

Sustainable Investment
Research Platform

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Long-Term Investors – Your Time Has Come

THE LAST THREE YEARS should have opened our eyes; we are on a collision course. Developed economies have hit the ceiling, and it is not realistic any more to discount growth rates that we have been used to. Growth can no longer be based on cheap energy and more and more credits. Emerging economies have no intention of giving up hope of a standard of living in parity with Western ideals. The path we are on is simply not sustainable.

When valuations become so low as they have in current crises that can be justified by an end-of-the-world scenario only, long-term institutional investors should step in. In a situation where investors cannot rely on expected returns that a sustainable economy cannot deliver, long-term investors need to ask themselves whether Responsible Investments (RI) can remain only a marginal piece, the icing on the cake, or should RI become an integral part of their investments. So far, RI has attracted only mild interest.

Different RI models can be applied to various asset classes. Exclusion and the thematic approach can be appealing, but the best in class is most suitable for RI and sustainable development. Exclusion is easy to understand and it can enhance the reputation, but it has been difficult to draw the line and implement on a larger scale. Thematic investments are attractive and easy to identify and implement, but as a quick fix, they can lead to new bubbles.

Sustainability has to be based on present industrial realities. It will not be possible to do without, for example, steel, cement, chemicals, and oil for a while. We need to accept the present economic sectors as a necessity for sustainable growth. In the different sectors, long-term

investors need to be able to distinguish between ESG leaders and laggards. The proactive leaders will shape their industries and have the potential to deliver sustainable growth. Long-term institutional investors counteracting short-term benchmarks are needed.



Lars G. Hassel

PROGRAMME DIRECTOR SIRP MISTRA

A Tool for Practitioners

WHAT HAS HAPPENED to the public debate, where public decisions are taken? The challenges facing the planet are urgent but have fallen into the shadows of the official debate. There are even those who think that the topic of a sustainable society with responsible companies is outdated.

Experienced professionals and organisations are tirelessly working to solve major sustainability issues, but receive little support from central decision making processes. To achieve change, we need a tougher political debate and politicians who are prepared to fight for a sustainable society. While academic research is progressing, companies still tend to engage only in the sustainability issues they are directly responsible for. Companies in particularly exposed industries such as oil extraction and garment manufacturing should, for example, be taking control and driving sustainability in a more insightful way.

What really will make a difference is when politicians take responsibility and, in dialogue with industry and other stakeholders, impose new levels of requirements. This includes the financial industry and long-term investors such as asset managers, pension funds and insurance companies. Financial market sustainability must be a part of management responsibility, including taking into account the environmental, social and governance dimensions of corporate activities. Risk assessments need to include sustainability risks and be priced accordingly. Managers must be trained and then held accountable for their responsibilities even in these areas. The winners will be those who are well prepared for the customers' demands that come with increasing public understanding for the necessity of sustainable solutions. Sustainability is not an option in the long run.

We face massive challenges that require drastic rethinking and a long adjustment period. Academic research within the area is important and, as I see it, a major part of the solution. Therefore I am extremely glad, that the research within the SIRP Mistra programme during 2011, has been both fruitful and productive. Our research is a great tool for companies and politicians aiming for sustainability.



Ingrid Jansson

CHAIR OF THE SIRP MISTRA BOARD

Awards

During 2011, several awards have been given to researchers in SIRP Mistra for their outstanding research, further highlighting the importance and relevance of sustainability in finance.



NADJA GUENSTER, Maastricht University, has received the 2011 Crowell Second Prize from the Quantitative group of Panagora Asset Management, in Boston, USA. The prize reflects the recognitions of Nadja Guenster's recent work on asset price bubbles, which she focuses on next to her research on sustainable investing. A dynamic strategy of riding bubbles, based upon real-time information, results in abnormal annual returns of 3 to 8 per cent.

The paper "*Riding bubbles*" and the presentation by its first author Nadja Guenster were judged to be "truly outstanding and deserving this recognition". The authors received 3000 USD in award money. Co-authors of the paper were Erik Kole of Erasmus University and Ben Jacobsen of Massey University. The prize is named after Panagora's founder Richard A. Crowell.



JONAS NILSSON, researcher at Umeå School of Business, has been awarded a three-year research scholarship for his research about consumer behaviour and SRI-funds. The Wallander foundation awards outstanding, young post-doctoral researchers within the economic disciplines.

In 2010, Jonas Nilsson defended his thesis, *Consumer Decision Making in a Complex Environment: Examining the Decision Making Process of Socially Responsible Mutual Fund Investors*, in which he identifies the information retail SRI fund investors are asking for before, during and after their purchase. Choosing an SRI fund (Socially Responsible Investment) is more complicated than choosing a traditional fund, since the investor desires to both receive a good financial return and to know that the investment contributes to sustainable development.

The award is 160 000 Euro. The objective of the scholarship is to give young post-docs the opportunity to become associate professors.



JOAKIM SANDBERG, research fellow in philosophy at University of Gothenburg, was awarded the Holm-

es Rolston III Early Career Essay Prize for his article "My Emissions Make No Difference". The prize is awarded by the International Society for Environmental Ethics and the Center for Environmental Philosophy and aims to encourage and support research in environmental philosophy by scholars in the early stages of their career.

The prize is named after Holmes Rolston III, in recognition of his pioneering work in the field of environmental philosophy. According to the prize motivation, Joakim Sandberg's essay "addresses an important and timely topic, the question of individual responsibility with respect to carbon emissions". The article was published in the fall 2011 issue of the journal *Environmental Ethics*.

SEBASTIAN SIEGL and **ANDREAS HOEPNER** from Åbo Akademi and University of St Andrews, were awarded a FIR PRI Research Grant of 3000 Euro.

The award was for their study, "*Does pension funds' fiduciary duty prohibit the integration of any ESG criteria in investment processes? A realistic prudent investment test.*"

The study, which analyses 1500 firms from 26 developed countries over a period of 65 months, shows that pension funds are not likely to compromise on their financial attractiveness by integrating environmental criteria in their prudent investment process. The conclusion is based on data from EIRIS Corporate environmental responsibility scores.

"The paper is highly creative and practical and an excellent example of interdisciplinary research. It tests whether investment approaches that use environmental information are consistent with fiduciary duty", stated the jury of the award.

Co-author of the study is Michael Rezez, University of St Andrews. The findings are expected to also apply to social and governance responsibility scoring, the planned subject of a follow up study.



Sebastian Siegl



Andreas Hoepner

A Call for Long-Term Perspective

The overall objective of the Sustainable Investment Research Platform was formulated in 2006, namely to find out how sustainable investment practices can create added value for institutional investors and identify barriers to mainstreaming such practices.

WHEN LOOKING BACK, the programme was launched very timely and coincided with the introduction of the UN Principles for Responsible Investment. Three main areas of research have been identified: the investment case, the sustainable company, and the issue of fiduciary duty related to short-termism and incentive systems in financial markets.

