Vrije Universiteit Brussel

Department of Economic, Social and Political Sciences and Solvay Business School

MASTER OF SCIENCE IN MANAGEMENT

Sustainability in the Financial Value Chain

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Academic year 2012-2013

Master thesis submitted to obtain the degree of
"Master of Science in Management"

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Preface

“Money should never be separated from mission. It is an instrument, not an end. Detached from values, it may indeed be the root of all evil. Linked effectively to social purpose, it can be the root of opportunity.” – Rosabeth M. Kanter

Acknowledgements

I express my gratitude to my promoter, Professor Nikolay Dentchev for all the guidance, advice and promptitude in helping me to develop my work. To my partner and friend Nicolay Verbraeken, for the support, help and patience. To all the interviewees, who so kindly accepted to contribute to this study. And to my family, always supporting and believing in me, even from far.

Abstract

Sustainable and Responsible Investment (SRI) is the practice of including non-financial criteria such as environmental, social and governance (ESG) issues in investment decisions. In theory, by changing the criteria of capital allocation, SRI would motivate companies to improve their sustainable performance. It seems like a striking idea combining profits and sustainability through investment. But is it really possible? Does SRI really have the ability of influencing corporations' behavior? In order to answer this question, a qualitative research was conducted, where we analyzed factors that we consider paramount for the effectiveness of SRI in achieving this goal. First we tried to understand what are the motivations guiding the main stakeholders in SRI, namely corporations, financial institutions (FIs) and investors. Then we tried to get a picture of important constraints to the effectiveness of SRI such as professional expertise in the field, sustainable quality of the funds and transparency. Finally, we examined the main factors which might limit SRI from having a real impact in companies and we give suggestions on how to overcome those limitations.

Our findings do not show any evidence that the motivations guiding stakeholders in SRI, or its present conditions of quality and transparency, would be able to deliver any significant corporate change through access to capital on financial markets. It is more likely, however, that the influence SRI has on companies' reputation brings about such change, rather than access to capital. Even then, the SRI market needs to be developed further and a minimal quality of SRI funds needs to be ensured. Further regulation can probably improve the balance between the quality and the economic appeal of SRI funds, thereby closing the gap between investors' financial expectations and the broader public interest. Moreover, change is required from investors towards a more active and involved attitude, as well as better cooperation between institutions and investors in order to cope with the current fragmentation in the SRI market.

Key Terms: sustainability, sustainable and responsible investment (SRI), corporations, financial institutions (FIs), investors.

Table of Contents

List of Abbreviations

AMWG: Asset Management Working Group

ASrIA: Association for Sustainable and Responsible Investment in Asia

AuM: Assets under Management

BEAMA: Belgian Asset Managers Association

CSR: Corporate Social Responsibility

DJSI: Dow Jones Sustainability Indices

ESG: Environmental, Social and Governance

ESPs: Employees Savings Plans (France)

EUROSIF: European Sustainable Investment Forum

Febelfin: Belgian Financial Sector Federation

GAAP: Generally Accepted Accounting Principles

GISR: Global Initiative for Sustainability Ratings

GRI: Global Reporting Initiative

GSIA: Global Sustainable Investment Alliance

KIID: Key Investor Information Document

MIS : Management Information System

NGO : Non-Governmental Organization

RFA: Réseau Financement Alternatif

RIAA: Responsible Investment Association Australasia

SIO: Social Investment Organization (Canada)

SRI: Sustainable and Responsible Investment

UCI: Undertaking for Collective Investment

US SIF: Sustainable and Responsible Investment Forum in the United States

UN GC: United Nations Global Compact

UNEP FI: United Nations Environment Program Finance Initiative

WCED: World Commission on Environment and Development

WRI: World Resources Institute

List of Annexes

Chapter 1 – Introduction

The financial sector, as many in the service sector, has long remained at a distance from environmental and social issues (Mulder, 2007; Richardson, 2008). Causal relationships between finance and its environmental and social impacts are spread over time, which masks the responsibility of the sector regarding these issues (Richardson, 2008). This responsibility should not be overlooked though, since the biggest part of development capital in the world is under the power of private financial institutions (FIs) (Hubbard, 2008). Therefore, those institutions play an important role in realizing more sustainable development by allocating and giving direction to investors' capital along various business value chains (Peeters, Defraeije, & André-Dumont, 2011; Richardson, 2008; Scholtens, 2006).

Considering the necessity to integrate the concept of sustainability in the financial sector, some new financial practices emerged, constituting what we now call *Social Finance* – the use of finance to impact positively on society and the environment (Weber & Duan, 2012). Topics in *Social Finance* include social banking, social venture capital, microfinance and Sustainable and Responsible Investment[1] (SRI) (Serrano-Cinca, Gutiérrez-Nieto, & Camón-Cala, 2010). This last topic is the focus of the present study.

SRI is a term used to refer to investment approaches which take Environmental, Social and Governance (ESG) factors into account to make investment decisions in order to generate long-term sustainable returns as well as sustainable economic, social and environmental systems (European Sustainable Investment Forum [Eurosif], 2012; Principles for Responsible Investment [PRI], 2012a; Responsible Investment Association Australasia [RIAA], 2011; Sustainable and Responsible Investment Forum in the United States [US SIF], 2012a). Many approaches can be used within the practice of SRI, but basically, the different strategies consist in screening assets according to negative or positive criteria, shareholder activism and community development (US SIF, 2012a). Interpretations for SRI vary widely, just like its goals. One of the most

[1] Also largely referred to as Socially Responsible Investment

omnipresent ones, however, and maybe one of the most meaningful is the goal of contributing to sustainable development by encouraging companies to improve their corporate social responsibility (CSR) and sustainable performance (de Colle & York, 2009).

The market for SRI has been flourishing and its growth has even been surpassing that of conventional funds (Eurosif, 2012, US SIF, 2012a). Some authors still claim that the former can yield comparable returns to those of the latter (Cortez, Silva, & Areal, 2009; Kreander, Gray, Power, & Sinclair, 2005; Mill, 2006; Statman, 2007). *But can SRI really create an impact on companies' behaviour?* The question is still unanswered (Bayot, Demoustiez, & Coeckelberg, 2009) and academics are not so optimistic (de Colle & York, 2009; Haigh & Hazelton, 2004; Hawken, 2004; Richardson, 2008; Scholtens, 2006).

The assumption that SRI could exert influence on companies is based on the premise that firms with reprehensible environmental or social behaviour are "*punished*", while the adepts of good practices are "*rewarded*" through the screening of investments. Investors can also try to change companies through active engagement with them. The literature, however, shows ineffectiveness in all approaches (de Colle & York, 2009; Haigh & Hazelton, 2004; Hawken, 2004; Heinkel, Kraus, & Zechner, 2001).

In order to bring further contributions to the discussion, and without the pretention of finding a definitive conclusion for the problem, this work examines the ability of SRI in influencing companies' behavior to make them more sustainable. We set out from the assumption that the effectiveness of SRI in accomplishing this goal strongly depends on the motivations of the actors involved in it, along with the quality of the process through which SRI is implemented (Richardson, 2008).

We investigate this research problem by answering the following questions:

1 - What are the motivations of the main players involved in SRI, namely corporations, FIs, and investors?

2 - Do the current conditions through which SRI is implemented (marketing, quality of methodologies, transparency) allow effective results on the CSR and sustainability performance of companies?

3 - What are the limitations impeding the effectiveness of SRI in promoting sustainability and which would be the steps to overcome these limitations?

In order to elucidate our questions, we have performed a qualitative case study research for which we have interviewed ten experts in the domain of SRI, amongst which researchers, employees from banks, representatives of non-governmental organizations (NGOs) and industry associations. We have then looked for trends between their comments and benchmarked them against related academic literature.

The paper starts with a literature review on key concepts and relevant issues around the field of SRI. The following section presents a description of the methodology used for the research and in the subsequent section we present our findings. The findings discuss the motivations of SRI, its current conditions as well as the limitations of SRI in promoting sustainability and presents possible ways to overcome those limitations. We then finalize with our conclusions and some suggestions for further studies.

Chapter 2 - Literature Review and Theoretical Foundation

2.1 – Sustainable Development

The emergence of the concept of sustainable development had its stage set by a number of historical antecedents (Vos, 2007). It was mainly in the 20th century that environmental problems changed in scale and reach. If these problems at first were mainly specific regional cases (e.g. concerning water or air pollution), to date we have knowledge of environmental problems at continental and even worldwide scale. The current list of environmental problems with which we need to cope includes desertification, tropical deforestation, acidification, climate change, ozone depletion, biodiversity loss and build-up of chemical substances in food chains and ground water, just to name a few (Jeucken, 2012).

As a result of the dissatisfaction about these infringements on the environment, especially between 1968 and 1972, the number of environmental action groups multiplied quickly in most western countries. It became clear that the growth-oriented progress needed to be dramatically revised in order to reduce the pressure on the environment and ensure survival in the future generations (Jeucken, 2012). One of the pioneer works in exposing the challenges of an economic expansion within limited resources was the 1972 report "*Limits of Growth*", commissioned by the Club of Rome (Meadows, Randers, & Meadows, 2004). Using system dynamics theory and a computer model, the book projected scenarios of world development and outcomes from 1900 to 2100. The scenarios showed that the interaction between population growth and natural resources use imposed limits to industrial growth. The radical conclusions and the methodology of the study were target of much criticism. Nonetheless, it was a remarkable wake-up call and it opened the path for a multitude of developments in the environmental field, including the introduction of environmental policy measures by governments in various countries (Jeucken, 2012; Vos, 2007).

During the 1980s and 1990s concerns about the environment increased as the world witnessed considerable ecological disasters such as Bhopal, India, in 1984, Chernobyl, former Soviet Union, in 1986, and Exxon Valdez, Alaska, 1989. These incidents added to other already existing and even more menacing problems, such as scarceness of drinking water, global warming, and the hole in the ozone layer (Jeucken, 2012). Such alarming environmental developments, next to the inequalities in the welfare distribution within and between societies called for the need of theorization on sustainable development (Dentchev, 2007). This can be regarded as a tipping point in the environmental consciousness, where environmental issues passed from being a discrete concern to be "regarded as pivotal for the human development" (Jeucken, 2012, p.21).

The most widely spread definition of sustainable development is that proposed by the World Commission on Environment and Development (WCED) in 1987, entitled "*Our Common Future*", also known as the "*Brundtland report*". The authors of this work defined sustainable development as: "development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (Brundtland United Nations Commission, 1987).

The concept of sustainability was originally used by biologists and ecologists to designate a safe rate at which renewable resources could be extracted or damaged by pollution without compromising the integrity of the ecosystem (Lélé, 1997). It then moved to economics, focusing on the relationship between natural and production processes (Goodland, 1995; Vos, 2007). More recently, the term started to be broadly used in business and management literature as well (Morrison, 2003). The implementation of the concept of sustainable development in the economy and the financial markets involves the integration of environmental considerations into all parts of economic decision-making (Richardson, 2008).

Regardless of the field in which the concept of sustainable development is used, most of the definitions have common core features. The first of which is looking at environmental problems in relation to economy and society (Vos, 2007). It is common, therefore, that some people define sustainable development as a balance between ecologic, economic and social factors (Jeucken, 2012). These three elements are usually called the "triple bottom line" and they are the origin of the three Ps: people, profit and planet (Elkington, 1998). Society (people) depends upon economy (profit), which in turn depends on the worldwide ecological system (planet) (Jeucken, 2012).

The interdependent relationships between those three elements are usually illustrated as a "triangle", a "three-legged stool" or overlapping circles in a Venn diagram, which intends to enhance the idea that sustainability is looking to systemic interconnections where the elements should support or underpin one another in a reciprocal relationship (Vos, 2007). Another core feature of the concept of sustainability is the fact that it focuses on intergenerational equity. Solow (1991) defends that, even though it is impossible to foresee the exact needs of future generations, we should conduct ourselves so that we leave to upcoming generations the option or the capacity to be as well off as we are. This means that, even if some resources may be exhausted, the environment which is left behind should include productive capacity and technological knowledge to provide such welfare.

Finally, a common aspect in all definitions of sustainability is the emphasis given on working beyond simple compliance with existing laws and regulations. For policymakers this can be translated as encouraging innovation beyond the minimum proposed by law. For business it means that going further than compliance with regulations can be seen as a way to achieve competitive advantage (Vos, 2007).

The prospect that businesses will have increasing influence on the environment will, both directly and indirectly, lead to various changes in public policy, consumer preferences, supplier relationships, stockholder expectations and competitor strategies. Furthermore, it will also increase NGO activism in favor of socially and environmentally sustainable initiatives from companies (World Resources Institute [WRI], 2005). Such changes are key drivers that have been inducing firms to revise their approach towards ecological issues (Lucas & Wilson, 2008; Mulder, 2007). It means that firms increasingly understand how significant the social and environmental impact of their business activities is. As such, they acknowledge that they hold a social and environmental responsibility, which is not bound to "doing something good for the environment and society", but also includes the integration of responsibility in business strategy (Mulder, 2007).

In what concerns public policies, even though we can notice endeavor of many governments in improving environmental laws and regulations, a truly ecological sustainable economy has not yet been engineered by any of this governments (Richardson & Wood, 2006). There is a need, thus, for the evaluation and consideration of different pathways to sustainability, from which finance is an example (Zadek, Merme, & Samans, 2005).

2.2 – Sustainability and Financial Value Chain: Making the Link

So far, environmental management practices have gained attention from academics and corporate management especially within the context of the manufacturing industry, which have a *direct high footprint* on the environment (Lucas & Wilson, 2008; Mulder, 2007). Such fact is to be expected, since one can easily visualize how the creation of goods consumes scarce natural resources in its production processes and releases undesired by-products on the environment (Lucas & Wilson, 2008). Other sectors that directly depend on the ecosystem have equally driven considerable attention to environmental management. Those are, for example, tourism, agribusiness, fishery and forestry (Mulder, 2007).

The financial sector, as many in the service sector, has long remained at distance from environmental and social issues (Mulder, 2007; Richardson, 2008). As a characteristic of the service sector, FIs provide products that have an intangible nature and are consumed as they are produced. It is therefore not so easy to visualize the potentially harmful environmental externalities of those activities. However, as with any business, a wide array of physical components and reliance in natural resources is involved to support them (Grove, Fisk, Pickett, & Kangun, 1996).

Yet, the reason why FIs should pay more attention to environmental and social issues is not exactly their direct ecological footprint, resultant of energy and paper consumption, for example (Richardson, 2008). A much more significant issue than that is the fact that the biggest portion of development capital in the world is not in the hands of governments, but under the control of private FIs – a diverse group formed by banks, pension plans, mutual funds, credit unions and others (Hubbard, 2008). As such FIs play, above all, an important role by giving direction to the capital in value chains, through the allocation of investors' money to businesses (Peeters et al., 2011; Richardson, 2008; Scholtens, 2006).

Corporations are often not self-sufficient and in order to assist their growth and new projects they need to turn to capital markets. As such, "financier's capital is transformed through scale, time and location into an instrument of development"(Richardson, 2008). The ownership of stakes in companies is also a powerful instrument of influence in favor of financiers (Gillan & Starks, 1999). By pressure of financial markets to maintain strong profitability, companies are obliged to provide financial reports several times during the year. Both the economic growth that it boosts and its social and environmental consequences are part of the caprices of the financial sector (Richardson, 2008).

By exerting such a role in the control of the stream of capital, FIs can be considered as potential sustainability regulators (Conley & Williams, 2011). For a long time, though, this role of FIs has not been so obvious. Traditionally, financiers have not been held accountable for the resulting impacts of the transactions they fund. Conversely, most of the investors typically ignore which type of projects and companies they are supporting, even more any subsequent social or environmental harm. Causal relationships between finance and environmental impacts are set far apart across time and space, which masks the holistic responsibility for the degradation (Richardson, 2008). For such reasons, FIs are named by Richardson (2008, p. 3) as "unseen polluters, who wittingly or unwittingly contribute to environmental and social problems they sponsor and profit from".

Seen the necessity to integrate the concept of sustainability to the financial sector, some new financial practices emerged, constituting what we call now *Social Finance* – the use of finance to impact positively on society and the environment (Weber & Duan, 2012). According to Benedikter (2011), Social Finance distinguishes itself from mainstream finance thanks to three core features. The first of them is working with a "*triple bottom line*", which means taking in consideration the three factors - profit, environment, and people - to judge investment and lending opportunities. The second feature is *maximized transparency* about where the money invested is going to. And the third feature is the endeavor to pursue *human development* through the emancipation and involvement of communities (Benedikter, 2011). Topics in *Social Finance* include social banking, social venture capital, microfinance and SRI (Serrano-Cinca et al., 2010). In this work we focus on the last one, Sustainable and Responsible Investment, analyzing its ability of promoting sustainability by influencing corporations' behaviors.

2.3 – Sustainable and Responsible Investment

2.3.1 – Definition

Sustainable and Responsible Investment (SRI), also known as Responsible Investment or Socially Responsible Investment[2] is a practice that cannot be easily defined. Its conception is largely influenced by culture, beliefs and motivation (Eurosif, 2012) . Whereas there is a great deal of consensus among the proponents of SRI, there is still much of heterogeneity about the definitions of SRI (Sparkes & Cowton, 2004).

During the research for this study, as expected, SRI-like investment approaches were encountered under various names. Even the abbreviation SRI is at times used to refer to Sustainable and Responsible Investment and at times to refer to Socially and Responsible Investment. We have tried, therefore, to find a "workable" definition for SRI, based on the definitions given by the main institutions promoting its practice around the word. Thus, in terms of scope, this work considers SRI as an "umbrella term" that encompasses all the investment approaches which take into account ESG factors in investment decisions in order to generate long-term sustainable returns as well as sustainable economic, social and environmental systems (Eurosif, 2012; PRI, 2012a.; RIAA, 2011; US SIF, 2012b).

SRI distinguishes itself from conventional investment for two reasons: the first is the time-frame, meaning that SRI aims the creation of sustainable, long-term returns and not only short-term returns. The second distinction is that SRI demands more consideration from the investors about wider contextual factors and not only pure financial information. These factors include the health and stability of economic and environmental systems as well as the developing values and expectations of the societies in which they are inserted (PRI, 2012a).

[2] Some institutions consider Sustainable and Responsible Investment as a distinct concept from Socially and Responsible investment defending that the first focuses on risk-adjusted financial returns. See, for example on http://fsinsight.org/topics/sustainable-and-responsible-investments#

2.3.2 – Heterogeneity in SRI

Sandberg, Juravle, Hedesström, & Hamilton, (2008), suggest that *heterogeneity* among SRI proponents can be found at four levels at least, namely *definitional*, *terminological*, *strategic* and *practical.* These authors argue that, nonetheless SRI has been gaining increasing attention from financial institutions, investors and academics, whilst the amount of money invested in such funds has been increasing significantly in the recent years (Eurosif, 2012; US SIF, 2012a). This kind of investment is, however, still in its infancy and this is reflected in the lack of uniformity in the four levels mentioned above.

Sparkes & Cowton (2004), from another point of view, consider SRI a mature practice, in the sense that it has increased its complexity and begun to enter the mainstream of the investment universe. But they still acknowledge that the SRI field has been marked by debate and lack of consensus in definition and terminology. According to Sandberg et al. (2008) this heterogeneity concerning SRI has at least three different reasons: cultural and ideological differences between different countries and regions, differences in values, norms and ideology between different SRI stakeholders, and differences in the market setting in which SRI actors operate.

The terminological heterogeneity of SRI is reflected in the variety of names under which it can be referred to, amongst which "ethical", "social", "green", "responsible", "sustainable", "societal", "impact" and "clean" investment (Eurosif, 2012) or still "mission investing" and "double or triple bottom line investing" (US SIF, 2012b). For the purpose of this work, these terms will be used indiscriminately as the context of particular passages may demand.

