Social Impact Ratings: How To Make Responsible Investment Appealing

Winner ex-aequo of the Robin Cosgrove Prize

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Plus de trois mille milliards de dollars sont placés dans les Investissement Socialement Responsables (ISR) à travers le monde.

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The investment sector plays a unique role in promoting ethical practices throughout the economy. With well over three trillion dollars invested in socially responsible investments (SRI) worldwide, environmental, social, governance and ethical factors (collectively, 'social impact factors') have a demonstrable impact on investment practices. SRI investors utilize various methods of influencing corporate practice, including social screening of investments, which can ultimately reward positive social impact with greater access to financing.

This paper proposes a method for incorporating social impact factors as a quantitative parameter in investment analysis and a means of facilitating such analysis in practice. These proposals have the potential to integrate social impact factors into quantitative portfolio management techniques that have traditionally been based only on risk and return.

Very broadly, SRI is the inclusion of any social or ethical criterion in the investment decision-making process. The first instances of socially responsible investing may be the Quakers' rules against investing in arms companies and engaging in the business of slavery as early as the mid-eighteenth century (Kinder, 2005; Kinder and Domini, 1998).

Social screening techniques within SRI

'Ethical exclusions' remain common to this day, as they are applied by investors seeking to avoid companies that manufacture products such as weapons, tobacco, alcoholic beverages, gambling and controversial media. One shortcoming of this mode of SRI is that it is not often clear exactly which companies ought to be excluded from investment. Particularly as companies become larger, more global and increasingly diversified, it is not clear where to draw the line from an SRI perspective.

For instance, a large printing company that makes labels for cigarette cartons might be excluded by an absolute screen on tobacco if even a minuscule percentage of its

Les facteurs environnementaux, sociaux, éthiques et de gouvernance (pris collectivement, « facteurs à impact social ») ont par conséquent un impact démontrable sur les pratiques d'investissement.

Les « exclusions éthiques » restent aujourd'hui courantes, étant appliquées par des investisseurs qui cherchent à éviter les sociétés qui fabriquent des produits tels que armes, tabac, boissons alcoolisées, ou qui sont impliquées dans les jeux de hasard et les médias à scandale.

profits are derived from such products. Furthermore, a company may be legally prevented from refusing to do business with a tobacco company, such as companies that are granted legally-protected monopolies (often in the transportation and telecommunication sectors), which can be required by law to serve all comers. The absolute nature of traditional ethical exclusions makes it increasingly difficult to apply them in a manner that reflects investors' intentions without overly restricting the pool of investment opportunities for socially conscious investors.

Towards the end of the twentieth century the introduction of relative social impact ratings (in contrast with absolute ethical exclusions) enabled more fulsome comparisons of companies on the basis of their social impact. SRI research firms evaluate companies on the basis of a variety of non-financial criteria from a broad stakeholder perspective. Social impact ratings can incorporate environmental sustainability, labour relations practices, community involvement and corporate governance, among other factors. By relying on these broader social impact ratings, 'positive screening' is able to overcome the identification problem encountered with ethical exclusions.

For instance, the social impact rating of a company that manufactures and promotes cigarettes would certainly suffer as a result of its product, while the social impact rating of a company that merely packages or transports the product may suffer only marginally, if at all. In addition, a relative social impact approach rather than ethical exclusion makes it possible to incorporate complex social and environmental factors that are not conducive to absolute determination of investment eligibility. Positive screening based on social impact ratings enables companies to be ranked along a spectrum of relative social responsibility.

A variety of social impact rating systems

Despite significant overlap in the factors assessed by social impact rating providers, the criteria and rating systems differ substantially among providers. Some examples are a numerical system of scores up to twenty (the Total Social Impact Foundation's TSITM Ratings for S&P 500 companies), a letter category system ranging from AAA to D (Reputex Ratings & Research Services' ratings for Australian companies) and a numerical range of positive and negative social impact ranging from +5 to -5 (dotherightthing Inc. ratings for specific events involving a given company).

Other research providers offer a narrative assessment of a variety of social impact criteria for rated companies, rather than distilling the rating to a number or letter (e.g. KLD Research and Analytics, Inc. ratings for S&P 500 and Russell 3000 companies). A proposed means of moving toward a uniform social impact rating system is set forth below.

Un défaut relatif à ce mode d'ISR est qu'il n'est pas toujours évident de déterminer quelles sociétés doivent être exclues de l'investissement.