Sustainable Investments and Markets

Understanding the risk/return implications of integrating environmental, social, and governance (ESG) factors into equity portfolio management (and other asset classes) is one of the programme's core research issues. Portfolio returns have attracted wide interest, not only among asset managers and institutional investors but also in the academic community. Research on this mature topic has, however, provided conflicting evidence in showing that both controversial and socially responsible stocks create superior risk-adjusted returns, and when screens are combined, the financial outcomes could be neutral.

SIRP researchers have been able to contribute to the alpha puzzle in two ways. A theoretical argument has been developed, namely that responsible investors have various motives and the socially responsible investment market different segments. The values-driven investors shun the controversial industries by sacrificing returns while the profit-seeking responsible investors look for superior financial returns in best-in-class portfolios. An awareness of the two segments and different investor motives and their financial outcomes is an important theoretical input in the debate on fiduciary duty.

The SIRP group has also been able to provide evidence that market participants have gradually learned to price in the difference between leading and lagging companies based on publicly available ESG information that can broadly reflect management competence. With mainstreaming ESG, mispricing leading to superior returns will come to an end and the investors need private ESG information linked to the firm's financial fundamentals in

SIRP Mistra Programme Board:
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SIRP Mistra Management Group:
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order to be able to exploit market imperfections and create abnormal returns. The group's research has now shifted to analysts' forecast accuracy, errors in forecasts, and the ability of firms to surprise markets which could be related to ESG performance. An indication of errors in expectations is that ESG leaders tend to have more positive earnings surprises.

Sustainable Companies

Related to portfolio studies and market efficiency of pricing ESG factors, the programme has also explored whether ESG factors have extra-financial value at firm level. The research shows that the commercial property sector is relatively efficient in pricing sustainability as proxied by energy efficiency and green labels. There is a firm belief that sustainability adds value to investors and property developers. The research has now been extended to the private housing sector and the private equity investments. In addition, the SIRP programme provides a sustainability bench-

mark for the real estate companies globally to assist investors in real estate investments. The credit market seems also to price ESG factors. Leading environmental performers show higher credit ratings and lower credit risks than lagging firms. We can make the following conclusions regarding ESG implications at the firm and portfolio level: back-testing over time indicates that ESG is priced at firm level and market imperfections cannot continue to provide abnormal risk-adjusted returns at portfolio level based on publicly available ESG rankings. Private information on firm fundamentals (e.g. by engagement) and errors in market expectations derived from sustainability or intangible ESG factors need to be exploited by research and practice.

Bonuses

The main rationale for offering bonuses is to increase employees' motivation to produce good results. It is therefore important to investigate whether it is possible to design bonus schemes such that delayed payouts will be equally motivating as immediate payouts. This question was addressed in two experiments in which participants chose between bonus payments paid out either frequently (four short-term bonuses) or infrequently (one long-term bonus). It was assumed that more-preferred bonus systems will be more motivating than less-preferred bonus systems. Consistent with research on time discounting, the results showed that a majority chose the short-term bonuses. To be equally attractive, the long-term bonus needed to be between 20 and 40 percent higher than the four short-term bonuses. Increasing uncertainty about the bonuses made choosing the long-term bonuses more attractive.

Two other studies showed that despite being more motivating, short-term bonuses tended to have negative effects on performance by making investments short-sighted. In another study, we asked whether long-term bonuses increase far-sighted investments. If investors choose between purchasing two stocks and the bonus depends on their value development, our previous finding that a short-term bonus is preferred to a long-term one implies that the stock whose value increases faster would be chosen. If this is stock in a company whose goal is short-term profit, purchasing stocks in this company may prevent purchasing stocks in companies with longer-term goals, whose stocks for this reason increase in value at a lower rate although it eventually exceeds the value of the short-term stock. Earlier research shows that choices among several stocks (portfolio construction) produce a strong tendency to diversify that increases with uncertainty. In line with this, we found that picking both a short-term and a long-term stock dominated and even more so when there was uncertainty about the future value developments. A benefit of choosing the long-term bonus was

the positive effect when there was no uncertainty. We also found that uncertainty-reducing information about others' choices tended to influence choices of either the short-term or long-term stock, thus counteracting diversification.

Fiduciary Duty

Part of the programme's ongoing research explores impediments to sustainable investing by exploiting the concept of fiduciary duty from a legal-philosophical perspective, and by mapping the values of the financial professionals and potential pension beneficiaries in Sweden and globally. Additionally, behavioural implications of short-term monitoring and rewarding mechanisms have been exploited in financial institutions.

One of the programme's core research issues concerns to what extent the fiduciary duties of institutional investors, i.e. their legal obligations to their beneficiaries, constitute impediments to their engagement in sustainable investment (and, if so, what can be done about it). Our in-depth legal analysis suggests that fiduciary duties, indeed, hinder effective sustainable investing as they are formulated in contemporary law. For example, while the so-called Freshfields Report promoted by the United Nations Environment Programme Finance Initiative has opened some doors in the area, institutional investors are not allowed to take a proactive stance on ESG issues that are not financially material (and where companies are not in clear violation of international treaties). The analysis suggests that even mutual funds that are marketed as ethical or sustainable have similar problems since some parts of fiduciary duty are common to all managed funds.

A possible solution put forward by SIRP researchers is to balance fiduciary duty with legislation on independent ESG obligations. Sweden is a good test case for this since the Swedish National Pension Funds (the AP funds) have been given (partially) independent ESG obligations. But while the AP funds may have been front runners in sustainable investment in the past, our empirical research suggests that they may be falling behind in this regard.

Another solution that we are currently exploring is to rebuild fiduciary duty from the bottom up, so to speak, starting with a survey of the value priorities of beneficiaries (especially future pensioners). Preliminary results indicate that a majority of beneficiaries prefer their institutions to take ESG issues into account, and many are also prepared to make financial sacrifices for this sake. However, when simultaneously surveying the value priorities of financial professionals, a somewhat different picture emerges. This raises the question of who actually sets the agenda at our financial institutions and whose interests they ultimately are supposed to serve.

During three days in late September more than 150 people gathered in Sigtuna for the latest findings within sustainable investments. Around 80 researchers presented during the conference, among them many SIRP researchers.

AT A TIME WHEN financial markets are in turmoil and with a mounting Eurozone crisis, delegates showed up in Sigtuna to clarify how the investment community can work to reach more sustainable markets and investment practices.

Lars G. Hassel, programme director at SIRP Mistra and Rob Lake, director of strategic development at UN PRI, kicked off the conference with a message to the participants that UN PRI now has 900 signatories worldwide with 30 trillion dollars under management.



Sigtuna Foundation



Lars G. Hassel



Rob Bauer

The questions often asked about responsible investments are firstly; will I make money? And secondly; what are responsible investments? Lars G. Hassel states that the role of the academic community is to define, explain and communicate what is implied by responsible investments.