2.3.3 – Brief Historic

The origins of SRI as currently practiced are strongly related to initiatives of religious institutions (Louche & Lydemberg, 2006; Schueth, 2003).The first reference to investment allocation that considers extra financial criteria dates back from the 17th century, in the Quaker movement, a Methodist group who avoided investments in weapons, slavery and alcohol. (Herringer, Firer, & Viviers, 2009; Louche & Lydemberg, 2006; Richardson, 2009; Schueth, 2012). In 1928 the first socially responsible mutual fund, the US Pioneer Fund, was created for Evangelical Protestants who opposed to invest their money in firms involved in the manufacturing of alcohol and tobacco (Beabout & Schmiesing, 2003). From the 1960’s onwards SRI experienced a rise in popularity in Europe as many churches and religious entities of different countries adopted ethical screens and launched ethical funds based on their moral values (Eurosif, 2012; Louche & Lydemberg, 2006).

The modern roots of SRI, however, seem to be encountered in the tumultuous political climate of the years 1960s and 1970s, when the US civil right movement, the war in Vietnam, the apartheid in South Africa and other events served to increase sensitivity to issues such as social responsibility and accountability (Eurosif, 2012; Schueth, 2003). The focus of SRI shifted then from the simple exclusion of specific products, referred to as “sin stocks” to an endeavor of changing companies behavior on social and environmental issues. This means that SRI became broader in focus. The exclusion of industries further expanded to include also military contract and nuclear power. The idea behind those exclusions were no longer the fact that they were morally objectionable, but rather that the profitability from such products impose intolerable costs on society (Louche & Lydemberg, 2006).

In the 1980s and 1990s a vast amount of new information about global warming and ozone depletion came to the attention of the public, turning socially concerned investors’ attention to environmental issues. On the retail side, the first SRI index fund was launched in 1990 by Kinder, Lyndenberg, Domini & Co., Inc., the KLD 400 Social Index, currently named MSCI KLD 400 Social Index (SRI World Group, 2013).

In the 2000s the concept of sustainable development is combined with the socially responsible aspect of investments and the notion of SRI is expanded from Socially Responsible Investment to Sustainable and Responsible Investment. Concurrently, with increasing evidence that extra financial information produces financial impact, a major alliance of institutional investors was formed to launch in 2006 the United Nations Backed Principles for Responsible Investment (PRI) (Louche & Lydemberg, 2011).

Nowadays SRI is an established industry, offering a wide variety of products to both institutional as retail investors. The demand drivers for those products are equally variable. While some investors may incorporate ESG for risk avoidance, some may exclude certain products out of moral values. Some look for business opportunities and expect SRI funds to outperform the market in terms of capitalization growth, based on an increasing demand for sustainable products and solutions. Some may aim for long-term financial stability and some seek to have social and/or environmental impact through their investments. Whereas the motivations for SRI may vary, a common point between all those approaches is the consideration of ESG criteria in investment processes (Eurosif, 2012).

2.3.4 – Why SRI?

"Sustainable development cannot be achieved without socially responsible investment" said the former head of the World Commission on Environment and Development, Gro Harlem Brundtland (Social Investment Organization [SIO], s. d. cited in; Richardson, 2008).

The current global population is of about seven billion and this number is likely to rise to nine billion by 2050. This growth is still combined with drastic increasing in consumption of energy, water and other natural resources. Our current patterns of economic activity, where many social and environmental impacts are kept off the balance sheets and outside the mainstream business and financial models, can simply not be sustained anymore without hard negative consequences (Global Sustainable Investment Alliance [GSIA], 2013). The market contains no instrument to scale the economy according to the carrying capacity of the planet. Thus, in order to achieve sustainability in a finite biosphere we must address the role of capital markets founded on the base of infinite economic growth (Richardson, 2008).

SRI is a practice that intends to cope with this market failure by creating ways to find and integrate critical value drivers into investment decision-making. This integration may include an analysis of the firm's track record and projects in relation to the three trend categories of our time, namely Environment, Society and Corporate Governance (ESG). These trends cover a broad range of issues which we constantly hear about in the media, including water, food and energy security, demographic changes, global warming, increasing regulation, litigation and civil activism, access and use of scarce resources, reputation and the mounting trend towards the cost of externalities (RIAA, 2011). Through the integration of such concerns in financial analysis, SRI intends to reconcile investors' financial interests with an effort to encourage the improvement of the social, ethical and environmental performance of corporations (de Colle & York, 2009), and thus creating financial profit alongside with social and environmental profit (Hellsten & Mallin, 2006).

Many academic works have been completed in order to evaluate the financial performance of SRI, from which some examples are Cortez et al. (2009) Girard, Rahman, & Stone (2007), Kreander et al., (2005), Mill (2006) and Statman (2007). On the other hand very few academics have tried to find out whether SRI can really make a contribution to sustainable development by changing the behaviour of corporations involved. Seeking to fill this gap, this study investigates the ability of SRI to generate change. Among others, the most important aspects examined are the motivations leading stakeholders of the movement, extra-financial quality and transparency in SRI funds, limitations of the system and possible ways to overcome those limitations.

2.3.5 – SRI Approaches

The terminology used to distinguish the different SRI strategies varies from institution to institution and in the related literature (see Annex 1: **Error! Reference source not found.**). However, even if the names used to refer to different strategies vary, they often share the same meaning. In this section a comparison was made between the strategies presented by seven important associations promoting SRI around the world. These are:

1) European Sustainable Investment Forum[3] (Eurosif)
2) Forum for Sustainable and Responsible Investment in the United States[4] (US SIF)
3) Responsible Investment Association Australasia[5] (RIAA)
4) Association for Sustainable and Responsible Investment in Asia[6] (ASrIA)

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[3] See: http://www.eurosif.org/

[4] See: http://www.ussif.org/

[5] See: http://www.responsibleinvestment.org/

[6] See: http://www.asria.org/

5) Social Investment Organization (Canada)[7] (SIO)
6) United Nations-backed Principles for Responsible Investment[8] (PRI)
7) European Fund and Asset Management Association[9] (EFAMA)

Strategies presented by different associations which share the same meaning or even a close meaning are grouped together below.[10]

1) *Sustainability Themed Investment* (Eurosif, SIO) / *ESG-Themed Investments* (PRI) / *Thematic Approach* (EFAMA) / *Thematic Investment* (RIAA) / *Screening* (US SIF, ASrIA[11]): selection of assets based on themes which are specifically related to sustainability. This may involve investing in companies that adhere positively to particular sustainable activities, such as eco-efficiency, healthcare, sustainable energy technology (PRI, 2012b; RIAA, 2011; SIO, 2013) or in companies that are particularly exposed to (or leveraged to) specific environmental and social issues (PRI, 2012b). Since 2008, in order to be counted in this approach, funds are required to pass through an ESG analysis or a screen of investments (Eurosif, 2012). This category also includes multi-strategy portfolios which may contain a combination of multiple issues related to ESG (Eurosif, 2012; RIAA, 2011).
2) *Best-in-class Investment Selection* (Eurosif) / *ESG-Positive Screening and Best-in-class* (PRI) / *Best-in-class* (EFAMA) / *Best of Sector* (RIAA) / *Screening* (US SIF, ASrIA, SIO): according to this approach investors choose for investing in companies which best meet given criteria within a universe, category or class (EFAMA, 2011; Eurosif, 2012; PRI, 2012b; RIAA, 2011) . This approach can also be called best-in-universe and best-effort (Eurosif, 2012).
3) *Norms-based Screening* (Eurosif) / *ESG-Exclusions* (PRI) / *Norms-based approach* (EFAMA) / *Responsible Investment Screening* (RIAA) / *Screening*

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[7] See: http://www.socialinvestment.ca/

[8] See: http://www.unpri.org/

[9] See: http://www.efama.org

[10] Comparisons based on the author's impressions. Interested reader should consult the source documents from the related organizations for more information on the definitions.

[11] AsrIA follows the same SRI classification as the US SIF.

(US SIF, ASrIA, SIO): this approach consists in the selection of companies for investment based on their compliance with international norms or standards covering ESG factors (EFAMA, 2012; Eurosif, 2012). Those are norms imposed by international institutions such as the United Nations (UN) (Eurosif, 2012). RIAA does not explicitly mention compliance with international norms as a criteria for "*Responsible Investment Screening"*, but as this strategy is described in a broad manner by that institution, an assumption is made here that "*Norms-based screening*" would be part of that approach. The same is valid for the "*Screening*" approach from US SIF.

4) *Exclusion of Holdings from Investment Universe* (Eurosif) / *ESG-Exclusions* (PRI) / *Exclusion approach* (EFAMA) / *Responsible Investment Screening* (RIAA) / *Screening* (US SIF, ASrIA, SIO): also referred to as ethical- or values- based exclusion (Eurosif, 2012). This approach excludes, from the potential investment opportunities, companies, sectors or even countries involved with activities considered unethical. Criteria for exclusion commonly include weapons, animal testing, tobacco and pornography. (EFAMA, 2012b; Eurosif, 2012; PRI, 2012c; RIAA, 2011;US SIF, 2012a).

As it can be observed, the "*Screening*" approach from US SIF was used as a general term for all the strategies presented above. And "*Responsible Investment Screening*" from RIAA was included both in "Norms-based screening" and "Exclusion of Holdings approach". The reason for this is that "Screening" and "Responsible Investment Screening" are described respectively by US SIF and RIAA in a broad manner. The two definitions are similar to each other and basically refer to the evaluation of investment portfolios or mutual funds taking in consideration ESG criteria. As such, high performers in CSR are screened positively. Conversely, companies with weak ESG records have their portfolio weights decreased or excluded through negative screening (RIAA, 2011; US SIF, 2012b).

5) *Integration of ESG Factors in Financial Analysis* (Eurosif) / *ESG-Integration* (PRI and RIAA) / Integration (SIO): this type of investment decision is based on financial analysis that explicitly considers ESG opportunities and risks that can impact (positively or negatively) on company financials (Eurosif, 2012; PRI, 2012b; RIAA, 2011). "More specifically, ESG knowledge is used to inform the analysis of risk, innovation, operating

performance, competitive and strategic positioning, quality of management, corporate culture and governance and to enhance financial valuation, portfolio construction, engagement and voting practices" (RIAA, 2011; p.8). US SIF does not include this approach in its set of strategies. EFAMA included it in its "Report on Responsible Investment 2011", but not in its more recent document, the "EFAMA Guidance on RI information in the KIID & Post Investment Disclosure 2012".

6) *Engagement and Voting on Sustainability Matters* (Eurosif) / *Engagements (three types)* (PRI) / *Engagement (voting)* (EFAMA) / *Shareholder Activism – Voting and Resolutions* (RIAA) / *Shareholder Advocacy* (US SIF/ ASrIA) / *Corporate Engagement and Shareholder Action* (SIO): refers to the active participation of owners of the corporation through voting of shares and engagement activities such as dialogue with senior management and/or boards of companies in ESG issues (EFAMA, 2012b; Eurosif, 2012; RIAA, 2011; SIO, 2013; US SIF, 2012b). This is a long-term process as it seeks to impact firms' behaviour towards those matters (Eurosif, 2012).
7) *Impact Investment* (Eurosif, RIAA, SIO) / *Community Investment* (US SIF/ ASrIA): consists in actively placing capital into specific projects aiming to solve significant environmental and social problems, while providing returns to the investor that range from principal to above market (Eurosif, 2012; RIAA, 2011). It distinguishes itself from philanthropy as the investor keeps ownership of the asset and expects to get financial returns (Eurosif, 2012). It has the advantage of providing solutions at larger scale once compared with philanthropy, since it leverages the private sector capital (RIAA, 2011).

   The related strategy presented by US SIF (2012) is "*Community Investing*" which consists in directing capital from investors to communities underserved by traditional financial services such as credit, equity, capital and basic banking products. The purpose of community investing is the generation of returns to investors, producing at the same time a social return by providing financial services to low-income individuals, and supplying capital to small businesses and vital community services, such as affordable housing, education, child care, healthcare and jobs that pay a living wage.

   Besides this specific type of "*Impact Investment*" Eurosif cites microfinance and French fonds solidaires.

8) *Engagement with companies on ESG issues* (RIAA): similar to "*Shareholder Activism*", but in this case engagement involves, besides assets owners, also asset managers or specialist firms (RIAA, 2011).

2.3.6 – An Overview of SRI in the Current Global Scenario

Seven regions around the world have created associations in order to promote and develop the concept and practices of SRI. These regions are Europe, Asia (excluding Japan), Japan, United States, Australia and New Zealand, Canada, and Africa. Recently a global organization – Global Sustainable Investment Alliance (GSIA) – has also been created with the purpose of creating cooperation between those seven regions[12] to increase the impact and visibility of SRI at a global level (GSIA, 2013). The data presented below was retrieved from the annual reports released by some of the members of GSIA and the GSIA report itself – the Global Sustainable Investment Review 2012.

According to this study, the current global market share of SRI amounts to US$ 13.6 trillion which represents 21.8 percent of the total universe of Assets under Management (AuM) within the regions studied. The market for SRI is led by Europe, where almost two-thirds of the world's SRI assets are managed. The United States and Canada have also a significant proportion of those assets and the three of them combined account for 96 percent of the assets covered by the mentioned report (GSIA, 2013).

As we look at the proportion of SRI assets in total AuM by region, Europe is also the region with the highest proportion, with a market share of 49 percent of total AuM considering ESG issues (Eurosif, 2012; GSIA, 2013). On the other hand, in the United States this proportion is of 11.2 percent and in Asia, not more than 3 percent. Canada and Australia/Asia fall in a middle-range with respectively 20 and 18 percent of SRI assets among total assets.

The strategies most widely applied by investors are in first place "Negative/Exclusionary Screening", followed by "ESG integration" and

[12] In fact, the membership associations from Japan and Africa are not members of the GSIA, on the other hand, the United Kingdom and the Netherlands have their own SRI associations, which are members of GSIA.

"Shareholder Engagement". However, grouping strategies across the regions together and making a ranking of them becomes problematic as in many cases there is no uniformity in denomination of strategies and in what is considered to be one strategy or not (GSIA, 2013). For example the strategy "Impact investment" is used with a wide range of connotations across different regions. This includes credit unions, loan funds and venture capital funds with a mission of serving low- to moderate- income communities in the United States (US SIF, 2012a), social impact bonds in Japan, microfinance investments in Europe and private equity funds with strong social and environmental mandates in Canada.

Regarding the proportional contribution of each strategy per region we can see that the desire for ESG strategies varies widely across the different regions in the globe (GSIA, 2013). Even among different countries in Europe this heterogeneity was perceived (Eurosif, 2012). GSIA defends that the lack of uniformity between strategies used, denominations and allocation of assets probably results from cultural and historical differences between regions. This in turn lead to different solutions for similar challenges in different legal frameworks and with different tax considerations which influence investment decisions (GSIA, 2013).

As we turn to the type of investors engaged in SRI strategies we see that the great majority of them are institutional investors. More specifically, these are professional investors or asset owners who manage assets on behalf of their clients and beneficiaries. This type of investors account for 89 percent of the total SRI figure of US$ 13.6 trillion, whereas retail investors are responsible for the other 11 percent (GSIA, 2013). This fact is especially remarkable in Europe, where 96 percent of the SRI assets reported are institutional. There are, however, different proportions among the countries in Europe. Belgium, for example, stands out in relation to many of the European countries, with a proportion of retail SRI market of 23 percent (Eurosif, 2012).

In terms of growth, allocation to retail has grown in a slower rate than to institutional, resulting in a drop of the proportional allocation of the former to SRI strategies. Nevertheless, considering the proportion of retail assets in Europe released by EFAMA in 2010 was 31 percent of the total assets, a proportion of 6 percent allocated to SRI shows potential for growth of SRI in retail assets.

Following the same trend, in the other regions of the globe institutional investors also prevail over individual ones, except in Asia, where retail investors remain the majority in the SRI scene. An interesting fact, however, is that the retail market in the United States, even if smaller than the institutional market, still has a significantly greater market share compared to the other regions. In comparison to Europe, Asia and Africa, the United States have the advantage of having a large market, free of fragmentations in terms of language and legislation. Such characteristics can aid the fund marketing, permitting it to reach a larger scale than elsewhere. This fact is a sign that communication and marketing play an important role in order to expand the reach of SRI to the retail market, and as such, should be taken as an example in Europe, Asia and Africa as well (Eurosif, 2012; GSIA, 2013).

Regarding asset allocation, the asset classes reflect the type of investor concerned. In Europe, for instance, where the vast majority of the investors are institutional, approximately 50 percent of the allocated assets are bonds. Equity is the second most popular type of assets among investors, with a percentage of 33 percent. These two types, which are more liquid monetary assets, are preferred in comparison to others such as hedge funds or venture capital, which are considered to be more exotic assets (Eurosif, 2012; GSIA, 2013). Even though the European SRI study has analyzed strategies separately, the combined growth of all these strategies on a European level outpaces the overall investment markets' growth rates (Eurosif, 2012). The same performance of SRI compared to overall investment markets was observed in the United States (US SIF, 2012a), in Canada (SIO, 2013) and in Australia and New Zealand in the financial year of 2011 (RIAA, 2011). In Europe, however, most of the growth of each individual strategy is the result of its adoption by a small number of large institutional investors. The growth of each strategy is also rather a result of the conversion of existing assets to SRI strategies than an outperformance of the market by new SRI assets or an inflow of assets from the retail market (Eurosif, 2012).

Finally, a noticeable outcome in the reports of all the regions is the significant growth of "Impact Investing" as an SRI strategy, even if the absolute market size for this type of investment is still relatively small (GSIA, 2013). This is interpreted by Eurosif as a growing interest of investors in being capable to assess the social and/or environmental impact of their investments (Eurosif, 2012).

2.3.7 – SRI: Driven by Principles or by Prudence?

Concerning the reasons driving SRI supply, according to Eurosif (2012), the main factor is the demand from institutional investors. This is followed by legislation both national and European, which has grown in importance and focuses on investors in an effort to safeguard Europe from future financial turbulence caused by short-sighted financial behavior. These two supply drivers are followed by international initiatives, external pressure and demand from retail investors. Nevertheless, those drivers cover the importance of other factors such as peer pressure and transparency. Institutional investors who present a higher process quality and transparency regarding the screening process and their expectations of the companies set an example for other investors.

Reasons for integrating ESG issues into portfolio management vary among investors. Some seek to maximize financial returns, some act in accordance with personal values and to further social goals (United Nations Environment Program Finance Initiative [UNEP FI] & Asset Management Working Group [AMWG], 2006), and some use it as a means to promote change in corporations' behaviour (Louche & Lydemberg, 2006).

This type of SRI which seeks to optimize returns is named by Richardson (2008) as *business case SRI.* This, he affirms, is an evolutionary form of SRI which attends to value-seeking investors. On the other hand, the practice of SRI which intends to align investment with principles or to promote social and environmental change is named by him as *ethical investment.* This, he states, is a revolutionary form of SRI, practiced by value-based investors. Both forms reflect a similar division of motivations for CSR found at corporate level (Vogel, 2006).

In *business case SRI* environmental and social issues are considered in investment decisions according to the financial materiality that they present, it is therefore a prudent way of investing. Financial materiality can be translated in the extent to which an issue poses tangible financial risks or lucrative business opportunities. These risks and opportunities can be tangible, such as litigations and regulatory sanctions, or intangible, such as reputational risks and brand name (UNEP FI, 2004). As such, ESG matters are treated in this case as factors that can affect a company's financial condition, rather than a finality in their own right (Richardson, 2008).

