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Institutional Investors and Sustainable Investment Decisions: A Survey on Indian Financial Sector as against select European Counterparts

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Abstract

Environmental, Social and Governance (ESG) challenges have changed the world of business investments altogether. Research findings have established to a great extent the validity of the arguments that the determinants of new investments should not necessarily be confined to the traditional parameters of financial factors. ESG issues could play a big role in addition to the known parameters of risk and return relationship. These now remain to stay for the coming years primarily because of the fact that unless ESG issues are factored into mapping the risk profile, the investors might be caught on the wrong foot and pay a heavier price. Particularly, in case of institutional investments, since those are purely custodial in nature, hedging the position seems extremely crucial. Since the institutional investors are the prime movers in the market, it becomes imperative to investigate into the depth of ESG acceptance among the custodial investors. We have attempted to investigate the same in Indian market by collecting and analyzing the first-hand account given by fund-managers and investment bankers based in Mumbai, India's financial capital. To get a comparative scenario, some European counterparts have also been brought under our survey. This paper attempts to document that with a critical appraisal of the situation.

Key words: *Institutional Investors, ESG Investing, Sustainable Investing, Corporate Finance, Risk-Return approach, Portfolio Diversification.*

1. Introduction

Environmental, Social and Governance (ESG) challenges have changed the world of business investments altogether. Sustainable investments are increasingly perceived as the key drivers of sustainable development. Research findings have established to a great extent the validity of the arguments that the determinants of new investments should not necessarily be confined to the traditional parameters of financial factors. ESG issues could play a big role in addition to the known parameters of risk and return relationship. Instead, in other words, the risk perspectives of new investments have undergone quite a formidable change. A substantial amount of risk is evidently perceived to come from a new set of factors called ESG in recent times. And these are now to stay for the coming years primarily because of the fact that unless ESG issues are factored into mapping the risk profile, the investors might be caught on the wrong foot and pay a heavier price. Particularly, in case of institutional investments, since those are purely custodial in nature, hedging the position seems extremely crucial. It has also been noted in several studies that when well geared hedging is done with the ESG issues in mind, it tends to offer better results. And the trend is really getting stronger day by day with the gradual increase in the acknowledgement level of such reality. In India too, the strategic importance of considering ESG factors has started taking roots with the facts like introduction of two sets of market indices, S&P ESG in 2008 and BSE Greenex in 2012, the latter being an active market portfolio too.

However, the BSE Greenex is not wholly ESG based, although it could also be taken as a good proxy. Since the institutional investors are the prime movers in the market, it becomes imperative to investigate into the width and breadth of ESG acceptance among the custodial investors. This paper attempts to do the investigation among a good sample of Mumbai based fund managers and investment bankers through surveys and personal interviews. To further cause by having a comparative view with a similar exercise among some German counterparts, Germany being undoubtedly the foremost nation in the European Union (EU). At the end, a broad based comparison is attempted with other two EU nations closely following Germany, Switzerland and Austria, on the basis of some secondary data collected. In terms of sustainable investments, overall volume of the market size in Germany, Austria and Switzerland totals 134.5 billion euros, institutional investors being the key drivers to growth. In these three countries, the volume of investments, where not only financial indicators but also ESG criteria has been taken into account, has increased by 12% within a year. Out of the three countries, there has been a strong growth in the area of sustainable investment funds and mandates in Austria, which has witnessed an increase of 29 % followed by Switzerland and Germany, each with a growth rate of 17%. Interestingly, in all the three countries the market for sustainable investments has grown at a rate higher than average for the conventional market.

The construct of the paper is as follows: Section 2 deals with the role and importance of institutional investors i.e. fund managers and investment bankers in India with the major findings from the surveys undertaken. In Section 3, we have tried to look at the global scenario i.e. the state of sustainable investments in Germany and the results obtained from the expert interviews. Section 4 includes the state of ESG investments in Switzerland and Austria. Section 5 mentions the limitations of the study. Section 6 i.e. the concluding section provides a brief analysis of the results obtained from the above mentioned sections and discusses the way forward.

