

# ethical fund

bringing the benefits of multimanager investment  
to ethical investors  
guide for investors



## at a glance

- 3 the problem with conventional ethical funds
- 4 our approach to investment management
- 5 the skandia ethical fund
- 6 the ethical screening process
- 8 it's all in the blend
- 9 availability
- 10 manager profiles
- 14 glossary of terms

# the problem with conventional ethical funds

People apply ethical and environmental concerns to many areas of their lives, for example by giving money to charities, buying fair trade products, choosing organic food or recycling household waste.

However, only a small minority put their money where their morals are by investing in companies that help rather than harm the planet, its people and its animals. This seems surprising given that the first ethical funds were launched as long ago as 1984 and there are now more than 50 ethical funds available to UK investors.

Some are put off ethical funds because of the perceived risk of investing in an ethically restricted portfolio. Typically, an ethical fund will have little or no exposure to sectors such as tobacco, armaments or pharmaceuticals, together with many large oil companies and banks, particularly those involved in the financing of environmentally damaging projects or oppressive regimes.

This is entirely proper as many ethical investors will wish to avoid such sectors and companies. However, it means that many ethical funds will tend to underperform when these sectors do well. It was this 'conflict of capital and conscience' that led the Department of Trade to reject the first application for an ethical unit trust in 1973, and the issue is as relevant today as it was then.

One solution to emerge in recent years is to 'accentuate the positive' by investing in companies that have environmental or social policies, support charities and the local community and have good employee relations. This is sometimes coupled with an 'engagement' approach which seeks to influence management to improve company behaviour. This enables many of the newer ethical funds to invest in companies which were previously 'off limits'. The fact remains, however, that many ethical investors still wish to avoid such companies. An arms manufacturer, a tobacco company or a pharmaceuticals

company that tests its products on animals may still be deemed unacceptable, however well it treats its staff or the community.

This is compounded by the fact that most ethical funds are run by a single manager, and are therefore unable to add value or diversify risk through manager selection. Investors in these funds are caught by the 'double whammy' of a single manager fund unable to diversify between managers and an ethically restricted portfolio unable to select from the full spectrum of stocks. Furthermore, many ethical funds invest exclusively in a single market, often the UK, and therefore do not benefit from international diversification.

However, there is an alternative approach which can help to overcome these concerns. It is called MultiManager investing, and it is an area in which we have particular expertise.

# our approach to investment management

In our opinion, no single fund management group can be the best in all areas at all times. Even the most admirable management groups will have periods of underperformance, whether because their investment style does not suit every market, due to fund manager changes or down to plain bad luck.

Our MultiManager approach is designed to diversify this manager risk within and across investment markets.

There are two approaches to MultiManager investing – ‘fund of funds’ and ‘manager of managers’. Funds of funds select from funds already available to retail investors, while manager of managers funds invest in specially-created portfolios which, in general, are only available to institutional investors.

Our solution is to combine both approaches to offer ‘the best of both worlds’. By using both existing funds and bespoke portfolios we can offer access to well known fund managers recognised as leaders in their field and other leading managers who may be less well known in the UK but are acknowledged as experts in their home markets.

Our unrivalled access to world-class investment managers is only possible through the size of our funds under management and the negotiating power it gives us.

We offer a collection of well diversified, carefully constructed funds, run by a range of world-class investment managers. Managers are selected for their expertise in particular areas – where they are free to deliver potentially strong performance – while the overall fund is managed to offset the risks taken by each individual manager.

Managers are then monitored closely to ensure they remain the optimum choice, while the overall make-up of the fund is kept under constant review with the aim of delivering more consistent performance within each area.

We seek outperformance (above average returns) primarily by using the most skilful managers rather than trying to ‘second guess’ markets or take major ‘bets’ on any particular sector (type of company), size of stock or investment style as we believe that this can introduce unnecessary risk into the funds. Each fund is therefore carefully constructed by our team of experts – one of the largest in the industry – to provide a well balanced and high-quality investment.

Skandia was named as Best Multi Manager Provider in the MoneyMarketing Awards for 2005, 2006, 2007 and 2008.



