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Can Sustainable Investing Save the World?

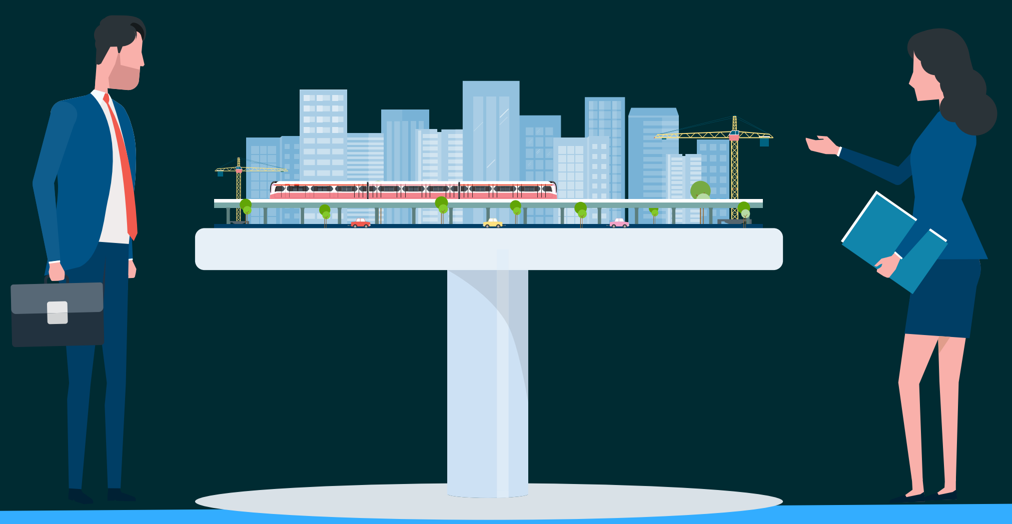
Probably not alone.
(We'll come back to this 😉)

But it can have an Impact. What's that, you ask?

Impact is the change in a certain parameter of interest - for example, clean drinking water - that is caused by your activities.

Impact is thus defined as the difference between status quo and additional performance resulting from an action.

We distinguish **company impact**, which is the effect the company has on the world, and **investor impact**, which is the change in this impact, that an investor causes.



But how can we measure this?

This is where ESG ratings come into play:

ESG is about what companies do with regards to Environment, Social, and Governance issues. It is all about how they behave!

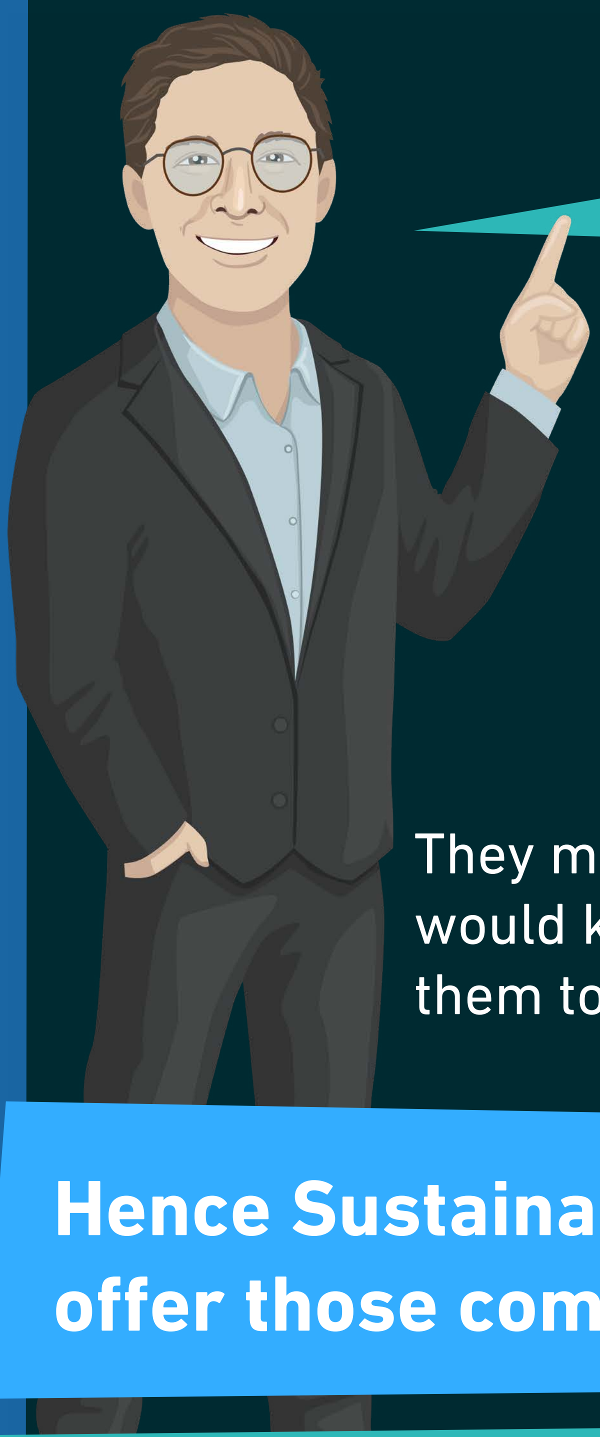
... a measure which is often complimented nowadays with a focus on Sustainable Development Goals (SDGs).