Les analystes spécialisés dans la recherche ISR évaluent les sociétés cotées sur la base d'un certain nombre de critères non-financiers en tenant compte de l'ensemble des intervenants. Les notations d'impact social peuvent se baser sur le développement durable, les relations de travail, le civisme et la gouvernance, entre autres facteurs.

Social impact ratings can facilitate socially conscious portfolio management based on quantitative methods. In 2001, Summit Mutual Funds, Inc. introduced the Summit Total Social Impact (TSI) Fund. Rather than resorting to ethical exclusions, the fund weighted its investments based on companies' TSI Ratings. The fund included all S&P 500 stocks but reweighted them on the basis of a social impact multiplier consisting of each company's TSI Rating divided by the median S&P 500 score.

Thus, the fund over-weighted companies with higher social impact ratings and under-weighted those with lower ratings. Prior to its closure in 2005, the fund consistently outperformed the S&P 500 Index by about fifty basis points.

Portfolio Social Impact Ratings

The assumption that investors make decisions on a portfolio basis is central to modern portfolio theory because the overall risk of a portfolio changes with the addition of investments that are not perfectly correlated. Hence the benefits of diversification, which can reduce portfolio risk without compromising the expected return of the portfolio. For socially conscious investors who adhere to modern portfolio theory, the introduction of 'Portfolio Social Impact Ratings' can permit investment decisions made on a portfolio basis to consider social impact ratings as well as risk and return.

Unlike portfolio risk, which is a function of the correlation of returns from assets in the portfolio, the social impact ratings of individual companies are independent and uncorrelated. A Portfolio Social Impact Rating can be calculated simply as the weighted average social impact rating of the companies represented in the portfolio. Some issues that could make this calculation more complicated are whether equity and debt investments should be treated in the same manner, whether short positions should offset long positions in calculating social impact ratings and the treatment to be afforded to derivatives. Although these specific questions are outside the scope of this paper, the answers and the general calculation of social impact ratings would benefit from standardization in order to achieve the full quantitative potential of social impact ratings.

Facilitating comparisons

Positive screening techniques demonstrate that social impact ratings can facilitate relative social impact weightings within portfolios rather than resorting to absolute ethical exclusions. Portfolio Social Impact Ratings have the potential to promote a similar transition for the field of fund management as a whole, by facilitating social impact comparisons of all managed investment portfolios including SRI and mainstream investments. For example, retail SRI is presently dominated by a limited, albeit growing array of

Pour les investisseurs socialement responsables qui adhèrent à la théorie moderne du portefeuille, l'introduction de « notations d'impact social d'un portefeuille » peut permettre des décisions d'investissement basées sur de telles notations d'impact social aussi bien que sur le risque et le rendement.

La notation d'impact social d'un portefeuille peut être calculée simplement comme la moyenne pondérée des notations d'impact social des sociétés représentées dans le portefeuille.

SRI mutual funds, so that there is an absolute distinction between SRI and mainstream investments for retail investors. The application of social impact ratings to retail investments is particularly relevant, as SRI mutual funds have recently been the fastest growing segment of SRI in the United States.

As there is already competition among SRI and mainstream fund managers for the attention of socially conscious investors, the ability to make social impact comparisons on the basis of Portfolio Social Impact Ratings could encourage mainstream fund managers to consider social impact in their portfolio management decisions, though not necessarily at the expense of traditional risk and return criteria.

The identification of a 'Socially Dominant Portfolio'

When selecting from among multiple portfolios with similar risk/return characteristics, the socially conscious portfolio investor prefers the portfolio with the highest social impact rating. In other words, a portfolio with a higher social impact rating and given risk/return characteristics dominates (i.e. is preferred to) a portfolio with a lower social impact rating and the same risk/return characteristics.

Similarly, a portfolio with a given social impact rating and more favourable risk/return characteristics dominates a portfolio with the same social impact rating and less favourable risk/return characteristics.

In practice, the socially conscious portfolio investor first identifies the risk-efficient portfolio(s), relying on modern portfolio theory. Given multiple portfolios with a similar degree of risk, the portfolio with the highest expected return dominates. Given multiple portfolios with the same expected return, the portfolio with the lowest degree of risk dominates. The Sharpe ratio is a convenient tool for analyzing expected return and risk in a single measure of the risk-adjusted performance of an asset, portfolio or trading strategy. The Sharpe ratio measures excess returns over the risk free rate divided by the variability of those excess returns, as measured by their standard deviation. According to modern portfolio theory, a portfolio with a higher Sharpe ratio dominates one with a lower Sharpe ratio, subject to any independent parameters, such as the investor's minimum required return and/or maximum level of acceptable risk. The rational investor selects the portfolio with highest Sharpe ratio among those that satisfy the independent parameters, if any.