# the skandia ethical fund

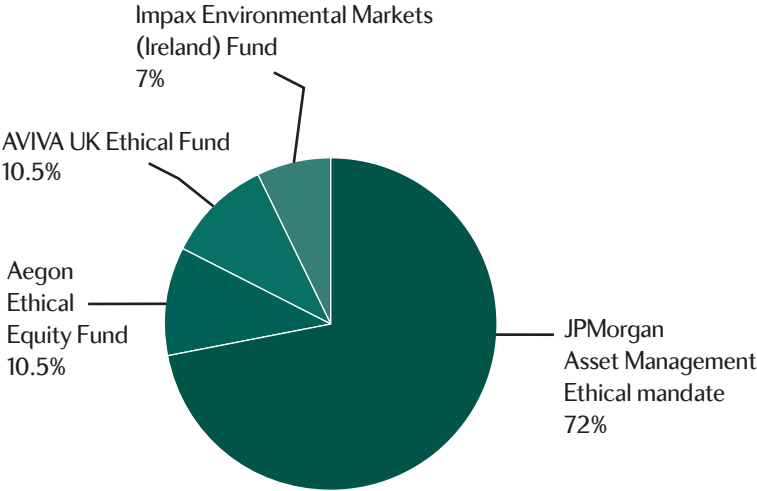
The Skandia Ethical Fund offers all the benefits of our MultiManager approach.

We have appointed JPMorgan Asset Management (JPMAM) to manage around three-quarters of the Fund through a bespoke portfolio created exclusively for the Skandia Ethical Fund. We appointed JPMAM as we wanted the majority of the assets to be managed by a leading mainstream global manager.

The JPMAM portfolio is complemented by holdings in three retail ethical and environmental funds, which we regard as among the best in the field.

For further information on the managers please see pages 10 to 13.

## managers held within the skandia ethical fund



Target allocation as at 30 April 2009.  
As the funds are actively managed, the actual allocations and managers are subject to change.

# the ethical screening process

Terms in *italics* are defined in the **glossary of terms** on page 14.

The ethical investment criteria applied to the Skandia Ethical Fund are among the strictest available, because this is what we believe the majority of UK ethical investors are looking for. The screening process is applied to the whole Fund to ensure that all stocks held satisfy the criteria. The criteria for screening are under constant review and will be adjusted to reflect changing circumstances and emerging concerns.

Please be aware that the Fund is unable to invest in certain stocks on ethical grounds, and as a result may be more *volatile* than some more diversified funds.

Reasons for **excluding** a company from the portfolio (the negative criteria) are currently as follows:

- **Animal testing** – companies which develop or manufacture animal-tested cosmetics, industrial or household chemicals, or pharmaceutical or healthcare products, or provide animal-testing services.
- **Factory farming** – companies involved in the rearing of animals in intensive conditions.
- **Environmental issues** – companies will be excluded where their activities have a significant negative environmental impact, such as mining, chemical manufacture and oil production, unless those companies undertake positive initiatives that effectively address those impacts (see positive criteria overleaf).
- **Human rights** – the portfolio will avoid companies with operations in developing countries and countries regarded as having oppressive regimes where evidence is held of their involvement, either by collusion or complacency, in abuses of human rights.
- **Armaments** – companies that manufacture or sell weapons or weapons systems, or provide strategic components or services specifically for military use.
- **Banks** – companies with commercial lending operations will be excluded if there is evidence that the bank has been involved in financing environmentally or socially controversial projects, particularly where such projects undermine stated environmental and/or social policies or objectives.
- **Gambling** – companies whose primary activity is the operation of gambling facilities.

- **Nuclear** – companies that are involved in the generation of nuclear power, or provide nuclear services to the military.
- **Pornography** – companies involved in the production or distribution of pornographic material.
- **Alcohol** – companies whose primary activity is the manufacture or sale of alcoholic drinks.
- **Tobacco** – companies whose primary activity is the production or manufacture of tobacco products.

Reasons for **including** a company in the portfolio (the positive criteria) are currently as follows. The positive criteria do not override the negative but are used to distinguish between companies if the negative criteria are passed.

- **Employee relations** – companies that operate equal opportunities policies or abide by codes of conduct regarding labour standards throughout their operations.

- **Social issues** – companies that provide socially beneficial products and services, such as social housing, home care and nursing, or demonstrate outstanding commitment to the communities in which they operate.
- **Environmental management** – companies that apply a systematic approach to the management of their environmental impact through, for example, environmental management systems, auditing and reporting.
- **Environmental products and services** – companies whose products and services produce environmental benefit, such as pollution control systems, waste management and recycling services, renewable energy and public transport.

We employ a specialist firm called Ethical Screening to determine which companies meet the ethical criteria. With a team of dedicated analysts who research stocks worldwide on our behalf, Ethical Screening provides a list of permitted investments to JPMAM and ourselves on a monthly basis.