2. Institutional Investors and ESG Investing

2.1 Importance of Fund Managers in ESG/Sustainable Investing

The institutional investors are the key drivers to sustainable investment. Different studies conducted by Mercer, IFC, World Bank and some of the other research organizations have highlighted the role of institutional investors specifically mutual funds and hedge funds in ESG investing. According to several reports, the genesis of ESG investing has started with the onset of the global financial crisis. The investors, institutional investors in particular have become quite aware of the risk perspective of the ESG factors. In this context, UN Principles of Responsible Investment (PRI) is perhaps the only overarching framework which provides the institutional investors a broad overview of the ESG risk factors in traditional investment analysis and also sets the platform to adequately address the ESG risk factors through its 6 major principles. The fact that the number of signatories to UNPRI including investment managers, asset managers and other professional partners has seen a significant increase since the inception of the principles is an indicator towards the acceptance of ESG factors in portfolio analysis.

The risk taking capacity of the institutional investors is lesser than other investors keeping in mind that they are custodial and fiduciary in nature. Apart from this, majority of institutional investors are interested in long term returns and enhancement of shareholder value. Hence they are aware of the fact that a company which well manages both its ESG performance in concurrence with the financial indicators, are companies which can sustain over the longer run. In fact, the individual companies have also understood this fact and the trend is quite evident in the west. ESG investing is the provenance of institutional investors wherein they consider ESG factors to illustrate quality management. Globally, it is their commitment in the long run. While we try to emphasize the role of institutional investors in ESG investment, research also indicates the several approaches which they undertake in integration of ESG factors in their portfolios.

a. Full ESG integration in portfolios

According to this approach, investors consider only positive ESG stocks while minimizing their negative exposure. Hence this approach includes companies which have positive ESG ratings.

b. Screening Approach

This approach is quite similar to the first approach wherein investors use issue-based screens while selecting stocks for their portfolios.

c. ESG branded investment approach

According to this investment approach, investors dedicate only a portion of their AuM to ESG investments.

d. Governance or active ownership approach

Investors take an active approach by engaging with their portfolio companies that are subject to ESG risks.

As a matter of fact, ESG factors are now not seen as merely reputational or brand enhancing factors but ignoring ESG factors can be considered as a breach of the investors' fiduciary duty. Thus some ESG research organizations are trying to quantify the ESG risk and estimate a 'sustainability alpha'. Although this is still in the nascent phases, there is lack of sufficient approaches to evaluate the risks and opportunities.

Some surveys have been conducted in the developed markets relating to the role of institutional investors in ESG/Sustainable investments. The findings of the study carried out by Ernst & Young are as follows:

a. There is no universal framework relating evaluation of non-financial disclosures. Institutional investors find this as a key barrier to quantify the data.
b. Materiality of the ESG factors was accepted by a large majority of institutional investors. The ones who did not accept it found ESG factors as non-material.
c. Majority of the institutional investors used non-financial performance as a good benchmark for risk.
d. Investors had revealed that companies disclosed their non-financial performance in order to build up a better corporate reputation.
e. The survey also highlighted that the findings varied across geographical regions.

As has been previously mentioned, a survey was carried out with mutual fund and private equity managers in Mumbai, India, to gauge their level of awareness and perception about the specific 'E', 'S' and 'G' factors and the extent to which they incorporate them in their investment decisions (Sinha and Datta, 2014). The following sections elaborate on this.