Business case SRI is considered by Richardson (2008) as being a natural evolution of ordinary investment. During most of the last century financial metrics were the unique tool supporting investors for their decision-making. In times when most of a company's value was tangible, this investment approach worked reasonably well. However, towards the end of the last century a drastic shift occurred in the balance sheets of many companies, from tangible to intangible assets, such as "goodwill", relationships, innovation, reputation, efficiencies and accesses to new markets (Hebb & Wójcik, 2005). This kind of intangible assets make now the majority of the value of the 21st century economy (RIAA, 2011). Such a transition in the valuation of a firm brought along a new source of risks to investors, and as a result, both the risks and the true value of a company could no longer be captured in traditional financial metrics. The reputational and environmental risks that investors have been facing in the last decades can be easily exemplified by environmental scandals like Exxon Valdez or Brent Spar and the loss of shareholder value resulting thereof (Hebb & Wójcik, 2005). As a consequence of such changes in financial valuation, investors and financial institutions started to integrate ESG issues in their financial analyse.

According to Richardson (2008), however, this kind of SRI that simply takes in account ESG issues according to their materiality has no clear distinction from ordinary investment. Considering ESG issues in financial decisions is certainly clever in conventional finance too. The main difference, thus, is that in business case SRI such matters should be routinely taken in account in order to enhance financial analysis.

Richardson (2008) defends, however, that *business case SRI* cannot bring great advancement towards sustainability due to its strategy. A strategy which basically involves light screenings that exclude only the most insidious companies, depending on profitability, courteous engagement with corporate management, and technical assessments revealing financial risks and profitable opportunities inherent to financial management. Richardson (2008, 2009) still affirms that the *business case* motivation is the dominant reason for SRI practice in the current financial markets. The report "*Show Me the Money*" released by UNEPFI and AMWG (2006, p.5) supports this statement, using the following words:

"The first – and for investors arguably the most important – reason to integrate ESG issues is, simply, to make more money. There is a hypothesis, which we support, that a more thoroughgoing and systematic approach to integrating ESG issues in portfolios will, over time and in general, result in better financial performance."

Another type of driver for the practice of SRI is applying ethical values which are important to the investor to their investment portfolio (Domini, 2001). Richardson (2008) names this type of approach *ethical investment* to make a distinction with *business case SRI*. Ethical investment does not ignore the bottom-line, as it is not a form of charity, yet it gives priority to ethical reasons. This means that, differently from *business case SRI*, the concern about financial performance is secondary and investors may accept lower financial returns. (Richardson, 2009, UNEPFI, 2006).

This group of investors include those who are sometimes described as "feel good investors" by the modern media, presumably because they feel better about themselves for having a socially responsible investment portfolio (Michelson, Wailes, Laan, & Frost, 2004; Schueth, 2012). But also included in this group are those investors who intend to promote change in corporations. By switching the criteria of capital allocation, they try to motivate firms to improve their environmental and social behavior (Richardson, 2008).

This form of investment is more likely to thrive in institutions more closely connected to the civil society. Some examples are religious institutions, such as Interfaith Center for Corporate Responsibility, credit unions such as Canada's Van City Credit Union, cooperative banks, charitable foundations and mutual funds that offer committed ethically screened portfolios, such as US and UK ethical funds and Domini Social Investments (Richardson, 2008, 2009, UNEPFI, 2006). Some SRI governance standards like the ones defended in the 2003

Collevecchio Declaration on Financial Institutions represent an even stronger expression of the ethical approach (Richardson, 2009).

2.3.8 – Regulation of SRI

So far, SRI policy reforms have tended to support market-based and informational standards that leave financiers with significant judgment over investment decisions. As such, SRI regulation normally includes mechanisms for financiers to report their SRI policies, proxy voting activities and environmental impacts of financial significance. In theory, such process standards enable the assessment, verification and communication of performance, and in this way they can put pressure on environmental laggards for improvement and reward good performers through competitive market advantages (Richardson, 2009).

In Australia, in the UK, and in several other European countries, including Belgium, occupational pension funds are required to disclose any policies they adopt for SRI (Peeters, 2011). In the United States and in Canada, mutual funds must disclose their proxy voting policies and voting records. Some industry initiatives for transparency have also been applied to SRI, like Global Reporting Initiative (GRI) [13] and Carbon Disclosure Project [14] . However, under such transparency regulations FIs may simply choose not to include ESG issues in their investments, as long as they disclose this choice. In Belgium, for instance, the regulation demonstrated to have zero impact in encouraging SRI practice, and very limited improvement in transparency was noticed (Peeters, 2011). In practice, their reports reveal very little about the methodology used in SRI implementation and rarely demonstrate the level of transparency and participation they require of the corporations that constitute their portfolio (Fair Pensions, 2006 in Richardson, 2009).

Another less common type of SRI governance can be found in normative standards, which provide substantive principles for investment practices. Examples of this are pension funds of some countries, like France, New Zealand, Norway and Sweden, which are obliged to adopt responsible and ethical

[13] See: www.globalreporting.org

[14] See: www.cdproject.net

investment approaches (Richardson, 2009). Some states, more seldom, have created regulations to ban certain investments, as it is the case of Belgium, where there is a prohibition on financing companies that produce, distribute, or are somehow connected to cluster bombs (Swaegers, 2010).

Another form of establishing standards in SRI are voluntary normative regimes, of which UN-backed Principles for Responsible Investment (PRI) have gained great attention in the SRI community. PRI proposes six core principles for SRI, each of them followed by a set of "possible actions". Although PRI is heavily subscribed, it is considered rather as a primary set of principles, due to its voluntary nature and lack of major changes expected from their signatories. The principles do not require any demonstration of social and environmental protection from their signatories. The tools at hand to ensure compliance are equally an issue, as signatories are not required to report publicly on their compliance with the principles (Richardson, 2009).

Other policy instruments have also been introduced by some governments in order to stimulate SRI. In the Netherlands, for example, tax compensations are granted to private investors investing in green institutions(Scholtens, 2011). In Australia and Canada corporate governance reforms were introduced to facilitate shareholder advocacy. Few developing countries, however, have introduced policy measures to incentivize SRI (Richardson, 2009).

2.3.9 – Challenges Facing SRI

In the academic literature dedicated to SRI, we can encounter a wide variety of drawbacks in the system. Some of them are issues impeding the development of the SRI market, for instance the lack of a definitional consensus and lack of professional expertise for the promotion of SRI. Other problems are related to the way SRI is implemented. Some strategies consider ESG issues to a very limited extent, which hinders SRI from making a real contribution to sustainable development.

The inexistence of a definitional consensus for SRI as discussed earlier in this study[15] is for many authors a critical point of the model (Herringer et al., 2009;

[15] See section 2.3.2

Schepers & Sethi, 2003; Sparkes & Cowton, 2004). Considering that SRI is rather a matter of voluntary choice than regulatory compulsion, a diversity of approaches of SRI can be encountered now among different markets and even within a single market. This diversity is a reflection of investors' different values in regard to the relative importance of social, environmental and economic considerations (Mackenzie, 1998; Sparkes, 2001).

Defining an investment as ethical is not so palpable since the concept of ethics is subjective by itself and it is not clear how much ethics should depend on universal ethical codes or how much it should depend on individuals' personal values and moral conducts to the social good (Hellsten & Mallin, 2006). Richardson (2009) exemplifies this issue through the argumentation given by a parliamentarian from Ireland when rejecting an amendment to require the National Pension Reserve Fund to invest ethically: "[a] major difficulty in deciding on ethical investment policy is where to draw the line in defining the parameters of the policy, given that there will inevitably be different opinions and intense debates on what constitutes ethical and socially responsible investment" (Parliament of Ireland & Select Committee on Finance and, 2006, p.5 cited in Richardson, 2009).

Sandberg et al. (2008), present two main reasons for which lack of standardization is considered problematic by some authors. The first one is that, from a scientific point of view it is hard to describe, understand and evaluate SRI. And the second one is related to the goal of "*mainstreaming*" SRI. Without a clear definition for SRI it is hard to introduce and explain its concerns and criteria to mainstream investors, and it is even harder to estimate the current size of the SRI market size (Schepers & Sethi, 2003). As we can see from the overview of SRI in the global scene[16], assets taking in consideration ESG issues represent currently a share of 21.8 percent of the total assets in the global market. And the most popular SRI strategies used worldwide are "Negative/Exclusionary screening", followed by "ESG integration" and "Shareholder engagement" (GSIA, 2013). It is, however, hard to tell what is behind these numbers and names, since there is no definitional standardization for strategies.

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[16] See section 2.3.6

However, in the same study made by Sandberg et al. (2008), the authors suggest that a conceptual standardization for SRI is not essential, and not even desirable. They proclaim instead that researchers should be more open for discussion in order to look for consensus, rather than expect a consensus from the movement. And in order to mainstream SRI, the authors defend an integration of SRI-like concerns in mainstream investment using the conventional financial language, without sticking to the SRI jargon.

For Richardson (2008) the main problem resulting from the lack of standardization in SRI is that FIs often market the concept indiscriminately and much of the financing under the name SRI hardly contributes to sustainable development. Richardson (2009) affirms that if in its origins SRI was purely motivated by ethics, since its renaissance in the financial markets in the late 1990s this ethical posture has unfortunately been forgotten by the actors in the investment chain. According to him, so called responsible investors increasingly justify their case for taking in account environmental and social issues in their financial decisions in the premise that it will increase their returns, whereas the objective of creating a positive social and environmental impact tends to be forgotten. ESG issues most likely get to the attention of investors when they present any perceived "*financial materiality*", which means posing tangible financial risks or lucrative investment opportunities.

This approach of investment, to which Richardson (2008) refers as *business case SRI,* on one hand contributes for the popularity of SRI practices. On the other hand it risks becoming business-as-usual, reducing SRI's capacity of leveraging effective change for environmental and social sustainability. The financial materiality of ESG issues is a relative measure, and what is material to the environment and society may not be material for a company. For example an environmental disaster priced at $1 billion might be considered immaterial for a multi-billion corporation, in spite of the enormous damage it may have caused to the environment. From the principles of *business case SRI*, this kind of events tend to be overlooked (Richardson, 2008).

Next to this, short-sighted financial motivation of investors is also one of the main obstacles to make SRI an effective contribution to sustainable development. First of all, investors consider short-term returns much more important than long-term. Companies have, for example, greater incentive to boost short-term earnings than to invest in sustainable practices such as greenhouse gas emission reductions. This sort of action which aims to adapt to environmental challenges like climate change are too long-term to be considered in the investor's normal time horizon. Second, investors tend to overlook low probability events - such as environmental catastrophes - in their calculations of investment returns. Even though cases like BP's Deepwater Horizon Gulf of Mexico are proof that such disasters do occur and have significant relevance to investors. Third, the value of intangible assets which are decisive for companies' long-term returns such as goodwill and human capital are hard to identify from the investors view (PRI, 2012a).

Seen that a great part of investors ignore the benefits of SRI on the long-term, in order to better promote it, it is essential for SRI providers to have a differentiated workforce, composed of employees who combine both financial skills and ESG knowledge (Herringer et al., 2009; Schrader, 2006). However, according to some authors, it does not appear to be a reality. Governing boards of pension trusts, investment funds and banks typically have the same financial background and commonly lack the expertise on ESG issues and do not have a deep understanding of modern social and environmental challenges (Gribben & Olsen, 2006; Richardson, 2008).

Another criticism from some authors is the limited extent to which some SRI strategies contribute to sustainability. One of those strategies is the integration of ESG issues in investment based solely in their financial materiality, as previously discussed in this section. And another approach which is often criticized is the exclusionary screening of assets, which intends to "punish" companies engaged in harmful activities by withholding investment (Hawken, 2004). According to GSIA (2013) "Negative or Exclusionary screening" is the most widely applied SRI strategy, corresponding to 60 percent of the total SRI assets globally. Hawken (2004) condemns such an approach because of the broad criteria applied in the exclusions, which allows virtually any publicly held company to be included in SRI funds. One controversial example given in his study was the inclusion of "Exxon Mobil", widely known by its poor environmental records, in a fund called Global Eco Growth Fund, which only screens on environmental impact.

From the point of view of de Colle and York (2009), excluding assets using product-based criteria, as it is mostly done in SRI, cannot effectively encourage companies to improve their CSR. The authors defend that "to effectively engage with companies, one must first become an active stakeholder: silence does not pay" (p.88). Furthermore, another flaw related to "Exclusionary screening" methodology is the fact that it cannot be felt by companies unless it is disinvested by a very significant share of investors. Heinkel et al., (2001) affirm that in order to increase socially responsibility of companies the number of invested shares needs to diminish so that the increase in their cost of capital exceeds their cost of reforming (i.e. a polluting firm cleaning up its activities). They find that roughly 25 percent of responsible investors are needed to boycott a firm into making them more responsible. Despite their growth, SRI assets account for a very small percentage of the register of any company, and therefore are not capable of creating any material impact on companies' operations. Moreover, even if SRI funds accounted for a significant share of equity markets, effects would just last in the absence of conventional investors who are willing to provide substitute capital to the firm (Haigh & Hazelton, 2004)

2.4 – Conclusions

SRI is a term used to designate investment approaches which take into account ESG factors in investment decisions, in order to generate long-term sustainable returns as well as sustainable economic, social and environmental systems (Eurosif, 2012; PRI, 2012a; RIAA, 2011; US SIF, 2012b). A standard definition for SRI does not exist though. The field of SRI has been marked by heterogeneity, probably due to cultural and ideological differences between different stakeholders in different countries and regions; and differences in the market setting in which SRI actors operate (Sandberg et al., 2008).

Approaches for SRI are found under different names according to the proponent institution. But basically, the most common types of approaches are the screening of assets based on negative or positive criteria, shareholder activism and impact investment or community development (Eurosif, 2012; US SIF, 2012a). From these strategies, "Negative" or "Exclusionary screen" is the most widely applied, accounting for about 60 percent of SRI funds.

The large majority of SRI investors are institutional and, probably as a result of this, most assets allocated to SRI are bonds, followed by equity (Eurosif, 2012). Regulation is one of the factors pushing institutional investors to apply ESG issues to their portfolios, but there is also evidence that they choose for SRI as a more prudent form of investing. This means that they take in account the *financial materiality* of ESG issues, or in other words, the intrinsic risks and opportunities of ESG factors (UNEPFI & AMWG, 2006). This sort of motivation is named *business case SRI* by Richardson (2008).

Differently from this, there are investors who try to reflect their values or principles in their investments (Domini, 2001), seeking to improve corporate social and environmental behavior by switching the criteria of capital allocation. In this case, ESG criteria are a priority in the investment, whereas in *business case SRI* the integration of ESG criteria is rather a means for profit optimization.

An important issue for the development and quality of SRI is the legal framework in which it is inserted. For instance, legal initiatives in some countries require pension funds to report on SRI policies which they adopt (Swaegers, 2010; Richardson, 2009; Richardson, 2008). Such policy has been adopted in Belgium, for example, but showed to have insignificant impact (Peeters, 2011). Some countries sought to oblige their pension funds to adopt ethical investment approaches (Richardson, 2009) and some, more seldom, have banned certain controversial investments completely, as it is the case of Belgium regarding cluster bombs (Swaegers, 2010). In the Netherlands, tax compensations are granted to SRI investors (Scholtens, 2011) and in Australia and Canada shareholder advocacy was facilitated by regulation (Richardson, 2009).

Besides such authoritative norms, there are still voluntary normative regimes, from which PRI is the main example. However it is considered as basic in terms of recommendations and it lacks compliance mechanisms (Richardson, 2009). As we could perceive, no country has yet sought to settle minimal requirements for SRI by means of regulation, so the definition of SRI varies according to the different institutions. There are divergent opinions in regard to the importance of it. While some see it as problematic as it limits the research, the estimations of market and its mainstreaming, others defend that a standard definition is not necessary and not even desirable. ESG issues could be integrated in investment without sticking to the SRI jargon (Sandberg et al., 2008). The critic to this, is that SRI risks becoming business as usual and lose its capacity of leveraging change (Richardson, 2009).

Another challenge in SRI is the difficulty of investors to perceive the long-term advantages of it, as they are mostly focused on short term financial returns (PRI, 2012a). For this reason, promotion efforts are paramount for the development of an SRI market. However, FIs do not always have a well prepared workforce for this (Herringer et al., 2009; Gribben & Olsen, 2006; Schrader, 2006). Finally, there are critics to the main strategy used in SRI – "Negative/Exclusionary screening" – both for its broad criteria, often "too inclusive" (Hawken, 2004) as for its incapacity to affect companies (de Colle & York, 2009; Haigh & Hazelton, 2004; Heinkel et al., 2001).

Chapter 3 – Methodology

The objective of this work is to explore how SRI can have an impact on sustainability through the companies that are part of SRI funds. The definitional scope of SRI used in this study is that of the modern SRI, meaning investment approaches which take in consideration not only the financial aspects of the investment, but also its ESG implications (Louche & Lydemberg, 2006). We have opted to explore the problem at hand by doing a qualitative case study research. According to Yin (1994, p.13), "a case study is an empirical inquiry that investigates a contemporary phenomenon within its real life context, especially when the boundaries between phenomenon and context are not clearly evident." Given the type of question this study intends to answer, and the type of phenomenon taken under analysis, the qualitative case study research appeared to be the most suitable methodology to be applied.

A case study's has the advantage of providing an in-depth understanding of the actors involved, interactions between them, their feelings and behaviours. As such, it can support the development of historical perspectives and assure high internal validity, which means that the observed phenomena genuinely represent the reality (Gagnon, 2010; Woodside, 2010). Yin (1994) also states that in case studies are useful when the investigator has little or no possibility to control the events, which further supports our choice for this methodology.

In order to gain a deep understanding of the current situation of SRI at local and global level, the study started with a thorough literature review about aspects of interest for the research. The sources used were mostly articles from scientific journals, books, reports from associations involved in SRI and information from the websites of these associations. The literature review provided us a good overview of the approaches currently applied in SRI, the associations which are playing an important role in the development of SRI market and the share of this market in relation to the broader universe of investments. It also gave us good insights about the motivations of the actors in the financial value chain triggered by SRI and which were the legal initiatives taken in the field so far. Still through the literature review we could perceive flaws in SRI which might be impeding its effectiveness in contributing to sustainable development.

Following the single case embedded design proposed by Yin (1994), where multiple units of analysis are used, we have conducted an exploratory research by means of qualitative semi-structured interviews (Saunders, Lewis, & Thornhill, 2009) with a diverse group of stakeholders in SRI. This group of stakeholders included researchers, specialists from rating agencies, a member of an advisory board for SRI in a bank, a specialist from a bank, an employee of an institution specialized in microfinance and two specialists from associations involved (see **Error! Reference source not found.**).

In total, nine interviews were held, with ten different respondents, of which a test interview was conducted to ensure a good preparation for the remaining ones. One interview was held with two interviewees at once, namely with a representative from the Belgian Asset Managers Association (BEAMA) and a representative from the Belgian Financial Sector Federation (Febelfin). From those nine interviews, six were held face-to-face, two by phone and one via e-mail. Except for the last one, all interviews were recorded and transcribed. A summary was then compiled with all the key points that emerged from the interview, as suggested by Saunders et al. (2009). Subsequently, qualitative data analysis was used to analyse the data found in the transcripts. The respondents' answers were compared and color-coded according to concept or group, in order to aid the analysis by searching for differences, commonalities and trends (Strauss & Corbin, 1998) (see example in Annex 4).

