

AT THE INTERSECTION OF ISLAMIC FINANCE AND RESPONSIBLE INVESTMENT



THE SIX PRINCIPLES

PREAMBLE TO THE PRINCIPLES

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

- 1 We will incorporate ESG issues into investment analysis and decision-making processes.
- 2 We will be active owners and incorporate ESG issues into our ownership policies and practices.
- 3 We will seek appropriate disclosure on ESG issues by the entities in which we invest.
- 4 We will promote acceptance and implementation of the Principles within the investment industry.
- 5 We will work together to enhance our effectiveness in implementing the Principles.
- 6 We will each report on our activities and progress towards implementing the Principles.



PRI's MISSION

We believe that an economically efficient, sustainable global financial system is a necessity for long-term value creation. Such a system will reward long-term, responsible investment and benefit the environment and society as a whole.

The PRI will work to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

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ISLAMIC FINANCE AND RESPONSIBLE INVESTMENT

RESPONSIBLE INVESTING GAINING TRACTION AMONG ISLAMIC INVESTORS

Several mainstream asset managers and banks that are signatories to the PRI offer access to Islamic windows, sukuk or Sharia equity funds. The PRI signatory base also includes investors in OIC¹ countries, some of which are partly or fully mandated to invest in a Sharia-compliant manner². Notably, almost half of the signatories in OIC countries joined the PRI in the last three years, signalling growing interest in responsible investment among Islamic investors.

The main drivers of signatory growth in OIC countries are the strong alignment of social objectives in responsible investment and Islamic finance, and the additional financial value of integrating environmental, social and governance (ESG) factors into investment processes – which can be combined with Sharia screening. As Islamic investors pursue sustainable risk-adjusted investment returns, integrating ESG factors into their decision-making can improve investment performance while aligning financial objectives with social and environmental goals.

THE INTEGRATION MODEL

ESG integration is “the systematic and explicit inclusion of material ESG factors into investment analysis and investment decisions”. It is one of three ways to incorporate responsible investment into investment decisions, alongside thematic investing and screening. All three ESG incorporation practices can be applied concurrently. Read [A practical guide to ESG integration for equity investing](#).

WHAT IS RESPONSIBLE INVESTMENT?

The PRI defines responsible investment as an approach to investing that incorporates ESG factors into investment decisions to better manage risk and generate sustainable, long-term returns.

Some institutional investors once believed that ESG issues were irrelevant to portfolio value, and therefore not consistent with their fiduciary duties. However, this assumption is no longer supported, as set out in the PRI's recent report, [Fiduciary duty in the 21st century](#). ESG factors are critical to performing effective risk and return analysis. Responsible investment does not necessarily involve narrowing the available investment universe. Nor does it involve relegating the pursuit of a financial return to unrelated objectives (social or ethical). It does, however, provide investors with an expanded set of tools to evaluate the operational performance and financial prospects of investee companies.

Institutional investors can practice responsible investment in several ways, including:

- integrating ESG information into quantitative and qualitative analysis (such as fundamental analysis of company value in equity investing or assessment of creditworthiness in fixed income investing), which could result in adjusting areas such as selection, weighting or asset allocation;
- engaging – either individually or alongside other investors – with investee companies/entities on the ESG factors identified as relevant to them;
- using shareholder voting rights to influence company behaviour;
- encouraging investee companies/entities to disclose information on the ESG factors that do or could affect them;
- monitoring overall ESG risk within the portfolio by measuring its carbon footprint, for example;
- helping to shape investor-relevant public policy;
- promoting wider acceptance and use of responsible investment within the investment industry.

¹ The Organisation of Islamic Cooperation.

² See table *PRI signatories in OIC countries*.

COMPARING RESPONSIBLE INVESTMENT AND ISLAMIC FINANCE

Exclusionary screening – including Sharia-screens or UN norms-based screens – is not a requirement of PRI membership but remains a common approach to responsible investment. According to the 2017 PRI reporting dataset, 405 signatories (32%) apply some form of norms-based or negative screening. The dataset further reveals that 235 signatories combine screening with an ESG integration approach, emphasising the complementary nature of exclusionary screens as practiced within Islamic finance and ESG integration. Indeed, there are a range of similarities and differences between Islamic finance and responsible investment.

SIMILARITIES

- strong emphasis on aligning finance with social good;
- seek to increase the contribution of the finance sector to the real economy;
- pursue a more resilient financial system void of unsustainable system risk.

