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Sustainability unwrapped a conversational podcast about responsibility, ethics, inequalities, climate change, and other challenges of our times. Where science needs practise to think about our world, and how to make our society more sustainable one podcast at a time.

Today we are going to talk how private investors can invest in sustainable way. My name is Hanna Silvola. I'm a accounting associate professor here at Hanken. And today we will discuss on sustainability investing with my co-author Tiina Landau.

Last year, we published a book on sustainable investing in Finnish. And now we are soon going to publish that book in English with the title, *Sustainable Investing Beating the Market with ESG*. I have academic background. I have been doing research on sustainability issues, reporting assurance, ESG investing, et cetera. Today I will have here my co-author Tiina. Tiina could you please tell a bit about your background?

Yes, thanks Han. Thanks for inviting me to this podcast. I have a background as a practitioner in sustainability. I've sort of worked in every side of the table, so to say. By now, I currently work in the industry as a sustainability manager at an energy and renewable energy company.

But before, when we were writing the book, I was working for years as a responsible person for Sustainable Investing at a major Finnish pension fund. In addition I've worked in management consulting, and asset management, and also various international projects, also focusing on sustainability topics.

Yes, that's very interesting. It seems that you have a lot of experience from the many side of sustainable investing and sustainability issues. The audience who is now listening and wondering what is sustainable investing, and how does it differ from traditional investing, how could you simply define what is sustainable investing?

That's a really good question. So the easiest way is to think that sustainable investing-- it means that you're considering environmental, social, and governance, topics as part of investment decisions. So it's basically-- it's like investing but you're just-- it's just to highlight the fact that before not everybody was considering these kind of topics that are not part of the financial statements, or so-- so this is now-- now becoming mainstream. And also there's many different methods and ways and how to put it into practise.

Well, if we think about this from private investor perspective. Is it somehow different than the fund for institutional investors? Like we know that many banks and big institutional investors, like pension companies, they are very active in sustainable investing. And they have a lot of resources, experts, professionals, working with the huge data set. And they have a lot of information to make the decisions. But how is that done with normal people like me and you? What sort of possibilities our audience could have for Sustainable Investing?

Well, nowadays, anybody can actually do sustainable investing, but as you mentioned there's of course, different types of resources, and amount of time that private investors are able to use compared with institutional investors. For private investor, you can first start thinking, do you want to invest directly? For example, in shares of companies? Or do you want to invest in funds? So that's of course a first decision. And after that, there's a lot of resources that you can use online that are more and more becoming publicly available.

So for example, there's this company called MSCI Sustainalytics, who have published their sustainability ratings for companies. So private investors can see basically averages of how sustainable a company is, that's of course a bit more art than science, but still really interesting-- this kind of a recap of risks and opportunities that the companies have-- and also some of these databases also include a bit of more qualitative description as well.

So private investors can also see what the strengths of the company is, or the problem is that might be faced with these particular companies. And when you invest in funds, there similar types of databases also available. But then that would be a review of the fund as a whole and all of its investments.

Yes that's very interesting. So if we today are going to talk about sustainable investing as a phenomenon, and then maybe give some tips how it can be done in practise, and then also about the information sources more in detail. So if we come back to the sustainable investing itself, I have understood that many people have mixed it up with ethical investing. Could you tell us something about this-- how ethical investing, and sustainable investing are similar or different? Or should we care about that at all?

I think it's always good-- so that when you have a conversation you're speaking about the same thing. So an ethical investor is mostly concerned where they don't want to invest. So there are some that have a religious, ethical background. And for example, there are these so-called sensitive stocks so

tobacco, or alcohol, gambling, and et cetera which they might want to exclude. And beyond that, they can invest in anything. And also, there, this is based on their values. So they're also willing to compromise on the profits that they're making. And also ethical investing is-- can also have this kind of environmental ecology background. And-- but basically it's more for values-- values question.

I think that I have also observed-- especially younger people are so keen on climate change issues that they really do not want to invest that often to the companies which are boosting climate change. And that's so important value for them personally, that they want to exclude the sort of investments from their portfolio. Have you noticed the same?

Yes I think that there's many private investors who want to invest there. Of course there are some who are in it to make some more money, and that, I guess goes more to the sustainable investing part of thinking, where you want to both have a sustainable future and to make profit along the way. But they are-- I think there are some that only-- it's a values question. They want to invest in these companies that are not harming the climate, and even if that comes at some kind of a cost to them.