Once the information from the interviews was processed, it was combined with the literature review to ground and benchmark the collected findings. After this, sound conclusions could be formed regarding some of the questions whereas some showed to require further investigation. These findings are provided in detail in the next chapter, and suggestions of further research are provided in the final conclusions of the study.

The interviewees were questioned about the perceivable motivations of investors, corporations and FIs participating in SRI, about the characteristics and limitations of SRI in promoting sustainable development and possible solutions for those (see questionnaire in Annex 3).

Although the information presented in the literature review is not restricted to the situation of SRI in Belgium, but rather in the global scenario, it is important to highlight that all the interviews were conducted in Belgium, and tend, therefore, to reflect characteristics of the Belgian market.

Chapter 4 – Findings

4.1 – Introduction

In this section we report the findings that resulted from the interviews, benchmarked against related academic literature. We have divided the chapter in sub-chapters according to different topics studied, in order to facilitate its reading and comprehension. Each sub-chapter is also divided in sections where we address different aspects of a topic. The first sub-chapter discusses the motivations of three main stakeholders in the investment chain – the corporations, the FIs and the investors. In the second sub-chapter we analyse if SRI has an effective capacity of promoting sustainable behaviour in firms. For this analysis we address crucial matters such as the level of expertise in ESG issues from professionals in FIs, the quality of SRI products available in the market, and how transparency is ensured to investors. In the third sub-chapter we comment what are the drawbacks that SRI faces in its purpose of encouraging sustainable behaviour of companies. In the forth sub-chapter we present then some insights for the improvement of SRI as a process. A partial conclusion is found at the end of each sub-chapter.

4.2 – Motivations in SRI

As this study intends to investigate how effective SRI can be in promoting sustainability in the financial value chain, we believed a primary question to address was what kind of motivations lead its different actors to engage in SRI. The actors on whom we focus in this case are companies included in SRI portfolios, financial institutions managing those portfolios and SRI investors. Hellsten & Mallin (2006) propose in their study that more theoretical and empirical investigation should be done on the motivations of players involved in SRI. Some of the questions raised by them were whether SRI is motivated by a serious commitment to promote sustainable development or if it is purely market rhetoric, as also defended by Richardson (2008, 2009). Are those actors genuinely motivated to use SRI as a means to promote change towards sustainability? In the next three subsections we respectively discuss the motivations that lead corporations, financial institutions and investors to take part in SRI.

4.2.1 – Corporations' Motivations in Participating in SRI

Companies do not actively choose to be included in SRI funds. They are selected by rating agencies (Hebb & Wójcik, 2005) or internally by FIs which provide SRI funds (Bayot et al., 2009). However, there are reasons for which they may see it as a benefit, thus motivating them to be selected. When the interviewees were questioned about this, the first answer was, nearly by unanimity, that most of the companies are interested in building a good image or reputation towards customers and investors.

After a series of corporate governance scandals, firms are increasingly demanded to demonstrate sound management and social awareness. Thus, companies in general have a strategic desire of maintaining or acquiring a positive reputation within their institutional environment (Wright & Rwabizambuga, 2006). This adds value to a brand and sets the firm in a favorable position in relation to its competitors, by increasing customer loyalty and allowing them to sell products at a higher price (Hebb & Wójcik, 2005; Nguyen & Leblanc, 2001; Wright & Rwabizambuga, 2006). Furthermore, firms with a good reputation benefit from greater access to capital markets and are exposed to less scrutiny in public hearings and approval processes, which in turn reduces cost overruns on firms' projects and interest litigation expenses (Wright & Rwabizambuga, 2006). Besides increasing financial performance of a firm, Schnietz and Epstein (2005) still affirm that a socially responsible reputation protects firms from financial losses during a corporate crisis.

For those firms that have understood the value of a socially responsible reputation, having their shares in SRI funds is "almost a certification to show that they are a good company", said a researcher in an interview. More specifically, corporations are interested in some SRI instruments, from which the most important are the *sustainability indexes*. "Some companies are very eager to get into those indexes and do everything to be awarded", said the director of Forum Ethibel, an agency which provides a sustainability index. The SRI advisor from KBC states that "not disclosing information about ESG issues can become bad publicity for a company". "Going into sustainability indexes is a way show that they answered the questions from rating agencies, which may indicate that they are transparent in their business", he continued.

Hebb and Wójcik (2005) affirm that many companies react to the reputational threat of exclusion from sustainable indexes by both raising standards and providing greater transparency of corporate responsibility. Fowler and Hope (2007) find anecdotal evidence on companies' websites and press releases that some corporations value inclusion in indexes such as Down Jones Sustainability Index (DJSI) and FTSE4Good. In their study the authors still mention an interview with an executive from FTSE in which he reports an increasing number of companies requesting detailed information on how to gain admission to the FTSE4Good index.

In a study done by Robinson, Kleffner and Bertels (2011), the authors found that the inclusion in the DJSI resulted in a increase in firms' share price and, conversely, they found that firms' value suffer a temporary decrease after being removed from that index. The grounded relationship between reputation and firms' value represents thus a good reason for which firms might be interested in being part of SRI indexes.

A second reason pointed out by the interviewees on the companies' motivations was the fact that some of them have a real ESG strategy. "Although it is not possible to generalize, there are some cases of companies who specifically profile themselves towards SRI investors and they even use CSR and sustainability management as a *hook* to get SRI investors", affirmed the representative from Eurosif. The reason why they do so, he explained, "is that SRI investors tend to be more focused on long term value. So there is a better balance between how the company and its investors' perspectives are managed. Companies tend to be managed for a timeframe of three, five, ten years or more and SRI investors perceive value on that".

The same respondent yet reported having heard from consultants that some companies partially measure their success by looking in their shareholder composition and the greater the number of SRI investors, the greater they perceive their success to be. He highlights that probably not many companies have an understanding of what SRI investors can mean to the company in terms of value. But some pioneers are realizing that this is an interesting group of investors who are possibly more aligned with the long term value creation of the company.

A third reason why companies may be interested in SRI which was mentioned by some respondents is to increase their access to capital in the financial markets. Although, all the respondents that mentioned this reason acknowledged that it has just a minimal importance if compared to reputation reasons. "If after a corporate scandal, some major size institutional investors decide to disinvest in a company, then they also have a problem with their liquidity, but still, the reputation impact stays bigger than the financial impact" exemplified the representatives from BEAMA and Febelfin.

The argument that liquidity is not the main benefit for companies taking part in SRI is supported by the ideas of Scholtens (2006), who affirms that the stock market hardly provides new finance to firms, and has therefore a limited impact on them. Furthermore, according to Heinkel et al. (2001) and Haigh and Hazelton (2004) the still small percentage of SRI investors in relation to neutral investors is not enough to create any effect on firm's cost of capital or the direction of corporations.

4.2.2 – Financial Institutions Motivations in Providing SRI Products

When interviewees were questioned about motivations for financial institutions to provide SRI products all of them made clear that it is not possible to make generalizations, as there are many types of financial institutions with different strategies and that the same is valid for companies and investors. However we did perceive a great consistence between the answers, which allowed us to trace categories of motivations.

The most mentioned reason for providing SRI products by FIs, as also presented by Eurosif (2012), was to attend to clients' demand, particularly from institutional clients. Consistently with the ideas of Jeucken (2012, p.84), some interviewees explained that there is a small but growing group of investors for which "financial return alone is not enough", or who understand the need to incorporate ESG issues in financial decisions. There is a market for SRI and, therefore, FIs need to satisfy this market and indeed regard this as an interesting business opportunity.

One of the interviewees, however, mentioned this reason, but with a reservation. According to him "the SRI market is supply driven. So it does not really come from the consumers. They sympathize with SRI ideas, but they do not go to the bank and ask for it". In any case, there was a significant consensus among the answers that product diversification is an important driver for the supply of SRI products, be it to attract a broader clientele or to satisfy current clients. The opportunities that arise from the offer of SRI products were described by another respondent as "surfing the green economy wave". "Every big actor now has at least one or two funds that they call SRI, but I am not sure it is part of their beliefs, it is more a question of serving different types of clients" she explained. Jeucken (2012, p.83) also comments this product diversification as "offering each customer a choice in the extent to which their savings or investment behavior is sustainable."

Another reason that was brought up during some of the interviews is that there is a minority of the financial institutions who offer SRI products for ideological or normative reasons, which means that they have a consistent ESG strategy, in which they believe and which is part of their values. Such institutions are those which have been doing this since the beginning, they said, rather than joining the movement for opportunistic reasons. For them, promoting sustainability in finance is "part of their DNA", to use the words of an interviewee. Herringer et al. (2009) also acknowledge both cases as reasons for offering SRI products - the investment philosophy of the institution or efforts to remain competitive and taking advantage of a specific investment mandate.

According to Jeucken (2012), activities like SRI can also have an image-making potential, and the same was said by a great part of the interviewees. Banks have been heavily criticized in recent years, especially after the financial crisis, so one of the ways they can try to improve their image is by providing sustainable financial products. Furthermore, some interviewees stated that, as a consequence of the financial crisis, some banks have understood that the incorporation of non-financial risks and opportunities is the right way to manage money.

Companies might be subjected to regulatory, reputational and litigation risks of environmental and social causes. If such risks are overlooked in the composition of a portfolio, it might have implications for the share price of the company and thereby for the performance of the fund, or even for investors' returns (Mulder, 2007). Following the precepts of SRI, as suggested by Simpson (2012), is an attempt to bring safety and soundness to the financial system. This is done by bringing order to the chaos and avoiding undesirable outcomes of modern capital markets' instability, caused by short-term focus and incapacity to set adequate pricing for important externalities, such as environmental damages. Some financial institutions became more aware of that after the financial crisis and even apply some SRI guidelines to all of its investments, respondents mentioned.

The growing importance of ESG issues in financial management was exemplified by the SRI advisor for KBC. "We (the external advisory board for SRI) used to be an island in the bank. We were part of the asset management department, with very few members and sporadic meetings. But then 2008 came and there was the big financial crisis. KBC was one of the victims. Now they are recovering and since last year we have moved in the hierarchy of the bank. It has become a much larger department, reporting directly to the CEO, not only advising for SRI investments, but also for CSR within the bank. So the bank itself wants to improve its CSR, ESG, etc. The president of the board of directors now participates in our meetings, because there is a feeling that the value of ethics has previously been underestimated. Many blame the financial crisis to irresponsible bankers and a lack of ethics, which is exactly what they are trying to improve".

4.2.3 – Investors' Motivations for Investing in SRI

"Investors have a unique kind of power: Their beliefs can shape markets. If they believe something is true, and invest as if it were, then it often becomes so." Those are the words used to introduce the report "Show Me The Money" from UNEPFI and AMWG (2006, p.6). If this premise is right, and if investors believe they can change companies' behaviour through their investments, then there would be higher chances that SRI would create impact on corporations' sustainable performance. Following this assumption we have interrogated the interviewees on what would be the main motivations of investors while opting for SRI.

Regarding this, again it is important to distinguish different types of investors and we start by making a difference between the motivations of institutional investors and retail investors. For both groups interviewees did point out a motivation of promoting change through SRI, but it does not appear to be the main reason for none of them. The interviewees who mentioned this kind of motivation affirmed that it comes from a small group of investors. As the research director from Eurosif explained, "they are referred to as social investors or impact investors and they will invest in projects that are specifically designed to create environmental and social impact, which means, to solve some sort of challenge, or to correct some sort of imbalance in social and environmental regulations. In many cases they are willing to sacrifice profits in order to do this, as long as there is some measurable social and environmental impact."

The SRI specialist from BNP Paribas Investment Partners mentioned as an example of this kind of investment a fund called "Aqua", offered by that institution. "It invests in the water market in the developing countries. Investors know that this investment provides water to some places of the world where it is a scarce resource. So they know that they are doing something good, somehow, and that they are involved in something concrete and nice in purpose".

According to the representative from Eurosif those are normally retail investors. Nonetheless, he says, institutional investors are increasingly becoming interested in this kind of investment too. As he explained, it is important for them to show that they have at least a small part of their portfolio, for example two percent, that is specifically designed to mitigate environmental and social challenges. Reports from Eurosif, US SIF, and GSIA, as presented previously in this study, also referred to impact investors as a small group, but in ascension, which gives a sign of increasing interest from investors in accessing social and environmental impact.

Regarding the main motivation of retail investors, the answers were consistent in saying that they do it for conscience reasons. It means that "SRI investors do not want to put their money in things they consider as wrong or they want to promote companies acting positively" said the representative from Forum Ethibel. "They do not want to invest in weapons, for example. They do not want their money to be used to produces mines, antipersonnel mines and cluster bombs. It eases their ideas", exemplified the SRI advisor from KBC. The representative from Eurosif, at his turn explained "those investors have a sort of moral and ethical objectives, or their decision can be leaded by public health, for example, not investing in tobacco companies because there are public externalities around it that will have negative impact on the society."

Those moral and ethical objectives are also pointed out by Lewis & Mackenzie (2000) and McLachlan & Gardner (2004). As Lewis & Mackenzie (2000) state in their study, the accumulation of wealth is a moral and psychological question for many or even all of us. As such, SRI is a way of applying investors' principles to their financial decision, just like they do for other activities in their lives. Or, in other words, those investors want to invest their money "in a manner that is more closely aligned with their personal values and priorities" (Schueth, 2003, p.190). They are sometimes referred to in the modern media as "feel good investors" (Michelson et al., 2004; Schueth, 2003). However they do not apply SRI for the totality of their investments (Lewis & Mackenzie, 2000).

The representative from Réseau Financement Alternatif (RFA) made also a point that SRI can be driven by the "*green wave*" of the moment. "Green is fashionable, thinking of the environment is fashionable, and being socially concerned is also fashionable" she stated. "Although I think the *green wave* for financial institutions is being used to get more clients, on the investment side I see it as something more sincere", she explained. Lewis & Mackenzie (2000) have made a similar point their study, where they found that there is persistence among some SRI investors even if they have lower returns than through conventional investment. This persistence, in the opinion of the authors cannot be seen as a mere fashionable or faddish behaviour in the market-place.

Applying ethical values to a portfolio can also be the case for some institutional investors. Examples of it are government and private sector funds, such as the Norwegian Government Pension Fund, the French Fonds de Réserve pour les Retraites, Storebrand Life Insurance and US and UK Ethical funds. Such funds apply ethical values to their portfolios regardless of the financial performance thereof (UNEPFI & AMWG, 2006).

In the case of institutional investors, however, the main reason for integrating ESG issues in their financial decision seems to be "simply to make more money" as stated by (UNEPFI & AMWG, 2006, p.4). Institutional investors increasingly recognize the benefits of ethical investment (Hellsten & Mallin, 2006). As the representative from Forum Ethibel affirmed, "even if they are not '*super green*', they are very conscious about reputation and risk thereof, also about accidents and extra costs, etc. So they know for very precise financial reasons why non-financial issues are important." The researcher from RFA in accordance to this said that "in the long term there are fewer risks in SRI. Maybe because of the financial crises people are more cautious about their investments and want to have other guaranties on the top of financial criteria."

The representative from Eurosif added to this reasoning, that the management of risks and opportunities from ESG can also be combined with ethical and social objectives. "If you manage the risks, then you looking for avoiding companies like 'BP', which has many issues about environmental, health and safety management. Or you are looking for opportunities in either changing consumption patterns (people are consuming more sustainable goods and services), or looking how engaging with populations affected can impact your investments", he exemplified.

The financial benefits of the integration of ESG issues in the investment valuation process, especially in a long-term perspective, are strongly argued by UNEP FI, which has released many reports on the topic. For example, in the report "Show Me The Money" (UNEPFI & AMWG, 2006) an argument given for this is that unpleasant surprises are what investors dislike the most, and, by looking at corporate environmental and social performance investors can have an extra measure to evaluate how well-managed enterprises are. Well-managed companies value opportunities in the day-to-day management of ESG factors and normally do not abuse the planet resources, do not unfairly exploit their employees, suppliers or their communities. As such, investors who evaluate a company from this perspective tend to be more prepared for events that surprise the inattentive.

A point made by a great part of the interviewees, and that is important to enhance here, is that there is growing evidence that the financial performance of SRI is not significantly different from that of conventional funds, as also found by Kreander et al. (2005). Without defending this statement here, as this is not the purpose of this work, what we would like to highlight is the fact that, except for a minority who is willing to invest in SRI funds even making losses (Lewis & Mackenzie, 2000), the majority of SRI investors just do so if they have nothing to lose. In other words, regardless of the motivations of investors, as they are provided with evidence that financial returns from SRI are not significantly different from those of conventional funds they have no reason for not doing it.

Another question brought up in the interviews which is partially related to the motivations of investors, was the reason why SRI has not reached the retail market with the same success as it has had within the institutional market. For this question we had different answers that in part overlap, as them all relate in some degree with the level of information that the two groups of investors have.

According to the answers of the respondents, the greatest problem in this case seems to be insufficient marketing efforts from FIs in promoting SRI, together with difficulties in communicating it to investors. One of the researchers interviewed affirmed that "retail investors are not aware of SRI, because financial institutions do not promote the products and do little communication within the bank". The SRI advisor for KBC affirmed that this is a real problem faced by the SRI advisory board in that institution. The advisory board insist that SRI products should be better promoted, but the product marketing department is reluctant in doing it. "They say that there is no demand from the market, the local consumers are not interested, they never ask for it. So they are not offering the product. They do not see why they should promote it" he reported.

Whereas most of the interviewees advocated that SRI market is supply driven and that it is the role of FIs promoting it and developing its market, the representatives from BEAMA and Febelfin were contrary to this statement. "FIs are giving a lot of commercial room for SRI, there are various sustainable financial products that can be sold, now it is up to retail clients to buy them", they defended. "Some banks are more proactive than others, but what we hear even from the most proactive banks is that the demand is not so large", they continued. "There is indeed room for improvement, and the products could be more marketed, but it is certainly not the case that they are not marketed. Now there was a little decline in the investment market including sustainable products, but two or 3 years ago they were better sold than the traditional investment products", they concluded.

The representative from BNP Investment Partners agreed that improvements can be done. To this respect he said: "This is the beginning. It has been ten years since BNP Paribas started to develop SRI. We want to target the institutional investors first to promote the strategies and then the retail. I think it is in process. We know that not all of the retail investors are aware of that, we have a lot of work to do in marketing, in promotion, etc".

The development of the retail market for SRI, as we can infer, demands special efforts. And the reason for this, as we could equally conclude from the interviews, is the difficulty in communicating or explaining SRI to the public. "Financial institutions face a challenge on how to explain it to the clients in a simple way", said a researcher. The representative from Eurosif further supported this statement by saying: "In SRI we use a lot of special terminology; people do not always understand them. And there is no unified SRI definition in Europe and globally. It is a complicated concept to talk about".

The challenge regarding terminology of SRI has been extensively discussed in academic literature (Sandberg et al., 2008; Simpson, 2012; Sparkes & Cowton, 2004). As stated by Simpson (2012, p.102) "The alphabet soup of shorthand in this arena – ESG, RI, SRI – reflects the proposition that current arrangements do not lead to optimal outcomes". This statement is further legitimated by the findings of the Global Sustainable Investment Review 2012 (GSIA, 2013), according to which the United States have a more well developed retail market for SRI if compared with most of the other regions analysed. This success, in turn is attributed to the lack of fragmentation in terms of legislation and language, which aids the communication and marketing of SRI.

Due to this lack of information, institutional investors and retail investors perceive SRI in different ways. Institutional investors, as discussed previously in this section, understand better the benefits of the incorporation of ESG issues in investment decision, whereas retail investors remain sceptical about it. "Institutional investors are more aware of how fast the market moves, they want to react fast. And they know that SRI is a new trend and it is really important as a strategy, so they want to be in this market too", said the representative of BNP Investment Partners to this respect.