Married to stocks

First to explain responsible investments was keynote speaker Rob Bauer, professor at Maastricht University School of Business and Economics (ECCE) and research leader at SIRP Mistra. Rob Bauer emphasized the importance of shareholder engagement as the long-term strategy for responsible investments.

“The importance of shareholder engagement is essential. Just investing in ESG stocks will not be enough in the long-term and ironically, it is a topic we do not discuss enough,” Rob Bauer stated.

As the term engagement was discussed, Rob Bauer referred to the context of institutional investment. Share-

holders are more or less “married” to certain stocks. Just like in a real marriage, this should be preceded by a period of engagement and discussion. Unfortunately, the lack of dialogue and engagement tends to result in a lot of degrees of freedom for company management. It is also increasingly apparent that the direct link and underlying theory between ESG criteria as a basis for investments, and performance, is unclear.

Shareholders need to organize

Rob Bauer makes the comparison to Tolkien’s *Hobbits* in the “Battle for Middle Earth”. A large group of shareholders (the *Hobbits*), small in size and rather poorly armed (a bunch of voting rights and voices), are fighting with company management (the *Orchs*), large and with powerful weapons (information asymmetry and management shareholdings) at their disposal. The *Hobbits* seem to be waiting for Gandalf to help unite them and conquer the enemy. Rob Bauer’s research focuses on the effectiveness of shareholder engagement. Rarely do we read about the effectiveness of engagement, either in terms of financial returns or in terms of ESG performance. Fortunately, the PRI conference addressed this issue in several sessions. It allows academics to scrutinize efforts by practitioners and encourages an objective dialogue between academics and practitioners.

Proposals as a tool

One way to engage with companies as a shareholder is to file shareholder proposals. Rob Bauer concludes that individual investors are the most active, in the US at least, but also the least effective. Unions and institutional investors

(pension funds) are becoming increasingly active and effective, especially in labour related issues.

There is information for fund managers to obtain here; for example, if a company chooses to enter into negotiation with the filer of the proposal, this is a sign of negotiation taking place. Between the lines, this means that the filing part has power, or has made a powerful proposal that could affect the management's reputation or bottom line. This could in the end lead to a proposal withdrawal.

Withdrawal rates of proposals related to governance are lower than CSR proposals. Maybe a CSR-focused proposal is an easier way for the company to gain goodwill with shareholders. Furthermore, if the management holds a lot of stocks, withdrawal rates are lower because they are confident to win in an eventual subsequent vote.

Studies show that shareholders (institutional investors) generally do not file these proposals often. These investors either might not have the resources, be subject to conflicts of interest, or simply are not aware of the issue. This implies that there is a very good reason for institutional investors to cooperate and negotiate with companies on both financial and ESG matters.

Except from Rob Bauer, other high profile keynote speakers were Gordon Clark and Michael Barnett at the University of Oxford, Meir Statman from Santa Clara University, Klas Eklund, Senior Economist at SEB and Rob Lake, Director of Strategic Development at UN PRI. Their extensive experience provided for high quality input to an interesting and valuable conference.

SEB to sponsor

SEB, one of Europe's leading banks, was the main sponsor of the conference. In addition to a financial contribution, SEB also hosted an interesting workshop about fiduciary duty and handed out the SEB Award of 5000 Euros to prominent researchers.

"SEB's institutional customers increasingly demand sustainable investments. Therefore research that investigates what value can be attributed to a company's work with its environmental and social responsibility is of particular interest. Beiting Cheng's research, as an example, proved that sustainability work and access to capital is highly interlinked. Such research can help investors make a better selection, eventually leading to better returns, and provide the companies with additional incentives for proactive sustainability work," says Cecilia Widebäck-West, Head of Corporate Sustainability at SEB.

Beiting Cheng, from Harvard Business School, was recognized for her paper *Corporate Social Responsibility and Access to Finance*. The paper has practical significance for both equity and debt investors and is of increasing importance



Practitioner Gunilla Hjalmarsson and keynote speaker Gordon Clark



Meir Statman



Beiting Cheng



Beiting Cheng, Cecilia Widebäck-West and James Gifford



The award dinner at the conference

Michael Barnett





Rob Lake



Practitioners enjoying a chat on the patio at Sigtuna Foundation



Ingrid Jansson

in the current financial climate. Co-authors were George Serafeim, Harvard Business School and Iannis Ioannou from London Business School.

“It was a great honour for us to receive the award and at the same time a reminder that more research with both rigor and relevance needs to be added to the agenda. Corporate social responsibility is not an additional tool or task for management, but a fundamental element that has been missing in corporate strategy. It leads us to rethink the very role of the corporation in society, and highlights the urgent need of refined research questions and innovative research designs, which is both a great opportunity and a big challenge facing CSR research today,” states Beiting Cheng.

In addition to the SEB Award, the Umeå School of Business Award for Best Student Paper was given to Ariel Meyerstein, University of California, Berkeley for his paper *On the Effectiveness of Global Private Regulation: The Implementation of the Equator Principles by Multinational Banks*.

“Papers presented and discussed at the PRI Mistra conference showed that we have now moved beyond identifying a simplistic link between socially responsible activities and financial returns. We have also become better at understanding the different priorities among environmental, social or governance challenges by different industries. Also, we are better at asking more refined questions about how pension funds, sovereign wealth funds, individual investors and institutional investors make use of nonfinancial information and react to the concept of socially responsible investing,” adds Beiting Cheng.

John Howchin, Secretary-General for the Ethical Council at the Swedish National Pension Funds and a member of the SIRP Mistra board, has followed the development of the research during a number of years.

“The quality of the research and the general level of the discussions at the conference were very high. We have certainly come a long way in recent years. The global financial system is in a crisis right now and I firmly believe some

of the research and lessons we have learned from our part of the system are crucial to resolving this crisis, for example proper ownership and long term investments,” states John Howchin.

However, another member of the SIRP Mistra board, Rob Lake at the UN PRI, hopes that future finance research will focus strongly on practitioners’ needs and less on aggregate ESG ratings. He also states that there is more to investment than finance.

“More interdisciplinary research is needed, bringing together fields as diverse as management, law, institutions, economics, ethnography, psychology, anthropology, politics, and international affairs. Moreover, research needs to be more strategic, addressing big picture issues such as strategic asset allocation, the impacts of externalities on large diversified portfolios, and the changing structures and governance of global capital markets,” says Rob Lake.

The PRI Mistra conference was one of the highlights in 2011 and a good opportunity to communicate and interact with practitioners and research fellows.

“The research in sustainable investments has produced many interesting results. Results that now need to be discussed between academics and practitioners. The conference provided a good opportunity for people to meet, and hopefully both the discussion and the strategic research will intensify in various ways,” says Ingrid Jansson, Chair of the SIRP Mistra board.

