 11: Importance of the reporting of ESG performance

How important is it that your pension/provident fund invests in businesses that	Mean	Standard deviation
Are proudly South African?	3.99	1.06
Clearly communicate their progress (or lack thereof) against stated environmental, social, and corporate governance goals?	3.87	1.04
Annually publish a report on their environmental, social, and corporate governance performance?	3.83	1.10
Receive awards in recognition of excellent corporate governance practices?	3.82	1.10
Follow the sustainability reporting framework of the Global Reporting Initiative to report on environmental, social, and corporate governance performance?	3.75	1.05
Are signatories of the United nations's global compact?	3.69	1.15
Feature in the JSE's socially responsible Investment (SRI) Index?	3.64	1.17
Are showcased in trialogue's annual CSI Handbook as leaders in the field of corporate social investment (CSI) in South Africa?	3.62	1.12
Feature prominently in surveys such as the financial mail/empowerdex Top Empowerment companies survey?	3.62	1.19
Receive awards for reporting on their environmental, social, and corporate governance performance?	3.59	1.16

JSE: Johannesburg stock exchange

of interest of the respondents in the RI policies of their pension/provident funds. The first focussed on whether the respondents had ever enquired about the policy of their pension/provident fund with regard to the evaluation of ethics and ESG criteria when investing the funds of members. Only 11% of respondents indicated that they had enquired about the RI policy of their pension/provident fund in the past. This finding might be ascribed to the low level of involvement/interaction of members with their funds in general.

The second question focussed on whether respondents would enquire about the RI policy of their pension/provident fund within the next six months, given the fact that they were exposed to the concept of RI in this study. In contrast to the 11% who had enquired in the past, a large number (62%) of respondents indicated that they would do so in the future.

SUMMARY AND CONCLUSIONS

The majority of the respondents in this sample could not define RI correctly. It was found that policies and practices pertaining to employees and trade unions are regarded as the most important investment criteria, whereas philanthropic activities of business are seen as the least important. The fact that South Africa is a highly unionised country might explain the reason that labour-orientated criteria obtained the highest mean scores in the sixty RI criteria investigated. Respect for universal human rights and the protection of the natural environment were also seen as important.

The seven ethics and ESG factors investigated in this study showed a high level of correlation and, thus, interrelatedness. This finding lends support to the notion that ethical, sustainable and developmental considerations cannot be considered in isolation when formulating and implementing an investment strategy.

It was further found that gender and level of education play a role in the perceptions of respondents about the relative importance of RI criteria. Females generally regard ethics and ESG criteria as having greater importance than do males. This could be as a result of their socialisation as caregivers (Gilligan, 1982:25), or the fact that they are more risk-averse investors, compared to men (Barber and Odeon, 2001:261). Women have been shown to take greater care in constructing their portfolios, and as having a longer term view (which is better suited to RI). The higher the level of education of the respondent, the greater the perceived importance of philanthropy, corporate policies and practices pertaining to society in general, as well as corporate policies and practices pertaining to employees and trade unions. It could be argued that individuals who are exposed to some form of tertiary education have a broader world view and an awareness of social justice.

Finally, respondents viewed corporate reporting on ESG performance as quite important, and expressed a marked interest in enquiring about the RI policy of their pension/provident fund in the future.

RECOMMENDATIONS

To promote the RI agenda in South Africa (and, through it, CSR efforts and ESG risk management of companies), it is recommended that asset owners take greater cognisance of the preferences of their members in terms of ethical and ESG criteria (perhaps by initiating their own research). They should also reformulate their investment mandates in line with the preferences of members, the requirements of the amended Regulation 28 of the Pension Funds Act (where applicable), the Code for Responsible Investment in South Africa, and the UNPRI (where applicable). This will enable fund managers to invest their assets in a more responsible manner.

Training on the integration of ESG considerations into investment decisions and ownership practices should also be undertaken at all levels of the investment value chain.

As large parts of South Africa are faced with drought as well as an energy crisis, it is essential that all companies pay careful attention to ways to conserve natural resources. With the rapid depletion of the ozone layer and available sources of clean water, it is also important that companies focus on reducing air and water pollution. All employees must be educated on different ways to conserve scarce resources. Top management of companies must be fully committed to ensure that environmentally friendly policies and practices are in place. Concerted efforts should also be undertaken to address the many and varied social challenges facing South Africa.

Future research on the topic could gauge the views of a larger sample of pension/provident fund members across South Africa, and could refine the questionnaire to focus on the issues deemed the most important in this study.

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