The representatives from BEAMA and Febelfin added to this the reasoning that "sustainability is also more spread among institutional investors. They are more familiar with CSR because they as a company may practice CSR themselves, they do research and they are more professional as investors, they think on a longer term. They can better evaluate the financial returns from SRI and they know that in the longer term SRI pays off, even because you have fewer risks." On the top of that, the timeframe for which institutional investors aim is different from that of retail investors, "especially pension funds and insurance companies have twenty, thirty or even fifty years perspective, and in that time frame ESG matters", explained the research director from Eurosif.

"Retail investors, on the other hand, often think that SRI is something that costs in performance", continued the same respondent. This opinion was shared with the majority of the interviewees. "If you offer a SRI product and a traditional one to retail investors and you say you do not know which one gives more return, they go for the traditional one, because they associate SRI with low returns", affirmed the representative of Febelfin.

The SRI advisor for KBC gave an example of why SRI still has this stigma, at least in Belgium: "In this country everyone thinks that SRI does not give the same return as normal products. And this is because in the beginning we had in Belgium what we called Krekelsparen – a savings account that gave less return than a normal saving account. The difference went to philanthropy, charities, and good causes. It was the first SRI product, and it had great publicity, people knew about that, and they knew the return was smaller and this is still in the market. So people make an association between this and SRI".

Finally, another reason why institutional investors may adhere to SRI more often than individual investors is the fact that they may face regulations pushing them to include ESG criteria in their investments. "They are facing external pressure from the media, NGOs and so forth", explained a researcher. The researcher from RFA in a similar reasoning said that "institutional investors also have a role to play in promoting ESG. If we think that many of them are public institutions, they should in a way show the example, whereas retail investors do not have the same pressure, they are not checked, not audited." An example of legislation targeting the institutional investors is the case of the Employee Savings Plans (ESPs) in France, which need to include at least one "fonds solidaires", typical French funds which include ten percent of impact investments and ninety percent of equity or bonds assets managed under SRI approaches (Eurosif, 2012).

4.2.4 – Conclusions

Seemingly, the main reason why corporations might have interest in being selected for SRI funds is to build a positive image to investors and customers, especially through the admission in sustainability indexes. There are proved positive correlations between a good reputation and the financial performance of a firm, which might be a good incentive to them (Hebb & Wójcik, 2005; Nguyen & Leblanc, 2001; Wright & Rwabizambuga, 2006). Other possible interests for firms are aligning their management strategy (for those which have a real ESG strategy) with investors' perspectives, as SRI investors are normally more focused on long-term value. And another reason of minor importance and very contested (Haigh & Hazelton, 2004; Heinkel et al., 2001; Scholtens, 2006), is the increasing of access to capital in the financial markets.

FIs, in turn, seem to be mostly led by the need to satisfy clients' demand or by the opportunity to broaden their clientele by serving a new type of customer (Jeucken, 2012). This, evidently, is not true for all FIs, as there is a minority which has a consistent ESG strategy, and for which the promotion of sustainability through finance is part of their philosophy (Herringer et al., 2009). For many banks, on the other hand, the offer of sustainable financial products is a consequence of the recent financial crisis. So like other companies, they felt the need of improving their image through the offer of SRI. And some have understood that they should manage money in a more cautious way (Simpson, 2012).

The motivations among investors also vary largely, as they are not a homogeneous group. If we talk about retail investors, the main motivation seems to be aligning their investment approach with their principles and moral. For this they are sometimes willing to giving up higher financial returns (Lewis & Mackenzie, 2000; McLachlan & Gardner, 2004). This can be the case for a few institutional investors as well, but for this group the main motivation seems to making investments in a more prudent way by paying attention in the financial materiality of ESG issues, as they tend to value long-term financial returns more than retail investors (UNEPFI & AMWG, 2006). There is still, a small group of investors, mainly retail, that does look for creating impact through their investments, by investing in projects specifically designed for solving environmental and social problems. This group has been growing at a fast rate, which shows the appetite of investors for measurable environmental and social profit (Eurosif, 2012).

Institutional investors constitute the large majority of the demand for SRI and we have tried to understand the reasons for this. We find that the unbalance between the sizes of retail and institutional markets for SRI is in great part related with the level of information that each one of them accesses. Due to their professional character, institutional investors are more aware of trends and recognize the benefits of the integration of ESG issues in their investments. Furthermore, they sometimes face regulations that induce them to do so (Eurosif, 2012). Retail investors, on the other hand, are not always aware of such trends and are often skeptical about the financial returns of SRI. For the development of the retail market, there is a need of more marketing efforts. Especially due to the variety of terminologies and lack of definitional standards, communication is an essential element.

4.3 – Effectiveness of SRI in Promoting Sustainability

The effectiveness of SRI as a tool for promoting sustainability depends on a series of aspects involved in its practice. First of all, in order to create an effect that can be felt on corporations, the number of SRI assets under management needs to increase (Haigh & Hazelton, 2004), and the development of the retail market would be a great step in this direction (Schrader, 2006). For the promotion of SRI among a greater number of investors, FIs offering these products should have a workforce not only well-educated in financial aspects of investment but also in ESG factors inherent to it (Herringer et al., 2009). Other important aspects influencing the effectiveness of SRI are the consistency in methodologies among different FIs and transparency policies that properly inform the investors about these methodologies and how or why a given company may be part of a portfolio (Dunfee, 2003; Michelson et al., 2004). And finally, but not less important is how SRI activity is supported by governments through legislations.

In order to have an overview on the situation of SRI in regard to those aspects, and thus getting insights on how effective it can be in changing companies sustainable behaviour, we have posed related questions to the respondents, whose answers are presented and discussed below.

4.3.1 – Financial Skills and ESG Knowledge Coming Together

Financial Institutions providing SRI products need to have a differentiated human capital. Financial skills and ESG knowledge are difficult to come by. Nonetheless, the combination of them is essential both for the management of SRI assets as to the promotion of sustainable financial products (Herringer et al., 2009; Schrader, 2006). According to Richardson (2008) though, the financial sector still lacks competence and expertise to integrate ESG issues in financial decision. Thus we have asked interviewees about how this issue can be perceived at this moment and the answers in general demonstrated that the efforts in combining these two types of expertise is something currently in process, especially at asset management level.

The representative from Forum Ethibel said that the level of preparation for integrating ESG issues in financial analysis varies according to the institution. “Some FIs are very well equipped and doing it very well and some others do it very poorly”. But asset managers increasingly recognize the importance of it, so more and more they are learning about ESG issues and their integration in financial analysis, as most of the interviewees answered.

The representative from RFA reported that it is becoming more common that asset management firms disseminate ESG data among all the departments instead of keeping it in the ambit of the SRI department, and that even Management Information System (MIS) has been put into place to aid this. In terms of internal promotion, the representative from BNP Paribas Investment Partners related that at that institution many workshops are promoted with local agencies, such as private bankers, directors and retail agencies. He still affirmed that all the employees are aware of SRI, even if they have different degrees of involvement.

Contrarily to this, other interviewees stated that at retail level employees still often lack expertise in SRI and ESG matters. Some of them mentioned cases of research in Belgium and in other countries using “mystery shopping” for SRI, where it was found that retail investment advisors are not enough familiar with those topics, as they provided very limited and inaccurate information to customers interested in SRI. In a study realized in Germany, Schrader (2006) reported that no advisor proactively showed the initiative of informing customers about SRI funds and some even falsely denied their existence.

While discussing this topic, some of the interviewees brought up an interesting issue: The fact that asset managers are gaining knowledge on ESG issues and their importance for investment does not necessarily mean that they will make high quality funds in terms of sustainability. One of the researchers made the following reflection: "What I hesitate about is: Can it be combined? My fear is that ESG criteria would be transformed to fit the financial models, rather than trying to change the models, diminishing the importance of ESG. It would be a complete failure from SRI."

In accordance to this statement, the representative from Forum Ethibel said that incorporation of ESG issues in financial analysis purely driven by performance is currently making the model to downgrade. He reported: "Some of our clients have left us to enter in their own models, and they have chosen for a real material approach, where you have 70 or 80 percent of selectivity in a sector, so you have every kind of company in a fund. They make good stories about those funds, sometimes very well documented".

The point of view of these interviewees is well aligned with the concept of *business case SRI*, extensively described and discussed by Richardson (2008, 2009). This author, just like some of our interviewees, considers that the integration of ESG issues in investment analysis just driven by the materiality of those, does not clearly differ from ordinary investment, and cannot bring great advancement towards sustainability. He enhances this with the ideas of Christoph Butz and Jean Laville: "Financial professionals and mainstream investors are now willing to take sustainability issues into account if (but only if) they can be reasonably assumed to influence the bottom line. On the other hand, by adopting the concept of financial materiality, the sustainable investment community is tacitly abandoning any aspiration to convey the global challenges of sustainability to the companies they invest in" (Butz & Laville, 2007 cited in Richardson, 2008 p.19).

4.3.2 – Quality of SRI Funds

In this part of the work we tried to investigate if the methodologies currently used in SRI funds can guarantee a good quality of those in terms of sustainability. In order to investigate it, we have posed questions regarding the minimal requirements for including a company in SRI funds, and what kinds of companies are included in those funds. Can they all be considered sustainable? What kind of proofs do they give of their good sustainable conduct? And further we have asked if, considering that SRI can bring comparable financial profits as conventional funds; can they really combine it with social profits?

When asked about what the minimal requirements are to include a company in a SRI fund, respondents where coherent in affirming that there are no standard minimal requirements for this at the moment, neither in Belgium, nor in Europe. In Belgium, however, the Law Mahoux can be considered as a basic requirement not only for SRI funds but to the totality of investments in the country. According to this law it is prohibited the direct and indirect financing of the manufacture, use and possession of antipersonnel mines and submunitions (Swaegers, 2010). Interviewees' opinions varied though, about the importance of standardization for minimal requirements in SRI. While some see the lack of it as a setback, some had the opinion that regulation should be avoided when it is not necessary, which presumably would be the case here.

Those who defend that there should be a minimal quality standard for SRI, argued that asset managers are mostly not strict enough in their criteria. "In the Belgian market for SRI you can find really everything: from very serious funds to those which are far from being sustainable", said the representative from RFA. Many examples were given of companies with unethical or unsustainable behavior which are found in SRI funds, among which "BP", known for its poor environmental records, "HSBC" which according to one of the interviewees is doing massive money laundry, "Total", which is violating human rights in Burma, "Veolia Environment", which violates human rights in Palestine and "RioTinto", which violates international environmental laws.

In the Belgian market, during many years, FIs have used the label from Forum Ethibel as a warranty for the quality of their sustainable funds. That institution, whose practice has been internationally recognized for its quality[17] was therefore in charge of defining the environmental, social and ethical criteria for selection of the companies, and also for controlling of the compliance with them. FIs who sought to be awarded with that label had therefore to respect the ethical criteria chosen by Ethibel (Bayot et al., 2009). Currently, as confirmed by the director of Forum Ethibel, FIs are following a trend of internalizing the process of selection of companies for SRI, which results in large variety of methodologies, many of which enhance the material aspect of ESG issues to the detriment of the real sustainable character of these. Furthermore, even if some FIs which still use the services from rating agencies for the selection of companies, there is no standardization between methodologies of rating agencies, which is also a drawback in the system (Gutiérrez-Nieto & Serrano-Cinca, 2007).

Some interviewees have given also examples of selection methodologies used in the Belgian SRI market whose sustainable character is questionable. "There is actually a fund on the Belgian market called '*China Sustainable*'. They invest in China and they took maybe 3 ESG criteria, but there is no clue about what the companies are doing. The same happens with thematic funds, for example '*New Energy Fund*'. They decide, for instance, that the company needs to have 25 percent of its turnover coming from renewable energy but the rest can come from anything. Then you find companies that even produce nuclear energy", said the representative of RFA. Another researcher also criticized the fact that some fund managers create a fund based only on "Negative screening" and call it SRI, or those who create "Best-in-class" funds using selectivity levels as low as the 75 percent best.

The representative from BNP Paribas Investment Partners affirmed in favor of this institution that they use as base for selection the principles established on

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[17] In 2001 the Swedish organization MISTRA mentioned Forum Ethibel as an example of "Best Practice" in regard to its research and advisory services in SRI. See: MISTRA, *Screening of Screening Companies*, 2001

the United Nations Global Compact (UN GC)[18], and further refine the selection through their own criteria, which ensures that they are selecting the best companies in terms of sustainability. In the opinion of RFA, however, it does not seem plausible to choose one specific convention to the detriment of the many others signed by Belgium (Bayot et al., 2009).

Taking this into account, the representative from RFA reported that this institution has developed a study in 2008 to define a proposition of legal norm for SRI methodology in Belgium. The proposition establishes three minimal requirements: the first is the negative screening of companies violating any convention signed by Belgium in terms of environmental law, human rights law, civil rights law, and governance or social law. The same is valid for states violating those rights consecrated by international conventions. The second requirement is appliance of positive screening whose criteria the asset manager is free to choose. And the third requirement is the provision of up to date and transparent information, audited by an independent organization, over the methodology and criteria used by the fund managers[19]. The director of Forum Ethibel defended that this is a very strong idea, because the government cannot influence investors in taking an ethical decision, but they can oblige them to respect the treaties that the country has signed. However, he said, corporations are too large to be controlled, which makes the law hard to be implemented.

Other interviewees expressed an opinion in disfavor of the implementation of such a law. According to those interviewees, there is no existent consensus on ideas such as ethics, sustainability or social responsibility, and it is not the intention of the financial sector to impose it to the investor. A general consensus, however, is that transparency in SRI should be enforced by means of legislation.

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[18] Set of 10 principles which voluntary signatory institutions should be committed to respect and promote within their strategies and operations. The principles refer to human rights, labor and anti-corruption, and are derived from the Universal Declaration of Human Rights, the International Labour Organization's Declaration on Fundamental Principles and Rights at Work, the Rio Declaration on Environment and Development and the United Nations Convention Against Corruption. See: http://www.unglobalcompact.org

[19] For more details see:

http://www.ecosocdoc.be/static/module/bibliographyDocument/document/001/234.pdf

The representative from Eurosif, advocated that "…]…focusing on reporting is what really works. Once you have to report on something, you have to think of it, and then it becomes part of your business practice".

Another initiative in the sense of establishing a methodology for SRI in the Belgian market are the recommendations provided by Febelfin[20] in cooperation with BEAMA. These recommendations, as the representatives of those institutions explained, are based on three pillars: the first are the minimal criteria for screening, based on the UN GC's principles and in the exclusion of companies and countries involved in the production and sale of weapons, anti-personnel mines, cluster submunition, and nuclear weapons. The second pillar is the accountability, which means that all the information about the fund components should be made available on the provider's website, and preferably audited by an independent specialized consultative body. The third pillar of this proposition is the freedom of choice of the investor. "He or she should be able to make an informed choice, according to his or her own beliefs. We will not as financial institutions decide for the client how he should interpret SRI, or ethical investing, etc", explained the interviewees.

This recommendation also provides a list of controversial activities, which includes nuclear energy, tobacco, alcohol, pornography, among others. "So if a fund includes companies or countries which are involved in what we listed as being controversial activities, it need to explain why this kind of activity can be still included in a sustainable product. There are good reasons to include nuclear energy, because there is also a link to the development of isotopes for medicine. But it needs to be made transparent to the retail client. Also the strategies need to clearly explained, if you follow one or several. Taking for example the '*best-in-class* method', it needs to be explained what is the percentage of the sector that is being selected".

At this part of the interview, we also asked if SRI funds only include companies that can be considered sustainable, and if they are companies which really integrate sustainability as part of their strategy. To this the great majority of the

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[20] For more details see:

http://www.bankingforsociety.be/sustainable-financial-products-recommendation respondents answered negatively. As discussed earlier in this section, there are a great number of examples of companies whose practices are questionable to compound those funds. We can use the words of one of the researchers to synthesize the ideas of the majority: "Most of the companies in SRI are '*gray*'. There is no organization which is only good or only bad. And SRI needs to be able to deal with such controversies, such dilemmas. Even because we do not know what that is: a sustainable and socially responsible company. We have to balance so many things when we think of it that makes it complicated. Furthermore, companies are so large. You just cannot control what is happening, and there are many of human beings involved, which means many mistakes".

Some of those companies have a real sustainability strategy, which integrates it to all the other functions and some have it as pure "window dressing". According to the director of Forum Ethibel there are many efforts to come to integrated reports, but very few that reach this goal. "We have seen an example of a very bright report of a company called 'Umicore', they are in the top hundred of the best sustainable companies in the United States. There you can see a real example of a company who has been thinking of everything, that has found the real motivations and really sees the value of integrating sustainability in the other functions of the company, and they show how it is related to financial performance".

The representative from BNP Paribas Investment Partners was one of the only ones who affirmed that all the companies in SRI are sustainable and socially responsible. However, he made a reservation to this, which is linked to the dilemmas just discussed. "Sometimes we have the 'Best-in-class' strategy and in this, for example, we take the car manufacturer sector. We are talking about cars, and they pollute. But then you select the companies that are doing their best to reduce that pollution or that have other positive initiative towards environment and society".

Assuming that the quality of SRI funds is also influenced by the source of information on which fund managers and rating agencies base themselves, we further questioned in the interviews about how reliable are those sources, in special CSR reports, which are the most used basis of information (Harte, Lewis, & Vogel, 1991). Respondents answered that indeed CSR reports are the most useful resource to rate a company for SRI. Those reports are voluntary though, and lack standardization, said one of the researchers interviewed.

According to Dunfee (2003) the reliability of CSR reports would be improved if they were audited by professional independent auditors. Nonetheless, just like methodologies and minimal requirements in SRI, the ways through which those reports are verified vary among fund managers and rating agencies. In the recommendations provided by Febelfin, fund managers are *strongly recommended* to have their sustainable products policy as a whole audited by an external auditor, but it remains as a voluntary initiative.

According to some interviewees, it does happen that CSR reports are monitored by one of "the big four"[21] auditors. "But what they do is checking the conformity of the documents with ISO 14000[22] environment certification. This is not really proving that this company is getting better. The ISO certification does not demand it. So there are very few report audits that can assure you that the company is getting better" affirmed the representative of Forum Ethibel.

Interviewees also mentioned that some rating agencies do on site visits to check information on CSR reports and talk to managers. Information from websites and external sources such as NGOs are also used. Some rating agencies may include in their evaluation the level of responsiveness to their questions from the companies, as it is the case of Vigeo, affirmed a researcher. She, affirmed, however, that a low level of responsiveness does not always impede a company from being part of SRI funds. "Sometimes a company discloses very little, but if it gives good financial returns it might be still included. Happens a lot in "best-in-class", because it depends on the sector, and some sectors in general provide more information than others".

4.3.3 – SRI and Transparency

Most of the interviewees defended that transparency is a key point for the effectiveness of SRI and should be enforced by means of legislation. In this work

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[21] KPMG, Delloite, Ernest & Young and PWC

[22] Set of criteria for environmental management system that can be also certified. See: http://www.iso.org/iso/home/standards/management-standards/iso14000.htm

we mean by transparency the disclosure of the portfolio holdings as well as methodology used by asset managers in the selection of investment. This in turn should specify which type of ESG issues are being taken into account in a certain financial product and to which extent they are taken into account.

What we could perceive is that disclosure in SRI is one of the various aspects of it that lack standardization. Fund managers have actually a diverse "*menu*" of transparency codes which they can follow to declare themselves compliant with SRI. Most of the proposed codes are industry initiatives such as PRI, UN GC, Global Initiative for Sustainability Ratings (GISR), Eurosif Code of Conduct and BEAMA Code of Conduct, this within Belgium.