“We were very pleased to be able to work together with PRI’s expanding academic network to organise the conference on sustainable and responsible investments. SIRP in itself is a very fortunate academic research network because of long-term and generous research funding provided by Mistra. The network has now a momentum to continue doing research on challenging topics in financial markets and beyond”, concludes Lars G. Hassel.

For more information about the presentations and papers, please visit the conference site at www.sirp.se.

Omissions Dominate Emissions

According to a 2011 KPMG survey the vast majority of large listed Nordic companies nowadays publish integrated or stand-alone sustainability reports.

MORE THAN 70 PERCENT of large Swedish companies published a sustainability report in 2011; in Finland and Denmark, reporting is even more widespread, with 89 and 91 out of 100 companies disclosing their sustainability performance, respectively. Good news indeed – and a further step towards the mainstreaming of ESG practices in the Nordic context.

However, what the KPMG survey did not make sufficiently clear is that quantity does not necessarily equal quality in this context: unfortunately, only a fraction of these sustainability reports provide data that can serve as a basis for even basic performance analysis. For example, a study of the Sustainable Value research group, reporting on a value-based assessment of the carbon performance of 120 Nordic companies, finds that less than 20 out of the 89 Finnish companies mentioned above disclose usable carbon performance data. Some companies choose to report qualitatively on their carbon performance, while the majority of those companies that do report emissions data only do so for selected parts of their operations.

These discrepancies in carbon reporting are not merely a Finnish problem: In her European-wide investigation of the completeness of GHG-emissions reporting by 438 companies, Andrea Liesen of the Sustainable Value research group finds similar inadequacies having examined more than 4,000 corporate reports: On average over the five year period from 2005 to 2009 only every fourth company reports GHG-emissions that cover the entire company. The vast majority of companies from the European Union report GHG-emissions on a selective share of their operations or limit their reporting to specific geographical areas, while other companies choose not to mention what is - and what is not - included in their GHG-emissions reporting. Put succinctly, today's corporate sustainability reporting is full of omissions not emissions.

The low quality in corporate GHG-emissions reporting comes as a surprise finding in the light of the longstanding efforts of great initiatives such as the GHG Protocol and the Carbon Disclosure Project. In fact, both initiatives require companies to report direct and indirect (Scope 1



Tobias Hahn



Andrea Liesen



Ralf Barkmeyer



Frank Figge

and 2) GHG-emissions on group-wide activities. However, between 2005 and 2009, on average only 15 percent of the reporting companies strictly followed these guidelines and reported complete direct and indirect GHG-emissions for a group-wide reporting boundary. This figure is alarmingly low and implies that an assessment of corporate climate change performance across company boarders cannot simply be done on the basis of the raw reported GHG-emissions data. Good news in this context is that a strong positive trend can be identified: from only 9 percent of companies reporting complete absolute levels of GHG-emissions in 2005, their share rose to 23 percent in 2009.

Despite this positive development the basic facts illustrate that incomplete GHG-emissions data currently represents a strong constraint for research on corporate climate change performance. Learning to detect and handle incomplete corporate environmental performance data will be crucial to users in the future.

Sustainable Value consists of Frank Figge and Tobias Hahn at Euromed Management School and Ralf Barkmeyer and Andrea Liesen at the University of Leeds.

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Book Release at SIRP

In March 2011, the Swedish section of SIRP released an anthology about their research in sustainable investments. The book *Hållbar utveckling – från risk till värde (Sustainable Development – from Risk to Value)* was written in cooperation with PwC and published by Studentlitteratur.



Tommy Gärling

Mingle after book release at PwC



THIS IS THE FIRST Swedish book that takes a broad view of how financial markets can become more sustainable. The book was written by Programme Director Lars G. Hassel, together with 15 of the researchers within the SIRP Mistra programme.

“Actively working with sustainable economy is no longer a side benefit, but a concern for business owners, directors, auditors, financial analysts, investors, managers and especially the employees,” says Lars G. Hassel.

The book release at PwC in Stockholm was very well attended and included presentations by Lars G. Hassel, Tommy Gärling and Henrik Nilsson.

Subjects covered in the book are, for example: *Sustainable Venture Capital Markets, Improving Measurements of Companies’ Environmental Performance, Impact of Incentives, Sustainable Development in Swedish Industry, Institutional Investors’ Fiduciary Duties* and *Sustainable Investment Portfolio Performance and Tracking Error*.

Delegated Portfolio Management

Any investment fund has to hire the best managers to allocate their funds. One of the key issues is how to select managers from a pool of candidates and what kind of contract to offer so that the selected manager has an incentive to pursue the interest of the investors.

GREEN INVESTMENT FUNDS meet the same challenges as mainstream funds with one additional element. The portfolio managers have to accept constraints that may restrict the way in which they invest. In fact, screening criteria imposed by social responsibility criteria may limit their possible allocations. This additional restriction may force a manager to demand extra compensation. In fact, it is often the case that SR funds demand higher fees than conventional ones.

To study this problem, researchers from the University of Rome at Tor Vergata, Annalisa Fabretti and Stefano Herzel, have developed a model of Delegated Portfolio Management (see SIRP WP 2010-07, to appear in the *European Journal of Finance*). In the paper, they propose an incentive mechanism to induce the manager to act optimally in the interests of the investor even in the case of asymmetrical information. They also examine the problem of evaluating the manager's skills and of selecting the best managers.

An interesting result of the paper is that the investor can offer compensation composed by two terms: the first one proportional to the difference in performance between a conventional and a Responsible Investment (RI), the second one dependent to the skills of the manager.

The latter term gives compensation for the unexploited ability of the manager due to the restriction in the investment set, however such a term is inversely proportional to the specific skill the manager has in the RI markets and vanishes if the manager only specializes in RI assets. Hence, this result provides formal proof of the fact that an intrinsically motivated manager does not require extrinsic incentives.

Moreover, according to this result an investor can attract managers with better specific RI skills from a group of managers with a given mainstream skill level; in fact by fixing a minimum desirable RI skill level and offering a bonus according to such a level, only managers with a higher RI skill level will find the contract interesting and



Annalisa Fabretti



Stefano Herzel

will accept the mandate. In other words the investor ought not to offer more money to attract better managers, with a stronger motivation to work on RI.

A paper by the same authors, to appear in the book 'Entrepreneurship, Finance, Governance and Ethics' edited by C. Mallin, D. Cumming and R. Cressy and published by Springer, extends the above results by determining the level of skill that a portfolio manager should have in order to offset the negative effect due to the restriction of the investment set, thus providing a theoretical grounding to the hypothesis that an active management strategy can offset the losses due to the reduction in the investment set.

Climate policy and Impact on Firms

There is no scientific consensus concerning the impact of stringent environmental policy on firms' competitiveness and profitability. Tommy Lundgren, researcher SIRP and Umeå Business School has published two studies, which have received great interest.

