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The Motivations of Institutional Investors towards the adoption of Sustainable Finance Practices



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**Master 2
Advances in Finance and Accounting
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Preface:

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SUMMARY

- ABSTRACT..... 6**

- INTRODUCTION..... 7**

- SECTION 1 : LITERATURE REVIEW 11**
 - PART 1 – FINANCIAL PERFORMANCE 12
 - I. Portfolio performance 12
 - II. Asset performance..... 15
 - III. Controversial methodology and data..... 16

 - PART 2 – ACTORS AND REGULATIONS 19
 - I. Actors 19
 - II. Regulations..... 21

 - PART 3 – NON-FINANCIAL MOTIVATIONS..... 27
 - I. Portfolio managers 27
 - II. Retail investors..... 29

- SECTION 2: RESEARCH PROBLEM..... 31**

- SECTION 3: METHODOLOGY 35**

- CONCLUSION 42**

ABSTRACT

Whilst there is a growing interest in the use of SRI and ESG practices in the strategies of institutional investors, there are very few articles that discuss the motivations of institutional investors to adopt these practices. This research project hopes to fill this gap in the subject.

Based on the literature review, we were able to make assumptions about the concerns of institutional investors when considering sustainable practices for their strategies. Three concerns were found. The first one is financial performance. The second one is regulations. The third one is non-financial concerns, for example reputation or climate goals.

These assumptions based on the literature review will help us create a questionnaire in order to gather our own data. This data will allow us to have a general understanding of the motivations of institutional investors to adopt SRI and ESG practices, which may or may not be in line with our assumptions.

INTRODUCTION

In order to understand the importance of the adoption of the approach SRI and ESG and the stakes involved, a very brief summary of the history of these concepts needs to be explained. The concept of socially responsible investing was started very early by a society called the Quakers in England in the 1600s for religious reasons. It was then developed by churches in the 1920s who chose not to invest in tobacco and alcohol. A few decades later, the first “ethical” mutual fund was created in the 1970s and was called Pax World Fund and was primarily concerned with weapons and war, they condemned the Vietnam war at the time. The approach became more recognised with a large divestment in South Africa because of Apartheid. It was then called “ethical” investing and is maybe one of the reasons why investors have such difficulty in understanding the concept nowadays, as it is not purely ethical anymore. In the 1990s, SRI then extended its definition incorporating environmental, social and corporate governance concerns in the decision making for investment, called the ESG criteria. It is at that point where SRI became an investment strategy seeking returns and performance. Investing had a new goal, which was not only financial. In the 2000s up until now, SRI has been highly recognised and analysed by many researchers. The high number of articles published cover many topics on this theme. However, one which is especially redundant is the financial performance of sustainable finance. Indeed, in a world where finance rhymes with returns, financial performance seems to be one of the main concerns for investors when adopting SRI and ESG practices.

Sustainable finance or ethical finance differentiates itself from conventional finance by the way the investors evaluate its performance. Indeed, the former is not only based on financial measures but also on ecological, social and governance ones. The financial and extra-financial performances are realised thanks to socially responsible investments (SRI) which have a long term vision and take into consideration the ESG criteria thanks to analyses and selection processes. According to the Principles for Responsible Investment (PRI)¹, “The PRI defines responsible investment as a strategy and practice to incorporate environmental, social and governance (ESG) factors in investment decisions and active ownership.”

The ESG criteria is quite straightforward, however, the definition is broad like the whole

¹ <https://www.unpri.org/>

concept of responsible finance. According to the website LelabelISR², “ESG criteria (Environmental, Social and Governance) are analytical criteria used to assess the consideration of sustainable development and long-term issues in corporate strategy.” They are a way of evaluating the potential outcomes of an investment according to environmental, social and governance factors. The method used to incorporate them in the investment strategy is open to the investors will. However, the key point of SRI is that the decision is driven by financial goals rather than ethical ones. It is a way of fully assessing the risks and opportunities by thinking “outside the box”. It may also facilitate the dialogue between the counterparties, which can be a way of adding value to the investment.

Since the beginning of sustainable finance many organisations have been created in order to raise awareness and regulate the sector. The United Nations Organisation has been a strong supporter of sustainable finance since the beginning. They supported responsible finance by launching the United Nations Environment Programme Finance Initiative (UNEP FI) in 1992 and then the United Nations Global Compact pact in 2000. The former entity then launched the Principles for Responsible Investment (PRI) which plays an important part in disclosing information about responsible finance. The PRI was created in 2006 at the New York Stock Exchange, its aim is to educate investors on responsible investing. It explains the strategy behind it and how to incorporate the ESG criteria in the decision making. Responsible investing is a way to take into consideration risks that would not be considered otherwise.

On a more national level, the Association Française de la Gestion Financière, in addition to the AMF, is a strong actor in responsible finance in France. It was created in 1961 and gathers all the professionals working in asset management. They can be asset management firms or asset management branches from banks or insurance companies. It has been a defender of sustainable finance since the beginning and communicates all the information around this theme. French actors are very engaged in this movement and France is one of the most active countries in the world. They take great interest in sustainable development, and asset managers take into consideration this notion thanks to SRI funds, integration of ESG issues, active ownership etc... What’s more, the AFG is a great way to communicate the regulation and/or expectation of the French Government or the European Union.

It is important to realise how significant sustainable finance is becoming and the two entities mentioned previously, along with others are the main reasons for this important development.

² <https://www.llelabelisr.fr/>

More than 9 500 companies based in over 160 countries are now committed to responsible and sustainable corporate practices under the UN Global Compact. More than 2 300 signatories to the PRI representing more than 80 trillion assets under management. Approximately one in nine dollars of professionally managed assets are involved in socially responsible investment and one out of 6 dollars in the EU. Nearly every Fortune 500 company releases some kind of sustainability report.

As we have just seen, actors are taking sustainable finance seriously and are becoming more and more influential in the finance sector. It seems that investors in this sector can be potentially impacted by their decisions and should be or are already concerned.

The exponential growth of sustainable finance is mainly explained by the fact that it has a bigger cause behind it. Indeed, the ultimate goals were defined in 2015 at the United Nations General Assembly where all of its actors articulated 17 Sustainable Development Goals representing many different areas in order to meet the 2030 agenda. The idea of elaborating goals in order to improve human lives and protect the environment actually started in 1992, we can observe that it started at the same time as SRI developed itself. However, nowadays it is the environment which is discussed the most as it is a threat to everyone and everyone is an actor in its degradation. This also means that everybody can be an actor in its recovery. Indeed today, investors are talking about climate risk. It is an aspect that has to be considered in every investment as it can have potentially great consequences.

We can see that the adoption of sustainable finance does not depend only on financial performance or regulations put in place by influential actors, there are also non-financial motivations. Some of them are climate risk and climate goals. Investors are becoming more and more aware of these notions and are starting to consider them in their strategies. Other non-financial motivations exist that we will see further in the literature review.

The reason why focusing on the motivations of institutional investors is so important is that the European Commission is counting on their investments in sustainable finance to achieve the climate targets set by it. Indeed, according to the Commission, an estimated “180 billion of additional investments, every year until 2030” is needed to reach the targets (European SRI study). What’s more, institutional investors have a key position as they are intermediaries between firms and retail investors, which also have their role to play.

Jonathan Peillex et al. (2014) and Arjalie’s (2010) carried out similar research but focused on factors like human resources slack, leverage or financial crisis that would encourage agents to

create SR funds. In our opinion, their research projects combined with ours and others will provide us with a better understanding of the perception of investors towards sustainable finance and what they expect from it.

Another key objective is to observe how well investors understand and define sustainable finance and the notions that come with it. For example, in the article Anett Wins et al. (2016), the authors found that 86.2% of SR fund investors think that sustainability in finance covers “ecological, social, ethical and economic issues”. However, for investors who are interested in sustainable investment only 66.7% have this view and only 42.1% for investors who are not interested in sustainable investment. Many other examples show that sustainable finance and other notions linked to it are still not clear for investors which has a negative effect on the adoption of SRI and ESG practices.