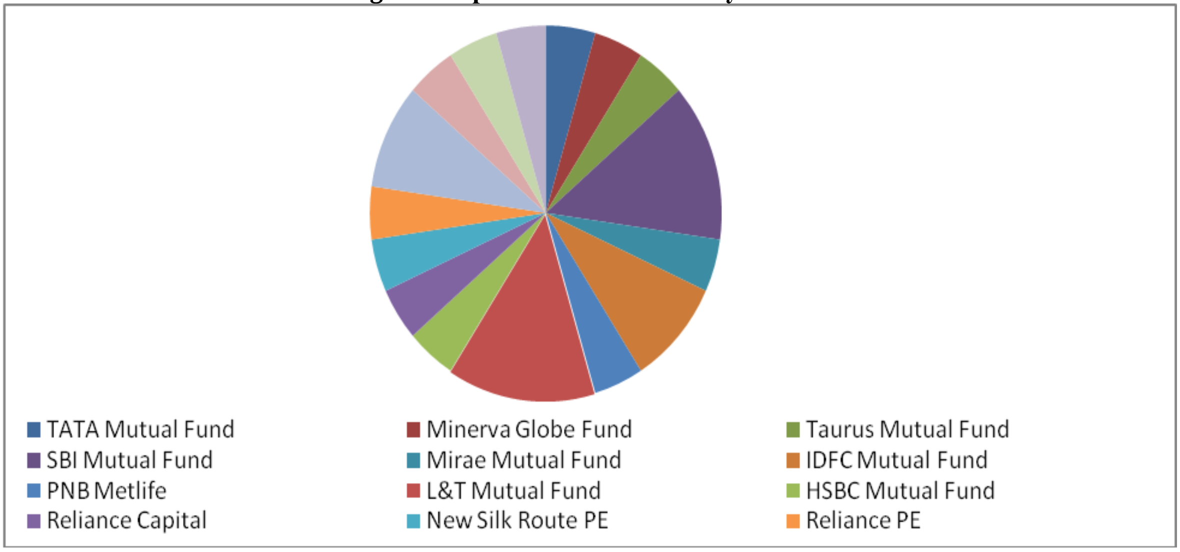
2.1.1 Methodology of the survey conducted

This survey was conducted among institutional investors in Mumbai, India, with the help of a structured questionnaire, which was distributed to them and consisted of their responses to incorporation of ESG factors apart from the financial factors undertaken in investment decisions. The structure of the questionnaire was divided into three parts: Section A consisting of the multiple choice questions with multiple responses, Section B is based of questions on a Likert scale of 1 to 7 to understand the perception of ESG factors among fund managers. The reliability of this section has been checked with the coefficient of Cronbach's alpha. The last section i.e. Section C comprises of questions. The responses have been analyzed with appropriate software and have also been cross-checked by interacting with other members and viewing their reports and factsheets. The sample consists of 16 AMC's involving 22 fund managers chosen from the Association of Mutual Funds in India (AMFI), based on a simple random sampling method. The sample has been again sub-divided into 18 MF managers and 4 PE Firms.

2.1.2 Major findings from the survey of Mutual fund and Private Equity Managers in Mumbai, India

i. The spread of the AMC's surveyed is illustrated in the table below.

Figure 1: Spread of AMC's surveyed



ii. The structure of mutual funds surveyed is highlighted as under:

Table 1: The Mutual Fund structure classification

Type of Funds	% of Responses
Debt	28
Equity	39
Hybrid	17
Index	5
Other	11
Total	100

iii. Most of the mutual fund managers surveyed considers financial factors like returns, benchmarks, HSES, promoter track records, innovation primarily for their investment decisions, although some of them also take into consideration some of the ESG factors as shown below. Most of the MF managers are concerned with corporate governance factors. As we find from table 2, the extent of environmental factors considered by MF managers is greater than PE managers.

Table 2: Factors Considered By Asset Managers In Investment Decisions

Indicators	**% of Responses**	
	MF Managers	PE Managers
Risk Profile of the Company	26.9	20
Capital Gains generated	16.4	26.7
Companies which take measures to reduce carbon footprint	10.4	6.7
Energy Efficient Companies	9	6.7
Companies with high retention rate of employees	14.9	13.3
Companies with least legal disputes	19.4	13.3
Other	3	13.3
Total	100	100

iv. In case of portfolio diversification, MF managers often take into consideration ESG factors apart from the other financial factors as has been represented in the following table below. In this case also the MF managers are much more aware of the environmental and social factors vis-à-vis the PE managers.