If multiple portfolios offer the same risk-adjusted returns as measured by the Sharpe ratio, those portfolios are equally risk-efficient. Provided more than one of these portfolios meets any applicable required return and/or maximum risk parameters, the investor must select from among multiple portfolios. In such cases, Portfolio Social Impact

Comme il y a déjà une concurrence entre les gestionnaires de fonds ISR et les autres pour attirer l'attention des investisseurs socialement responsables, la possibilité de faire des comparaisons d'impact social sur la base de la notation de chaque portefeuille peut encourager les gestionnaires traditionnels à prendre en compte l'impact social dans leurs décisions, sans pour autant abandonner les critères établis comme le risque et le rendement.

Ratings can facilitate the identification of a 'Socially Dominant Portfolio'. The socially conscious investor selects the portfolio with the highest Portfolio Social Impact Rating from the risk-efficient portfolios.

In search of social impact rating standards

Despite the analytical potential of social impact ratings, most investors are unable to implement even the simple portfolio management technique described above. Because fund managers generally do not release detailed information regarding their portfolio holdings, most investors lack the information necessary to calculate Portfolio Social Impact Ratings. Furthermore, the process of obtaining social impact ratings and most underlying company data can be time-consuming and costly, even in cases where it is publicly available. Finally, ratings prepared by different social impact researchers are not generally comparable, as there is no universal standard for the criteria and calculation methodology of social impact ratings. In order to fully harness the quantitative potential of social impact ratings, it is necessary to develop a widespread, standardized rating system.

The United Nations' Principles for Responsible Investing (the 'UN Principles', launched in 2006 as an initiative of the UNEP Finance Initiative and the UN Global Compact) have been signed by over 150 signatories including institutional asset owners controlling over two trillion dollars, investment managers managing over three trillion dollars and professional service partners. The UN Principles could form the foundation for standardized social impact ratings. The first and third UN Principles (UNEP Finance Initiative and UN Global Compact, 2006) read, in part, as follows:

'We will incorporate ESG [environmental, social and governance] issues into investment analysis and decision-making processes.

Possible Actions:

- […] Support the development of ESG-related tools, metrics and analyses […];
- Ask investment service providers (such as financial analysts, consultants, brokers, research firms, or rating companies) to integrate ESG factors into evolving research and analysis […].

We will seek appropriate disclosure on ESG issues by the entities in which we invest.

Possible Actions:

- […] Ask for standardized reporting on ESG issues (using tools such as the Global Reporting Initiative);
- Ask for ESG issues to be integrated within annual financial reports […]'.

The signatories to the UN Principles clearly acknowledge that social impact factors are relevant to investment analysis. However, being basic principles rather than clear rules, the UN Principles are not specific

Les signataires des Principes des Nations Unies reconnaissent clairement que les facteurs d'impact social sont pertinents pour l'analyse de l'investissement. Cependant, étant des principes de base et non des règles claires, les Principes des Nations Unies ne sont pas assez spécifiques en eux-mêmes pour pouvoir faciliter l'introduction des notations d'impact social dans les méthodes quantitatives qui sont fondamentales pour la gestion actuelle des investissements.

enough per se to facilitate the incorporation of social impact ratings into the quantitative methods that are central to contemporary investment management. The following discussion proposes a voluntary compliance system of uniform Global Social Impact Rating Standards (the 'Standards') designed to standardize the criteria and calculation of social impact ratings in order to supplement these aspects of the general UN Principles with specific Standards.

The Standards would afford incentive for companies and fund managers to comply voluntarily, despite the associated costs. By setting out clear requirements for compliance, the Standards would also provide a convenient avenue for focused investor pressure to encourage compliance by companies and fund managers.

Rules rather than principles

The most viable means of encouraging uniform social impact ratings and disclosures would be a system of voluntary compliance, similar to that employed by the existing UN Principles, but based on specific rules rather than broad principles.