Interviewees affirmed that from these codes, the Eurosif Code of Conduct is the most used among fund managers. It provides detailed requirements and guidelines on the disclosure of basic details about the fund management company and the funds, their ESG investment criteria, their use of ESG research process in the investments to build and maintain their portfolio, their approach to engagement and their voting policy (Peeters, 2011). The researcher from RFA affirmed that this code has the weakness of not having a verification mechanism, but it is certainly a good first step towards standardization. Besides that setback of the code of conduct, Peeters (2011) still points out a poor supply chain accountability, focused only on the fund manager, limited quality management considerations and scope restricted to the retail market.

One of the sources of information mentioned by some interviewees, where investors can find details on SRI funds, is the Key Investor Information Document (KIID), which sometimes provides information on ESG criteria. According to the representative from Eurosif a regulation proposal is passing through the European Parliament, according to which asset managers have to disclose in the KIID whether they consider ESG outcomes from their funds.

In fact, two similar laws already exist in Belgium, commented the director of Forum Ethibel. In 2003, a regulation was created to oblige pension systems to disclose whether they consider ESG aspects in their investments or not. It was a model first created in the United Kingdom, which was followed by several countries in Europe. In 2004, the model was also extended to Undertaking for Collective Investments (UCIs). By forcing pension funds and UCIs to consider the possibility of incorporating ESG issues in their investments, these transparency legislations aimed to encourage the adoption of SRI by those investors (Peeters, 2011; Swaegers, 2010).

However, in 2008 a study was assigned to Forum Ethibel by the Federal Public Planning Service, in order to evaluate the impact of such laws, and the result was that those regulations improved transparency to a small degree, but did not have any effect in stimulating SRI. The ineffectiveness of those laws, according to the study, was probably due to their open-end character. Since no benchmark or standard for SRI was provided, the laws lost their authority, being regarded as a "*soft laws*" (Peeters, 2011).

Some respondents mentioned yet a law proposal under discussion, which intends to set minimal requirements for SRI and working with "*black-lists*". This means that the companies considered the most harmful would be excluded from SRI portfolios. The director of Forum Ethibel defended that this is a solution, but with limited scope. "The positive side of it is that as an investor you know that at least the worst companies are excluded by law from your portfolio", he said. "But on the other hand it is not so simple to build such a '*black list*'. It takes years of research and engagement, as it is done by the Petroleum Fund of Norway".

Another SRI instrument which was referred by some interviewees as a good source of transparent information is the system of product labels, offered for example by Forum Ethibel in Belgium and Novethic in France. They can aid to diminish asymmetry of information and give a good indication of the quality of SRI funds to retail clients, as they provide distinct features such as external verification, disclosure of all portfolio holdings, specific quality management requirements, quality control and benchmarking for differentiated labels (Peeters, 2011).

Still in Belgium, retail clients searching for information on SRI products have the option of consulting the *lists of sustainable financial products* offered by BEAMA[23] and Febelfin[24]. The lists provide detailed information on financial products in the

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[23] See: http://www.beama.be/en/duurzame-icbs-en

[24] See: http://sustainableproducts.febelfin.be/Investment-Product

Belgian market which follow the Febelfin Recommendation, discussed in the previous section. For each product on the list, the retail client can find details on minimal criteria, sustainability strategies, underlying assets and accountability items such as the transparency code used and a webpage from the provider dedicated to the product.

4.3.4 – SRI: Improving Companies' CSR?

In this work we acknowledge that there are a myriad of interpretations for SRI with a multiple variety of goals. One of the most omnipresent ones, however, and maybe one of the most meaningful, is the goal of contributing to sustainable development by encouraging companies to improve their CSR and sustainable performance (de Colle & York, 2009). But to which extent has SRI been achieving this goal? Does it constitute a real stimulus for the improvement of firms' sustainable performance? We are aware of the subjectivity of this question, and we understand that deeper empirical research would be necessary to answer to it more consistently. Nevertheless, we sought to get already some insights on it, based on the impressions of the experts interviewed.

Respondents, in general, answered that this is hard to tell, as there are no studies yet from which to draw a conclusion. Furthermore, measuring the influence of SRI in companies is something problematic as SRI is only one of the many instruments or means to change the behaviour of companies. There are laws, consumer boycotts, pressure from environmental and social activist groups and fiscal stimuli, which are also efforts to improve firms' sustainable performance. If a company presents some improvement, it is impossible to tell how much of it is influenced by each of those instruments. In general, though, the respondents leaned to the scepticism that SRI has been exerting significant influence on companies. Some interviewees even highlighted that SRI can only be effective in combination with those other instruments, as "companies are not very impressed by SRI alone".

Some interviewees affirmed that there cases of SRI-oriented shareholder engagement which were successful in positively influencing the behaviour of companies. The representative from BNP Paribas Investment Partners affirmed that when a company is excluded from their portfolios they are normally open to negotiation. Some companies go to a watch list if they are open to discussion and asset managers think they are interesting. Some of them become SRI compliants after going to the watch list, by reducing their carbon emission or doing other efforts. "But very often it is hard to convince them. They do not really understand the advantages of sustainability", he said.

In an effort to find more information on this topic, we have found a study done by Sjöström (2008) where all the academic literature on shareholder engagement was reviewed. The author found that there are divergences between studies, but most of them tended towards a sceptical view on the effectiveness of shareholder activism, being it limited to modest and corporate-specific changes.

Unfortunately, cases of unsuccessful engagement with companies were easily exemplified. The SRI advisor for KBC reported a case related to "Total", a company in the oil industry: "We decided with the board o KBC that 'Total' would no longer be considered as a sustainable company, and would no longer be part of our SRI products. It was about violation of human rights in Burma. So we wrote a letter to the company to communicate that decision. They were very discontent. We had to go to the headquarters and explain to them why we had made that decision. So, on one hand they do listen, they are impressed by what we do. A small bank in Belgium was capable of getting their attention by excluding them from their lists, which shows some degree of impact. But on the other hand they did not do anything to change that situation".

The representative from Eurosif also reported a case involving "Chevron", which is being accused of infringing the rights of indigenous people in relation to certain projects in Ecuador. "Many investors in the US are pushing Chevron in order to manage this risk properly", he said. "And instead of trying to be constructive with investors they are pushing them back, saying that they do not really want to talk about it".

There is, however, some contradiction on interviewees' comments regarding failure of shareholder engagement. This is because on a another stage of the interviews, when asked about how SRI could be more effective in changing companies, a solution pointed by many of them was the increasing in shareholder engagement efforts. Studying in which conditions shareholder engagement can be effective is perhaps a topic within the domain of SRI that merits further empirical research.

Another of the SRI instruments which was mentioned by respondents as being possibly effective in influencing companies are the sustainability indexes. As mentioned previously in this work[25], these indexes are regarded as a powerful image building tool for firms. As the representative of Forum Ethibel stated, "by trying to get in those indexes they might step by step become more sustainable". As also explained previously, there are very good financial reasons for which firms might be interested on being admitted in those indexes. And even if the primary motivation for this stays financial, the fact that it encourages factual reporting and sustainable activities from companies might be regarded as a positive impact of sustainability indexes on them (Lior, 2013).

"The problem with this is that there are only a few *strong* sustainability indexes", warned the director of Forum Ethibel. Many of them use very low selectivity, and are more focused on the financial aspects of the investment than in the sustainability performance of the companies. Then he further supported his statement: "DJSI is a typical example. They look for sustainability opportunities in a very clever way. And they find some good investments. The problem is that it is poor in terms of selection and sustainability. And also if you go into the details of the investment criteria, they say that if they cannot get 50 percent of the market cap in one sector, they just quit the criteria and they go for the next good opportunity". Thus, even if SRI indexes might have an impact on firms, it may be limited by the quality of the index. Moreover only a tiny fraction of total AuM uses sustainability indexes, which further reduces their impact (Fowler & Hope, 2007).

The disinvestment campaigns done by the Petroleum Funds of Norway[26] were also an example given on the interviews of how SRI can impact companies for reputational reasons. The representatives from BEAMA and Febelfin further explained the implications of such campaigns: "Neutral regulators, pension funds and institutional investors have the potential of causing negative impact in a company. If some well-known institutional investors divests from a company, the message goes further than in the firm itself. Other companies and other

[25] See section 4.2.1

[26] Commented on section 4.3.3

investors see that message and may follow the same reasoning. Maybe the impact is on a longer term, they cannot expect that from one day to another a company will stop their controversial activities, but they might start to review their policies. The fact that a company is discontent about being excluded from SRI already shows it meant something for them. And in other decisions of the board of this company they will remember that. They will be more interested in the social impact of their decisions".

For such companies, SRI may be one of the causes for which they change their sustainability performance, but there are other firms, for which SRI is rather a consequence. The SRI advisor of KBC gave the example of "Colruyt", a chain of supermarkets: "They were already doing a lot in CSR. But that was part of their culture, their own ethics, and their beliefs. But they were not reporting on that, so our bank did not consider "Colruyt" eligible to SRI according to our methodology, because we were lacking information. Now they are in it and they provide information, but SRI was a consequence. They were not motivated by SRI, it is rather in their culture. And that is why I believe that in the long run there might be changes, but it is very difficult. Change needs to come from within the company. They need to believe in it".

4.3.5 – Conclusions

In order to further develop the market for SRI, the expertise in ESG issues of professionals providing it is a crucial element (Herringer et al., 2009; Schrader, 2006). We could conclude based on the interviews and literature that at asset management level there is an increasing recognition of the importance of ESG matters in financial analysis, as well as and increasing efforts to improve the understanding of it. At retail level, on the other hand, professionals are often unprepared to promote SRI, providing limited or inaccurate information to customers (Schrader, 2006).

The increasing understanding of asset manages on the relevance of ESG matters in financial analysis, does not imply that the sustainability quality of the SRI funds is improving though. Commentators have reported a tendency of internalization of the selection process for SRI funds by FIs. Often, asset managers use the same conventional models, adapting ESG issues to it, rather than creating new models truly founded on sustainable criteria.

For this reason, there are in the Belgian and international markets, funds whose sustainable quality is dubious, including companies well-known for their poor sustainable or socially responsible performance. This is not surprising though, as there are no standard minimal requirements for the practice of SRI, and not even a common definition for SRI. Each FIs or rating agency charges itself of elaborating its own methodology for SRI, which is many times based on voluntary conventions such as the UN GC (Bayot et al., 2009).

Many commentators argue that minimal requirements for SRI should be imposed by law, in order to improve the consistence of methodologies, its understanding and quality. However, many others defend that such imposition is not and necessary and even not desirable (Sandberg et al., 2008). For the later ones, SRI needs to reflect what ethics, sustainability and social responsibility are for each investor, and, being those concepts intrinsically subjective, it is not a task of the financial sector imposing it to investors. For those commentators, what really matters is a high level of transparency. Or, in other words, investors need to be able to make a well-informed decision, but based on their own principles.

Regarding transparency in SRI, there also problematic issues though. Starting by CSR reports, on which asset managers and rating agencies base themselves for screening of companies. Those reports are voluntary, lack standardization, and are not mandatorily audited by external professionals. Going to asset management level, disclosure is not less of an issue. There is a wide array of codes of conduct on which asset managers can base their disclosure policies, all of which come from voluntary industry initiatives and lack a system of verification. For this reason, the system of labels remains one of the best sources of information for investors on the quality, composition and methodology used in SRI funds.

Given the conditions above mentioned, if we then try to get a global picture of SRI, and look if it has been exerting some influence on companies, we tend to be rather skeptical. Some say that SRI can only be effective as a part of a whole set of initiatives, such as consumer boycott, legislations and NGOs' pressure. Examples of unsuccessful shareholder engagement with companies are also more numerous than the opposite (Sjöström, 2008). All in all, the greatest effect of SRI in companies seems to be neither a result of "punishment" by their exclusion from SRI portfolios, nor of shareholders' engagement, but simply the effect the SRI can have on their reputation, especially through sustainability indexes.

4.4 – Limitations of SRI in Promoting Sustainability

As we could perceive from the previous sections, SRI faces limitations in its mission of encouraging companies' CSR and sustainable performance. One of the most basic of these limitations is the unsubstantial size of the movement (Richardson, 2008). In this section we discuss what factors are hindering the growth of SRI, and consequently its impact on firms. Besides, we discuss other limitations of SRI, related to definitional fragmentation, to approaches used, and investors' attitude towards SRI.

4.4.1 – SRI Market Size: Still Unsubstantial

It is well agreed among various commentators in SRI, including the experts interviewed for this study that the movement needs to grow in order to create a real impact on companies. Some authors defend that a larger number of SRI investors would raise the cost of capital of companies excluded from SRI funds, forcing them to become more sustainable (Heinkel et al., 2001). Other authors argue that this theory is largely unfounded, even if the movement grows. But a larger number of SRI funds under management are still necessary to enforce the "voice" of SRI towards corporations and governments (Haigh & Hazelton, 2004).

Whatever statement is true, we can affirm that the movement needs to grow. In this study, we further defend that, even if SRI is unable to directly impact firms by altering their access to capital, it can impact them by affecting their image positively or negatively. According to our interviewees and many authors, corporations do value the inclusion in sustainability indexes (Fowler & Hope, 2007; Hebb & Wójcik, 2005; Robinson et al., 2011). Therefore we can assume that if a greater number of investors adhere to SRI, the visibility and awareness about those indexes will be increased as well as the efforts done by firms to the admission therein.

What is then hindering the growth of SRI? There is no absolute answer for this question, but rather an array of flaws in the "process" involved in its practice, as well as a reluctant attitude of stakeholders in the movement. In regard to the process of SRI, a first and important setback, emphatically mentioned by our interviewees and academics, is the multi-variety of definitions, methodologies, strategies, and codes of conduct among different providers or associations involved in the sector. Even before some of the interviews done for this work, it was common that the interviewees asked what was meant by SRI in this study. The question does not surprise, since both in the literature as in practice SRI can assume a wide variety of significations. Herringer et al. (2009), for example, encountered the same issue during his study.

As we previously discussed[27], such diversity might be a cause of confusion for investors, which makes development of SRI market even more of a challenge. According to many interviewees, a large amount of investors, especially individual ones, are not aware of the existence of SRI, and from those who are aware, many are skeptical about the financial viability of it. This, in turn shows that providers' endeavor in promoting SRI is still insufficient.

4.4.2 – Why Definition Matters

The inexistence of a standard definition for SRI not only hinders the growth of its market. Due to the lack of common sense in it, every provider is allowed to create and market SRI funds in the way they understand it or in the way that shows more opportune, very often a loose way (Richardson, 2008). An article in the Financité Magazine (June, 2013, p.4-9) extensively argues that SRI funds hardly differ from conventional funds. If we look, for example to a classic stock index, the CAC 40, and a SRI index, the ASPI Eurozone, 80 percent of the firms composing the indexes are exactly the same (Hernalsteen, 2012).

In the same article of that magazine we find an interview with Gaëtan Mortier, one of the best SRI analysts according to Thomson-Reuters. The content of the interview shows that, like some of our interviewees argued, SRI rhetoric is passing through a change to fit conventional financial models and now social and environmental criteria are let in second plan. Asset managers seek to have multi-sector portfolios to diminish risks, like this it is common to find a oil company in a SRI portfolio because it is the best of its sector, even if its department of renewable energy is responsible for less than 3 percent of its turnover (Cloot &

[27] See section 4.2.3

Roland, 2013). In section 4.3.2 various examples are given of companies which can be found in SRI funds whose social and ethical performance is questionable. Due to the permissiveness of SRI strategies such as "Best-in-class" and "Negative screening", the use of strategies separately makes SRI even more ineffective, said the representative of RFA.

Besides compromising the quality of SRI funds, this lack of standardization limits also the efficiency of shareholder representations. The SRI advisor for KBC exemplified this: "There are hundreds of banks and other institutions such as NGOs involved in SRI and there is no unified view on it. We are all writing to the same company, but as we are not "speaking the same language", what companies do is paying other companies to answer to all those letters. New firms have emerged to serve this issue, answering to questions very friendly, very politely, it's a new business. There is too much diversity, multi-variety SRI, that it cannot be effective".

As previously commented though, some other interviewees and authors[28] defend that standardization in SRI is not a necessity (Sandberg et al., 2008), as SRI needs to be able to reflect principles and values which are particular for each investor. Although we recognize the strength of this argument, there are some principles such as those recognized in human rights treaties that cannot be overlooked in an investment called "Socially Responsible Investment". In a study made by de Colle and York (2009, p.87) this idea was very well expressed: "If SRI funds are just individually tailored products, what is the justification to call such instruments SRI – *socially responsible investing*? If, for example, a particular individual investor requires, according to his personal values, to only invest in funds that exclude alcohol and include fire-arms, whose 'social' context are we talking about?"

4.4.3 – The Challenge of Proving Social Profits

One of the clear limitations of SRI is the lack of means to demonstrate to investors how much environmental and social profits they can generate through their investments. The prescription that SRI "promotes sustainable development"

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[28] See sections 2.3.9 and 4.3.2

is too vague to be meaningful both for investors and financiers. FIs need to be able to legitimate their SRI approaches internally, to their board of directors, and externally, to their beneficiaries. And institutional investors have the necessity to compare portfolio performance from different asset managers. Therefore, concrete formulae to quantify those values, as well as a simple way to demonstrate it become crucial to the improvement of SRI quality (Blanc, Cozic, & de Barochez, 2013; Richardson, 2008).

Many of the interviewees affirmed that the reason why individual investors decide to invest their extra money in microcredit funds or impact investing is because it is very clear what happens with the money in these cases. The director of Forum Ethibel further explained: "Most of microcredit funds are very transparent regarding the destination of the money. They publish every result they have with your investment. That is what people like. So I can imagine that if you could make such a transparent social return visible to investors in their SRI funds, for sure there would be an interest".

We have then asked to interviewees how can social and environmental benefits from SRI be accessed, and few were the examples of initiatives to solve this issue. Demonstrating environmental and social profits is still a challenge of the sector. "For the moment I have not heard of an asset manager that has come as far as doing that consistently, but this is something they are working at", said the representative of Eurosif.

The representative from BNP Paribas Investment Partners answered that this institution periodically releases extra-financial reports to fund managers and other clients, providing quantitative and qualitative information on the ESG characteristics of SRI portfolios. These include ESG ratings of the portfolio and characteristics of individual securities, performance indicators such carbon footprint, job creation and board independence, and an overview of the proxy voting activity during the past calendar year.

In the literature we find two types of metrics to quantify social and environmental performance, commented by Richardson (2009) namely social accounting and sustainability indicators. Social accounting seeks to provide means to quantify the collateral benefits (e.g. public infrastructure and environmental protection) and costs (e.g. harm to environmental resources) of economical activities (Mook, Quarter, & Richmond, 2007; Unerman, Bebbington, & O'Dwyer, 2010). This system of accounting differs from usual methodologies associated with the Generally Accepted Accounting Principles (GAAP) by concentrating on community and environmental impacts of firms' activities, rather than factors restrictedly linked to corporation financial health.

Even though social accounting is intended to price social welfare, rather than serving corporate business needs, its ability to improve SRI quality is questionable. It entails an idea of cost-benefit that does not necessarily ensure the integrity of environment and society, as these factors may be underweighted by seemingly more pressing values (Richardson, 2009). The danger of instrumental ecological calculations is exemplified by Birsch and Fielder (1994) through the "Ford Pinto" case in the 1970s, where a cost-benefit calculation determined that correcting a defective fuel system design in one of the companies' cars outweighed the expected litigations costs of deaths and/or injuries. The usefulness of social accounting, however, increases in the presence of certain economic policy instruments, such as taxes charged to polluting companies, which in turn would create costs to be considered in investment decisions. In this case, social accounting can be a valuable instrument to price cost of social and environmental behaviour and facilitate cost-effective solutions, but it stays incomplete as it does not encompass sustainable performance standards (Richardson, 2009).

