

WHAT IS responsible investing?

MARCH 2026

Responsible investing has been one of the fastest growing trends in finance over the past few years. Each investment philosophy seeks long-term financial returns through managing risks and identifying opportunities, while prioritising social, ethical and governance-related considerations. Responsible investing is not just an investment strategy, it's a way to have a positive impact on the world.

What are common types of Responsible Investing strategies?

Socially Responsible Investing (SRI) is one of the earliest forms of responsible investment strategies. It focuses on avoiding investments in industries and companies that are considered harmful or unethical. This includes sectors such as alcohol, tobacco, gambling, firearms, and oil or other energy sources that contribute to global warming.

The main goal of SRI is to align investment choices with personal values and societal concerns, ensuring that the investor's money supports positive social and environmental outcomes. By excluding certain industries, SRI aims to promote a more ethical and sustainable approach to investing.

Environmental, Social, and Governance (ESG) investing involves selecting companies that excel in sustainability and ethical practices, ensuring they look after all their stakeholders. This approach integrates environmental, social, and governance factors into the investment decision-making process.

- Environmental considerations: These include how a company addresses climate change, manages waste, and reduces pollution. For example, a company might invest in renewable energy or adopt eco-friendly manufacturing processes.
- Social considerations: These focus on how a company treats its employees and the communities where it operates. Issues like modern slavery, human rights, and labour practices are key.

WHAT IS responsible investing?

A company with strong social practices might have fair labour policies and contribute positively to local communities.

- Governance considerations: These involve the principles and practices that guide a company's leadership and decision-making. Factors such as board diversity, executive remuneration, and transparency are important. Good governance ensures that a company operates ethically and is accountable to its stakeholders.

The underlying assumption of ESG investing is that a company's financial performance is influenced by these factors, in addition to traditional economic factors. This means that companies with strong ESG practices are believed to be better positioned for long-term success and sustainability.

Ethical investing shares similarities with other responsible investing styles, but they tend to be more personalised. This is because ethical investing decisions are based on an individual's own moral principles and lifestyle choices.

For example, an ethical investor might:

- Avoid companies involved in activities they personally find objectionable, such as animal testing or fossil fuels.
- Choose to invest in companies that align with their personal values, such as renewable energy, fair trade, or companies with strong labour practices.

The key difference is that ethical investing is highly individualised, reflecting the unique values and beliefs of the investor. This approach allows investors to create a portfolio that not only seeks financial returns but also aligns closely with their personal ethics and lifestyle.

Sustainable investing applies a positive filter to investment decisions by directing investment capital to companies that are proactively working towards solving environmental problems, such as renewable energy, combatting climate change and/or the destruction of the environment. This is slightly different from ESG investing, where investment decisions may be based on a company not harming the environment, rather than proactively improving it.

Impact investing is similar to ESG investing in that it considers a company's commitment to corporate social responsibility. However, it places a much greater emphasis on creating positive social outcomes. This means that, in addition to looking at environmental, social, and governance factors, impact investing specifically targets investments that generate measurable social benefits.

Examples of areas where impact investing focuses include:

- **Affordable housing:** Investing in projects that provide housing solutions for low-income families.
- **Sustainable agriculture:** Supporting farming practices that are environmentally friendly and sustainable.
- **Healthcare:** Funding initiatives that improve access to medical services and health outcomes.
- **Education:** Investing in educational programs and institutions to enhance learning opportunities.
- **Micro-financing:** Providing small loans to entrepreneurs in developing nations to help them start or grow their businesses.

The goal of impact investing is to achieve both financial returns and positive social or environmental impacts, particularly in areas that need it the most, such as developing countries. This approach aligns financial goals with broader societal benefits, making it a powerful tool for driving change.

Faith-based investing involves selecting stocks and other assets based on specific religious values and ideals, with the goal of ensuring the investments align with the ethical and moral principles of a particular faith.

WHAT IS responsible investing?

For example, a faith-based fund might:

- Avoid investing in companies involved in activities that are considered unethical or immoral according to their religious beliefs, such as gambling, alcohol, or tobacco.
- Focus on companies that promote positive social values, such as charitable work, community support, and ethical business practices.

The goal of faith-based investing is to achieve financial returns while staying true to the investor's religious convictions and promoting values that are important to their faith community.

The Responsible Investment Association of Australasia (RIAA) has developed a good framework for understanding the various types of Responsible Investing styles. Further details can be found here: https://responsibleinvestment.org/what-is-ri/ri-explained/.

Why is Responsible investing growing in popularity?

There are generally four key drivers behind the rising popularity of responsible investing.

1. A growing awareness regarding the impact of external factors such as climate change and supply chain issues. After many years of foundational efforts to standardise and enable sustainable investing, the COVID-19 pandemic has focused investors on the vulnerability and resilience of the financial system and intensified discussions around sustainability.

2. Potential for outperforming returns. According to Morgan Stanley Institute for Sustainable Investing, sustainable funds outperformed traditional peer funds and reduced investment risk during coronavirus in 2020[1]. It is believed that there is a positive relationship between a company's relative market performance and its sustainability rating. This is attributable to the idea that a company focused on sustainability issues is an indication of a quality Board and business management practices.

3. Resilience. Companies that operate with high standards of sustainability are likely to be resilient during uncertain times. They could perform better in areas such as customer relations, supply chain, sustainability, and culture. They could also be more resistant to threats caused by governance and sustainability issues.

4. Regulation. Globally many countries are starting to develop policies focused on sustainability. Some jurisdictions have started to introduce legislations designed to address key ESG issues. For example, Australia introduced the Modern Slavery Act 2018, which requires certain companies to report on modern slavery risks in their supply chains.