In the introduction, we saw how broad the subject is and the multiple factors on which SRI and ESG practices depend to be adopted around the world. We also mentioned how important this subject is and that over the years it will be an increasing issue and will undoubtedly become one of the main focus of governments. With this in mind, this research project will be divided into three sections. The first section will be the literature review divided into three parts. The first part of the section will focus on the financial performance of sustainable portfolios and assets but also the limitation of the articles on the subject.

The second part will consider the actors and the different policies and regulations which are having and will have impact on the sector.

And the third part will focus on the non-financial motivations.

The second section will concentrate on the research problem, which will naturally emerge from the literature review.

The third section will be a description of the methodology that will be used, in order to demonstrate that our research problem is plausible.

Finally, the conclusion will be the opportunity to highlight the main arguments but also the possible limitations of the research.

SECTION 1: LITERATURE REVIEW

Our literature review is based on the adoption of sustainable finance practices by institutional investors.

In the first part, we will be studying the financial performance of socially responsible finance by first focusing on socially responsible fund portfolios then focusing on the assets that constitute it and lastly by discussing the controversies of the research projects on this subject. The second part of this literature review will focus on influential actors and regulations, which seem to have an important impact on the sector.

The last part will discuss non-financial motivations for adopting SRI and ESG practices in regards to portfolio managers but also retail investors who are increasingly interested in the topic and might have a strong impact on portfolio manager's decisions. Non-financial motivations seem obvious when talking about ethics because we usually associate the latter with non-financial factors, however, it is not so when talking about finance. This is why it is interesting to see the relation between the two.

A few authors have already worked on the reasons why SR funds are created (J. Peillex et al, 2014; D. Arjalie, 2010). They analysed the importance of size, financial performance, leverage, media coverage, ESG performance or the role played by the financial crisis and the societal actions like the PRI which we will be discussing in the second part.

One article, by A. Wins et al (2016), is particularly interesting as it used the same methodology as we will. By the use of a questionnaire, the authors analysed sustainable investors, conventional investors which were interested in the subject and conventional investors which were not interested in the subject, that worked in private German mutual funds. They found that all the investors thought that SR actions of a company affect its price positively but that the performance of SR funds was worse than conventional funds. What's more, they concluded that the first obstacle of the adoption of sustainable practices is the financial performance and also that investors feel they are not informed enough.

PART 1 – FINANCIAL PERFORMANCE

In this part, we will be discussing the financial performance of sustainable practices and how it is perceived. By analysing the financial performance of sustainable finance regarding the portfolio of funds but also focusing on the specific assets, we might be able to discover if it is or can be a real motivation for institutional investors.

In the first subpart, we will be analysing financial performance of ethical fund portfolios.

In the second subpart, we will briefly discuss the financial performance of socially responsible assets.

Finally, in the third part we will be discussing some controversial aspects about the research projects we analysed in the previous parts.

I. PORTFOLIO PERFORMANCE

First of all, we can clearly see in the many different articles we studied that the conclusions on the performance of socially responsible portfolios differ quite strongly. However, we notice that the opinion we see the most is that sustainable practices do not have a positive or a negative impact on returns. What's more, we realise the difficulty of the theme as the results are never clear and can be influenced by many factors.

In this part, we are trying to consider if financial performance can be a motivation for investors to adopt socially responsible practices. In other words, can these practices enhance performance or returns for an institutional investor, as we take into consideration that this point has a high chance to be one of their objectives.

As previously mentioned, we want to know if financial performance is one of the main motivations for institutional investors to adopt socially responsible practices. In order for us to conclude this, the articles would have to show a clear positive impact.

Not many have reached this conclusion but some have (T. Verheyden et al. 2016; E. Dimson et al. 2015). T. Verheyden et al. (2016) compared an unscreened portfolio with a portfolio where two different ESG screens were applied. The authors found results on the rates of return, the downside risk and the portfolio diversification. They found that "ESG screening has very little impact on the original universe, with returns being slightly higher but strongly

correlated, while risk is slightly lower”. However, the results are influenced by the region, with better results for the European Union and North American regions and the industry. What’s more, they found that even if the unscreened portfolio showed a higher diversification ratio, the difference with the ESG screened portfolio is very small and that on average the screening “does not lead to large diversification losses”. They actually conclude by saying “the amount of specific risk introduced by ESG screening is more than offset by the excess risk-adjusted returns it provides relative to the unscreened universe”.

Another domain where sustainable finance has proven to be financially performant is active ownership. E. Dimson et al. (2015) found that “ESG engagements generate a cumulative size-adjusted abnormal return of +2.3%” after the initial engagement and +7.1% for successful engagements and no market reaction for unsuccessful engagements. They conclude that, “active-ownership engagements increases shareholders’ value on average and the positive returns are apparent for engagements on both CG and ES themes”. CS meaning corporate governance and ES meaning environmental and social.

These findings could be a justification for adopting sustainable practices, however, a much larger number of research projects concluded that they have neither a positive nor a negative impact on the financial performance of funds. Moreover, this conclusion led to some hypotheses on the subject, where one in particular has often been mentioned, it questions whether or not socially responsible funds are distinguishable from other conventional funds. This is an important point as the first should have different practices and strategies or else, there would be no point differentiating them, return wise or any other way.

As we have said previously, many articles have not reached a clear result between a positive impact or a negative impact. However, their conclusions provide important information. (S. Utz et al. 2014; R. Bauer et al. 2007; R. Bauer et al. 2004; A. Gregory et al. 2005; S. Hamilton et al. 1993; R. Burlacu et al. 2003; “Sustainable Investing, establishing long-term value and performance”, M. Fulton, B. M. Kahn and C. Sharples, Deutsche Bank Group Advisors 2012; C. Revelli et al. 2013).

Rob Bauer has written two articles that conclude there is no significant differences in return between ethical and conventional mutual funds and that investors can allocate their money to ethical funds without being subject to a negative impact. One of them concentrates on the Canadian funds and the other one on the UK, German and USA ones. However, what is interesting is that the authors had some difficulty in differentiating between socially responsible funds and conventional funds in the first article but not in the second. This

realisation is important, as it is often mentioned in articles (S. Utz et al. 2014; S. Hamilton et al. 1993). In the article written by R. Burlacu et al. (2003), the authors also found that there are no significant financial performance differences between the two funds. Three hypotheses were found coming from that result. The first one is that sustainable finance may have no costs, the second one is that a temporary disequilibrium may exist and the third one which joins our previous conclusions is that ethical funds might not be as ethical as they let investors believe. We will not be discussing them here. Nevertheless, it is interesting to see that the subject is complicated and is more than just a matter of financial performance.

There is also evidence that SRI mutual funds do not deliver the same amount of returns as a conventional fund (S. Jones et al. 2008; L. Renneboog et al. 2008; N. Amenc et al. 2010).

In the article written by G. Capelle-Blancard (2010), which actually shares many points with the other articles cited previously, SRI screening can have a cost but only “industrial screens (such as avoiding sin stocks) pull down financial performance”. The author concludes that it is possible to impose some restrictions based on ethical values by using the best-in-class approach, which has a minor impact. However, this method can be in some sense controversial because ethical funds that follow this strategy are sometimes barely different to conventional ones which brings us back to the previous observation.

Another important point which has been mentioned quite often and is a strong belief in sceptic investors is that sustainable finance involves more costs and so can impact the returns. Three specific costs are highlighted. The first one is related to the fact that investors need to gather specific information on sustainable finance practices in order to determine which stock belongs to the SRI universe. The second one is linked to the fact that to be sustainable an investment must meet certain requirements which weakens the diversification opportunities. The third one is linked to active management, if the SR portfolios are small their management might generate higher information and transaction costs and managerial fees. However, these arguments are often dismantled by the articles mentioning them, proving that the cost may not be a legitimate reason for not engaging in sustainable finance (C. Revelli et al. 2015; L. Becchetti et al. 2014; J. M. Puashunder 2016).