According to (Richardson, 2009), for the purpose of measuring sustainable performance, more useful tools are the sustainability indicators. These tools were also mentioned by the representative of RFA, who referred to a study made by "Novethic". According to this study, ESG indicators are "a measurement of the real impact that portfolio companies have on their environment and stakeholders, in proportion to the investment made. This is a quantitative assessment measured in a concrete unit (e.g. tones of greenhouse gas emissions, numbers of jobs, etc.) carried out ex-post and based on data published by the companies, or estimates when such data are not available" (Blanc et al., 2013, p.2) . They can be useful in decision making processes by translating environmental, social, and economic data into performance standards (Richardson, 2009).

A large variety of sustainability indicators have been developed till the moment, from which "eco-footprint" is the most widely spread. In the extra-financial reports released by BNP Paribas Investment Partners, just mentioned above, we find examples of sustainability indicators too. Nonetheless, the reliability of sustainability indicators is compromised by the lack of consistent information released by companies and incoherence between the many methodologies proposed (Blanc et al., 2013; Richardson, 2009). Even though, Richardson (2009) defends that with further refinement sustainability indicators can provide the basis for portfolio selection, and even replace shareholder value as the main measure for corporate success.

Although new sustainability metrics have been developed for various scales of economic activities, indicators for FIs' portfolios as a whole have not yet been properly designed. The development of such indicators at portfolio level rather than simply at individual firm level is important in order to provide a more wide-ranging picture, consistent with universal investor thesis. To this respect, one innovative effort to measure an entire investment portfolio, mentioned by some interviewees, is Trucost's annual "carbon counts" survey. In this research UK investment funds have the carbon intensity of their portfolios (a seminal indicator of sustainability) measured and ranked. In 2007, 185 investment funds were evaluated and it was found that one quarter of SRI funds were more carbon-intensive than the benchmark (Trucost, 2007).

Such methodology, however, as most of the others found in the market, is based in one single indicator, and seen the complexity of some issues related to sustainability, we should be aware that neither sustainability indicators, nor social accounting can reflect social and environmental aspects of investment in its totality. Evaluation of fairness in the distribution of benefits and burdens of use of the environment are examples of how complex such issues can be. Whereas FIs may easily respond to discrete social problems, for instance by excluding from their portfolios firms that exploit child labour or practice racially discriminatory hiring, they can barely address social and economical inequalities inbuilt in a capitalist economy (Richardson, 2009).

4.4.4 – Investors' Attitude: a Key Matter

In a previous section[29], while discussing which factors motivate investors to choose for SRI, we found that institutional investors seek to incorporate risks and returns inherent to ESG issues in financial decision, otherwise they do it under pressure of regulation. Retail investors, in turn, would do it to promote social change or to "feel good" about their investments (Michelson et al., 2004; Schueth, 2003). According to our interviewees, the later seems to be the main motivation though, and it is one of the reasons why SRI cannot have a great impact on companies.

One of the researchers expressed this through the following words: "Do they really want to create change? Many do not. SRI is just to give them a good conscience. I really think they are very conservative in their approach. Investors are not bold enough. They do not push the companies. They do not look at the future of the companies but at their past performance". As mentioned in previous sections, "Negative or Exclusionary screening" is the most used SRI strategy worldwide, accounting for 60 percent of the SRI AuM. If on one hand such strategy serves to give a "clean conscience" to investors, on the other hand it is not designed or not able to promote change (Sparkes & Cowton, 2004).

As many interviewees explained, when investors look to a company's past performance or to its products and simply exclude it from a portfolio, the company itself remains uninformed. "Companies need to know what is happening. We have to give information about that. We need to publish which companies we consider to be 'good', which we consider 'bad'. We have to engage with them, we have to write letters, to participate in the general assembly and vote. Buying and selling stocks might be good for the conscience, but it will not promote CSR" said the SRI advisor for KBC.

In other words, interviewees and authors such as Sparkes and Cowton (2004) advocate that SRI without shareholder activism cannot bring any contribution to sustainable development. There are, however differences in the way such approach is taken by investors. In Europe, according to GSIA (2013) and Louche

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[29] Section referred: 4.2.3

& Lydemberg (2006) the main form of shareholder activism is trough direct dialogue or letter writing to companies. Sparkes and Cowton (2004) point out some criticism to this approach though. According to them, many NGOs condemn it for its "*behind the scenes*" character that makes it a useless and discrete exercise.

For those authors, activism through the filling of shareholder resolutions is a more effective approach, as resolutions are public documents and a form to exercise shareholder democracy provided with greater transparency and disclosure. Nevertheless, in the case of Europe, barriers to engagement and voting still exist and these issues are expected to be addressed by new legislative proposals (GSIA, 2013).

4.4.5 – Conclusions

To affect companies by influencing their access to capital, strengthen the "voice" of SRI and bring more attention to SRI within companies, or still, increase visibility of SRI indexes, the SRI movement must grow. One of the main factors hindering the growth of SRI is the multi-variety of interpretations and methodologies existing for it, which is cause of confusion for investors and calls for greater marketing efforts.

The variety of interpretations of SRI and the lack of standard minimal requirements still imposes a limit to the sustainable quality of SRI funds, as asset managers are free to create those based on their own interpretations or convenience. Besides, the diversity of visions in SRI weakens the power of shareholder activism, as they address different issues to the firms, instead of talking with "one voice" towards them.

In addition to these limitations, there is still a difficulty of legitimizing SRI towards boards of directors of the provider institutions as well as to interested investors. This is because SRI lacks of mechanisms to measure and prove its effects on companies. Some tools have already by developed by certain institutions, such as sustainability indicators. However they are mostly focused on only one or a few parameters such as tones of greenhouse gas emissions, and do not reflect a global picture of factors involved in sustainability. Moreover, the reliability of sustainability indicators is compromised by the lack of consistent information released by companies and incoherence between the many methodologies proposed (Blanc et al., 2013; Richardson, 2009).

Finally, another setback in SRI is the attitude of investors. What they basically do, according to our interviewees is looking at the past of the company or at its products and excluding it from a portfolio. This might appease one's conscience, but as the company remains uninformed it is more likely that it will not address the issues which motivated the investors to disinvest from it.

4.5 – Steps towards the improvement of SRI

During the literary study conducted for this work we could perceive a wide array of limitations to the growth and effectiveness of SRI, which we have confirmed during the interviews just presented in the past sub-chapter. Having those limitations in mind, we further questioned our interviewees about how to overcome those limitations. Answers had little variation, so we could synthesise them in three main issues: First, a series of regulatory reforms should be done, targeting firms, FIs and investors. Second, cooperation between stakeholders should be increased. And third, investors should adopt a more involved and active attitude. Below we discuss each of these issues in detail.

4.5.1 – Regulatory Reforms

Implementation of legal reforms was the most frequent answer from interviewees to our question on how to overcome limitations faced by SRI. Suitable laws and public policies will be decisive for improving the impact, extent and quality of SRI as well as mitigating numerous market institutional barriers to it (Richardson, 2008). We can illustrate this using the words of Hebb and Wójcik (2005): "While investors [30] provide the leverage for improved firm-level standards, nation states provide the muscle. Unlike voluntary corporate reporting mechanisms such as the Global Reporting Initiative (GRI), companies that do not comply with state regulation are in breach of law and subject to legal penalty". Interviewees suggested mainly legal reforms on corporate and FI levels. We present below possible reforms in those levels as well as at investors level.

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[30] Author's adaptation: The original text refers specifically to pension funds.

Present regulatory standards to promote SRI have a weakness of not implying an obligation on FIs to consider social and environmental impacts of their transactions. Nor does it permit affected third parties to implement their rights. There is a distinction between taking the interests of various parties into consideration and owing a duty to those parties. Under the current regulatory standards in general, FIs owe a duty solely to their beneficiaries and not to society as a whole. In this way, social and environmental issues are considered in investment portfolios to the measure that they present any *financial materiality* which is supposedly prudent to be taken into account. Global finance, which enables financiers to invest in markets with weak human rights and environmental standards, must be countered by sustainability standards embedded into financial markets, such as requirements to promote SRI (Richardson, 2009).

Reliance on existing environmental regulatory controls that target the "*front-line*" business such as mining and manufacturing firms do not suffice to raise social and environmental standards for many reasons. Targeting the financial sector through SRI could enforce the effectiveness of presently often ineffectual "*front-line*" regulatory controls, as companies passing the rigors of SRI standards should be easier to regulate at operational level. Financiers' strategic economic position can also be exploited by policy-makers to defeat traditional barriers to such regulation" (Richardson, 2009).

Obligations of FIs should be redefined along a spectrum of an ever-increasing exactitude (Richardson, 2007). In this context, Richardson proposes a series of reforms in fiduciary duties for SRI. An alternative in order to strengthen these duties would be the regulation on procedures to increase the chances that FIs would consider social and environmental impacts of their portfolios. For example, financiers should be required to not only make their SRI policies available – as required in some jurisdictions – but also their investment methodology and implementation efforts. Additionally, financiers' disclosures on SRI could be audited by third parties and deficiencies publicly revealed (Richardson, 2009; Swaegers, 2010). Despite of all the arguments against the regulation of a minimal norm for SRI, we defend that it should be implemented as it would ensure a minimal quality standard for SRI funds. An example is the model proposed by Bayot et al. (2009) for Belgium, which has as basis the respect for international treaties signed by the country.

Another possible improvement in legislation, although more invasive, would be the authorization of outside stakeholders to participate in financial institutions' governance, as representatives of particular social and environmental interests, or by requiring financiers to consult with third parties. Already in the Equator Principles[31], signatory banks are required to consult local communities which may be affected by the projects they plan on financing (Richardson, 2009). One reasoning for this type of reforms is the fact that governing boards of FIs do not always have a complete understanding on modern social and environmental challenges (Gribben & Olsen, 2006). Governing boards, which would include key representatives of stakeholders could be a means of democratically diversify the range of point of views that inform SRI policies and thereby reinforce social legitimacy of ethical investment decisions (Richardson, 2009).

There are, evidently, critics on such alternatives for regulatory reforms. Jensen (2000) affirms that the potential multitude of interests that financiers would need to consider would bring excessive complications to decision making. To this respect, Richardson (2009) proposes that a solution to accommodate stakeholders' voice would be the creation of external entities, such as national ethics council responsible. These could be a source of guidance for financiers on difficult ethical questions, avoiding trial and error. Such councils have been already established in Norway and Sweden in order to guide their public pension funds.

Continuing on the spectrum of possible reforms, regulation could prescribe sustainability indicators to effectively set fiduciary performance benchmarks. Indicators used could be carbon footprint of a portfolio or other broad indicator that would allow a more complete view of the environmental performance of a portfolio. This approach would not require accounting for social and

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[31] Equator Principles is a risk management framework, adopted by financial institutions, for determining, assessing and managing environmental and social risk in projects and is primarily intended to provide a minimum standard for due diligence to support responsible risk decision-making. See: http://www.equator-principles.com

environmental cost and benefits of investments. Instead, it would require that portfolios stick to prescribed sustainability benchmarks, whatever the methodology used. In order to reinforce such regulation, sanctions could be imposed to FIs that fail to meet the standards, including restrictions on future investment decisions or penalties to reflect social cost (Richardson, 2009).

Redefinition of fiduciary obligations, however, does not suffice to keep the ethical character of SRI. Another priority in terms of regulatory reforms is the improvement of quality of corporate environmental and social reporting. Having companies to report regularly and comprehensively is paramount for the generation of consistent information in which to base SRI decisions (Harte et al., 1991; Hebb & Wójcik, 2005). In the current SRI scenario, such information is certainly not enough to induce SRI if financial implications of corporate behavior cannot be demonstrated to financiers. On the other hand, without such information, financiers mandated to invest ethically would face enormous difficulties in choosing the most ethical firms (Richardson, 2009). In some jurisdictions corporate social and environmental reporting standards have already been determined by legislation, examples are the Netherlands, France, Sweden and Denmark, among various others (Eurosif, 2012; KPMG, 2011).

Further reforms should also be made in corporate governance in order to liberalize the use of shareholder resolutions (GSIA, 2013). Social investors sometimes count on shareholder advocacy as a tool to promote change in recalcitrant firms from within (Richardson, 2009), and it is, moreover one of the potentially powerful instruments by which financiers can try to influence companies' policies, when acting under the interest of institutional investors (Guercio & Hawkins, 1999). Nevertheless, in some jurisdictions shareholder activism still encounters significant barriers, such as restrictions on the type of matters that can be raised in a shareholder resolution and the rather passive culture of voting, nurtured by proxy contest rules (Sarra, 2003). Besides the liberalization of shareholder resolutions, investment institutions could be obliged to register their share votes, in order to stimulate them to formulate and manifest on all issues to be voted at shareholder meetings (Richardson, 2009).

Another field to be explored is that of the economic instruments such as pollution taxes and tradable emissions allowance. Such instruments can quantify positive and negative externalities of companies' activities for reflection in financial indicators such as earnings, competitiveness, and, ultimately share prices, among others. Attributing prices to externalities of firms, on turn, should influence the allocation of capital, setting polluters in competitive disadvantage (Richardson, 2009). An example of the influence of economic instruments in SRI is that of the Netherlands, where tax incentives to green project investments are granted, inducing about fifty percent of its investments in SRI (Scholtens, 2011).

"States must also get their own house in order" (Richardson, 2009, p.568). Public finance, such as public sector pension funds, plays a key role in promoting change towards sustainable development (Hess, 2007). States could monitor public capital to address crucial social and environmental issues, as it already happens, to some extent, in the national pension plans in Scandinavia and France, which are required to invest ethically and socially responsible (Eurosif, 2012). Still, by means of their central banks, governments could influence capital allocation by giving preferential treatment to those industries considered the most environmentally critical (Richardson, 2009).

4.5.2 – Cooperation between Stakeholders

Whereas there is a great divergence in opinions about the imposition of minimal requirements for SRI through legislation [32], there was a general acknowledgement among our interviewees that the diversity of definitions and approaches in SRI represents a limitation of the system in many ways. Firstly, it might hinder the development of its market: "Maybe if there was something more robust (a definition) it would be easier to communicate that to investors who are not necessarily interested in spending time trying to understand this concept" (Anders Nordhein, head of research at Eurosif). Secondly, it might compromise the sustainable quality of the funds: "If you go to different asset managers, they both claim they do SRI, but they do completely different things. Some take 80 percent of the reference index and they call it SRI. Some are very precise and go for a much stricter selection of 25 percent or 15 percent" (Herwig Peeters, director at Forum Ethibel). And thirdly, variety of approaches reduces the effectiveness of SRI in promoting corporate change: "There is too much

[32] See sections 4.3.2 and 4.4.2

diversity, multi-variety SRI, that it cannot be effective. Financial institutions should speak with 'one voice' towards companies" (Kurt Devooght, researcher and member of external advisory board for SRI at KBC).

Therefore, if a consensus in SRI cannot come from legal imposition, at least for the moment, it can only come through cooperation and coordinated action between institutions. Both fund managers and institutional investors need to join forces between themselves if effective change is to be created. Céline Louche, researcher in the domain of SRI used the following words to express this during her interview: "If SRI actors want to create a change, they need to cooperate to each other. Acting on their own they do not have the power for it. Investors do not have the truth (…) nobody does. Therefore it is important to increase dialogue".

Financial institutions need to be able to find common objectives, specific issues that must be addressed in "one language" if they want to be listened by firms. In the same way, institutional investors can enforce their voice by making common representations on environmental and social issues to firms. And still, if those investors act in concert to lobby governments to price externalities, their financial performance should be also enhanced, as the firms which SRI funds invest in would normally benefit from such pricing. An example of how coordinated action from investors can deliver efficient results is what happened during the Apartheid in South Africa. Attending to Mr. Nelson Mandela's request, investors removed their assets from companies practicing discrimination, forcing them to abandon these policies (Haigh & Hazelton, 2004).

There are indeed some steps that have been taken in order to create cooperation between institutions. Examples are voluntary pacts such as PRI, GRI, UN GC and regional membership associations such as Eurosif, US SIF and the various others presented previously in this work. However the variety of terminologies, methodologies and quality of products that can be found within and between markets shows that those initiatives have been failing to bring consensus to the sector to date. Very recently, the creation of GSIA has taken place, which is a global initiative of cooperation between regional associations. It is still to be seen if any advancement will come out from this new attempt.

4.5.3 – Activism Improvement

So far, there is a rather pessimistic prospect on how SRI can exert influence on companies. The most basic form of SRI - the exclusionary screening of assets - is deemed unlikely to alter firms' cost of capital, which would supposedly be the trump of SRI to promote corporate change (Haigh & Hazelton, 2004; Heinkel et al., 2001). Many of our interviewees stated that shareholder activism needs to be an intrinsic part of SRI, as it is probably the most efficient way of promoting sustainability through SRI. On the other hand, Haigh and Hazelton (2004) and Sjöström (2008) argue that attempts of shareholder engagement have been mostly unsuccessful to date.

Keeping in mind a critical point of view that shareholder activism might not bring changes in the desired proportions and time frame (O'Rourke, 2003; Sjöström, 2008) and that it might not be the best vehicle to change corporate behaviour, we still adopt a position in favour of such initiatives within the ambit of SRI. Even without providing immediate results, SRI resolutions from shareholders can work by alerting boards of directors of potential troubles lying ahead, increasing their attention and sense of caution to ESG issues. Furthermore, since institutional investors are increasingly adhering to SRI, more leverage is created on companies, pushing them to improve their CSR (Sparkes & Cowton, 2004).

Still, shareholder activism brings more visibility to CSR issues further than the environmental or sustainability department. It also offers access to campaigners to companies previously closed to them, and gives them the possibility of addressing CSR through engagement and building of trust. As such, CSR might be seen by companies as an opportunity rather than a threat as it becomes somehow voluntary (O'Rourke, 2003).

Nonetheless, shareholder activism depends on preparation, argumentation, following up with agendas, and many times conciliating agendas, which might be costly and time consuming, especially in relation with the results that might be achieved. Further, there are legal restrictions to its use, for example, limiting the extent of proposals to "ordinary business" (O'Rourke, 2003). Sparkes and Cowton (2004) also stress that the most successful cases of shareholder activism were result of coordinated actions between investors, which brings us back to the discussion of the previous section.

For what it seems, actors in SRI already have a clue of what should be done if effective change is to be created, using very basic terms they need to be proactive in the use of their rights and they need to act in concert. But then we come back to our first question: Are they really motivated to promote changes? Not according to our impressions.

4.5.4 – Conclusions

According to our interviewees, in order to improve SRI and make it more effective in changing corporations' sustainable performance, three main changes need to happen: legislation in the sector should be improved, stakeholders should cooperate between themselves and investors should be more engaged with companies they invest in.

There is a large set of suggestions given in the literature for legal reforms in SRI. The most urgent ones would be strengthening fiduciary duties of FIs so that they consider social and environmental impacts of their portfolios. Some requirements could be making SRI policies available, as well as investment methodology and implementation efforts. The reports could also be audited by a third party (Richardson, 2009; Swaegers, 2010). In spite of the divergent opinions about imposing a norm for SRI by law, we are in favor of such measure. SRI seeks to attend to interests which concern the society and environment in general. As such it should be addressed also within the political sphere. While we acknowledge that strictly restrictive policies would not succeed, we defend that at least international treaties signed by a country should be respected in SRI (Bayot et al., 2009).