(DON'T!) WASTE WATER

The three mechanisms of Investor Impact

If Sustainable Investing wants to change the world, it can play on three levers:

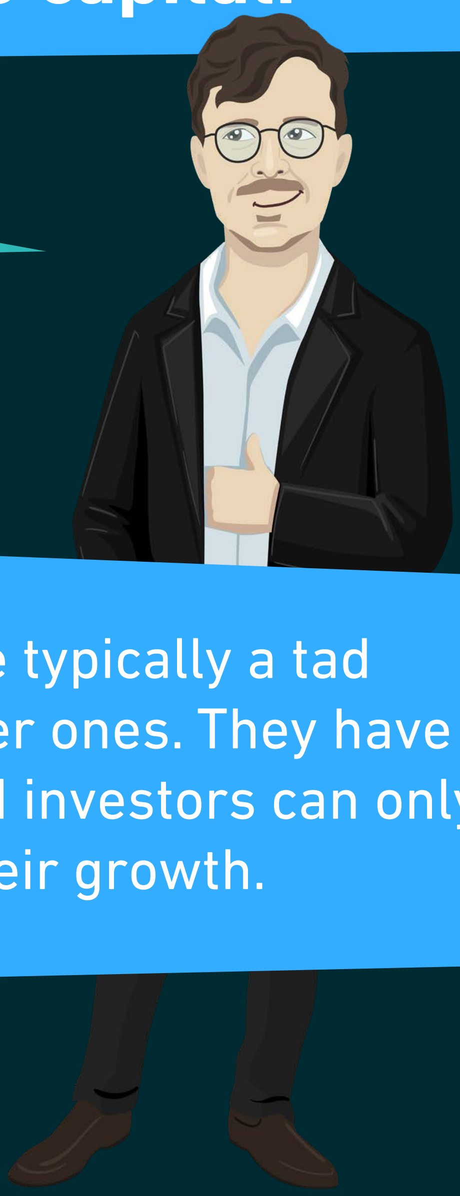
1. Grow Green Companies



Sometimes companies, especially in developing markets, struggle to tap into capital that allows them to grow.

They may do a lot of good things, though. And they would keep doing it if an external hand was to help them to grow!

Hence Sustainable Investing's first lever: offer those companies better access to capital.



That's the classic impact investing space!