To conclude, there is no clear answer on the financial performance of ethical fund portfolios. Some positive and negative evidence exists, especially on the fact that sustainable practices can be more costly, but a lot more exists on the neutral impact of its performance. From this last conclusion the authors came up with the hypothesis that ethical funds might not be very

different from conventional funds. This would put into question the real objectives of these types of funds.

II. ASSET PERFORMANCE

In order to have a complete opinion on the subject it seemed interesting to analyse not only the socially responsible funds performance based on their portfolio but also on the specific assets they invest in. This would allow us to have a more comprehensive view of what could be financial performance as a motivation for institutional investors. Unfortunately the literature is not as complete as for the previous theme.

The overall conclusion regarding the financial performance of socially responsible stocks is not clear like for the portfolio performance. It seems that at some point they do deliver abnormal returns compared to conventional stocks (M. Statman et al. 2008; Denis Dupré, Isabelle Girer-Potin, Sonia Jimenez-Garces et Pascal Louvet 2009; M. J. Charlo et al. 2013). Alexander Kempf et al. (2007) analysed stocks included in the S&P 500 and the DS 400 and used a basic strategy which consisted of buying high socially responsible ratings and selling low socially responsible ratings. They discovered that this strategy led to a high abnormal return. However, this extra return led to two questions, “Does it result from a temporary mispricing in the market or does it compensate for an additional risk factor?” The first question is dealt with by Denis Dupré et al. (2009). The authors explain that the increase in price of socially responsible stocks are justified by the emergence of social ratings. Indeed, social ratings encourage investors to buy socially responsible stocks which drives the prices up. However, they conclude by saying that another empirical study could show that at first the prices would go up and so inflate the returns but then after some time the demand and offer would equilibrate to an inferior level to conventional stocks.

Another point has to be mentioned. In the article of M. Statman et al. (2008), they do demonstrate that socially responsible stocks had a return advantage compared to conventional stocks, however, the extra return was compensated by the loss of not investing in sin stocks. In fact, H. Hong et al. (2007) show that socially responsible investors pay a financial cost by not investing in these types of stocks and consequently have an impact on their market.

To conclude, it seems that socially responsible stocks have a positive impact on financial performance. However, this raises the question of whether or not they are for the moment

mispriced on the market as they are a relatively new product. What's more, there is evidence that socially responsible investors are missing out on the financial performances of sin stocks which could cancel the benefits of ethical stocks.

III. CONTROVERSIAL METHODOLOGY AND DATA

As we can see in the previous parts, no clear results can be found and the general conclusion is that socially responsible finance has neither a positive nor a negative impact on returns for different reasons. However, it seems that investors are quite pessimistic about its financial performance despite the studies. One of the reasons might be because the methodology and the data are questionable in this theme of study.

According to the European SRI study elaborated in 2018 by Eurosif “financial advisers still today perceive sustainability-oriented products as presenting a negative trade-off with returns – despite multiple studies pointing to the opposite”. Is it a sign of bad faith or do they truly think sustainable finance will deliver a smaller return? It is difficult to say. In any case as the study says, it highlights the information asymmetry between clients and advisors. Another example can be observed in the article published by Arno Riedl and Paul Smeets in 2016. Thanks to a survey, they showed that conventional funds and socially responsible investment funds are rather pessimistic about the financial performance of SRI funds. Only 16.5% and 14.5% of them think that SRI will deliver higher returns. They observe that the strongest reasons for investors to pursue SRI is intrinsic social preferences and that they are ready to lose a portion of financial performance to it. This explains in part one of their conclusions that investors who think SRI equity funds perform better are not more likely to hold them.

One explanation that can put investors off the studies on financial performances of sustainable finance is some controversial points on the research project of the articles.

First of all, let's consider the time frame. According to C. Revelli et al (2015) long term studies tend to attain more robust results. The reason for this is that the shorter the horizon the more difficult it is to isolate the specific effects of practices on the actual result. Secondly, they highlight that researchers use models often used by portfolio managers for evaluating conventional finance returns and so are not adequate for this situation. This implies that depending on which model the researchers use, the results won't be the same. This belief is

shared by J. M. Puashunder (2016) who states that “SRI measurement deficiencies stem from intangible and time-inconsistent payoffs as well as measurement errors”. Still in Christophe Revelli’s article, the authors depict the fact that depending on whether the SRI portfolio, used as data, exists or whether the authors created a synthetic one, the result is not the same. Indeed, when evaluating existing financial performance SRI had a clear negative impact but for synthetic portfolios, it was a clear source of value. The reasons can be many but in any case it is a good point to bear in mind when analysing articles’ methodology. Even if these issues are not discussed in every article, we can say with confidence that all authors are aware that their methodology is not perfectly adequate to evaluate sustainable finance.

The other issue comes from the data itself. In addition to the fact that it can be biased by all the different criteria mentioned previously, like for the area of the sample, the asset class used by the sample, the specific strategy etc. another issue comes straight from the data which was highlighted by A. K. Chatterji (2015). The research is based on the fact that many articles on the subject of SRI rely on data provided by raters, usually the same ones, and that if these raters had a measurement error, for example, then all the research could be biased. This idea came from the observation that the ratings of different raters had low correlations between each other. The result showed that raters did not agree on the same definition for responsible investment and also did not measure the notion in the same way. This would suggest that depending on which raters the authors used their data from, their results would be different and influenced by the methodology used by the raters. This is quite an important statement, which underlines the fact that most articles published on this topic have already biased data. This part has underlined the fact that it could be complicated for investors to have a clear idea of the financial performance of socially responsible practices.

To conclude, the first two parts focused on the financial performance of socially responsible portfolios and assets. The results were ambiguous but led to important hypotheses. The first hypothesis is on ethical funds and questions how different they are from the conventional ones. The second one is linked to the assets and questions whether they are actually mispriced and will in the future stabilize to a lower price than conventional stocks.

At last, there is evidence that the methodology and the data used for these articles might be biased, which incites us to be careful with the results.

The evidence from the three parts suggests that investors could understandably be confused

by the financial performances of ethical finance and might be pessimistic as the hypotheses do not provide a positive image.

PART 2 – ACTORS AND REGULATIONS

In this part, we will be focusing on the motivations that institutional investors could have regarding the current regulations and the future regulations of socially responsible practices. Indeed, it seems that investors are taking more and more seriously the potential legislation around environmental, social and governance criteria. This could be a motivation for investors to anticipate them before they get penalised.

The objective therefore, is to analyse all the actors and the regulations on sustainable finance in order to have an opinion on whether they could be potential motivations for institutional investors to adopt socially responsible practices.

I. ACTORS

The first main actor is the United Nations Organisation who as we have said in the introduction launched the United Nations Environment Programme Finance Initiative (UNEP FI). The latter is a partnership between UNEP and the financial sector who work with over 200 institutions in order to analyse the impact of sustainable practices on the financial sector. It also launched The United Nations Global Compact and the Principles for Responsible Investment (PRI) as well as other initiatives like for example, the Equator Principles or The Green Bond Principles. The Equator Principles was created to offer help to financial institutions “for determining, assessing and managing environmental and social risk in projects”. Currently 105 financial institutions over 38 countries have adopted this framework. The Green Bond Principles, is a guideline to “recommend transparency and disclosure and promote integrity in the development of the Green Bond market”. It has been formulated by the International Capital Market Association (ICMA). The latter regroups around 600 members in 62 countries and works on regulatory and market practice issues on four main market areas: primary, secondary, repo and collateral and green, social and sustainable. (Equator Principles³; International Capital Market Association⁴).