If a company held by the Skandia Ethical Fund no longer meets the criteria, the stock will be sold in a timely and ordered manner.

The retail fund managers held by the Ethical Fund use their own ethical research teams and/or the Ethical Investment Research Service (EIRIS) to screen investments. In addition, Ethical Screening periodically reviews the retail funds to ensure compliance with our ethical screening criteria.

The screening process acknowledges that ethical issues are wide-ranging and it is impractical to list all issues of concern. The Fund is operated on the basis that additional exclusions may be made where a company's operations are judged to be unacceptable to the typical investor in the Fund. Examples include involvement in the fur industry, the sale of whale meat and significant involvement in genetic modification.

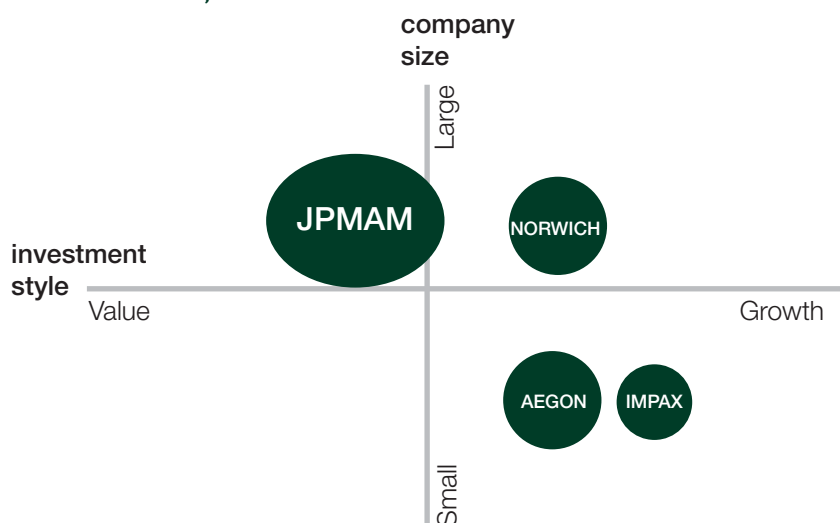
# it's all in the blend

Ethical funds are typically more *volatile* than the market as a whole, outperforming when permitted stocks and sectors do well and underperforming when they are no longer in vogue. The Skandia Ethical Fund cannot eliminate this risk entirely, but seeks to minimise it by diversifying the portfolio internationally and across managers.

The four managers selected to run the assets in the Skandia Ethical Fund are chosen not only on the basis that they are among the leading managers in their fields, but also because they offer complementary investment approaches.

Below is a simple illustration of the relative positions of the four managers, based on a combination of investment style and company size weightings, compared with the average ethical fund. Blending the managers in this way means we are able to balance investment styles and spread risk, with the aim of reducing volatility and increasing potential returns.

## ethical blending



For illustrative purposes only, comparing the relevant positions of the Skandia Ethical Fund's component managers.

Source: Skandia Investment Research



# availability

You can invest in the Skandia Ethical Fund as a unit trust or ISA investment from as little as £1,000 lump sum or £50 per month. You can also consolidate your existing ISA investments via ISA transfers or through the Selestia Investment Solutions investment platform.

If you invest directly with Skandia Investment Management Limited, there will be an initial charge of 5% and an annual management charge of 1.25%. The total cost of all annual charges and expenses, including the annual management charge, is estimated as 1.91% and you can sell your investment at any time with no additional charges.

Minimum investments and charges may differ slightly if you invest via Selestia Investment Solutions or other fund platforms.

The Fund is available across the Skandia product range, which includes Skandia's investment bonds, pensions and offshore investment bonds.

You should note that the performance of the life, pension and offshore funds will not be the same as for the unit trust because of taxation adjustments, life company fund charges and the investment process. Your financial adviser can provide full details.

# manager profiles

## JPMorgan Asset Management Ethical Portfolio

### J.P.Morgan Asset Management

A diversified portfolio of 60 to 70 stocks, driven by a strong philosophy which seeks to exploit market inefficiencies.

#### Fund Manager – Howard Williams.

JPMorgan Asset Management (JPMAM) have a respected, well organised and well resourced team of global sector analysts located in London and groups of regional analysts located round the globe. The team is backed by an organisation that provides support in terms of systems, people and management.