Yeah, you already mentioned profit. Some people argue that the sustainable investing is not a rational choice, and you need to make compromises regarding profits based on the investigations that be made in the book. We found a lot of evidence that actually-- you can do quite a profitable investing with a sustainable strategy. Have you noticed the same debate in your work or in-- during your career?

Yeah, I think so because that's actually one of the coolest things I think about the book-- the research that you went through, about the profit. Because before that, I think the whole discussion was about anecdotes. So there were some-- like a lot of investors, and I think that's still happening that they sort of make this kind of a-- well, I think-- when you think about risks, and this kind of accident can happen, that can cost a lot to the shareholders.

But that was-- when you think about it logically, you understand that if there's a huge safety hazard, there can be fines that the company has to pay. They might lose their customers. So when you-- like in this everyday thinking, then of course, that makes sense. But there was a lot of contradictory research that was going around. And also the Finnish sustainable investment forum had a working group to address this question.

So this was sort of the hot potato. Is it is there profit in it? Or are investors leaving money on the table when they are doing sustainable investing? So I think it was really important that we do have this research now. And also there's been more and more evidence coming up also this year, with the

COVID situation, and the majority of sustainable funds outperforming their more traditional peers.

Yeah that's what the records actually show at the moment. So if we think about the reasons for Sustainable Investing it's institutional investors like pension companies, they pretty often do it for risk management purposes. But more and more often, they are looking for good business potential from the invested companies. They want to actually do profits and the good profits. What do you think about the motivations of private people? Are they the same as for institutional investors?

I think when I've spoken private-- private investors, it's more often it seems to be a value based. Thinking that-- sort of that, where do I want to be involved? Do I want to have my money and make my profit with a sustainable company or that is according to my values? Or something that is not so much? So I think private investors, many of them seem to think about the impact.

But on the other hand, for everyone, it's sort of-- like you're saving for your own future-- maybe for-- maybe you want to buy an apartment, or have money when you retire, or something else, or life events. So then of course, it's easier for everyone to make these kind of sustainable investing decisions, when you know that it's not like you're going to lose all your money when you decided to do. So probably I think-- I would think that both aspects matter.

Yeah, actually you pointed out very relevant issue in my mind. I think that's the time orientation. And in sustainable investing we pretty much look at the value, and risks, and profit of the long term. And we as a private investors we really often have quite a long time orientation in our mind, like the retirement, or education for our kids, et cetera.

Yes, exactly, but on the other hand also, there's pension fund of course-- who have to think of the same considerations. So even though they are reporting their-- or might be reporting their returns on a quarterly basis, then they still they have this really long responsibilities. So I think overall, there's really a lot of institutional investors as well who need to think about the long term. So that's why I think probably sustainable investing is also becoming more and more relevant

Yeah, that's true. So we have been talking about sustainable investing a bit now, and we have mentioned the terms E S and G. I guess all these three letters are not that familiar with every one. Could you please somehow describe and explain what are these three fancy letters?

Yes, definitely. And that's-- I think that's like the issue. That's something that's really in the main investor world-- like what is speaking about sustainable business? Partly as was tradition referred to in the corporate world. So ESG is-- if you remember one term I guess from this discussion, that's the

one. So E stands for environmental, topics like energy efficiency, climate impacts environmental pollution, et cetera are included in that one.

As social, so S, that includes human rights, Labour Standards, impacts on communities and society, isn't even like-- that can be this privacy-- data privacy issues that have been really high on the discussion lately. And then governance, that's something that's where ESG a sustainable business concept you should defer for one another.

Edgy or the governance, that's how the companies are acting-- have it ethical business practises, how it does their board composition looks like? Do they have enough independent board members? Compensation related topics, so what is the long term and short term incentives, and how are they aligned with responsible practises? These kind of things are what investors are speaking of when they are evaluating sustainable topic.

So in brief, ESG is a term used mainly by the investors. And it's a somewhat the synonym to sustainability.

Pretty much yes, although now of course it's like this-- alphabet soup that some have been referring to as a justified comment I guess. So luckily companies sell more and more, trying to adapt the same language using ESG as well.

Yeah, that's true. So we have these three letters in our mind. And as investors, we should have a look on ESG level of the company. What do the company report on the environmental impact, social impacts, and the level of governance? And based on that, we should somehow define how sustainable this company is.