³ <https://equator-principles.com/>

⁴ <https://www.icmagroup.org/>

A different type of actor are governments. For example, the French government is very active and in 2005 it raised awareness on sustainable development and CSR policies with the “Charter for the Environment” which is an annex to the French Constitution. A few years later, the Ministry of Ecological and Social Transition and the Ministry of Economic and Finance created labels in order to promote and help investors define sustainable finance.

China and the European Commission also took action by announcing that they were taking the initiative to join capital markets with sustainability goals (“Global guide to responsible investment regulation”, PRI, MSCI 2016). The European Commission also launched the High-level Expert Group on Sustainable Finance (HLEG) which has for its mission to analyse the challenges and opportunities for sustainable finance in Europe (“European SRI study”, Eurosif 2018; Climate Action in Financial Institutions⁵).

The UK government initiated, in 1997, SRI disclosure requirements for pension assets which was followed by many other EU countries. It also has, along with the Financial Reporting Council (FRC), set up the Stewardship Code.

Another example is the Belgian government, who in 2007 “adopted a law that forbids Belgian investors to financing or investing in any Belgian or foreign company that is involved with anti-personnel mines and cluster munitions in any way” (R. Steurer 2010).

In the US, the government tries to act through the retirement system ERISA with for example the introduction in 2008 of two bulletins, one on Economically Targeted Investments and one on Shareholders Rights. Another US actor is the SEC who introduced disclosure requirements on climate change and on conflict minerals (“Fiduciary Duty in the 21st century”, United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015). In fact, according to the report “The road ahead” by KPMG and written by J. L. Blasco and A. King in 2017, “the world over from Latin America to Japan, the US and the EU, to India and Taiwan are bringing in new layers of regulation for environmental, social and governance (ESG) disclosure.”

Private actors are also active in the field, for example the UNEP FI has asked one of the largest law firms in the world, Freshfields Bruckhaus Deringer, to work on the question if pension funds and insurance funds are legally permitted to integrate sustainable practise in their decision-making. This is closely linked to the fiduciary duty that we will describe in the third part. This “partnership” resulted in the famous “Freshfields report” published in 2005 which concluded that the ESG issues in investment decisions were actually aligned with

⁵ <https://www.mainstreamingclimate.org/>

fiduciary duty and were therefore required. Another report is due in the second half of 2020 which will build on the previous one and will focus on integrating the ESG issues into institutional investment (“Fiduciary Duty in the 21st century”, United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015; Freshfields Bruckhaus Deringer⁶; Finance UNEP Initiative⁷).

This gives us an indication of how important sustainable development is becoming and how committed the actors already are.

II. REGULATIONS

In the previous part, we mentioned disclosure and reporting, which actually seems to be an important aspect when talking about sustainable finance regulations.

Three key leaders were mentioned in the introduction. The Global reporting Initiative (GRI), the International Integrated Reporting Council (IIRC) and the Sustainability Accounting Standards Board (SASB) US based. If we take the first actor as an example it has established the Sustainability Reporting Standards which are “the first and most widely adopted global standards for sustainability reporting”, indeed “93% of the world’s largest 250 corporations report on their suitability performance” (Global Reporting Initiative⁸). In the report entitled “Global Guide to Responsible Investment Regulation”, they analysed the 50 biggest economies in the world, 38 out of them “had, or were developing, some kind of government-led disclosure guidelines for corporations covering ESG issues”. They explain that even if they are only voluntary they do play an important role in raising awareness. What’s more, nearly half of them are taking action by implementing certain kind of rules for pension funds and ESG criteria. A good example is the EU’s revised Institutions for Occupational Retirement Provision (IORP II), which requires the European occupational pension funds to report how they take into account their long term investment that considers the ESG issues and economical growth. The overall goal is to ensure that assets are invested in the best interest of beneficiaries, consider all risks and are properly diversified. (“Global guide to responsible investment regulation”, PRI, MSCI 2016; “Fiduciary Duty in the 21st century”,

⁶ <https://www.freshfields.com/>

⁷ <https://www.unepfi.org/>

⁸ <https://www.globalreporting.org/>

United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015; European Commission⁹). The three actors mentioned at the beginning of this subpart organised the Sustainable Stock Exchanges (SSE) in 2009, which has as a mission “To build the capacity of stock exchanges and securities market regulators to promote responsible investment in sustainable development and advance corporate performance on environmental, social and governance issues” (Sustainable Stock Exchanges¹⁰). They provide guidance on sustainability reporting.

Another key actor is the Financial Stability Board (FSB), which was established in 2009 by the G20. Since its creation it “has assumed a key role in promoting the reform of international financial regulation and supervision” (Financial Stability Board¹¹). It has set up the Task Force on Climate-related Financial Disclosures (TCFD) which has as an objective to “develop voluntary, consistent climate-related financial risk disclosures” (“Global guide to responsible investment regulation”, PRI, MSCI 2016)

In terms of other regulations, it is hard to know their results and how efficient they are as they are relatively new and it will take a few years before observing their true impact. However, seeing how sustainable finance is growing and what has been done until now, it seems to be working well. Indeed, only by looking at the numbers of agents who take part in the different organisations that we mentioned in the introduction and latterly in this part is a positive sign. In the report titled “Global guide to responsible investment regulation”, they found “a strong correlation between responsible investment regulation and better ESG risk management by companies”. This shows that regulations could be a serious motivation for institutional investors in the adoption of sustainable practices especially if we take into account how recent the policies are. In any case, still according to the report “Global guide to responsible investment regulation”, just by introducing “new rules, or even voluntary initiative” has a positive impact as it raises investors’ awareness and enhances advisers knowledge. Indeed, these initiatives open up the vision of investors. In the report titled “Fiduciary Duty in the 21st century” they found that in interviews, some agents said that “being a PRI signatory is now seen as a core expectation of investment managers” in the UK. What’s more, the interviewees agreed that there will be a strong chance that in the UK institutional investors will link responsible investment with their fiduciary duty. They explain that this phenomenon will be

⁹ <https://ec.europa.eu/>

¹⁰ <https://sseinitiative.org/>

¹¹ <https://www.fsb.org/>

strongly motivated by “a combination of peer pressure, market demand, reputational pressure and regulatory pressure”.

The various actions that are put into place for raising awareness have led to various SRI practices, which are supervised by the United Nations. According to the article written by J. M. Puashunder et al. (2016), “Standardized SRI policies could help regulatory enforcement and monitoring to overcome principal-agency discrepancies, conflicts of interest, and corruption.” The reason is that the financial world is becoming more and more complex with new risks, which increases the complexity of decision-making. Raising awareness on the fact that SRI practices can be a means to mitigate financial crises is a way to help financial stability. In fact, sustainable practices can be a way of regulating investors and help governments introduce new regulations. In the article of L. Albareda et al (2007), the authors explain that corporate social responsibility (CSR) could be a way “to meet policy objectives on a voluntary basis”. CSR practices mainly impact companies and not institutional investors but it will undoubtedly have indirect repercussions on their investment decisions. A good example, still with CSR, is the “Charter for the Environment” which was included in France’s constitution in 2005. In the article, they mention that according to an EU research project on the “Rhetoric and Realities in CSR”, “conventional social and environmental regulations not only curtail the scope of voluntary CSR but also provide points of orientation”. The fact that it provides some sort of orientation goes in line with the fact that sustainable practices are answering a bigger cause and it is in the best interest of agents to pay attention to them. Indeed, the fact that sustainable finance has a bigger cause to it, gives a new dimension to the notion.

The establishment of the Sustainable Development Goals gives an objective and some sort of orientation to investors, where SRI strategy is the best way to accomplish them for the moment. This helps investors understand the reason for adopting these practices and this strategy “proved to be the fastest growing strategy” according to the European SRI study. In this study they explain that “A good mix of legislative push, coupled with the possibility to link sustainability targets to financial outcomes and other examples of soft law, continue to represent the main drivers for SRI demand and will certainly continue to be so for the years to come”. In any case sustainable finance is just starting to grow and will be a main discussion for many years in the future. As a matter of fact, in the KPMG survey, according to Mr Blasco who is at the Global Head of Sustainability Services at KPMG, agents should get ready for

more reporting regulation on the subject, that “reporting integration is the new normal and “non-financial” is the new financial”.