FROM THE TRADITIONAL 'static' point of view there are productivity losses to be expected. On the other hand, the so-called Porter hypothesis suggests the opposite; i.e., due to 'dynamic' effects, ambitious climate and energy policies could actually be beneficial to firms in terms of enhanced profitability and competitiveness.



Tommy Lundgren

The study *Climate Policy and Profit Efficiency* is based on Sweden's manufacturing industry during 1990 to 2004. Tommy Lundgren's main purpose is to specifically assess the dynamic effects of the Swedish CO₂ tax on firm profitability. The empirical methodology is based on stochastic frontier estimations and the results confirm the Porter hypothesis for some sectors, while rejecting it in others. Thus, in general, the argument that stringent environmental policy has positive dynamic effects that an offset cost related to environmental policy is not corroborated.

Tommy Lundgren's second study, *Environmental Performance and Climate Policy* analyzes environmental performance (EP) at firm level and the effectiveness of environmental policy along with other possible determinants.

In particular, the empirical analysis aims at exploring the relationship between the actual EP of firms in terms of CO₂ emissions per output unit, and one aspect of Swedish environmental policy, the CO₂-tax. To achieve our objective we use a panel data of Swedish manufacturing spanning over the period 1990-2004.

The results suggest that EP has improved in all sectors of manufacturing. The study also shows that production increases while emissions decrease in many sectors, indicating a decoupling of economic growth and environmental degradation. Furthermore, firms' EP responds to changes in the CO₂-tax and fossil fuel price, but is more sensitive to the tax, indicating different EP behaviour among firms depending on why the cost of fossil fuels change.

Several sectors also display a positive tendency over time in EP, which may suggest that EP is to some extent stimulated by an overall boost in environmental awareness in society and among firms.

In January 2011, Tommy Lundgren held a seminar about his research at the Swedish Environmental Department and the audience showed great interest for his findings. In August, Tommy Lundgren was invited to the University of Otago in New Zealand to present his research.



SIRP Mistra internal workshop in Bilbao, May 2011



Good Performance of Factor-neutral Sustainable Equity Portfolios

Research conducted by Rickard Olsson at Umeå School of Business demonstrates that it is possible to construct portfolios with strong financial performance while satisfying stringent sustainability criteria as well as typical institutional risk management constraints.



Rickard Olsson

THESE RESULTS BEAR directly on the objective of the Mistra research programme, which is “to find out how sustainable investment practices can create added value for institutional investors and identify barriers to mainstreaming such practices”. The results should also help sustainable funds in setting investment objectives and in performance evaluation.

According to prior research, sustainable mutual funds appear to perform no worse than other mutual funds and sustainable funds constructed by researchers often display positive risk-adjusted returns.

A mainstream argument, however, is that the high risk factor exposures and tracking error of sustainable equity funds hamper sustainable investing among investors such as institutions, which operate under tracking error and risk constraints.

The on-going project evaluates the performance of portfolios aimed at fulfilling both sustainability criteria and typical investor constraints on factor exposures and tracking error.

A combination of positive and negative screening is used to define increasingly sustainable investable sets of stocks, from which increasingly sustainable portfolios are constructed. While factor exposures and tracking error are controlled by using portfolio optimization and factor models, Olsson examines how risk-adjusted performance varies with portfolio sustainability (screen stringency). This is done for many levels of portfolio sustainability and across all areas of sustainability. The portfolios are long-only, since many investors are precluded from taking short positions.

The main findings on S&P500 stocks with KLD ratings for 1992-2010 are encouraging for sustainable equity investing. Most sustainable funds return more than the S&P500. Most factor neutral sustainable portfolios enjoy statistically significant positive Carhart alphas and generally outperform equal- and value-weighted portfolios. No sustainable portfolio has a significant negative alpha.

Portfolio optimization is seen to reduce factor exposures and tracking error relative to equal- and value-weighting. The study also documents the relation between tracking error and screen stringency.

Moreover, results obtained on additional sustainable strategies, including best-in-class screening, multi-dimensional screening and portfolio sustainability score maximization, reinforce the main findings.

The study also addresses some issues largely unnoticed in prior research. The standard Carhart factor model is replaced by an alternative model in order to avoid potentially inflated alphas for the S&P500 universe. Ties among sustainability scores occur. A simple tiebreaker procedure reduces ranking ambiguity and also portfolio turnover.

The next project phase will evaluate the impact of transaction costs including price impact on the performance of sustainable strategies. Whether portfolio optimization under transaction cost control can improve sustainable portfolio performance net of transaction costs will also be examined.

Sustainable Investments and Markets

Sustainable Investment Portfolios

Jeroen Derwall, Kees Koedijk, Rob Bauer

This project represents the first comprehensive review of SRI performance that addresses the need for a specific focus upon individual criteria underlying SRI (i.e. ESG and ethical screens) in order to better understand the return and risk features of SRI approaches. The results clearly show that better understanding is needed regarding whether or not investor preferences are strictly financial. Also the question whether investors/analysts properly anticipate the relation between ESG and firms' cash flows over both the short-term and long-term is addressed within this theme.



Rob Bauer

Ethical values and trading decisions of institutional investors

Jeroen Derwall, Nadja Guenster



Jeroen Derwall

We compare the trading behaviour of socially responsible (SR) institutional investors to conventional investors. Because SR investors should not only care about the risk-return trade-off but also about social implications of their investments, we expect a different response to financial news: if a company experiences bad financial news but at the same time keeps its CSR standards high, SR investors should be less inclined to walk away. If a company experiences good financial news combined with high CSR ratings, we expect SR investors to favour the company even more.

Sustainable Investment Portfolio Performance and Tracking Error

Rickard Olsson

Evaluates the performance of equity portfolios to satisfy both stringent sustainability criteria and other typical institutional investor risk constraints. Portfolios are constructed for different levels of portfolio sustainability

(screening stringency) and different sustainability criteria. The main results for S&P500 stocks with KLD ratings in 1992–2010 indicate that the constructed factor neutral sustainable portfolios often generate significant Carhart alphas and generally outperform equal- and value-weighted portfolios. Results on additional sustainable strategies, including best-in-class screening and portfolio sustainability score maximization, reinforce the main results. The evidence on the performance, factor exposures and tracking error of different sustainable strategies should help in setting investment objectives and performance evaluation. The project demonstrates how portfolio optimization can be used to construct high-performing sustainable portfolios to meet typical institutional risk constraints.

The impact of credit and ESG ratings on Analysts' Forecasts

Stefano Herzel, Pontus Cerin, Rocco Ciciretti, Alessandro Giovannelli

The recent financial crisis showed that traditional ratings are often inadequate to assess the effective risk of financial investments. The aim of this project is to measure the importance of social rating (ESG) on professional analysts' forecasts of financial performances. To this goal, we merged in a unique dataset the I/B/E/S Detail data on Analyst Forecasts, the social ratings provided by KLD, and the leading macroeconomic news from 1997 to 2004. We are also proceeding into the integration of data from Asset4 and traditional credit rating agencies. The on-going econometric analysis is providing empirical evidence to assess the information content provided by ESG rating on analysts' forecasts, after controlling for macroeconomic news releases.