The resources are organised in such a way that the ethical portfolio managed solely for us receives a high level of management.

For stock selection, Howard Williams applies an ethical overlay to JPMAM's mainstream stock recommendations.

The analysts use a proprietary *quantitative* ranking tool for ideas generation, which favours stocks with *momentum* and *value*. Shares are scored between 1 and 5 depending on the strengths exhibited for the various characteristics.

Whereas a typical ethical fund manager will tend to have a persistent emphasis towards smaller companies and *growth* stocks, JPMAM seeks to run a more balanced approach across company sizes, countries and investment styles. This philosophy ensures a balanced portfolio with good *growth* and *value* characteristics.

## Aegon Ethical Equity Fund



A diversified portfolio of 80 to 100 securities resulting from a pragmatic philosophy focusing on three key disciplines – leadership, teamwork and communications.

**Fund Manager – Audrey Ryan.**

Aegon believes that teamwork is the best way to achieve its goals. Strong leadership, combined with the empowerment of individuals, is the key to success. Healthy debate is encouraged with *themes* and ideas challenged. There is buy-in from the whole team on any course of action, which ensures consistency.

Ryan’s philosophy is based on the twin beliefs that investment research must be alive to the next big *theme* and that valuation is key – focusing on company *fundamentals*, valuation measures and technical drivers. Not only is there no distinct *style bias*, the process also amalgamates *top-down macroeconomic* work with *bottom-up* stock picking.

The Ethical Investment Research Service (EIRIS) provides the ethical screening service for the fund and Aegon obtains advice from EIRIS where companies are assessed for positive attitudes towards their workforce, the communities in which they do business and the ways in which they protect the natural environment.

Ryan constructs her portfolio by bringing together mainstream equity views and the ethically screened stock list. Ryan also brings with her previous mainstream experience in smaller companies. Aegon takes its corporate responsibilities seriously and is a more active shareholder than many ethical fund managers.

## AVIVA UK Ethical Fund (AVIVA Investors)



A *top-down, Growth At a Reasonable Price (GARP)* philosophy results in a 50 to 70 stock portfolio.

**Fund Manager – Peter Michaelis.**

AVIVA is clearly committed to Socially Responsible Investment (SRI), with over 13 years in managing SRI funds and one of the largest and most experienced teams in the industry. The team believe that SRI will help alleviate poverty and environmental destruction and at the same time deliver above-average investment returns.

The process is built around rating companies on their ability to improve or detract from society (eg those that deliver better quality of life or reduce the strains on global ecology). They believe they will be able to select companies that will in the long run deliver better than average impacts on society and better than average investment returns.

The process starts with a *thematic* analysis. This involves reviewing key ethical *themes* that will lead to certain industries and stocks becoming winners or losers. They focus on identifying the social and environmental factors that will have the greatest impact at the financial level for the company. These are then rated on 'business sustainability' and 'visions and strategy' in what they call their 'sustainable ratings matrix'. A portfolio of 50 to 70 stocks is then constructed from the positive stock selection that results.

## Impax Environmental Markets (Ireland) Fund



The fund was launched to enable investors to benefit from rapid and sustained growth anticipated for cleaner and more efficient delivery of basic services of energy, water and waste.

**Fund Managers – Bruce Jenkyn-Jones and Ian Simm.**

Investments are made predominantly in quoted companies which provide, utilise, implement or advise upon technology-based systems, products or services in Environmental Markets, particularly those of alternative energy and energy efficiency, water treatment and pollution control, and waste technology and resource management.

Companies are selected on the basis of their potential for generating capital growth, on a *bottom-up* basis

While the strength of the technology is an important factor in the selection of the stocks, the team believes in rigorous fundamental analysis and focus on five attributes when choosing portfolio investments: compelling business proposition based on proven technology, management quality, identification of new growth markets, development of global environmental and energy policies and regulations, and finally valuation anomalies and sector volatility. Much of the research is undertaken in-house, but with the increasing number of brokers covering these companies, external research is also used.

# glossary of terms

## Bottom-up analysis

The search for outstanding performance of individual stocks before considering the impact of economic trends. The companies may be identified from research reports, stock screens etc (as opposed to *top-down* analysis).

## Fundamentals

Information relating to the economic well-being of a company such as revenue, earnings, assets, liabilities and *growth*. These factors are used to determine the worth of an investment in fundamental analysis. A company with little debt and a lot of cash is generally considered to have strong fundamentals.