Table 3: Factors Considered By Asset Managers in Portfolio Diversification

Indicators	**% of Responses**	
	MF Managers	PE Managers
Stability in Returns of the Stock	21.2	40
Low risk and moderate returns of the stock	15.4	20
High risk and high returns of the stock	9.6	0
Stocks of companies providing disclosure to financial and operational information	26.9	20
Stocks of companies which has a high community impact	11.5	0
Stocks of companies with lower GHG emission	5.8	0
Other	9.6	20
Total	100	100

v. Asset managers are increasingly considering ESG factors for screening of their portfolios, with greater emphasis on corporate governance factors. However, the MF managers also take into consideration the environmental factors as compared to the PE managers. The following table is indicative of the same.

Table 4: Factors considered by Asset managers in screening Portfolios

Indicators	**% of Responses**	
	MF Managers	PE Managers
Listed on a Stock Exchange	17	0
Effective Management	29.8	50
Profits and Dividends	29.8	33.3
Stocks of Companies following proper environmental norms	17	16.7
Other	6.4	0
Total	100	100

vi. In terms of research related activities of companies, fund managers consider investing in companies with research conducted in the domain of corporate governance. The mutual fund managers comply much more with the CSR guidelines than the PE managers. Apart from this, the MF managers also consider factors such as disclosure and reporting, innovation of equipments to reduce GHG emissions, developing company valuation models and also consider companies which take adequate measure in the sphere of water management.

vii. Although the fund managers are becoming aware of ESG factors in their investment decisions, rarely few of them have international partnership with sustainable framework. Only three of the asset managing firms namely, HSBC, SBI and Multiples PE consider partnerships with UNPRI, Auto Euro III Emission norms and Equator principles respectively.

viii. MF and PE managers mostly report financial and corporate governance factors to their clients.

ix. Most of the MF firms surveyed publish annual and financial reports, although some like L&T are also publishing sustainability and disclosure reports.

x. While trying to identify newer opportunities for investments, MF managers are highly concentrating on companies having good corporate governance. On the other hand, PE managers surveyed only consider financial factors for newer investments. But compared to the PE managers, the MF managers also take into consideration corporate governance factors like companies with better CSR approach; enforce environmental factors like companies with better energy efficient practices; and social factors like companies with high labour intensity of business.

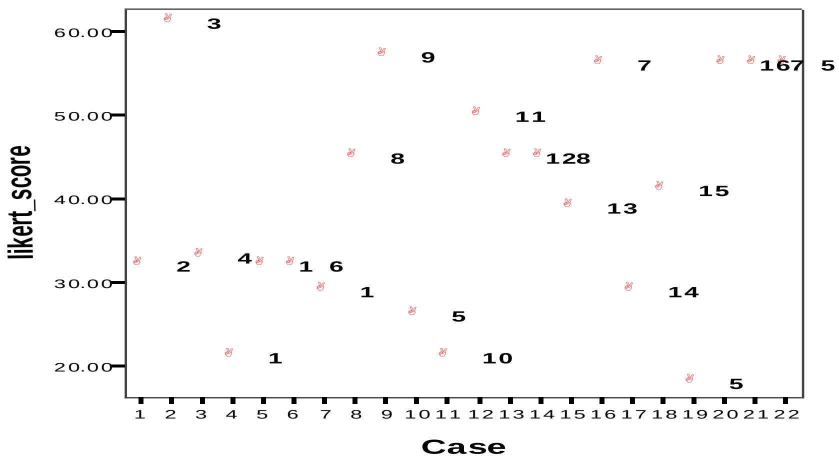
xi. Regarding mode of applying pressure on individual companies to improve their ESG performance, most of fund managers do not apply pressure. In case they apply, the general mode is private meetings between fund managers and company directors. On the other hand, PE managers surveyed usually conduct only private meetings between fund managers and company directors.