This means of implementation could be conceptually based on the Global Investment Performance Standards (the 'GIPS®'), which were introduced in 1999 and are administered by the CFA Institute's Centre for Financial Market Integrity. The GIPS are based on rules rather than principles and are widely recognized as the current global best practice in investment performance reporting. While compliance is not mandatory, investment managers claiming compliance with the GIPS must make a variety of prescribed disclosures, avoid other prohibited disclosures and rely on pre-defined uniform calculation methodologies in reporting past performance. The GIPS have fostered investor confidence throughout the world by ensuring 'fair representation, full disclosure and apples-to-apples comparisons' (CFA, 2005) among compliant fund managers. They have been adopted as the country standard for performance reporting in 26 cases, including several developing countries.

The issue of compliance

The proposed Standards would require companies claiming compliance to publicly disclose a standardized rating calculated according to the prescribed methodology together with certain underlying factual disclosures (e.g. workforce demographics, details of environmental impact etc.). Like the GIPS, the Standards would be based on rules rather than principles.

In practice, companies could engage independent rating providers to produce these ratings in much the same manner as companies engage credit rating providers to assess their creditworthiness. In turn, investment managers could claim compliance with the Standards only if the underlying company social impact

Dans cette perspective, la conformité aux Standards pourrait en dernière instance finir par être perçue comme le prix à payer pour obtenir le financement d'une entreprise ou la gestion d'actifs, tout comme bon nombre de sociétés et de gestionnaires de fonds sont disposés à encourir les coûts relatifs à la réglementation actuelle sur les titres.

ratings and the methodology used to compile the Portfolio Social Impact Ratings are prepared in accordance with the Standards. To be successful, the Standards would have to be general enough to provide meaningful data for comparisons among companies and fund managers yet specific enough for those comparisons to offer substantive value to socially conscious investors. They would also have to be adopted by a critical mass of companies and fund managers.

Voluntary compliance would allow market forces to govern the pace of adoption of the Standards. Positive externalities could lead to broad compliance with the Standards despite their voluntary nature. When a voluntary compliance scheme is successful, the value of compliance increases as more entities claim compliance. Based on the increase of SRI funds as a proportion of total investment funds, and particularly the rapid growth of SRI mutual funds, compliance with the Standards could afford a competitive edge to compliant companies with respect to their financing options and to investment managers with respect to their assets under management.

In the extreme case, compliance with the Standards might ultimately be regarded as a necessary cost of obtaining corporate financing or assets under management, much as many companies and fund managers are willing to incur the high cost of securities regulatory compliance in order to be eligible for public investment. Thus, if the Standards are appropriately defined, natural market forces could eventually lead to widespread adoption without legally mandating compliance.

Law is not a viable means

The law is not a viable means of implementing well-formulated Global Social Impact Rating Standards. Foremost, the large number of legal jurisdictions and securities regulators and the persistent lack of harmonization make it logistically unfeasible to require globally uniform social impact ratings and disclosures for all regulated companies and fund managers.

If mandatory Standards were implemented with due attention to the variations among existing regulatory regimes, they would be too broad to offer useful information for investors. On the other hand, if mandatory Standards were specific enough to be valuable for investors, broad legally-mandated compliance would disturb the capital markets by imposing uniform standards through otherwise unharmonized regulatory regimes.

Neither of these options could satisfy both investors and regulators. Despite the present trend in some jurisdictions in Europe and, to a lesser degree, in the US, that requires disclosure of some social impact factors, uniform rules-based Global Social Impact Rating Standards are not a good candidate for implementation through legislation.

Box 1:
Quantitative Application of Social mpact Ratings for a Two Stock Portfolio

The following is an illustration of the quantitative concepts discussed in this paper, based on a simple two stock portfolio of financial services companies using actual economic data. All figures are rounded to two decimal places.

The table below sets forth the assumptions used in this model. Fannie Mae (FNM) and Morgan Stanley (MS), respectively, received the highest (14.6) and lowest (8.2) TSI™ Ratings for financial services companies in the S&P 500, as rated by the Total Social Impact Foundation, an American not-for-profit organization (these ratings are from December 31, 2003, which is the last time for which TSI™ data is available). The expected annual return for each stock is based on analysts' average 2007 target prices and the risk free rate is assumed to be the yield on a 10-year United States Treasury bond at the time of writing (4.69%). The stocks' expected excess returns are their respective expected returns minus the risk free rate. The stocks' standard deviation and correlation are calculated based on their respective excess stock returns over the last ten years. The Sharpe ratio is calculated from this data.