At corporate level, reforms should require companies to report on environmental and social performance on a regular basis and following standards, as example of the Netherlands, France, Sweden and Denmark (Eurosif, 2012; KPMG, 2011; Richardson, 2009) and still reforms should be made to liberalize shareholder resolutions (Richardson, 2009). Instruments such as pollution taxes and tradable emissions allowance could also make a great contribution as they help pricing positive and negative externalities, setting polluters in disadvantage (Richardson, 2009). Taxation reforms can also stimulate the adoption of SRI by investors, as in the Netherlands, where tax advantages are granted to investors investing in green funds (Scholtens, 2011). In the case of public pension funds, SRI could be transformed in a requirement, as is happens in Scandinavia and France (Eurosif, 2012).

Finally, a change in attitude from stakeholders needs to take place if it is to transform SRI in an effective tool for sustainability. Shareholders need to become more active in the firms they own, and they need to do it in cooperation with others. Seen there is a great disagreement about what SRI is and many are against the imposition of one common definition, consensus should then be found through cooperation, so that investors and FIs speak to companies with "*one voice*". In the same way, SRI investors can "*join forces*" to lobby governments to price externalities of firms and liberalize shareholder resolutions. Furthermore, the cases in which shareholder engagement succeeded to date, where result of coordinated action between investors (Haigh & Hazelton, 2004). This should lead investors to revise their approach.

Chapter 5 – Conclusion

The objective of this study was to investigate if SRI really has the ability to have an impact on corporations, improving their sustainable performance. Our conclusion is that SRI may have the potential to have such an impact, but it does not yet have the ability to do so. We did not find in the literature, neither heard during the interviews any evidence that the motivations guiding stakeholders in SRI, or its conditions of quality and transparency, would be able to deliver any significant change at this point.

The most commonly used SRI strategy is the "negative or exclusionary screening" of assets (GSIA, 2013). The effectiveness of it in influencing companies' sustainable behavior is contested for different reasons. First, SRI funds account for such a small percentage of the register of most companies, that they are unlikely to affect their cost of capital if investors decide to disinvest in them (Haigh & Hazelton, 2004). Second, even if a large portion of the shares is disinvested from a company and raises its cost of capital, the effects would just last in the absence of alternative capital. Third, if the company is not informed, it is unlikely that they would look to SRI as a cause for the problem (de Colle & York, 2009; Haigh & Hazelton, 2004). And fourth, the criteria for exclusions tend to be so broad that they are considered "too inclusive". It suffices to say that companies like "BP", "Monsanto" and "Exxon Mobil" can be found in SRI funds. In other words, the change in capital allocation from common profitability criteria to real ESG criteria, on which SRI is founded, does not actually take place or is too unsubstantial (Hawken, 2004).

What we could perceive though, is that SRI can be a means for companies to enhance their reputation, especially through the admission in sustainability indexes. Considering that reputation is one of the most valuable intangible assets to companies, we infer that SRI is more likely to affect firms through their reputation than through access to capital. We therefore believe that if the number of AuM using sustainability indexes increase, these indexes will gain more visibility and therefore have more influence and impact on companies' sustainable behavior. However, the impact that such indexes can have depends on the methodology employed in their construction and on their performance (Fowler & Hope, 2007).

Looking at another level of the financial value chain – the financial institutions – the main motivation for offering SRI products seems to be an effort to remain competitive by diversifying products and taking advantage of the ascension of this new market (Herringer et al., 2009). Conley and Williams (2011) in their work refer to FIs as *potential sustainability regulators*. In spite of this potential, it is unlikely that they have been exerting such a role. For most of the FIs it is important to be in the market of SRI, which does not mean that there is a real will to promote sustainability. As a consequence, asset managers do not have a real concern in creating funds with a high sustainable quality. The necessity of creating profitable funds remains crucial, so what happens is rather a conversion of conventional funds into SRI by picking characteristics or projects of companies which "fit" in ESG criteria.

Interviewees did report that there is a growing interest from asset managers in integrating ESG criteria in financial analysis, especially since the recent financial crisis, in an effort to safeguard the financial system from further turbulences. This is, in turn, is due to the growing evidence of the *financial materiality* of ESG issues in the evaluation of risks and opportunities of investments, which Richardson (2008) refers to as *business case SRI*. However, in this case, ESG issues are taken into account *only* if they bring some *financial materiality*. The reason why it does not necessarily represent a progression in sustainable development is that some issues might have high materiality for the environment and society, but they are overlooked if they cannot be felt in finance (Butz & Laville, 2007 in Richardson, 2008).

However, it would not be fair to make generalizations by saying that all FIs have been misleading investors with their SRI products. There are indeed high quality SRI funds in the market too. The reason why quality varies so much between institutions is the lack of a common definition for SRI, as well as standard minimal requirements and methodology for fund creation. In other words, asset managers are free to create SRI funds according to their understanding of it, or in the way that seems most opportune.

Turning our attention to investors, we also find out diverse motivations. A great part of the retail SRI investors, like in the beginning of SRI, are driven by their ethical values (Domini, 2001), which means that they seek to exclude from their portfolios companies related to controversial products such as weapons, alcohol, tobacco, etc. Commentators criticize this passive attitude as it may appease investor's conscience, but it does not promote change. A small, yet increasingly larger, group of investors do have a real wish to improve environmental and social welfare. They often choose for impact investments, which are specifically designed to create measurable environmental or social impact. (Eurosif, 2012).

Institutional investors, are sometimes also guided by ethical values, and some countries' public pension funds even face legal requirements to adopt SRI (Eurosif, 2012). But in general, the first reason why they apply ESG issues to their portfolios is the concern about the *financial materiality* of those issues (UNEPFI & AMWG, 2006). As institutional investors are more professional in their investment approach, they are probably more aware of trends like SRI, which is probably the reason why they own the large majority of SRI assets (GSIA, 2013). Therefore, the development of the retail market for SRI will demand increasing marketing efforts from FIs, as for the moment studies have shown that professionals at retail level are often unprepared to promote SRI (Schrader, 2006).

A part of the challenge of developing the SRI market is communicating it in a comprehensible way to investors. The current variety of terminologies and approaches used between different institutions can only lead investors to confusion. We do not have knowledge of a country which has already sought to impose minimal requirements for SRI in order to standardize it and ensure a minimal quality. The same is valid for transparency requirements. FIs have a wide array of choices of recommendations and codes of conduct on which they can base their SRI policies, such as "Eurosif code of conduct" or PRI. But these are voluntary guidelines which lack compliance mechanisms (Richardson, 2009).

Besides all those limitations of SRI, another reason why we cannot say that it has been improving corporations' sustainable behavior is simply because its outcomes cannot be measured. To date, a few sustainability indicators for SRI have been developed for this purpose, but they normally focus on only one or a few parameters such as tons of greenhouse gas emissions, and do not reflect a global picture of factors included in sustainability. Moreover, the reliability of sustainability indicators is compromised by the lack of consistent information released by companies and incoherence between the many methodologies proposed (Blanc et al., 2013; Richardson, 2009).

How then could all those limitations be overcome? There is probably no single answer, but we suggest that changes strongly depend on the support of legislation and on the attitude of investors. Starting at corporate level, legislation should ensure regular and standardized extra-financial reporting which would aid benchmarking sustainable performance of companies and the quantification of environmental and social profits. At FI level, fiduciary duties should be strengthened so financiers would be forced to consider the environmental and social impacts of their activities. Furthermore, minimal requirements for SRI should be set, in order to protect investors from poorly defined SRI products. Many critics are opposed to norms for minimal requirements, as SRI should reflect the diversity of principles from investors. But on the other hand, SRI is founded on general interests of the society and environment and as such it should be treated as a political matter (Bayot et al., 2009).

It is possible that returns will be compromised if it is to ensure a high sustainable quality of SRI. And it is clear and understandable that investors do not want to lose money and will only choose for ethical products if they have good reasons to do so. In this case, a possible way to solve this unbalance and stimulate the SRI market would be through tax compensations for SRI investors, following the example of the Netherlands (Scholtens, 2011). Yet, public pension funds could be required to adopt SRI approaches in their investments, as it happens in France and in Scandinavia (Eurosif, 2012). Economic instruments such as pollution taxes and tradable emissions allowances for companies could also be used. These help the quantification of externalities, setting polluters in competitive disadvantage which would be reflected positively in the performance of SRI (Richardson, 2009).

Finally it is essential that investors become more actively involved and start using their ownership rights if they really intend to change corporate behavior. Acting in concert and speaking as “one voice” would even strengthen them in being heard by companies. The current lack of consensus in SRI results in isolated messages coming to companies and saying different things. A few cases of shareholder engagement have succeeded to date and they were all results of coordinated action between investors. This should be taken as an example that impacting companies is possible, but it requires more than buying and selling shares.

This study contributes to the research in the field of SRI by showing issues that will require increasing attention from financial institutions, investors and legislators if SRI is to be transformed in a tool for sustainability. Due to time constraints we have interviewed mostly "neutral" actors in SRI. So we did not hear the point of view of corporations and investors, which could be interesting to include in further studies. But as mentioned, we do not intend to find final concluding answers to our questions, rather advancing the discussion and highlighting points of interest.

We also suggest future research to focus on instruments of SRI which are deemed promising, such as sustainability indexes and shareholder engagement. For both cases it would be interesting to analyze the characteristics of best-practices and their impact. Regarding sustainability indexes in particular, further research could also examine the quality of these indexes and the steps taken by companies for the admission to them. The development of tools to measure the sustainable impact of SRI is also crucial and merits future research.

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Annexes

Annex 1 – Comparison of SRI strategies

Annex 2 – List of interviewees

Annex 3 – Questionnaire: Sustainability in the Financial Value Chain

Annex 4 – Color coded comparison of interview answers

Annex 1 – Comparison of SRI strategies

<table>
<tr><th>Eurosif</th><th>PRI</th><th>USSIF/ ASrIA</th><th>SIO</th><th>EFAMA</th><th>RIAA</th></tr>
<tr><td>Sustainability themed investment</td><td>ESG themed investment</td><td rowspan="4">Screening</td><td>Sustainability themed investment</td><td>Thematic approach</td><td>Thematic investment</td></tr>
<tr><td>Best-in-class investment selection</td><td>Positive screening and best-in-class</td><td rowspan="3">Screening</td><td>Best-in-class</td><td>Best-of-sector</td></tr>
<tr><td>Norms-based screening</td><td rowspan="2">ESG exclusions</td><td>Norms-based approach</td><td rowspan="2">Responsible investment screening</td></tr>
<tr><td>Exclusion of holdings from investment universe</td><td>Exclusions approach</td></tr>
<tr><td>Integration of ESG factors in financial analysis</td><td>ESG integration</td><td></td><td>Integration</td><td></td><td>ESG integration</td></tr>
<tr><td>Engagement and voting on sustainability matters</td><td>Engagement</td><td>Shareholder advocacy</td><td>Corporate Engagement and Shareholder action</td><td>Engagement (voting)</td><td>Shareholder activism - voting and resolutions / Engagement with companies on ESG issues</td></tr>
<tr><td>Impact investment</td><td></td><td>Community investment</td><td></td><td></td><td>Impact investment</td></tr>
</table>

Annex 2 – List of Interviewees

No.	Date	Institution	Interviewee	Designation	Comments
1	3/04/2013 (test interview)	PlaNet Finance Group	Jente Minne	Intern	International socially responsible group present in 88 countries whose mission is to tackle poverty by developing microfinance products and services. Website: http://www.planetfinancegroup.org
2	16/04/2013	Réseau Financement Alternatif	Annika Cayrol	Researcher	Not for profit organization promoting ethics and solidarity in the financial sector through initiatives in information, education, economic empowerment and government advice. Noticeably, RFA evaluates financial products according to their ethic and solidarity character. Website: http://www.financite.be
3	16/04/2013	Hogeschool-Universiteit Brussel(HUB) / KU Leuven	Lieve De Moor	Associated Professor of Finance	Develops extensive research in SRI, having published a diversity of journal articles and other working papers on the subject.
4	17/04/2013	Vlerick Business School	Céline Louche	Assistant Professor	Teaches and researches into the area of Corporate Social Responsibility (CSR). Her main research interest is the construction of the CSR field with a special focus on SRI and stakeholder processes.

5	18/04/2013	KBC Bank & Insurance	Kurt Devooght	Member of the External Advisory Board for SRI	KBC is a Belgian multi-channel bank offering the widest choice of SRI funds in Belgium. The external advisory board for SRI is a committee of Belgian professors helping KBC to control and select companies which are considered to be ethical or socially responsible to include in SRI funds. Website: www.kbc.com
6	19/04/2013	Belgian Financial Sector Federation (Febelfin)/ Belgian Asset Managers Association (BEAMA)	Tom Van Den Berghe/ Andy Vangenck	SRI & CSR Manager/ Officer Asset Management and Private Banking	The two associations work in partnership to provide recommendations followed by their members, offering sustainable products. Websites: www.febelfin.be | www.beama.be
7	19/04/2013	Forum Ethibel	Herwig Peeters	Director	Consultancy agency for CSR and SRI. The organization sets out European standards which are widely socially accepted. It provides a quality label for financial products and portfolio control, among various others services related to SRI. Website: www.forumethibel.org
8	17/05/2013	BNP Paribas Investment Partners	Loïc Gourgand	Product Marketing Specialist	International bank with focus in Belgium, where it is the second major actor in terms of SRI products offered. Website: www.bnpparibasfortis.be
9	05/06/2013	Eurosif	Anders Nordheim	Head of research	Pan-European network of institutional investors, financial service providers, academic institutes, research associations, trade unions and NGO's developing sustainability through European financial markets. Website: http://www.eurosif.org

Annex 3 – Questionnaire: Sustainability in the Financial Value Chain

Brief case description: Sustainable and Responsible Investment is a practice that arose as a means to conciliate investors' financial interests with the interests of society and the environment. However, the ability of SRI of creating a positive societal and environmental impact on the companies participating in it remains a question mark for academics studying the field. This work intends to study how the practice of SRI can impact on sustainability through the companies taking part in it.

Respondent	
Representing	
Designation	

Question 1 – What motivates corporations to participate in SRI?	
Question 2 – What motivates financial institutions (asset managers, investment banks) to offer SRI products?	
Question 3 – For what reasons are investors investing in SRI?	
Question 4 – Recent reports show that institutional investors are the major players in SRI. Why hasn't SRI reached retail investors with the same success?	

Question 5 – Investment managers working with SRI should combine both financial skills and ESG (Environmental, Social and Governance) skills in order to properly inform investors on how ESG matters can influence financial performance. Is this currently a reality?	
Question 6 – Are the minimal requirements that make a company eligible to participate in SRI strict enough to ensure that this is a sustainable company?	
Question 7 – How are companies participating in SRI monitored in terms of CSR/sustainability? (e.g. are they providing CSR reports? Are reports audited?)	
Question 8 – Is there a true <u>integration</u> of the sustainability function and financial function to be noticed in companies participating in SRI?	
Question 9 – Which are the transparency policies in force in Europe/Belgium currently? Are those policies respected? (i.e. regulations to ensure that the investment is directed to sustainable activities and not something else)	
Question 10 - Are <u>all</u> companies participating in SRI sustainable and socially responsible?	

Question 11 – Can SRI really align financial profit and social/environmental profit?	
Question 12 – To which extent are CSR practices from companies (e.g. measuring, integrating, reporting on sustainability) motivated by SRI?	
Question 13 - How can social returns from SRI be demonstrated to investors?	
Question 14 – What are the main limitations of SRI in promoting CSR?	
Question 15 – What would be the steps to overcome those limitations faced by SRI?	

Annex 4 – Example of Color Coded Comparison of Interview Answers

	A	B	C	D	E	F
1	Answers comparison	RFA	Forum Ethibel	PlaNet Finance	Prof. Céline Louche	Prof.Lieven De Moor
2	**Question 1** - For what reasons are companies participating in SRI?	Main: Image Greenwashing Real ESG strategy Promote ESG	Companies do not directly participate to SRI. They are involved into it by banks, by investors, asset managers or index builders. They are involved in CSR, or responsible business, but indirectly they are participating in SRI. And for what reasons they may like it: because they want to show that they are ok, that there are fewer risks involved in what they do... Not all of them do it, off course. Those that are interested, they understand that is important in terms of publicity, reputation, image, to show that they are aware of what is happening in the world, and that they have answered the questions. That is a very general reason. Specifically, they are very much interested in specific SRI instrument, from which the most important one is Sustainability indexes. Some of the companies are very eager to go into those indexes and they do everything to be awarded. And the indication from Ethibel, some of them know we are very demanding, we look in quite profundity, and we are more selective than others, so if they can come to our index (ESI) it is a big motivation.	There are several reasons: sometimes it's related with the thing they are doing, for example in micro-finance, companies are sustainable driven from the beginning and they start with donations but at a certain point it's not enough anymore and they need to issue shares. But basically for any company the intention is to attract more investments (more liquidity).	They don't always have the choice. Some of the screening agencies ask the company if they want to participate, but sometimes they are just screened by the agencies, for example Vigeo screens companies based on the information that they find on the web or they ask stakeholders. Now why companies may be happy to participate in those funds, there are actually many reasons, one of them is reputation, so SRI for them is almost a certification to show that they are a good company. They can also use this as a tool to provide them an assessment, I don't know to which extent. Providing benchmarking. It's not a company that can decide to participate, but the rating agencies. What can also happen is that the rating agency provides the benchmarking to the FI and then the asset manager decides to include companies or not.	•increased exposure to new investors •social interest of existing investors •image building to customers •financially interesting SRI opportunities
	Question 2 - For what reasons are financial institutions (asset managers, investment banks) participating in SRI?	Surf green economy wave fashion. Now every big actor has at least 1 or 2 funds that are called SRI, but I'm not sure they really believe on it I think it's more a question of diversity, and giving what the clients ask for) Client demand Portfolio diversity Promote ESG is real strategy (mostly the actors that have been doing SRI for a long time) Depends of the actor	A bit the same. There are opportunistic visions or there are really though reasons for them to do that. So FIs really believe it is necessary to include non-financial risks into their investment decisions. It's a pure question of risk rating, which is very important. This is an important driver internally. Externally they often sign for PRI (Principles for Responsible Investment). Or they want to offer these products because clients ask for that. But even that is not really sure, because SRI market is really supply driven. So it does not really come from the consumers. They sympathize with SRI ideas, but they do not go to the bank and ask for it. And then, off course, since the financial crisis, FIs try to have a better image, and that is one of the possibilities for them to have a better image. But here we are going down to the really well motivated banks/asset managers, who really know why they do it and they can show that there is a difference and that it's important to have this in mind.	For some institutions this is their business: to collect funds and invest just in Socially Responsible things (it's their market). Some other institutions want to get a broader clientele, not only hard investors, but also investors with other interests. Some other organizations are interested in having a better image.	It's important to understand that FI, companies, investors are not homogeneous groups: there are many different types of FIs, same goes for investors. But for financial institutions in general it's purely a business decision, to attract more clients or to satisfy clients (product diversification). For some of them it is also a reputation element. Banks are being criticized, so they want to show that they also care, they also doing something for the environmental and social issues. It could be also normative reasons, which means, they believe it's important to invest in certain companies and not in all companies. I cannot rank these motivations. It depends on the FI. If you think of Triodos, those normative approaches would be more important. Actually with Triodos there is a forth element for this question that is creating change in the financial sector and in companies. So there are two labels: if you take a bank like Fortis or Dexia Asset Management, the product element is very strong. Another possible element is influence of a person - a "champion" - who leads the project. But about the integration of SRI in the FI, I'm ot so sure, I think they	•diversification opportunities •demand for SRI products from customers •financially interesting SRI opportunities (ex. carbon certificates in exchange for water investments, KBC)