When talking about regulation and sustainable practices, France is a very good example. Indeed, according to the “Global guide to responsible investment regulation” study, its “Energy Transition Law has identified failure to adapt to climate change as a major market failure” and is the origin of a “broad action plan for transitioning to a low-carbon economy”. What’s more, it includes a very important part which is referred to as “Article 173”. This article “requests asset owners and asset managers to report on how they include ESG and Climate in their investment process and decisions”. Actions towards ESG and climate issues are not mandatory but reporting them is. The way it has been implemented is clever as it plays on reputation and isomorphism, because a company who does not take into consideration sustainable practices will automatically be pointed at. In addition, for “those above 500 million euros [AUM] must also describe means employed to support the Energy and Ecological Transition”. This idea of encouraging agents to adopt sustainable practices has also been done through the PACTE law. This law was adopted in 2019 and includes measures on Corporate Social Responsibility and retail investors as we can see in one of the 10 major measures of this law titled “Rethinking the role companies play in society”. The civil and commercial codes have been modified in order to include ESG issues in companies’ activities thanks to this measure (European SRI Study, Eurosif 2018; Gouvernement¹²).

Another way to raise awareness is through labels. Two exist in France one is called ISR and the other GreenFin. The first one involves an auditing from Afnor Certification and EY France to ensure that specific criteria are respected, these criteria are divided into 6 themes. These themes cover the general objectives of the fund, the analysing methodology and notation of the ESG criteria, how well they are considered in the portfolio, the engagement policy within companies it invests in, transparency and the way they measure the impact of their ESG performance. The second label is audited by the same organisations and is especially recognised by the fact that it excludes companies which are in the nuclear and fossil fuels sector. It works in the same way as the first one but seems to be more demanding. They are not only a great way to raise awareness in institutional investors but also in private investors. As an example, the ISR label has its own website where they explain the concept

¹² <https://www.gouvernement.fr/>

and offer many resources including official researches on the topic that we personally used. (“La gestion Investissement Responsable”, AFG 2018; Lelabelisr¹³; Gouvernement).

Another country which is active, particularly in Governance, is the UK. The best example is the Stewardship Code. It was introduced in 2010 and its aim is to encourage investors to engage with the companies in which they invest and disclose how well they respect the Stewardship Code (“Fiduciary Duty in the 21st century”, United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015). It is closely linked to active ownership, which we mentioned in the first part. The Stewardship Code is actually very efficient. In point of fact, according to the “Fiduciary Duty in the 21st century” report, “UK asset owners, in particular the larger funds, increasingly see ESG integration and stewardship as standard parts of their investment processes” and in 2014 the Financial Reporting Council (FRC) mentioned in its review that “the proportion of asset owners where ‘all’ or ‘some’ mandates refer to stewardship had increased to 83% (from 71% in 2012 and from 65% in 2011)”.

For the US, the SEC plays a main role, “following a mandate in the Dodd-Frank Act, the SEC adopted its final rule on conflict minerals which requires public companies to disclose information about their sourcing of certain metals from countries that have been ravaged by civil war and insurgencies” (“Fiduciary Duty in the 21st century”, United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015).

Even China, which is the biggest polluter along with the US, launched in 2016 “Guidelines on Establishing the Green Financial System with the Governor of the People's Bank of China providing a clear articulation of the link between finance and ESG, commenting that establishing a green finance system has become a national strategy.” (« Global Guide to Responsible Investment Regulation », PRI, MSCI 2016). Lastly, the major player is the EU. In 2016 it announced that they would develop a sustainable finance strategy thanks to policy measures in order to fulfil the EU 2020 targets and the “EU’s commitments to the COP 21 agenda and the SDGs”. What’s more, “The European Parliament is currently working on three pieces of legislation to implement the Paris Agreement: the post-2020 carbon market (EU ETS) reform, the 2030 targets effort-sharing regulation and the regulation on greenhouse gas emissions and removals from land-use, land-use change and forestry.” (“European SRI Study”, Eurosif 2018).

¹³ <https://www.lelabelisr.fr/>

This large and comprehensive analysis of the actors and the regulations of sustainable finance shows us how serious actors are taking this notion and how regulations are already being implemented around the world and that it is just the beginning. It seems that these are a serious potential for being a motivation for institutional investors to adopt sustainable practices.

PART 3 – NON-FINANCIAL MOTIVATIONS

In this part we will first focus on the non-financial motivations that are directly related to portfolio managers and then we will focus on the non-financial motivations related to retail investors.

I. PORTFOLIO MANAGERS

The first notion we will be focusing on is the fiduciary duty of investors. We have made reference to it a few times before and it seems to be a concern for investors. Future potential changes to its definition could be an incentive to adopt sustainable practices. Indeed, according to the “Fiduciary duty in the 21st century” report, fiduciaries are taking their duties very seriously and so it could play a critical role. The report concludes that, as it is such an important notion, its definition should be modernised in order to ensure that “these duties are relevant to 21st century investors”.

After the 2008/2009 Subprime Crisis which had an impact on the entire world, the vision of the banking system changed and it became crucial to change the definition of fiduciary duty and take into consideration some sort of social responsibility. This concept is defined by the fact that those who manage other people’s money have the obligation to act in the best interests of their “clients”. In the financial world, the best interest is usually focusing on the best possible returns. The misconception of the ESG factors leads investors to think that taking them into consideration would be a breach of their fiduciary duty as they are not expected to provide higher returns. However, the work of the PRI tries to demonstrate that on the contrary, investors must consider these criteria as they are a way to quantify risks and opportunities, which are not evaluated if they are not taken into account. In fact, one of their missions is to raise awareness among investors in order to break down misconceptions. They do it by explaining that “responsible investment does not necessarily require investing in a specific strategy” or that “responsible investment does not require sacrificing returns” (PRI¹⁴). A report elaborated by the UNEP FI “stresses the point that a failure to consider long-term investment value drivers including ESG issues in investment practises is a failure of fiduciary duty”.

¹⁴ <https://www.unpri.org/>

As we have said previously, fiduciary duty is imposed on a person who has an obligation towards someone else. It is particularly important when there is an asymmetrical relationship between them. Here, an asset manager for example has usually more expertise and more knowledge than his client in managing his money. The most important duties which are imposed on him are loyalty and prudence. The first, loyalty, asks that “Fiduciaries should act in good faith in the interests of their beneficiaries, should impartially balance the conflicting interests of different beneficiaries, should avoid conflicts of interest and should not act for the benefit of themselves or a third party.” The second, prudence, asks that “Fiduciaries should act with due care, skill and diligence, investing as an ‘ordinary prudent person’ would do.” (“Fiduciary Duty in the 21st century”, United Nations Global Compact, UNEP Finance Initiative, PRI, Inquiry 2015). By analysing this definition, we can see that it is quite extensive and leaves the fiduciaries with a wide range of interpretation.

This is one of the reasons why, despite the conclusion of the Freshfields Report that we mentioned in the previous part, investors do not use these practices as they do not contribute to financial returns.

In the “Fiduciary duty in the 21st century” report, they suggest focusing more on the climate change risks. For example, investors would be required to “show that they have recognised relevant risks” or “analyse how climate change might affect investment returns over the short, medium and long term”.

Climate risks are indeed, a good way to raise awareness among the investors. According to P. Krueger et al. (2019), the authors found that only 3% didn’t think that temperature would increase, 16% for a one degree increase, 30 % by up to 2°C and 40% more than 2°C. This shows that investors, despite neglecting the risk for the moment, do consider that climate risk will be a subject of discussion. However, it seems that “The effects of regulatory (changes in regulation) and technological (climate-related technological disruption) risks are seen as somewhat more important overall than those of physical risks (changes in the climate)”. What’s more, according to investors, the reasons to incorporate climate risks are “to protect their reputation, moral/legal considerations and the belief that climate risks affect portfolio risk and returns.” This demonstrate that investors would not only incorporate climate risks for financial reasons but would also incorporate them for other reasons as described previously.

