INSEAD

The Business School for the World®

KNOWLEDGE

Finance as a Force for Good

Industry experts discuss how investors, businesses and society all benefit from sustainable finance.

Sustainable investing, previously a niche specialisation, has become increasingly commonplace in recent years. Globally, **more than a quarter** of professionally managed assets are now invested according to environmental, social and governance (ESG) principles. In addition, many mainstream financial institutions are publicly committing to sustainable investing as the way forward. Investors can choose from a wide range of sustainable products and funds and are increasingly able to monitor the sustainability of their investments, even those without a "sustainable" label.

The new normal of sustainable investing, and sustainable finance more broadly, was one of the topics discussed at **The Force for Good Conference** held in October 2018 on INSEAD's Europe campus. Keynote speaker Paul Polman, then CEO of Unilever, reminded attendees that "you cannot outsource your responsibilities". He declared that "business cannot be a bystander" as public debt and wasteful consumption continue to grow.

Experts representing a large asset manager, a global bank and a new accounting standards board shared their perspectives on the role of finance as a force for good. I led a conversation with Gert-Jan Sikking, Senior Responsible Investment Advisor at PGGM Investments; Anjuli Pandit, BNP Paribas UK Head of Corporate Sustainability; and Jean Rogers, founder and former CEO of the Sustainability Accounting Standards Board (**SASB**).

Our panellists spoke about how sustainable investing has evolved, from simply excluding certain industries (for example, tobacco or firearms) on moral or ethical grounds, to a much broader investment philosophy that encompasses a range of approaches including ESG integration, corporate engagement, and investing in companies that are specifically focused on finding solutions to the world's sustainability challenges.

The sustainable investor: Long-term sustainability risks and opportunities

With €220 billion of assets under management invested for the long term according to responsible investment principles, PGGM, a Dutch pension fund asset manager, has long been a leader in this field.

Sikking spoke about three aspects of PGGM's sustainable investment philosophy: not investing in certain companies (ones known to participate in child labour, conventional weapons or tobacco); integrating ESG principles into the investment processes of its clients; and finding avenues to ensure more money funds sustainable projects.

"We want to allocate more money to the companies that have a societal contribution to the global challenges we are all facing," he said. In 2014, one of PGGM's clients, a pension fund for the healthcare sector, decided to focus on the themes of climate, water, food security and healthcare.

A pension fund's decisions reflect its long-term vision: "Our investment belief is that sustainability pays off in the longer term," said Sikking. He also noted that academic research corroborates this, citing **George Serafeim**, a professor at Harvard Business School, who has found that firms with a good performance on material sustainability issues significantly outperform those with poor performance.

The sustainable bank: Purpose in industry

BNP Paribas, recently voted the world's best bank for sustainable finance in Euromoney's annual **Awards for Excellence**, incorporates sustainability throughout its businesses, from asset management to corporate banking, including choosing which companies to work with.

Pandit said the banking industry needs to be more aware of purpose, like individual firms in other industries. The purpose of a clothes manufacturer isn't to make money, it's to make affordable, fashionable clothing. Banks also need to find their own purpose. Some, like BNP Paribas, have embraced the concept of sustainable finance "in a way which I think has surprised everyone", said Pandit; the bank "mapped our entire loan book across the **United Nations Sustainable Development Goals**." The SDGs were agreed upon in 2015 in the hopes of resolving 17 social and economic development issues, like clean water and sanitation.

To fill the gap left by tobacco and coal investments, the bank's portfolio had to shift. As Pandit said: "Go towards building natural capital. Go towards renewable energies. Go towards the gap technologies that we need to solve the energy transition, like batteries. What is the long-term impact of a given industry, and how does it relate to what we think banking's role is in society?"

For Pandit and the other panellists, the questions have more urgency since **COP 21**. The Paris Agreement gave purpose, not only to its 195 signatories, but also to industry.

Pandit also spoke about how asset managers' clients and asset owners need data: "The more information you have about a company, the more you know whether you want to invest in it." From gender equality in the workplace or diversity on the board, to human rights in the supply chain, to water management, or a company's carbon footprint – firms that report on these aspects of the business are considered well run.

Fortunately, thanks to the efforts of our third panellist, reporting of this kind is on the cusp of becoming standardised.

The new sustainability accounting standards: Niche no more

SASB, founded by Rogers in 2011, develops and disseminates industry-specific sustainability accounting standards. The focus for SASB is on helping businesses around the world identify and report in a standardised fashion on sustainability topics financially material to their investors. This means those issues reasonably likely to impact a company's financial or operating performance.

Large investors are listening to their clients who want information about sustainability "integrated into decision making and into portfolio construction. They are seeing the writing on the wall. And frankly after **disaster** after **disaster**, where corporate value really has been affected, whether it's automobile safety and airbags and product recalls, or whether it's data privacy and data security, these issues do actually affect either price and or long term valuation," Rogers said.

Remember that huge asset managers such as Vanguard, Fidelity and BlackRock are starting to talk about sustainability because they have seen how it benefits their clients, said Rogers. They have seen evidence that sustainability factors improve companies' financial, operating and long-term performance. Managed well, these factors can positively affect returns, and vice versa.

Rogers spoke about the **UN Principles for Responsible Investment**, whose first principle concerns the incorporation of ESG issues into investment decisions. "This is now a trend that speaks to the demand of investors, who take risks, and maximise returns over the long term," she said. The best way to do that is with real data.

"SASB has built an infrastructure for the capital markets, so that these factors can be analysed by industry," Rogers explained. Part of her message is that sustainability differs from one industry to the next. Climate change, for example, affects a real estate company in a different way than a healthcare company or a bank.

Mainstream investors are looking for less risky outcomes. Rogers described how screening out sin industries created the first generation of sustainable investments. But these early iterations were likely to underperform because investors didn't consider a company's underlying decisions – how it was managed, for example. The decision not to invest in tobacco or guns only limits the investible universe. Now sustainable finance looks at business models, performance, SDG inclusion and risk diversification. The bigger picture is the underlying basis for investment, Rogers said. The key is strengthening that investment approach and making it more resilient and less volatile for the long term.

These issues are important "from a macroeconomic and societal perspective. And investors are actually a part of society, too," Rogers explained.

Sustainable global growth

Shortly after the conference, we learned that William D. Nordhaus and Paul M. Romer won the **Nobel Prize in Economics** for their work towards bringing us closer to "how we can achieve sustained and sustainable global economic growth". The voices from the world of investing, banking and accounting standards made it clear that sustainable finance is more than feel-good window dressing, it's good not only for society but for business and investors as well.

Lucie Tepla *is an Affiliate Professor of Finance at INSEAD. She is also a programme director of* ***Transition to General Management****, one of INSEAD's Executive Education programmes.*

Follow INSEAD Knowledge on ***Twitter*** *and* ***Facebook****.*

Find article at
https://knowledge.insead.edu/blog/insead-blog/finance-as-a-force-for-good-10751