Table 1: Asset characteristics and risk free rate

	Expected Return	Risk Free Rate	Expected Excess Return	Standard Deviation	Sharpe Ratio	Correlation of Excess Returns	Social Impact (TSI) Rating
FNM	8.60%		3.91%	0.26	0.15		14.60
MS	13.90%		9.21%	0.38	0.24		8.20
General		4.69%				0.40	

The following table includes the relevant calculations for each of 11 different combinations of the two stocks, ranging from the portfolio that is 100% invested in MS (portfolio 1) to the one that is 100% invested in FNM (portfolio 11). The table is followed by a narrative of how the proposed quantitative concepts can be applied in practice.

Table 2 : Calculations for various portfolios of FNM and MS

Portfolio	FNM Weight	MS Weight	Expected Portfolio Return	Expected Portfolio Excess Return	Portfolio Standard Deviation	Portfolio Sharpe Ratio	Portfolio Social Impact Rating
1	0%	100%	13.90%	9.21%	0.38	0.24	8.20
2	10%	90%	13.37%	8.68%	0.35	0.25	8.84
3	20%	80%	12.84%	8.15%	0.33	0.25	9.48
4	30%	70%	12.31%	7.62%	0.30	0.25	10.12
5	40%	60%	11.78%	7.09%	0.29	0.25	10.76
6	50%	50%	11.25%	6.56%	0.27	0.24	11.40
7	60%	40%	10.72%	6.03%	0.26	0.23	12.04
8	70%	30%	10.19%	5.50%	0.25	0.22	12.68
9	80%	20%	9.66%	4.97%	0.25	0.20	13.32
10	90%	10%	9.13%	4.44%	0.25	0.17	13.96
11	100%	0%	8.60%	3.91%	0.26	0.15	14.60

Portfolio Social Impact Ratings

For each portfolio, the final column calculates the Portfolio Social Impact Rating based on the weighted average social impact ratings of FNM and MS.

Socially Dominant Portfolios

Pursuant to modern portfolio theory, Portfolios 2, 3, 4 and 5 are risk-efficient portfolios insofar as they offer higher risk-adjusted returns than all other portfolios (i.e. they have the highest Sharpe ratio, 0.25 after rounding). However, assuming each portfolio satisfies any applicable required return and/or maximum risk parameters, these portfolios are equally preferred because they offer a similar Sharpe ratio. Portfolio 5 has a higher Portfolio Social Impact Rating (10.76) than each of Portfolios 2 (8.84), 3 (9.48) and 4 (10.12). On this basis, Portfolio 5 is the Socially Dominant Portfolio and is preferred by the socially conscious investor.

Ainsi, si les Standards sont définis de manière appropriée, les forces naturelles du marché pourraient finalement leur permettre de s'imposer, en l'absence même de législation contraignante.

Furthermore, avoiding a legally mandated compliance model could help to ensure that developing countries are not left behind. If compliance with the Standards was mandated by law, it is conceivable that the less developed capital markets and less robust regulatory regimes that exist in some developing countries could cause these markets to be left out of the initiative altogether.

Natural market forces will set the pace of adoption

An implementation mechanism that relies on voluntary compliance is more capable of permitting companies and fund managers in each market and jurisdiction to comply with the Standards at a pace that is dictated by natural market forces. With globalization of the capital markets and the investment sector, respectively, companies and fund managers increasingly compete for financing and assets under management throughout developed and developing markets. For this reason, implementation through voluntary compliance rather than legislation is the best means of ensuring truly global standards that are eventually adopted by a critical mass of companies and fund managers in all markets.

Notwithstanding the problems inherent to legally mandated compliance, companies and fund managers could still be encouraged to claim compliance with the Standards and provide the relevant disclosures in their regulatory filings as a best practice (e.g. in annual reports, as suggested in the third UN Principle, above). This would invite regulatory sanctions for false claims of compliance, due to the severe repercussions of including misleading information in a regulatory filing.

This means of guarding against false claims of compliance is similar to that employed by the GIPS. While refusing to comply with the GIPS does not violate any law, a false claim of compliance can lead to sanctions. For example, according to the CFA Institute's Centre for Market Integrity, the United States Securities and Exchange Commission has sanctioned investment managers for falsely claiming compliance with the GIPS. Similar to the GIPS, the most viable means of implementing the Standards is a voluntary compliance scheme that relies on regulatory force only to avoid false claims of compliance without actually making compliance mandatory.