II. RETAIL INVESTORS

As we said in the introduction, the adoption of SRI and ESG practices will accelerate thanks to the demand coming from the retail investors. In fact, the European SRI study highlights the growing trend of retail investors towards SRI with a growth of 30.7% in 2017. What's more, they add that "Institutional investors are clearly at the forefront of this plan, but it has been increasingly recognised by the industry that retail investors are key to ensuring that sustainable investing becomes truly mainstream."

However, some practices, for example "window dressing" or "green washing", can make the idea of sustainable finance less attractive to retail investors. These practices can be seen in selfish investors who invest in a very small fraction of SRI funds simply in order to vaunt and enhance their reputation. In some way, we can link this with our findings in the financial performance parts where ethical funds and conventional funds are difficult to differentiate. These practices are harmful to sustainable finance because it gives a negative image to agents, which are not well informed. This could be connected to the notion of intrinsic social preferences and social signalling mentioned by A. Riedl et al. (2016). The first one is when investors believe in the cause and the second is when investors adopt these practices purely for reputational reasons. (R. Steurer 2010; L. Becchetti et al. 2014; A. Riedl et al. 2016). The first ones to be harmed by this trend are the retail investors who are usually the least informed.

If we take France as an example, after the Transition Law, which we mentioned earlier, the AMF "recognized that progress were made by players and recommended that all products targeting retail investors should get a label, either SRI or TEEC" (« European SRI Study », Eurosif 2018). A few years later, the PACTE law made it mandatory to offer responsible products in saving plans and life insurance.

The reason for these changes is that investors are becoming more interested and more informed due to a new generation, which seems to be more sensitive to the cause. One example, which could be studied is the amount of students that choose for their masters thesis a subject linked to sustainable finance compared to the previous years. In point of fact, still according to the European SRI study, "3 out of 4 investors say sustainable investments have become more important to them in the past five years. And figures are even higher for younger generations". In the paper A. Riedl et al (2016), the authors explained that socially

responsible investors are more likely “to hold a university degree, rate their investment knowledge higher” and “of the individual characteristics only the educational level and age exhibit robust statistically significant effects.”

In this third part, “non-financial motivations”, we have considered evidence that fiduciary duty, climate risk, reputation and the demand of retail investors can also be high potential motivations for institutional investors to adopt sustainable practices. The first notion showed us that maybe other factors will be taken into consideration in the definition of fiduciary duty. This would be quite an innovation and would be a sign that agents are taking sustainable practices seriously. We also realised that investments are possible for purposes other than just financial ones, like climate goals and climate risk. However, these practices can also be used in a more pejorative way like for example reputational purpose only. Finally, demand is increasing as agents are more informed and the new generation have broader objectives than just financial performance, which means that not only will it grow but it will also change. These different notions seem important enough to be potential motivations along with the ones we described in the previous parts for institutional investors to adopt sustainable practices.

SECTION 2: RESEARCH PROBLEM

This work project has been written having in mind that sustainable practices will at some point be evident for investors. The reason for working on this theme is that it is a hot topic and it seems that it will be so for many years to come. What's more, this subject is linked to a bigger cause, which is climate risk and it will only accentuate the importance of the subject over time. In our opinion, this Master's thesis topic will be one of many this year. Our generation and the ones to come seem to be more concerned in the evolution and innovation of practices that have an impact on our planet.

In order to elaborate the research problem, we will analyse what we have found in each part of the literature review and then combine these findings in order to define a problematic which will fill a gap in the academic sector and be of interest to the professional sector.

The first realisation is that when talking about the finance sector, financial performance is the first notion that comes to mind. With that said, we decided to focus first on whether or not financial performances of socially responsible finance could be a motivation for institutional investors.

The part was divided into three subparts. In the first one we realised that the main opinion of authors was that sustainable practices did not have a positive nor a negative impact on ethical portfolios or on funds in general. However, from this result a few hypotheses were formed. One of them suggested that ethical fund strategies were not so different to conventional funds, which in our opinion will give a negative image to investors. In the second subpart, we focused on responsible assets. Here, the results were also not leaning towards a clear positive or negative impact. However, one hypothesis was mentioned, which suggested that the assets were mispriced and that the prices would stabilize to a lower price than conventional stocks. What's more, using a sustainable strategy would mean not being able to invest in "sin" stocks which would result in an opportunity loss. The third subpart mentioned the possibility of having biased methodology and data in the articles dealing with financial performance of sustainable finance.

This part gives us very good insight into how institutional investors could see financial performance and how they could interpret it as a motivation or not to adopt sustainable practices.

The second part discussed the matter of actors and the regulations of sustainable finance. It seems that many efforts were made to inform and somehow advise on sustainable finance, this is why they appeared to be potential motivations for institutional investors. Indeed, in the first subpart we observed the large number of actors that were concerned and active with regards to sustainable finance. In the second subpart many measures were mentioned and analysed, which gave the impression that this subject was taken seriously and that the actions put into motion would have an important impact around the world in the future.

The evidence displayed in this part showed that regulations might be a serious motivation for institutional investors as they are backed by influential actors.

The last part focused on non-financial motivations. We first analysed investors' fiduciary duty, this notion could have been dealt with in the second part, however, the potential new definition would oblige investors to take into consideration extra financial aspects. In fact, climate risk and climate goals could be a part of it. In any case, investors are already taking them seriously and it would not be surprising that they would be a serious motivation for them to adopt sustainable practices.

Another serious potential motivation is the increase in demand for these kinds of products. As a matter of fact, evidence showed that a change of mentality is appearing, especially from the new generations. However, this leads to another motivation, reputation, which can have a potentially negative impact by sharing a misleading image of sustainable finance.

We see in this part that there is not only one potential non-financial motivation but a few of them, which is important to point out as it is not a common phenomenon in the finance sector.

The literature review leads us to the fact that there are many potential motivations that would encourage institutional investors to adopt sustainable practices. The first one we think of is financial performance as the sector is mostly focused on obtaining higher returns but for sustainable finance other arguments are at play. Indeed, we also focused our intention on regulations and other non-financial motivations like fiduciary duty and climate risk. This means that when deciding to adopt sustainable practices, investors are taking into consideration many different arguments and not only those linked to financial performance. This makes the decision process a lot more complex than for conventional finance, which brings us to the objectives of this research project.

The first objective would be to see whether or not institutional investors, when deciding to adopt sustainable practices, are taking into consideration more than just financial performance

aspects. The literature review suggests that there is a high probability that this is the case. However, the main objective would be to know what their motivations are and which are the ones that influence them the most. This leads us to the research problem:

What are the motivations for institutional investors to adopt sustainable practices?

This question is a legitimate one. Firstly, because institutional investors motivations are usually focused on financial performance but in the literature review we have seen that this is not the only motivation for adopting sustainable practices. Understanding their motivations would be a way to observe their state of mind and realise if they do believe in this sector and realise what they want or expect from investing in it.

Secondly, institutional investors are very important actors in the finance field. What's more, they are intermediaries between retail investors and companies and therefore, their position is key for the development of sustainable finance.

Thirdly, this question fills a gap in the field as the motivations of institutional investors have had very little attention.

As we have seen in the literature review, we do have a few ideas on what may be the incentives for institutional investors. This gives rise to three more specific questions:

Are the motivations linked to financial performance?

Are the motivations linked to regulations ?

Are the motivations linked to non-financial ones ?

These questions are a lot more precise and will help us go further in our research project. In addition, they will be an important help in the elaboration of our methodology as working from a large research problem is not easy.