xii. According to the MF and PE managers surveyed, majority of their clients do not place importance to include ESG criteria in their portfolios. Clients are mostly interested in the performance of their portfolios and hence enforce only financial returns on the same.

xiii. Most of the MF managers and PE managers do not have an adequate ESG management system at present, but are quite hopeful about having a rigorous ESG mechanism in the future. Given the fact that the risk taking capacities of these two asset classes are different, most of the asset managers are assertive that investment tools such as company valuation models need to be developed further to adequately capture ESG data. In fact, according to some MF managers, one needs to see whether that would lead to strengthening the business model of the company. In this context, it is also pertinent to mention that none of the asset management companies has calculated its sustainable "assets under management" (AuM).

xiv. As some of the questions were perception based, Likert scores were also calculated to get an approximate idea of the fund managers who believe that factoring of Environment, Social and Governance factors into investment decisions can add value to their portfolios.

Figure 2: Perception of Fund Managers about ESG factors in investment decisions



2.2 Investment Bankers and ESG Investing

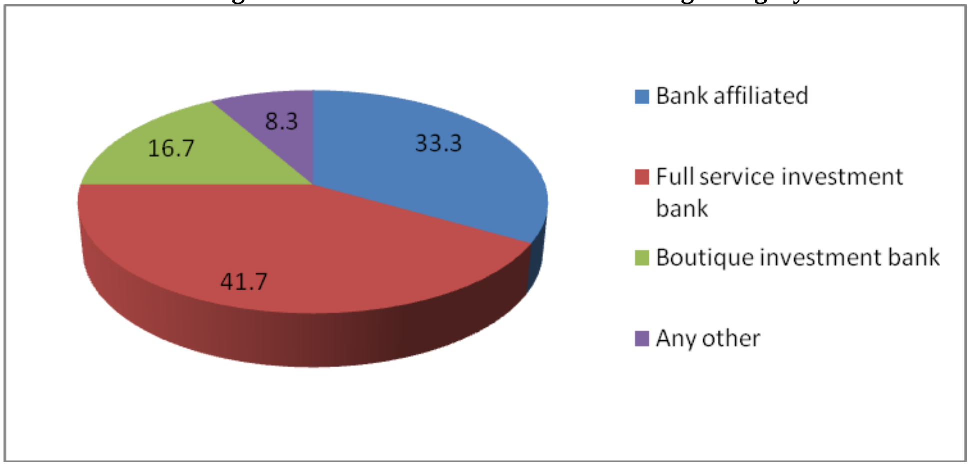
2.2.1 Importance of Investment Bankers in ESG/Sustainable Investing

The role of the investment banking firms in ESG investing has been steadily increasing in the last few years. Apart from their conventional role of assisting individuals, corporations and governments in raising capital by underwriting or acting as the clients' agent in the issue of securities, investment bankers are also taking an active role in ESG/sustainable investments. Although there has been adequate number of studies pertaining to the role of fund managers in ESG investing, there is limited literature as to how investment banks can accentuate this process. As we all know that the two main lines of business of investment banking, i.e. the buy side and the sell side. The role of investment banking in sustainable investing is primarily concerned with the buy side. This involves the provision of advice to institutions concerned with buying of investment services. As a matter of fact, investment bankers can play a very crucial role in advising their clients during mergers and acquisitions. Apart from this, they can also offer sustainable investment products or strategies. Investment bankers can play a positive role in assisting their clients with their investment portfolios, which can include specific ESG factors. Project financing is also an area wherein investment bankers can finance for green sustainable projects which emphasizes on inclusion of sustainable factors along with the profitability of the projects. Although the role of investment bankers in sustainable investing have not been sufficiently explored in literature, they can themselves put in place a tangible ESG framework which can be embedded in their mainstream investment assessment. Investment bankers can also consider international partnerships with sustainable frameworks like UNEP FI, UNPRI, 2 degree Investing Initiative, Carbon Disclosure Project, and Climate Principles etc. To understand the significance and position of Indian investment bankers in ESG investing, a survey was carried out in Mumbai, India. The methodology and findings of the survey are illustrated in the forthcoming sections.