And how it's improving its business operations, and reducing, let's say, environmental harms and improving social impacts et cetera. So if this is the way how we actually evaluate or analyse ESG level of the company, how this can be done in practise? So when we think about the options, how can we invest? And what sort of strategies are available for private investors? How could we start in the beginning?

As I mentioned, a good way is to look at the [INAUDIBLE] ratings. So for example, if you invest in fund [INAUDIBLE] that I mentioned earlier, but also in addition to company thinks they have these kind of bond ratings where you can see what kind of topics are highlighted-- like if there are funds that invest in the more sustainable companies, or has some kind of a theme. For example, climate solutions or something related to water efficiency.

And also there's another alternative to look at Morningstar, which has the sustained [INAUDIBLE] [excess ?] in their ratings. So they have also made this kind of information publicly available. So you can see how sustainable the funds compared to their peer group. Then of course, the funds publish quite a lot of the information themselves. So if you're ready to put a bit more time to it, you can go through their own reporting. And they might say if they have some kind of a philtre so some kind of a topic, or more of environment with increasing, but this could be also a social system the topics that are considered.

And especially if there's some kind of problems that the companies have had, such as violations of international norms. The house managers might start engaging with these companies to have improvement. And also there could be some exclusion. So if you want to invest in fund, and it's really important to, that-- for example, there's no tobacco companies in the fund, and you should look at the fund's principal to see if they have such an exclusion in place.

So if we have some persons in the audience who have never invested, and that would be the first time when they now get motivated, that well I-- it might be quite a good choice to make some investments. And if the person would like to invest in sustainable fund, how does it happen in practise? You go to the website of your bank, for example, and then start searching funds, right.

Yes, so that's usually some kind of-- there could be a philtre for example, that has some of the words like, SRI, social responsibility headline or ESG, which we discussed. So that's a good hint that, OK, this focus is on sustainability. Or some banks also have a section that you can select is kind of a fund. So the main decision you have to make is also that-- do you want to invest in actively managed fund or passive funds? So actively managed fund means that there's a portfolio manager who is also often looking at the sustainability topics-- that what kind of risk there are specific that companies making their own decisions.

What do you think, should we then have a look on what's included in the fund-- like, they usually give a list of the biggest companies or ownership in the fund? So can we do something for that? Or is that enough if we just have a look on the investment strategy of the fund, and have a look on ratings? Can we somehow benefit of having a look on the companies itself, which are included in the fund?

Yes, I think so because when you look at the principles of the fund, then that basically tells you what was the aims of the fund. And then when you look at the investment, you see what's the actual-- what happened in practise? So it is just like the thought and the concrete are the two sides of the coin. And of course, sometimes it can happen the opposite as well-- that if you only look at the investments,

they the most sustainable companies in these sectors. But it might not have been the purpose of the fund to select, it just happened as a side product for example.

They wanted to have good quality companies, and then those ended up also being the most sustainable ones. So if you want to look at the investments as such, of course you can see the largest holdings and see this just in ratings. But also, if you have a bit more time you could Google the companies, maybe look at their sustainability reports, or for example if climate is your most-- thing that where you're most interest that you could have a look at another acronym, CTP, which is an organisation that is focused on environmental information and it actually publishes some of the same reports that are publicly available where you can actually read also about the companies sustainability and especially on the climate plans and their performance.

Fund might be the easiest choice for the beginner. And then once you get a bit more aware of investing or you have background on investing a bit, then private investors usually stop to invest in individual stocks. And they are looking for the interesting companies. So what do you think, what are the important things in investing in stocks compared to funds? So in funds your resources and your money is distributed among many companies. But the risk is becoming a bit higher when you select individual companies.

Yes, that's something that I guess the personal password-- that you want as a fund investor, you're quite happy that the system be rating. Somebody else is doing the analysis. But when you're investing actually in stocks, then maybe you want to start understanding that the ratings are actually weighted averages, or very different topics. But then actually-- like how do [? ways ?] human rights management, with energy efficiency, with more diversity, and the kind of topics.

So you understand this a bit more nuanced, and actually there's-- if you just want to avoid risks, it's possible that they could be one risk that can actually be a game changer for the environment and for the whole company performance. Or on the other side, that you might want to invest in some kind of a solution and sustain the opportunity. For example, a company that has some ground breaking technology, that can help mitigate or adapt to climate change impacts.

| that's very interesting. So it seems that once we select individual stock instead of fund, it seems that we need to invest more time in searching through companies, to do a bit more work and learn things. So do you have any practical tips on how to learn more?