DIFFERENCES

	Responsible investment	Islamic finance
General investment approach	Holistic approach that aims to include any ESG information that could be material to investment performance.	Values-based approach that mainly focuses on exclusionary screens on specific social and economic grounds.
Active ownership	Strong emphasis on being active owners and to engage with companies on ESG issues (including proxy voting).	No widespread practice of engagement or active ownership.
Avoiding investments in highly leveraged companies	Not widely considered.	Sophisticated approach to analysing financial structures of corporate entities to understand cash flows and avoid investments in companies with excessive leverage.
Impact	Not widely considered, but there is a growing focus on environmental and social impacts of investments (including contributions to the SDGs).	Sharia scholars assess the compliance of financial products from a structural and legal perspective – the focus is not on actual impact or real economy outcomes.

PRI SIGNATORIES IN OIC COUNTRIES

	HQ COUNTRY	SIGNATORY CATEGORY	SIGNATORY DATE	AUM (US\$BN)
Access Bank PLC	Nigeria	Investment Manager	08/06/2009	0.0027
Actera Group	Turkey	Investment Manager	30/08/2010	1.636
Borsa Istanbul	Turkey	Service Provider	20/01/2010	-
Catalyst Investment Management	Jordan	Investment Manager	30/01/2017	0.05
Corfina Capital	Indonesia	Investment Manager	14/01/2015	0.04
Corston-Smith Asset Management	Malaysia	Investment Manager	06/05/2008	0.2716
Garanti Asset Management	Turkey	Investment Manager	23/08/2011	4.0423
Hawkamah Institute	UAE	Service Provider	22/04/2009	-
Ithmar Capital	Morocco	Asset Owner	14/11/2016	3.0
Kehati - The Indonesian Biodiversity Organization	Indonesia	Asset Owner	03/02/2009	0.015
Khazanah Nasional Berhad	Malaysia	Asset Owner	01/02/2017	35.0
PT Batavia Properindo Aset Manajemen	Indonesia	Investment Manager	05/02/2016	1.6
Sustainable Development Strategy International Group	Iran	Service Provider	11/05/2015	-
SEDCO Capital	Saudi Arabia	Investment Manager	16/07/2014	4.685
Sustainability Excellence Management Consulting Ltd	UAE	Service Provider	24/02/2015	-
The Abraaj Group	UAE	Investment Manager	28/04/2009	9.5
TVM Capital Healthcare Partners	UAE	Investment Manager	27/05/2015	0.05
TOTAL AUM				\$64.40

HOW THE PRI CAN HELP

By joining the PRI, you become part of a leading, global network of more than 1,700 signatories, representing over \$68 trillion in AUM. You benefit from an internationally-recognised set of Principles and demonstrate your commitment to responsible investment via an independent link to the United Nations.

The PRI supports its signatories to create a more sustainable financial system through:

- numerous asset class-specific guides, toolkits and case studies;
- opportunities to attend and participate in events and workshops with other signatories, facilitating networking and knowledge-sharing;
- access to the PRI's Collaboration Platform, a private online resource, which allows signatories to learn, engage and collaborate with companies, policymakers and academics, as well as over 1,700 fellow investors and service providers;
- the PRI's Academic Network, which offers signatories access to key academic research findings and the opportunity to collaborate with academics;
- the PRI Academy, a CFA-accredited online training system that can be tailored to staff and trustee needs;
- the Reporting Framework, which offers guidance on how communication between corporate plans and beneficiaries can be structured;
- dedicated network managers around the world offering local support.

The Principles for Responsible Investment (PRI)

The PRI works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

More information: www.unpri.org



The PRI is an investor initiative in partnership with [UNEP Finance Initiative](#) and the [UN Global Compact](#).

United Nations Environment Programme Finance Initiative (UNEP FI)

UNEP FI is a unique partnership between the United Nations Environment Programme (UNEP) and the global financial sector. UNEP FI works closely with over 200 financial institutions that are signatories to the UNEP FI Statement on Sustainable Development, and a range of partner organisations, to develop and promote linkages between sustainability and financial performance. Through peer-to-peer networks, research and training, UNEP FI carries out its mission to identify, promote, and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.

More information: www.unepfi.org



United Nations Global Compact

The United Nations Global Compact is a call to companies everywhere to align their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption, and to take action in support of UN goals and issues embodied in the Sustainable Development Goals. The UN Global Compact is a leadership platform for the development, implementation and disclosure of responsible corporate practices. Launched in 2000, it is the largest corporate sustainability initiative in the world, with more than 8,800 companies and 4,000 non-business signatories based in over 160 countries, and more than 80 Local Networks.

More information: www.unglobalcompact.org