Arguments for standardized ratings

At present, a social impact rating provider must define its own rating criteria and calculation methodology, gather relevant information for each company to be rated and calculate and update the social impact rating according to the calculation methodology. This process is complicated and expensive due to the diversity of existing rating systems and limited publicly available information about relevant corporate practices. Widespread adoption of the Standards could be expected to

La recherche requise pour produire des notations d'impact social est chère, du fait qu'elle nécessite un fournisseur spécialisé dans l'élaboration d'un système de notation assorti de critères définis et d'une méthodologie de calcul permettant de comparer les données relatives à chaque société, avant de les intégrer dans une notation d'impact social total.

reduce these costs due to standardization and economies of scale.

Standardized ratings would eliminate the need for each rating provider to develop its own rating scheme and for each company to be rated by several providers. The burden of turning up data relevant to a company's social impact rating would fall to the company seeking to claim compliance rather than external rating providers. The company is in the best position to gather the relevant data, while an independent rating provider is in the best position to provide unbiased evaluations of that data. In this manner the role of the rating provider could evolve from a research function to a corporate service function whereby the rating provider produces ratings in accordance with the pre-defined Standards using data that is furnished by the company. Independent audits are already the norm for environmental sustainability reports and it is quite conceivable that the audit methodology could be standardized and extended to include other social impact factors.

An undifferentiated product

Furthermore, as noted above, there are positive externalities associated with a voluntary compliance scheme because the value of compliance increases as more companies and fund managers comply. The pace of adoption by companies and fund managers can be expected to accelerate with time. Due to standardization, a social impact rating prepared in accordance with the Standards would be an undifferentiated product. As the market for this product grows, an economy of scale would result. In contrast with the present growth of SRI, which has led to more research providers offering competing rating schemes, the service of producing social impact ratings could be commoditized through standardization. The cost of obtaining social impact ratings could reasonably be expected to fall as rating providers compete to offer a standard service in contrast with the present competition to offer a custom product.

Similar to the GIPS, a key benefit of the proposed Standards would be the uniformity of social impact disclosures, which would facilitate reliable comparisons. If widespread voluntary compliance with the Standards can be achieved, the proposed Portfolio Social Impact Ratings and the method for identifying Socially Dominant Portfolios described above would be much more practical for most investors.

Further to these simple proposals for socially conscious portfolio management, more complex quantitative social impact metrics could also be developed once standardized ratings are widely available. Given accepted techniques for the incorporation of social impact ratings into quantitative investment analysis, investors would have the necessary information to make informed socially conscious investment decisions among all available investment portfolios.

Malgré le fait que certains investisseurs ISR, particulièrement ceux qui se basent sur des croyances religieuses, peuvent être tentés par des critères d'exclusions absolus, une sélection positive et une analyse quantitative fondées sur les notations d'impact social relatif recèlent un potentiel élevé pour la plus grande partie de l'univers d'investissement ISR.

By facilitating comparisons among a wide variety of mainstream and SRI investment portfolios on the basis of social impact, the Standards would expand the scope of investment opportunities that are available for consideration by SRI investors.

A great potential

For investors seeking to consider social impact in addition to return and risk, social impact ratings can enable all of these factors to be incorporated into quantitative investment analysis. Portfolio Social Impact Ratings and the concept of Socially Dominant Portfolios supplement modern portfolio theory with an analytical technique for socially conscious investors. Just as the reliance on standard deviation as a quantifiable risk measure has facilitated quantitative risk analysis, social impact ratings have the same potential to apply a quantitative analytical approach to SRI. Some SRI investors, particularly those who base social screens on religious beliefs, may be committed to absolute ethical exclusions. However, positive screening and quantitative analysis based on relative social impact ratings still hold great potential for a large segment of the SRI investing world.

For this potential to be fully realized there must be a uniform social impact rating system. The UN Principles have laid the groundwork for incorporating social impact into investment decisions but specific rules-based standards are necessary to fully realize the analytical value of social impact ratings. Global Social Impact Rating Standards could be developed from the UN Principles if the signatories to the Principles are committed to incorporating social impact factors in quantitative investment analysis. The CFA Institute's GIPS are a good model for voluntary compliance with clear, pre-defined rules that facilitate reliable comparisons. If properly formulated, the Standards could play an important role in bridging the gap between traditional SRI and the quantitative techniques that lie at the root of modern portfolio management. •

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