I think a sustainable report is a good starting point. And in our book, we have this case study where we have set an example of how-- what do you look in the sustainability report? And I think one rule of

thumb base that you're always thinking, that-- first you have to think of what are the material topics? So topics that can affect the profits of the company or perceptions about the company. And for this there's this another acronym. And this is where you start to understand that there really is a lot of these alphabet combinations, but try to keep them to a minimum.

So basically so there's SASB, which is a US based organisation that has defined for each sector, what are the most material standard topics. And that's a good starting point. So if you're looking, for example, at a clothing company and it makes it easier when you're seeing that, OK, these are the topics like for example, supply chain sustainability, and whatnot that you can find there. And then of course you can think yourself if there are some other topics that you personally value in addition to those that you'd like to include.

And then you start looking at the sustainability report to see what is the company saying about those topics. And do they have numbers that they're reporting? Are they going to the right direction or the worst direction? Are they expand their gaps? For example, are they telling how many audits they have their suppliers, and who is doing the audits, what kind of findings? It's always worth to, remember that if the company tell us about the process, that's nice, but if you also need some kind of concrete evidence that actually found some problems. Because there are always some problems. You just need to be able to identify and address them.

Yeah, so you mess up this Sustainability Accounting Standards Board, and it's a very nice framework to find this material factors of sustainability on each industry. So if I would be interested, let's say, on a car manufacturing, then I will have a look on the sustainability report. I'll find out the material ESG factors from there. And I have understood that it would be quite nice to take, then, some company either and compare what sort of ESG factors will the other company on that car manufacturing industry actually disclose. Because they basically should disclose somewhat the same information, or say ESG factors, or methods. But is that the reality?

I think that sort of the ideal world, but if you're really [? sick ?] then how many private investors or even institutional investors are always looking at all of the car manufacturers and comparing them? So that's of course good if you do that. However, companies might be reporting actually based on different topics because it's not completely standardised. When you look at European companies, they're usually using another system of reporting tradition, where the companies themselves are actually defining what is material for that company.

So that's why they might end up in some different conclusions. But actually I would use the

sustainability rating information to compare-- also to have some kind of idea of how the companies compare with one another. And especially in the case of car companies, and others that have some kind of a climate impact, I would also look at them. [? CDP ?] that's what a climate analysis but also this, and some other research for example, the transition pathway initiative seems quite interesting for some sectors to look at their climate impacts and how they're managing them.

Yeah so it seems that if you really want to investigate and analyse 80 factors of each companies that you are interested, it would actually require quite a lot of time and resources and knowledge. So it might be easier to trust, on at least to some extent, these third party ESG ratings.

Yes, exactly. That's actually how institution investors do as well. So they use the ratings and the background reports as a starting point. And then they do their own analysis. So that's sort of your first step that helps with many companies, so at least you get some information. And then it depends-- and then organisations like how many persons you have or are dedicated to that or, especially if you're not there are many, many investors who actually help train their portfolio managers and financial analysts to do the system analysis as part of their normal job as well.

Yeah so when I come back to funds and compare funds and stocks, it come to my mind that actually it would be also quite interesting and important to have a look on the sustainability of the fund provider itself. How responsible business they are doing in their own activities? Do you agree or what do you think about this?

I, think that's a good idea, but just not sure how we can do it in practise. Of course, if there has been some scandals who have come into light, then you might want to take that into consideration. But the actual key I think, is when you invest in a fund it's sort of like, who does the sustainable investing better than others? Who has more knowledge and competence? In that you can look at the persons who work in that fund management company. Do to have some kind of ESG expertise? In their versions, are they using some kind of systemic analysis? And what do they report themselves about what they do?

That's actually a great point because it must be pretty much about the knowledge of the fund manager-- how they are doing things, and what sort of theme they have behind the fund-- resources and education on this field.

Yes, and also of course, what impact does it have in the final investment decision? So that's another million question. Did it have a-- personally, when I was evaluating funds, I often asked examples of sustained analysis because that's where you get closer to the bottom of things. Because if you ask

them ask them to share what they have done, that can be a very different qualities.

Yes, I can imagine that. So in addition to this publicly available disclosure is given by the funds, or companies itself, do you have something else in your mind? How can you learn more about sustainability investing as a phenomenon? So how to become more familiar with the topic and are there any other third party reports or internet sources from where you can learn more?