## Growth investing

A strategy in which an investor seeks out stocks deemed to have good growth potential. In most cases, a growth stock is defined as a company whose earnings are expected to grow at an above-average rate compared with its industry or the overall market.

## Macroeconomics

Economic analysis concerning broad trends and influences on the economy, such as the interaction of fiscal and monetary policies, Gross Domestic Product (GDP), balance of payments etc. As opposed to microeconomics which focuses on individual units such as companies and markets to assess their influence on the economy.

## Momentum investing

Investment based on a rising trend in a company's earnings or price movements. A momentum manager will seek to ride out the trend and sell the stock once it has peaked.

## Quantitative analysis

An approach to investment management which seeks to use statistical or numerical methods, rather than more subjective (or qualitative) factors.

## Style

The investment approach a manager takes to achieve his or her objectives. There are many different kinds of style, but the two most common are *value* and *growth*.

### **Thematic**

A fund manager may construct a portfolio by weighting it towards particular industries or sectors expected to benefit from demographic, social or other changes. This is known as thematic investing.

### **Top-down analysis**

A country's economy is considered before deciding in which industry to invest. Economic conditions determine which industries or sectors will produce good returns and then attractive stocks are bought within those industries.

### **Value investing**

A value investor is one who seeks to buy shares when they are underpriced and to take profits when they appear overvalued. The Price/Earnings Ratio is a key measure for the value investor. Deep value refers to stocks with particularly strong value characteristics.

### **Volatile**

Volatile refers to a statistical method that measures how much a series of values has moved up and down around its average, known as volatility. The higher the volatility, the less consistent the historical performance has been.

For more information on the Skandia Ethical Fund please speak to your financial adviser.

Skandia Investment Group is part of the worldwide Skandia Group, itself owned by Old Mutual plc. Old Mutual plc is a public company limited by shares, incorporated in England and Wales under registered number 3591559.

Registered Office: 5th Floor, Old Mutual Place, 2 Lambeth Hill, London, EC4V 4GG.

This material is issued by Skandia Investment Management Limited, a member of the Skandia Group.

**[www.skandia.co.uk](http://www.skandia.co.uk)**

**[www.skandiainvestmentmanagement.com](http://www.skandiainvestmentmanagement.com)**

**[www.royalskandia.com](http://www.royalskandia.com)**

Calls may be monitored and recorded for training purposes and to avoid misunderstandings.

Selestia Investment Solutions investment platform gives you access to an ISA and Collective Investment Account provided by Skandia MultiFUNDS Limited, a Collective Retirement Account and Collective Investment Bond provided by Selestia Life & Pensions Limited and an Offshore Collective Investment Bond distributed by Skandia MultiFUNDS Limited for Old Mutual International (Guernsey) Limited.

Skandia fund platform gives you access to MultiISA and MultiFUND provided by Skandia MultiFUNDS Limited and to products provided by Skandia Life Assurance Company Limited.

Skandia Life Assurance Company Limited, Skandia MultiFUNDS Limited, Skandia Investment Management Limited and Selestia Life & Pensions Limited are registered in England & Wales under numbers 1363932, 1680071, 4227837 and 4163431 respectively. Registered Office at Skandia House, Portland Terrace, Southampton SO14 7EJ, United Kingdom.

All companies are authorised and regulated by the Financial Services Authority with FSA register numbers 110462, 165359, 208543 and 207977. VAT number for all above companies is 386 1301 59.

Old Mutual International (Guernsey) Limited is regulated by the Guernsey Financial Services Commission and is licensed to write long-term business under the Insurance Business (Bailiwick of Guernsey) Law 2002. Registered number 2424. Registered Office at Fairbairn House, PO Box 121, Rohais, St Peter Port, Guernsey GY1 3HE, Channel Islands.

Royal Skandia Life Assurance Limited is registered in the Isle of Man under number 24916. Registered and Head Office: Skandia House, King Edward Road, Onchan, Isle of Man, IM99 1NU, British Isles. Phone: +44 (0)1624 655 555 Fax: +44 (0)1624 611 715. Authorised by the Isle of Man Government Insurance & Pensions Authority. Authorised and regulated by the Financial Services Authority for business conducted in the UK. Some of the FSA's rules do not apply to non-UK based insurers. FSA Register number 142309. [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register).

**When printed by Skandia this item is produced on a mixed grade material, which uses a combination of recycled wood or paper fibre from controlled sources and virgin fibre sourced from well managed, sustainable forests.**