2. Make Brown Companies Greener

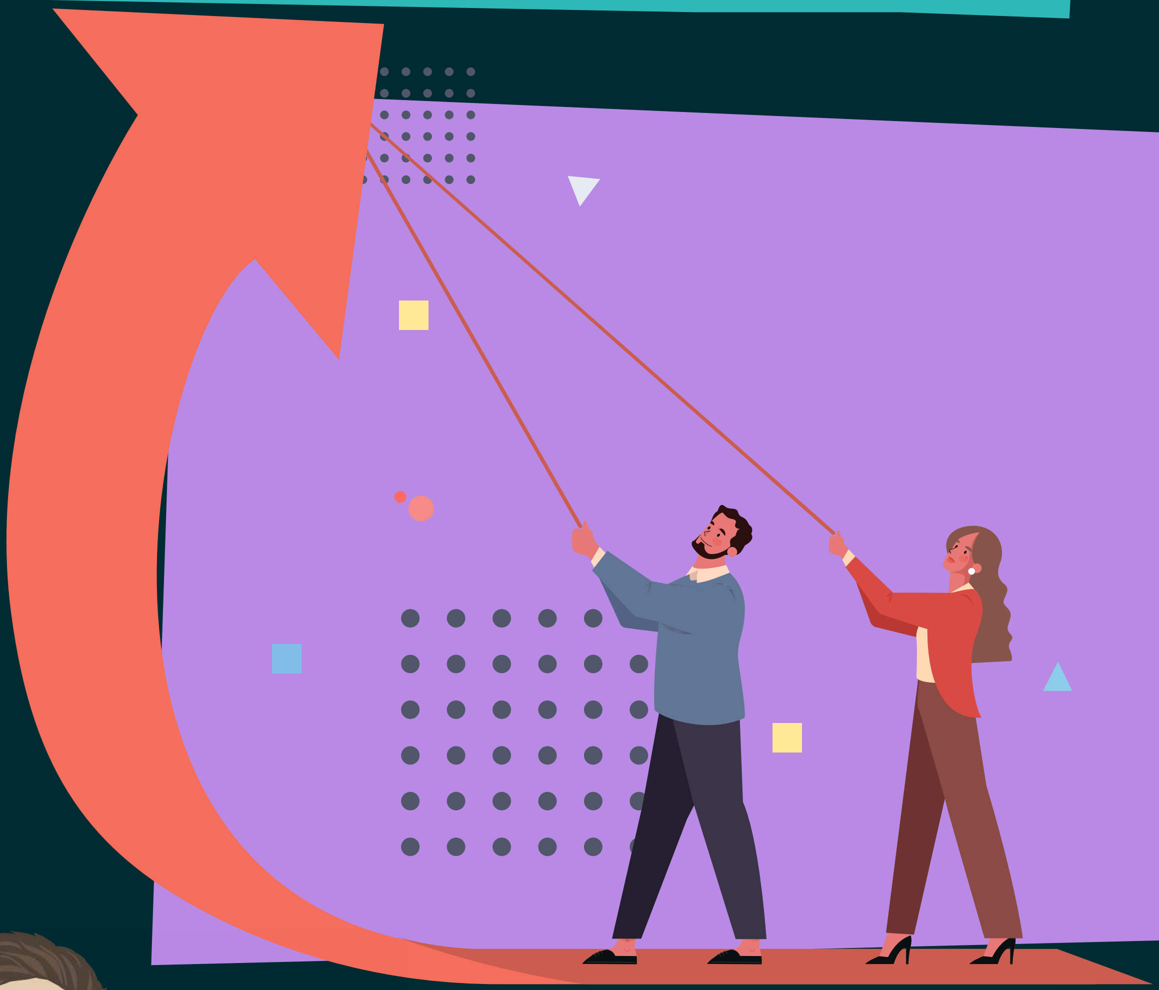
These companies are typically a tad larger than the former ones. They have access to capital, and investors can only marginally impact their growth.

Here, you can leverage shareholder engagement, enter into a dialogue with top management on how their environmental policy should look like, or even vote on their board.

(DON'T!)
WASTE WATER

For instance, Gollier and Pouget (2014) showed that 8% of investors pushing into the same sustainable direction may incentivize the new technologies required to mitigate climate change.

These are all theoretical models. The question is: what happens in the real world! 50% of the funds in Switzerland apply some sustainability strategies in their investment process. That's already far above this 8%, and yet, it did not solve climate change.



Why? Because the cost of change for a company may be much higher than the impact of Sustainable Investing on its stock price.

We're not sure about how these incentives work for the big tickets. It's much more efficient on small improvements!

For the "big ticket" impacts, Sustainable Investors shall rather focus on the third lever:

3. Activism

Sustainable investing cannot stop climate change on its own. Some issues require political change.

Yet, investors can leverage a range of indirect impacts to ignite transformation, such as stigmatization, endorsement, benchmarking, or demonstration.

If the University of Cambridge says 'we're out of oil!' it's a political message. It's not a crackpot idea anymore to say that this sector is inconsistent with the future.

... and looking at the science, we know that we all would be better off in 30-50 years if we have tough or stringent regulation now!

(DON'T!)
WASTE
WATER

This leaves us with a closing question:

Is lobbying for good still an underused power of sustainable finance?

We also discussed:

- How the tobacco example reminds us that screening strategies are limited by the barriers to change
- How there are always sin stock funds to counterbalance green stock funds - and how those perform unfortunately stupidly well
- How impact investing worldwide is still of the same magnitude as subsidies to the Fossil Fuel Sector
- How the recent Swiss referendum on CO2 law, ignited by a fossil fuel companies industrial group, proves that there is still a long way to go
- How pension funds could leverage their long-term positions in companies to foster an attitude change towards regulation
- How diversification across the three mechanisms probably offers the best yield
- Creating a special water activist fund, accelerating early water companies' growth, creating new business models, taking risks... and much more!

Don't miss a single bite: head over to dww.show!