When I was starting system investing there wasn't much available. I actually went to my faculty in the University. And there was a researcher who gave me a bunch of articles that he got-- that was when I was going to my first interview. And after that, I've learned through trial and error basically. So I've been asked to really look into some company. And then I've been making some kind of conclusions, and then having these lively conversations with the portfolio managers of what is useful, what is not.

And then of course, if you-- when you read hundred of these analysis of others, and a lot of the reports, you sort of come to some conclusions that-- what is what the portfolio managers fund maturing the investment decisions. And of course I've had a lot of discussions with professionals in other countries, and also I've been lot of what they do and what both of us like the themes but individual companies as well. But that's of course, wouldn't be available to everyone. But I wanted to make this available.

That's one of the reasons why I wanted to write the book with you. So to come up with this-- we already touched a bit about what are the sustainability ratings, and how to use them. But that's a really long discussion, so it's better to have in a long book, than short ones. Should go on, but you know of course there's a lot of system investors, web publishing blog post, and writing on Twitter, and there's some YouTube videos online of some famous lectures, et cetera. So there's a lot of information out there that you can start with. And of course PRI, the principles for so much investing, they have published some guidelines.

Yeah I have the same feeling that nowadays, during the recent-- let's say two, three, four years, we have got quite the many and high quality resources or sustainable investing. And more is coming all the time. So I guess it will reflect the interest on this topic. So-- Yeah, please go ahead.

Yeah, definitely I agree. So nowadays it's more like you have the selector right ones like what is useful for you. And that's, I guess, the only way-- is to start reading. And yeah, PRI is a good starting point. But for that-- and some of the companies themselves also publishing interesting reports that can be beneficial to all.

Yes PRI is really doing very good and there is huge amount of information on their website. So we wrote the book on sustainable investing, and there we gave a lot of examples, staircases, and there is really. Much information on sustainable investing. What's your favourite part in the book?

I must say it's the KLP case with marsh, the shipping company.

I think tell a bit about that.

Yeah, I know. I do really love this [INAUDIBLE] case as well. But let's speak about this. So it's hard to compare but, I get the one. So basically there's this kind of ship-- where ships go to the end of their lives-- they are sold to cash buyers. And many of them are disposed in the beaches of South Asia. So basically under a tidal wave, they'll just go in-- go towards the beach, and when the water goes down, then they are left at the beach.

And then they start dismantling the poor conditions. This is one of the system investing forerunners, KLP has been engaging with many companies on the topics, to improve the conditions in the shipyards and send us how the ships are being allowed. This expert, Martha [INAUDIBLE] from KLP, she has given an interview and told about this phenomenon and the great work they have done to engage with marsh but also other companies.

And also there's points of view of marsh, and the development, what they have done, and about the legislative environment. So I see it all, especially in my mind what happens there. And then you can actually ask. Martha has told us. You can actually go to the Google Maps and just put the name of the area along in India and you actually see this cut up a coastline full of these ships there.

Yeah that was quite a trucking for me when I saw that first time. So it seems that the institutional investors and fund managers they are doing a lot of things to provide better options for Sustainable Investing or private investors. So what's your last tip for all of our audience as private investors? What are the major things to have a look of this investment block when considering whether to invest in sustainable pockets?

That's a good question. So first this-- don't try to do everything alone. Even, institutional investors they're not trying to just figure out if there is a possibility to use some kind of a shortcut, such as ready somebody else has done reports or ratings. Don't take advantage of that. But also take it with a grain of salt. So don't take it as the ultimate truth. It might lead you to the right direction.

But you can also make your own views when you read a bit more and get more familiar with the topics. So that's one thing, and also, you can do both sustainable investing and with when you invest

in funds or direct shares. So just you have to decide what is your-- what is your preference and then there's always sustainable options available, as long as you just spend a bit of time to have a look around.

Yes I think that's a great conclusion. So it seems that ESG or sustainability is not a reason why not to invest in profitable way. Thank you Tiina for coming as a guest to this Hanken podcast on Sustainability Unwrapped. My name was Hanna Silvola. I had a very nice talk with Tiina Landau, my co-author in the book, *Sustainable Investing Beating the Market with ESG*. Many Thanks Tiina. Many thanks audience. Have a good luck with your sustainable investments.