Alessandro Giovannelli

A microstructural investigation of socially responsible investment

Stefano Herzel, Annalisa Fabretti, Marco Nicolosi, Flavio Angelini, Imon Palit



Imon Palit

Seeks a better understanding of the link between CSR practices and SRI. We show evidence of a reflexive effect between the trading behaviour of investors and CSR practices. For a clearer understanding of this link we empirically investigated micro-structural market data to study the correlation between CSR

practices and the trading behaviour of investors. Matching companies from Thomson Reuters Asset4 CSR ranking and London Stock Exchange order book datasets, analysis shows evidence that companies with higher CSR rankings are more robust to endogenous high frequency speculation. This is of benefit to practitioners looking for more stable and sustainable investment.

Sustainable and Commercial Property

Nils Kok, Piet Eichholtz, Andrea Chegut, Erkan Yonder

Aims to fill an important knowledge gap by focusing on energy efficiency, sustainability and corporate governance in global property markets. We aim to investigate environmental sustainability in the direct property market, the determinants of residential and commercial energy consumption, and especially how sustainability might add value to property developers and investors (listed and unlisted). The Global Real Estate Sustainability Benchmark (GRESB) is the first global effort to survey and assess the environmental performance of real estate companies and funds, assisting pension asset owners to take ESG into account in their real estate allocation.



Andrea Chegut

Sustainable Venture Capital Investments

Anders Isaksson



Anders Isaksson

Explores how private equity (PE) and venture capital (VC) funded ventures create sustainable growth. This includes research on both the supply side (investor behaviour) and the demand side (firm/entrepreneur) of private equity. The studies on investor behaviour explore how (and value of) ESG factors are incorporated in investment decisions, while studies on firm behav-

our investigate how entrepreneurial motives and values are linked to environmental concerns. Finally, empirical analysis is performed on cleantech VC investments in order to investigate to what extent cleantech is driven by VC investments. The project can help entrepreneurs to better understand how venture capital investors think and act, and investors are given the opportunity to develop best practice models and to use industry benchmarks. Policy makers will better understand how sustainable VC and entrepreneurship are best supported.

Sustainable Housing: The case of the Swedish private housing market

Pontus Cerin, Nils Kok

Explores whether there exist economic implications of energy performance as specified in the mandatory Energy Performance Certificates during sales of private houses in Sweden. Unique aspects – other than energy consumption – such as type of energy, suggested costs for energy improvements, heating technology, materials and radon are also tested against sale prices of Swedish housing. Since buildings account for about 40 percent of energy consumption within the OECD – and the existing building stock constitutes the vast lion share of these – the results of this project are paramount to investments towards sustainability. A market premium is detected for energy efficiency displayed in energy performance certificates. Buyers of properties also demand a rebate for cost efficient suggestions for energy improvements to compensate for the renovation burden.

The Role of ESG in credit markets

Daniel Hann, Jeroen Derwall, Rob Bauer, Roger Otten



Daniel Hann

The project intends to shed light on how companies' ESG profiles are related to their credit standings. The empirical studies altogether investigate the direct and indirect effects that various aspects of ESG may have on credit risk. The studies in project A10 provide evidence that better ESG tends to be associated with more conservative capital structures, higher credit ratings, and lower corporate bond yield spreads.

Sustainable Companies and Ratings

Improving Measurements of Companies' Environmental Performance

Anders Biel, Ulrika Lundqvist, Sofia Poulikidou

Aims to develop relevant sustainability evaluation criteria, both present and future oriented, for the two business sectors “automobile” and “forestry and paper”. This work includes presenting a transparent methodology for the operationalization to develop these criteria and for ranking the performance of companies based on these criteria. Based on a life-cycle model and three different weighting methods of environmental consequences, results show among other things that the use of fossil fuels in vehicles contributes to approximately 70 percent of their total environmental impact.



Sofia Poulikidou

Sustainable Corporate Governance

Lars Hassel, Henrik Nilsson with Eli Amir, London School of Economics, Juha-Pekka Kallunki, Oulu University



Henrik Nilsson

The project extends the resource-based view on environmental performance of the firm by introducing board composition and board member characteristics to explain leaders and laggards on environmental performance and environmental reporting. The project creates an ethical compass of the board by using the past criminal records of the CEO and directors as a proxy for the diversity of the board. The research demonstrates, among others, that the proportion of convicted board members in SIX 300 companies are negatively related to environmental performance and reporting quality. The papers have a potential to demonstrate the importance of a diversified board member structure and competence for the sustainability of the firm.

Value-based Sustainability Analysis of Nordic Companies

Ralf Barkemeyer, Breeda Comyns, Frank Figge, Zoe Foss, Tobias Hahn, Andrea Liesen

We have completed a pilot study of the carbon performance of 25 pulp & paper companies worldwide; for this pilot study, we have developed and successfully applied a web-based data collection mechanism aimed at a more efficient way of collecting corporate environmental performance data. We have also collected carbon performance

data for more than 200 Nordic companies from a range of different sectors, which will form the basis for the environmental sustainability performance analysis of Nordic companies with the Sustainable Value approach. The results of the analysis will provide tangible benefits for financial market actors and in particular SRI practitioners.

Sustainable Development in Swedish Industry

Tommy Lundgren SIRP/CERE, Runar Brännlund CERE, Per-Olov Marklund CERE, with Lammertjan Dam University of Groningen, Rolf Färe, Shawna Grosskopf Oregon State University

Adds knowledge about how policy induced and voluntarily adopted social responsibility behaviour affects the economics of a firm and their contribution to sustainable development. Results show that internal and external environmental policy indeed has an impact on the behaviour and performance of the firm. While some firms become more efficient or profitable due to policy, others experience the opposite. At sector level, carbon emissions per unit of output during 1990–2004 has decreased, mostly due to the introduction of a CO₂ tax in 1991. The project gives insights into relationships between many aspects that are relevant for understanding how to incorporate industrial firms into a sustainable society, and hence of interest to numerous stakeholders in society; policy makers, firm managers, and institutional and private investors, as well as academics.

The missing link between returns and CSR scores – Latent variables

Elena Stanghellini, Marco Nicolosi

The ability to comply with CSR standards varies across industrial sectors and from one ESG aspect to the other. For example, firms in the Financial sector may encounter less difficulty to comply with the Environment than firms in Oil and Gas. We built a latent variable Item-Response Model that takes these issues into account and measures the CSR ability of a firm accordingly. We used it to rank firms and to study the performances of Equally Weighted, Value Weighted and mean-variance optimal portfolios that select the best ones and exclude the worst ones. We also started to explore the dynamic version of the model.