As we pointed out earlier, this research project will be beneficial for academic research as it will fill a gap. Little information has been collected on the motivation of institutional investors towards sustainable practices. It will also be a way to understand how investors are considering sustainable finance and if they are taking it seriously. As they are impacted by companies and demand, their observation will also show how they perceive the evolution of both sectors and might be a starting point for new research projects.

For the professional sector, this work will clearly enlighten investors on the stakes that are involved in sustainable finance and the consequences they will endure if they do not consider sustainable finance as a serious sector. Indeed, this project will underline the real motivations of adopting sustainable practices and will convey important information to investors who are not well informed.

Most importantly, this research project will greatly help the actors mentioned in the second part of the literature review. Indeed, the information which will be collected will be crucial for future strategies on the communication of sustainable finance to investors. By knowing what investors think and the motivations they have, governments and organisations will be able to target specific elements which will greatly help their objectives towards the sector.

The data we will collect from the questionnaires and interviews is crucial to the study. Therefore, it will not be possible to form hypotheses or propose a theory on the subject until these have been carried out.

SECTION 3: METHODOLOGY

This research theme seems to be data-driven which means that any hypotheses or results depend on the data that has been gathered. (C. Revelli et al. 2015). It appears to be one of the reasons why research projects on this topic can be controversial, as mentioned in the literature review, because depending on where the data has been found and how well it has been selected the results can differ widely. This is the reason why for this research project, we will be gathering our own data with our own methodology. In order to do that, the best way in our opinion, would be to create a questionnaire and send it to agents chosen on the basis of specific characteristics that have been thoroughly defined beforehand. The details of the questionnaire will be dealt with later on.

By doing it this way, we will know exactly how our data might be biased and analyse it appropriately. What's more, this method will allow us to possess the most up to date data. This is a key point, as the practices are evolving rapidly and opinions are also shifting quickly. By collecting the latest information we will be sure that the respondent had the possibility to provide answers taking into account the latest news, policies and actions on sustainable practices.

Using a questionnaire is a good choice as it is reasonably quick to create compared to other methods. It is also relatively cheap and is a way to gather large amounts of information enabling us to get the general opinion on the subject, which is what we are looking for. The idea would be to send the same questionnaire twice, with a decent period of time between them, to see if opinions have changed. This will confirm or not the fact that sustainable finance is increasing at a high rate, however, it will depend on our time frame as the results will then have to be analysed a second time.

In addition, personal interviews should be done before and after the questionnaires have been sent. The first one would allow us to have information on how to create and send the questionnaire in order to obtain the most accurate answers possible. The second round of interviews would be in order to gather the general opinion of the questionnaire itself and identify the possible aspects of it that could lead to biased answers. It will also be an opportunity to collect more data as we will explain later on. The personal interviews would only be done with a few agents not with the whole sample. They will incur extra time and costs but they will allow us to gain time on creating the official questionnaire and finding any

factors that can bias the results. The extra costs will depend on how many interviews are realised.

The overall aim of the questions of the questionnaire will be of course to answer the research problem put forward in the previous part.

The research problem naturally emerged from the literature review. We focused our attention on financial performance, regulations and other non-financial motivations as these seem to be the most important for institutional investors. However, when analysing each one of them it seemed that some could be potentially more relevant than others. Indeed, when observing the financial performances, results were unclear and did not convey a clear positive result. This would mean that even if financial performance seems to be one of the most important incentives for investors, for socially responsible investors it might not be the case. As for the regulations, the literature review gave the impression that it had a consequential impact on the sector and that influential actors are taking part in its development which would assume that investors would take this for a significant motivation. These are only assumptions for the moment but the objective of them is to help us create the questionnaire and to have a common thread in order to gather the different motivations of institutional investors and to hierarchize them.

The goal of the questionnaire is to answer the research problem “What are the motivations of institutional investors to adopt sustainable finance?” Respondents will be asked whether or not the motivations we mentioned in the literature review are encouraging them to adopt sustainable practices. Questions will also be asked as to whether they have any other incentives for adopting them.

The questionnaire will start with the main questions we want answers to, that way we get the respondent interested and motivated.

It will be divided into 5 categories. The first one will focus on financial performance, the next one on regulations, the third one on non-financial motivations, the fourth on other motivations that have not been mentioned and the last one on personal information from the respondent. The personal information will be asked at the end. As mentioned in the paper J. Rowley (2014) there is a chance that personal questions will put the respondent in an uncomfortable position and discourage him from answering the other questions.

The first three categories will consist of mainly closed questions and maybe one open question in order to obtain the opinion of the investor. Closed questions are quick and easy for

the respondent to answer which makes it more pleasant for him. However, the questions must be very well formulated in order to have a viable answer at the end. Examples of questions would be (for the regulation part):

- 1/ Would you adopt or have you adopted sustainable practices for any regulation concerns?
- 2/ When considering a new financial strategy do you consider potential new environment, social or governance regulation?
- 3/ Do you consider the United Nations Organisation declarations on the subject?

The time gained thanks to the closed questions enable us to ask more open questions in the fourth category where investors would be free to mention other incentives that we have not discussed.

The last category will be dedicated to “personal questions”. As said previously, we want the questionnaire to be as anonymous as possible so that investors answers are the least biased possible. However, questions on age, the position in the firm or the country they work in will be necessary as they will give us important knowledge when analysing the results. Questions on how they perceive sustainable finance will be asked by way of listed or ranking questions but not by open questions.

The best way to answer the research problem properly would be to gather the most information possible on the respondent’s fund in which they work. This would suggest asking them the name of their workplace, which is not viable for an anonymous survey. We will therefore only be asking it during the interviews.

The information gathered will focus on the financial performance and the different categories of investments which will depend upon the strategy used and the sector they invested in. The information on financial performance should not be too complicated to collect. However, the information on the investments will not be as easy. Thankfully, the regulations on the disclosure of extra-financial aspects will help us get the minimum required for our analysis. The aim would be to link the respondent’s answers with the characteristics of their fund to see if they are in line with each other. If they are, this would suggest that the motivations of investors are justified and that sustainable finance is the answer.

A few examples should be given to explain how this idea could be implemented. Let us take for example an investor who works at a SR fund and has financial performance as a motivation for adopting SRI and ESG practices in his strategy. If we observe that the financial

performance of his fund or his strategy is better than the average conventional ones, then his motivation has been justified thanks to sustainable finance. Another example would be that if this investor has instead climate goals as a motivation for adopting SRI and ESG practices and his fund or his strategy is primarily investing in ecology projects then his motivation is also justified.

The analysis of the motivations of investors and the characteristics of their funds will be a way of justifying and understanding the answers of the respondents and of evaluating how well sustainable practices fulfil their engagement.

In our opinion, it is very important to focus our attention towards the performance of SR funds. Even if it is not precisely our topic for this research project, the fact that the motivations of investors are not only focused on financial performances, questions the actual evaluation of SR funds. Indeed, investors are interested in aspects other than financial performance as many articles suggest, it is therefore important to evaluate funds on other aspects. For example, in our literature review we mention regulations and climate goals. The evaluation of a fund should then be focused towards its ability to take into consideration potential regulations that can impact their investments or towards their proportion of investments that are helping to reach the climate goals.

The information gathered from the questionnaire will give us the answer towards our research problem, which is the motivations of investors towards the adoption of SRI and ESG practices. We will have data on what motivates investors in sustainable finance which will help the actors in charge of the development of this notion. We will also have knowledge on how well SR funds are in line with investors' motivations and how much progress there is left to make.

Now that the orientation and the aim of the questions have been discussed, the agents to be targeted must be defined.

First of all, the area should be considered. We have seen in the literature review that many countries all over the world are playing a part in sustainable finance, this means that to have the most complete data, countries all around the world should be targeted. This is not reasonable for obvious reasons, this is why the survey should be narrowed down to the most active countries which means EU, UK and the US. We chose to focus only on the EU, the reason is explained in the following paragraph.