Responsible investing metrics

Responsible investing metrics are tools used to evaluate a company's exposure to various risks, such as environmental, social, and governance (ESG) risks. These metrics help investors, such as fund managers, understand how well a company manages these risks and aligns with responsible investing principles.

However, there is no standardised method for calculating or presenting ESG metrics. Different analytical approaches can be applied, and companies may prioritise different areas based on their values and business strategies. This means that not all ESG issues are given equal weight by every company.

Just as investors have diverse values and motivations, companies also vary in how they address responsible investing issues. This lack of standardisation can make it challenging to compare companies directly, but it also allows for a more tailored approach to investing based on individual preferences and priorities.

1. Morgan Stanley, Sustainable Funds Outperform Peers in 2020 During Coronavirus, available at https://www.morganstanley.com/ideas/esg-funds-outperform-peers-coronavirus viewed 4 February 2025

WHAT IS responsible investing?

Environmental

Conservation of the natural world

- Biodiversity
- Climate change
- Carbon footprint
- Deforestation
- Greenhouse gas (GHG) emissions
- Recycling
- Resource depletion
- Waste and pollution
- Water and energy efficiency

Social

Consideration of people & relationships

- Child labour and slavery
- Community engagement
- Employee diversity, treatment, and compensation
- Equal opportunities
- Ethical supply chain sourcing
- Health and safety
- Human rights
- Philanthropy
- Working conditions

Governance

Standards for running a company

- Board diversity and structure
- Bribery and corruption
- Business ethics
- Compliance
- Executive remuneration
- Political lobbying and donations
- Tax strategy
- Whistleblowing schemes

How can I incorporate responsible investing into my portfolio?

Incorporating a Responsible Investment philosophy into your investment portfolio can be done in several ways. One approach is to invest directly in shares of companies that meet your Responsible Investment criteria. However, this requires significant research and knowledge, which not all investors may have.

A more accessible option is to invest in socially responsible, ESG, or other ethical-style funds. These are managed funds and exchange-traded funds (ETFs) specifically designed to include companies or other investments that adhere to various socially responsible criteria. Portfolio managers of these funds carefully select companies that comply with their adopted principles, making it easier for investors to gain exposure to responsible investing without needing to pick individual stocks themselves.

If you're interested in this approach, we recommend you discuss it with your financial adviser. They can help you incorporate socially responsible funds into your investment portfolio and ensure that your investments align with your values and financial goals.

WHAT IS responsible investing?

What approaches do fund managers undertake to apply responsible investing?

When assessing an investment universe for socially responsible attributes, fund managers use various screening methods to narrow down the companies they can invest in. These methods can vary depending on the fund manager's perspective on different factors.

- Negative screening: This involves excluding certain industries or companies, such as those generating revenue from tobacco, gambling, armaments, or adult entertainment. Other activities like junk food, genetic engineering, or logging might also be screened out. Depending on the investor's beliefs, they might apply a hard screen (completely excluding an industry or company) or exclude companies that generate more than a certain percentage (e.g., 10%) of their revenue from these negative sectors.
- Positive screening: Fund managers look for companies in industries they want to invest in from a responsible investing perspective, such as renewable energy, wind, and solar farms.
- Thematic investing: This approach focuses on investing in specific themes or trends rather than individual companies. In responsible investing, this could mean investing in trends like sustainable farming, clean technology, or health.
- Impact investing: This involves investments that generate both financial returns and measurable social and environmental benefits. For example, investing in affordable housing.

The goal of the fund manager is to ensure that the companies they invest in align with their responsible investing beliefs and achieve the desired outcomes. Each investment vehicle has its own specific definition of what responsible investing means to them, the factors they want to invest in, and the attributes they look for in a sector or company.

Your financial adviser will be able to recommend responsible investment fund managers that are suitable to your needs.

WHAT IS responsible investing?

Common responsible investing terms

Here's a brief overview of the key terms related to responsible investing:

- **Active ownership**: Using shareholder power to influence corporate behaviour through direct engagement, filing shareholder proposals, and proxy voting based on ESG guidelines.
- **ESG (Environmental, Social, and Governance)**: The three main criteria used by responsible investors to screen and select companies for their portfolios.
- **ESG integration**: Systematically including material ESG factors in investment analysis and decisions.
- **Norms-based investing**: Excluding investments that do not comply with international standards, such as the United Nations Universal Declaration of Human Rights.
- **Screening**: Filtering companies based on their involvement in positive (beneficial) or negative (undesirable) activities.
- **Stewardship**: Responsible management and oversight of capital to create long-term value and sustainable benefits for the economy, environment, and society.
- **Principles for Responsible Investment**: A UN-supported body promoting responsible investment through voluntary principles that signatories commit to.
- **Values-based investing**: Excluding investments based on ethical, values-based, or religious criteria, such as gambling, alcohol, or pork.

If you are interested or want to learn more about responsible investing, please speak to your financial adviser.

This publication is prepared by Hillross Financial Services Limited (Hillross) ABN 77 003 323 055 AFSL 232 705. ("Licensee"). This publication is not intended to contain personal financial, taxation or legal advice and should not be relied on as such. Any advice in this article is general advice only and does not take into account individual objectives, financial situation or needs. You should obtain specialist financial, taxation or legal advice relevant to your circumstances before acting on this information. Whilst every care has been taken in the preparation of this information, the Licensee does not guarantee the accuracy or completeness of it and does not guarantee any particular outcome. Past performance is not indicative of future results. This publication is not available for distribution outside Australia and may not be passed on to any third person without the prior written consent of the Licensee. Published March 2026.