Elena Stanghellini

Incentive Systems

Impact of Incentive System and Monitoring Frequency on Portfolio Managers' Investment Decisions

Tommy Gärling, Maria Andersson



Maria Andersson

Surveys show that practice in Sweden is to incentivize portfolio managers based on short-term performance. In general people prefer to reap immediate benefits. This is confirmed by the results of our experiments in that short-term bonuses paid out every year are preferred to nominally equally large long-term bonuses. We have also shown that shorter evaluation intervals lead to worse performance than longer evaluation intervals. A third question addressed during 2011 is whether investors diversify portfolios by taking both short-term and long-term value development into account.

Incentive Schemes for CSR Asset Management – Delegated Portfolio Management in a Dynamic Setting

Stefano Herzel, Annalisa Fabretti, Marco Nicolosi, Fausto Gozzi

The objective of this project is to formulate a theoretical model for the study of the incentive systems for CSR Asset Managers. Under the working hypothesis that it is possible through the active management of a SR fund to obtain financial performances that are comparable or even better than those of a conventional fund, we propose a way to set the incentives according to the skill of portfolio managers and to the difficulty of their task. An important aspect of the project is the empirical validation of the hypothesis.



Marco Nicolosi

Fiduciary Duty

Institutional Investors' Fiduciary Duty

Tommy Gärling, Joakim Sandberg

Aims to assess the extent to which the obligations that large financial institutions (e.g. pension funds) owe towards their beneficiaries (e.g. future pensioners) constitute an impediment to their effective engagement in sustainable investing. Our in-depth legal analysis suggests that fiduciary duties indeed hinder effective sustainable investing as they are formulated in contemporary law. Moreover our theoretical-exploratory work suggests that

it is difficult to fix this problem by any simple reformulation of those duties. Sustainable investing simply cannot be expected to always be in the interests of beneficiaries (irrespective of whether one understands these interests as financial, social or ethical). The project aims to make clearer both the current legal reality and the political possibilities for the future, which may help both legislators and representatives of the financial institutions.

A legal framework for fiduciary responsibilities encompassing the integration of SRI/ESG criteria

Sebastian Siegl

The legal interpretation of how the use of SRI/ESG considerations relates to the fiduciary duties for institutional investment managers' is unclear. To some extent this follows from the fact that the rationale used to motivate a new interpretation has largely been based on arguments related to the financial performance of SRI/ESG investment strategies. While the financial performance of SRI/ESG strategies is of paramount importance within the existing framework, a new framework could be based on other parameters such as a widened interpretation of the concept of "interest of the beneficiary" and a clear framework for SRI/ESG information disclosure. Either way it needs to be clarified how the inclusion of SRI/ESG criteria should be made not to conflicts with fiduciary duties.

Impact of Value on SRI Practice: A Comparison of Financial Professionals & Beneficiaries

Ralf Barkemeyer, Frank Figge, Andrea Liesen, Tobias Hahn, Frank Müller, Andreas Hoepner

We have finished a pilot survey into perceptions of SRI practitioners and will send out the final survey in late 2011. We are currently updating the Trends in Sustainability database, which will be launched in early 2012. We have also collected a large database of independent variables, which will be used to analyse and explain different sustainability agendas in different countries. We are also generating a database of international SRI practice, which will be ready by the end of 2011. Practitioners will benefit from the identification of issue areas in which there is a mismatch between the sustainability-agendas of SRI practice and those of their beneficiaries. The Trends in Sustainability tool will appeal to both the SRI community as well as a wider layperson's audience.

Fiduciary Duty, Future Scenarios and Value Priorities among Beneficiaries of Pension Funds

Magnus Jansson, Joakim Sandberg, Anders Biel, Tommy Gärling



Magnus Jansson

Aims to identify value priorities among beneficiaries of pension funds, taking into account temporal distance to time of retirement and dependency of future pension. A mail survey to a general sample of a net size of 1,000 Swedish future pension fund beneficiaries will address changes in value priorities and potential trade-offs

between sustainability values and individual financial outcomes during the adult life cycle. Provided that value priorities change during the life cycle, investment institutions could vindicate a broader mandate in their fiduciary duty.

Global Surveys and Experiments

Rob Bauer, Paul Smeets, Arno Riedl, Piet Eichholtz, Nils Kok

To understand the behaviour of individual investors with regard to socially responsible investing, we completed a large-scale research project in cooperation with Robeco. We surveyed and conducted experiments with about 3,000 individual investors on socially responsible investing and related issues. The project will give insights into the reasons why investors buy socially responsible mutual funds and what keeps other investors from not buying them. We will also provide insights into the optimal marketing strategies that



Paul Smeets

can be used by mutual fund families and banks to increase the number of socially responsible investors. The second project involves the Global Real Estate Sustainability Benchmark (GRESB), which is the first global effort to survey real estate companies and funds on their environmental and social performance.



Nils Kok

ESG Factors and Investment Decisions

Jonas Nilsson



Jonas Nilsson

Deals with the role of ESG factors in the decision making of investors. The overall aim is to increase knowledge on how investors combine financial and ESG factors when making the decision to invest according to sustainable principles. Results indicate that ESG factors are important to retail investors as ESG fac-

tors increase satisfaction with mutual funds. However, the complexity of the marketplace is a significant challenge for investors that wish to include sustainability in their investment decision. Moreover, investors do not seem to be consistent in their ESG preferences as they show considerable support for many (sometimes opposing) ESG strategies. This insight can help providers of SRI to produce better services and tools for decision-making.

Sustainable Governance among Swedish Pension Funds

Ian Hamilton

Examines how two different responsible investment strategies emerged among five national pension funds as a response to the national directive for responsible investment. Strategies on how to integrate environmental, social, and governance (ESG) factors in investment decision making are important for pension funds as they traditionally have focused on values-based risk management and seldom on the profit- or alpha-seeking opportunities of integrating ESG with the financials. The diversity of the pension system in Sweden allows the study to compare a national systems-oriented pension plan (income pension system) with a market-oriented (premium pension system). The main conclusion of this study is that the characteristic of pension schemes will have implications for how pension funds interpret and execute their fiduciary responsibilities given the exact same directive.



Ian Hamilton

Shareholder Activism, Corporate Governance and the Board of Directors

Rob Bauer, Frank Moers, Lei Chen, Michael Viehs



Michael Viehs

The overall aim of this project is to study whether shareholder activism and quality of the board of directors are effective governance tools. The results of this paper series will be beneficial for several parties, namely corporate managers, investors, and regulators. Our papers show how investors can monitor corporate managers, and which necessary steps can be undertaken by regulators to enhance the efficiency of corporate governance. Furthermore, we show the consequences of externally imposed regulations on the functioning of the board of directors. This project comprises several papers: three of them deal with shareholder activism and its effectiveness, while one describes the labour market for independent directors.