When mentioning sustainable finance at least 3 different agents are playing a major role, fund managers, corporate managers and retail investors. Collecting data on their motivations for choosing sustainable practices would be very interesting for the general subject, particularly because each agent is linked to the other. However, in our research project we are focusing only on institutional investors and this makes it easier to target them.

Agents receiving a questionnaire must be already using sustainable practices or are interested in adopting them. Answers coming from investors which are not interested could be valuable data but it would not answer our research problem as they would at best have one or two motivations. Also, they would probably have more reasons why they do not want to adopt sustainable practices which is not the subject of the questionnaire and will not be helpful for the project. In order to filter the agents, a first question on how interested they are in adopting socially responsible strategies will be asked before the beginning of the questionnaire.

When sending the questionnaire we will be focusing, as said previously, on the EU for two specific reasons. The first one is that the potential sample targeted won't be too large which makes the diffusion of the questionnaire simpler. As we would like to target every fund manager independent of the size of its fund, not having too big an area to focus on will help. It will nevertheless be big enough to have a general opinion on the subject. The EU is a wide area composed of many countries, which are relatively different from one another in many domains. This difference will inevitably influence the answers and this should be taken into account when studying them. Indeed, according to the article S. Yan et al. (2018), the adoption of SRI practices may depend on different factors which are usually linked to the country itself. First of all, financial logic plays an important role when it is closely linked to profit maximisation. In this case agents take for granted that financial practices are aimed only at a profit objective. In this kind of society, the SRI approach will have more difficulty being adopted as agents will not associate it with their own objectives. Three other factors were mentioned and even though the results of how influential they are in the adoption of SRI practices were not conclusive, they are interesting to bear in mind when analysing the results. The three factors are: the influence of unions, religion and parties (green political parties for example). Depending on how influential they are in the country, they might have an impact on the adoption of SRI practices.

This would justify the question asking them what country they are from without the risk of revealing their identity. Having the general point of view of the EU investors on the subject and then having one for individual countries would add value to the work and would be a way of recognising the potential factors that would bias the results.

The second reason for focusing on the EU is that it is a highly active region for sustainable finance and has the most promising measures for the near future in this domain, which can be a reason to assume that these investors are the most informed.

The questionnaire will be sent by email and given in a paper format at conferences. The biggest flaw of a questionnaire is the potential lack of response. An original idea would be to create a small game at the end of the questionnaire and then publish some sort of ranking where the agents with the highest score would win a prize. This would work as it would create competition between the investors in a domain where rivalry is high.

The result of this method is entirely dependent on the questions asked, so great consideration should be taken when formulating them. The post personal interviews and sending a beta questionnaire first in order to identify the errors, should help.

Before starting the actual questionnaire some questions should be asked. First, as said previously, we should know whether or not the agent is concerned about sustainable finance and is interested in implementing it in his strategy. This will give us an indication of how ethical finance is perceived around funds in Europe. This will also enable us to separate agents which are already using sustainable practices and the ones which are not. For the latter it would be interesting to know the probability of them adopting these practices in the next year and separate those who have a high chance from those who have not. This will be important when considering their answers to the questionnaire.

One of the positive aspects of this questionnaire is that every response will be helpful to answer our research problem, there are no overall potential unclear results at the end.

However, we could anticipate a few scenarios. The worst-case scenario would probably be the fact that our hypotheses on the potential motivations for institutional investors are wrong. This case will still be interesting but it would mean that our questionnaire is not adequate as it will mainly focus on the motivations mentioned in the literature review. What's more, our research project would be questioned and would not be very insightful.

The best-case scenario would be that the respondent agrees on the motivations we put forward and answers the questions in a pertinent way so we can collect the data on the specific motivations that are the most important for them and the reason why.

As it is a questionnaire, the risks come from the questions themselves and the respondents. However, as described previously these risks have been carefully considered. The methodology is not too complicated and it is realistic. The area is not too large so it will be

feasible to carry out and not too expensive to collect the data. Analysing the results in the way we want will take time but will be worth it in the end as it will answer our research problem and many potential biases will be identified.

CONCLUSION

Through this research project, we wanted to fill a gap in the literature relating to sustainable finance. The motivations of institutional investors for adopting SRI and ESG practices have not been thoroughly analysed. In this research project we wanted to focus on a large range of motivations, not only the financial aspect but also on factors which are linked to the ethical aspect of sustainable finance. In the literature review we observed that the interest of investors seemed to be focused on financial performance, regulations and non-financial motivations like fiduciary duty or climate goals. It seems that sustainable finance has produced new interests for SR investors who are more concerned about the impacts of their investments than conventional investors.

This topic is important, especially today, as the realisation of the climate goals for the entire planet relies in part on the investment decisions of institutional investors. If they believe in sustainable finance and adopt its practices there will be a chance to attain the targets. Understanding their motivations towards the adoption of the SRI and ESG practices will be a way for organisations, governments and private actors to develop sustainable finance in the correct way.

The literature review provided us with guidance on how to tackle the subject. Financial performance seemed to be an important consideration in sustainable finance, as one would expect for any area of finance, it was therefore important to analyse articles mentioning this factor. We saw that the results of the performance of SR portfolios or assets were not precise enough and that there was no clear-cut answer. This enhanced the debate whether sustainable finance provided a positive or a negative effect on performance, a fact which could be confusing for investors. This confusion on the financial performance of sustainable finance could suggest that the investors who are interested or who have already adopted SRI and ESG practices are less interested in financial performance than conventional investors.

Another factor which seems to be very important in sustainable finance is regulations. We decided to associate “actors” as they are closely linked to regulations. We observed that many actors represented by organisations, governments and private actors have a very important role in the sustainable finance sector. Many of them are considerably influential which makes their role in the creation of regulations even more important.

As sustainable finance is relatively new and is starting to be used to reach targeted climate goals, regulations are put into place in order to introduce some sustainable practices or at least to report the fact that companies are or are not using them. We could suggest, based on what we have just mentioned, that investors could see these regulations as a motivation to adopt SRI and ESG practices or at least be concerned about them.

Non-financial motivations also have an important place in the literature of sustainable finance. In this part we analysed fiduciary duty which can also be linked to the “Actors and Regulations” part. However, we focused on the fact that its definition should be redefined in order to include the new interests of investors and invite them to take into consideration climate risk. We also analysed climate goals and climate risk which could have an influence in the investments strategies of investors.

Fiduciary duty, climate goals and climate risk are increasingly important factors which will have an impact on institutional investors as the demand of retail investors for sustainable finance is growing at a high rate. The way of thinking of the new generation of investors will also be a reason for the development of those factors in the investment strategies.

In conclusion, a multiple of non-financial reasons could be a motivation for institutional investors to adopt SR practices.

The knowledge brought by the literature review gave enough information to create a questionnaire. This questionnaire has the objective of collecting enough data in order to understand what the motivations for institutional investors to adopt SRI and ESG practices are. It will focus on the assumed motivations of investors, found thanks to the literature review but will also give the respondent the opportunity to answer freely on other motivations.

Interviews will also be conducted. The answers of the interviewees will be coupled with financial information and also investment information on their funds. This will enable a comparison of their motivations with the characteristics of their fund in order to realise if their motivations are in line with their funds objectives. This will add precious value to the paper as we will not only know the motivations of investors for adopting SRI and ESG practices but also how credible sustainable finance is today.

The limitations of the research project are primarily focused on the methodology. A questionnaire has many beneficial points but also has a few negative ones. The first one is on the amount of respondents. In order to have viable data a minimum of answers must be

gathered or else it can not be used. The same problem arises for the interviews, even if a much lower number is expected, a minimum of them have to be carried out in order to have concluding results. The second limitation is on the quality of the questions as the data collected depend on them and their quality will be crucial to answer our research problem.

For further research, it would be interesting to focus on the non-financial motivations in more depth. Future authors could use this work as a base for their study using conclusions from the questionnaires and interviews on the non-financial motivations of investors.

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