# Ask McCaskill

*FINANCIAL ADVICE STRAIGHT FROM THE EXPERT*

**Q: "Recently I heard some discussions about ESG investing for the environment. What is it? And how does it work?"** K. B. - Frederick, MD

**A:** Investors are increasingly advocating for greater transparency about how and where their money is invested, with many emphasizing the ability to generate wealth in a responsible manner—without sacrificing investment principles. Sustainable investing empowers investors to do just that by integrating Environmental, Social, and Governance (ESG) criteria into the investment decision-making process. Let's explore the terminology, differentiated approaches, potential long-term advantages, and how to adopt an ESG framework.

**Understanding the Terminology**

Sustainable investing has evolved significantly over the past 20 years, including the breadth of investing approaches and terminology used to describe them.

**Assessing the Advantages**

In addition to gaining greater transparency, adopting an ESG framework can provide investors with a more comprehensive assessment of a company's risks and opportunities. It also lends them a greater ability to invest according to their values or to actively engage with companies in which they invest to enact positive change.

- **Prioritizing values.** An underlying benefit of ESG investing is investors' ability to align their investments with the causes or values most important to them. While each investor's goals and ideals are different, common themes include combating climate change, achieving gender equality, and advocating for equitable labor standards.
- **Risk management.** By integrating ESG factors into the investment analysis process, investors can identify material insights into a company beyond what traditional financial metrics provide. Companies that embrace ESG criteria can be better positioned to mitigate forthcoming risks and identify strategic opportunities than those that ignore their ESG impact.
- **Shareholder activism.** With ESG and impact investing, investors can exercise their rights as shareholders to engage and communicate with corporate management teams. Most commonly, this is done through proxy voting or filing shareholder resolutions, as investors seek to create awareness, enact positive change, or influence a corporation's ongoing policies and behaviors.
- **Competitive performance.** In addition to managing risk, ESG-minded companies may offer enhanced risk-adjusted returns, or the potential return for the level of risk associated with an investment, relative to traditional investments over the long run. According to Morningstar data, ESG indices outperformed traditional counterparts across various regions over one-, three-, and five-year periods, due to the higher-quality nature of ESG-oriented strategies and companies.

**Assessing the Disadvantages**

While ESG investing strategies can offer investors many long-term advantages, potential drawbacks do exist. Without a universal standard for defining ESG or its criteria, many investors are left to interpret what constitutes an ESG strategy—though industry-adopted prerequisites exist. Additionally, companies may tend to accentuate certain areas of ESG in which they excel, while de-emphasizing their efforts or practices in areas of which they lack or are inferior.

If you determine that adopting an ESG investing approach is right for you, we recommend adhering to a simple three-step framework when getting started.

- **Define your long-term investing goals.** After reviewing your investment objectives, we will work together to assess whether ESG investing fits into your overall financial plan.
- **Narrow your focus.** Looking beyond the discovery stage, we can work together to identify your investing priorities and shape our ongoing process. This will allow us to assess the level of ESG integration that is right for you while evaluating an appropriate asset allocation that aligns with your goals, risk tolerance, and time horizon.
- **Take a long-term approach.** As long-term investors, it is vital that we continually review your desired outcomes and expectations alongside your financial returns. With ongoing dialogue, we can define success or modify your plan to address your changing preferences.

If you are interested in using a sustainable investing strategy or are looking for additional information, please feel free to contact our office.

**To submit questions for future articles**

**Email to scott@mccaskill-financial.com or Call our office at 301.668.7366**