NATALIA SEMENOVA,
Åbo Akademi University

“The Value Relevance of Environmental and Social Performance”

With the growth of the UN PRI and the focus on ESG integration, it can be expected that the market learns to differentiate between ESG leaders and laggards. The thesis has

examined if E and S have extra-financial value for investors to explain stock prices by applying a conventional accounting valuation framework.

Natalia Semenova’s research demonstrates that environmental performance has value relevance beyond financial fundamentals. When it comes to the social performance dimensions, community and supplier relations enhance market value while higher ratings on employee relations are related to lower market values.

The complexity of the universal relationships is further examined by looking at two dimensions of environmental performance and by introducing environmental risk as an industry factor. Environmental preparedness (talk) pays off across industries, while the benefits of core environmental performance (walk) is company specific and varies across industries and their inherent environmental risk. Environmental performance is priced higher and it also increases operating performance for companies in low-risk industries, such as banks and insurance. In high-risk industries, such as oil and gas and utilities, environmental leaders are rewarded only if they are highly profitable. Superior environmental performance comes with lower financial performance and is costly.

The outcomes of the research are consistent for the MSCI US companies (2003–2008) and for the Swedish SIX 300 companies (2005–2008). To enhance the validity of environmental performance ratings provided by GES-Investment Services, the research also demonstrates that publicly available ratings converge to a uniform metric and provide consistent estimates across industries.



DANIEL HANN,
Maastricht University

“Stakeholder Theory in Finance: On the Financial Relevance of Nonfinancial Stakeholders”

This doctoral dissertation presents evidence that non-financial stakeholders affect the financial position and decisions of firms, thus supporting the view that their role in the interpretation of classic

finance problems needs to be reconsidered.

The traditional finance literature assigns little importance to the role of stakeholders other than that of investors and managers, when assessing the economic circumstances of the firm. Daniel Hann has studied the influence of key nonfinancial stakeholders on the cost of capital, stock return performance, and financing decisions of firms: Consistent with the theory that employee relations affect the financial standing of firms by influencing organizational performance and risk, his research shows that the quality of employment policies and practices explains the cross-sectional variation in credit risk.

Hann also finds comprehensive evidence that corporate environmental management is associated with significant differences in the cost of debt and credit ratings of borrowing firms, corresponding with the increasing legal, reputational, and regulatory risks associated with climate change and environmental incidents.

His research contributes to the on-going debate whether customer satisfaction is associated with abnormal stock returns, by rejecting the hypothesis that investors fail to correctly anticipate the future earnings effect of customer satisfaction, and thus excluding errors-in-expectation as a plausible cause for mispricing.

Finally, his analysis suggests that customers are able to influence the financial decision making of firms, by showing that firms certify their commitment to customer claims through the adoption of a more conservative financing policy.



MAGNUS JANSSON,
University of Gothenburg

“Psychological influences on the adoption of socially responsible investments”

The major bulk of research on SRI has investigated the financial performance of SRI compared to conventional investments. Other concerns, besides financial, have

attracted less attention. In this thesis behavioural determinants of SRI were investigated among groups of investors.

Magnus Jansson has investigated what impedes and motivates different types of investors in Sweden to adopt SRI. His research shows that there are important differences in motives for adopting SRI. While the main drivers behind SRI among institutional investors, independent of whether they are SRI or non-SRI, are financial and market concerns. Private and institutional asset owners also take normative concerns into account.

Institutional and individual asset owners thus have heterogeneous motives for SRI. However, also for individual asset owners beliefs about the return on SRI is the main determinant for being a socially responsible investor, while institutional asset owners are more influenced to take SEE-issues into account in order to reduce their financial and reputational risks.

The research indicates that among private asset owners a short-term profit maximization investment strategy impedes SRI while institutional asset owners focus on risk minimization, which in turn promotes SRI.

The SRI market in Sweden is almost totally dominated by institutional investors while the retail market has to a great extent been neglected by providers of financial products. One possible explanation for this could be that fund companies and other providers of investment products underestimate the importance of social, environmental and ethical issues for their private and institutional customers. Results from the thesis confirm that fund companies indeed underestimate the importance of SEE-issues, while they simultaneously overestimate the importance of financial return for their private and institutional customers.

As such, fund providers also seem to neglect the importance that altruistic values have in shaping investors' beliefs about the financial rationality of SRI.



SEBASTIAN SIEGL,
University of Gothenburg

“The legal implications of managing a SRI mutual fund”

The regulatory view on ethical criteria in fund management is that a fund's purpose is to generate maximal risk-adjusted return. Hence, acting in the best interest of the

unit holders has typically been interpreted as achieving best possible financial returns given the fund's risk profile.

SRI funds however, often have complimentary goals, and whilst SRI investments are now being justified by performance, the doctrine is also full of examples where SRI investing is said to have other objectives, such as creating a more sustainable society.

Other objectives are legally permitted under the precondition that they are clearly communicated in the fund's investment policy. Hence it can be put in question whether the lawmaker has made the right assumptions about how fund investors make an investment decision.

Furthermore, SRI funds are far from homogenous and without a wide-ranging or universal definition or a formal standard this makes it difficult for individual investors to understand what defines a SRI fund. This stresses the importance of making available standardized, transparent easily understandable and comparable ex ante purchase information enabling the fund investor to properly evaluate the fund's financial and SRI profile.

The information requirements that have been specified in the mutual fund legislation by the lawmaker and the Supervisory Authority, are clearly focused on the fund's risk and return objectives denoting what asset classes, sectors and regions the fund is allowed to invest in.

That SRI mutual funds sometimes exhibit mutual purposes and do not solely strive to achieve risk adjusted returns is not always conveyed properly to the mutual fund investor. It should therefore be more clearly specified what information a mutual fund company must provide to an investor ex ante and ex post a fund purchase also fixing what type of information concerning the fund's SRI objectives that a mutual fund company must provide to prospective and existing customers.

“Mistra has shown great leadership in the foundation world by working to align its investment approach with its mission. By funding SIRP, Mistra took an innovative additional step. SIRP has fostered the development and publication of research which, I believe, is not only of assistance to other foundations wishing to pursue the same journey but which also has significant relevance to the broader investment community. The need for a long term perspective in the capital markets is greater than ever.”

David Blood, Senior Partner, Generation Investment Management

Sustainable Investment Research Platform is a unique international and interdisciplinary research programme and involves 50 researchers in seven European countries.

The objective of SIRP is to find out how sustainable investment practices can create added value for institutional investors and identify barriers to mainstreaming such practices.

The research includes: *Sustainable Investments and Markets*, *Sustainable Companies and Ratings*, *Incentives Systems* and *Fiduciary Duty*.

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For more information, please visit www.sirp.se.

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The map depicts the participating Universities and Institutes in SIRP Mistra

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