2.2.2 Methodology of the survey conducted

The sample of investment bankers in India was chosen from AIBI i.e. Association of Investment Bankers in India. Detailed questionnaire was sent to all the Chief Financial Officer's (CFO) and/or Chief Investment Officer's (CIO) listed in AIBI for their responses. Telephonic interviews were conducted with 12 key persons who had shown their interest. The structure of the questionnaire is as follows: Section A consisted of multiple choice questions with multiple responses and descriptive questions. Some of the descriptive questions were asked simultaneously with the multiples choice questions to get their spontaneous responses. Section B consisted of perception based questions on a Likert scale of 1 to 5 to understand their perception of ESG factors towards sustainable investing. The responses have been analyzed with appropriate software and have also been cross-checked by interacting with other members and viewing their reports and factsheets. The structure of the Investment banking category is illustrated as follows.

Figure 3: Structure of Investment Banking Category



2.2.3 Major findings from the Interviews

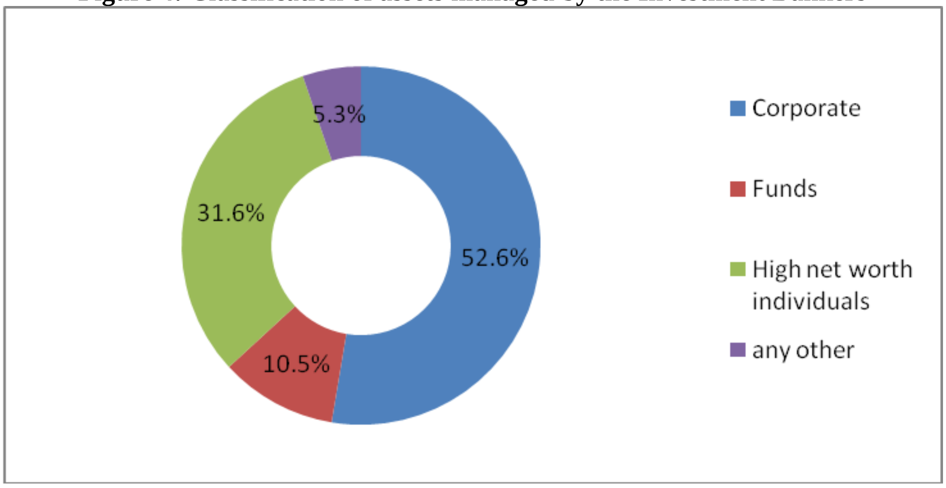
i. The classification of key activities of the investment bankers is the following:

Table 5: Classification of Key Activities

Key Activities	**% of Responses**
Mergers and acquisition advisory	21.6
Private placement of securities	16.2
Private equity advisory	16.2
Public offering/underwriting of securities	10.8
Merchant banking	10.8
Trading of securities	5.4
Financial restructuring advising	2.7
Securities finance	2.7
Prime brokerage	2.7
Trading and creation of derivative instruments	2.7
Any other	8.1
Total	100

ii. The classification of assets of clients managed by the Investment Bankers surveyed is highlighted as under:

Figure 4: Classification of assets managed by the Investment Bankers



iii. The investment bankers surveyed mostly provide their advisory services in Private Equity and Merger & Acquisitions.

Table 6: Advisory services provided by Investment Bankers

Advisory Services	**% of Responses**
PE Advisory	20.8%
M&A Advisory	20.8%
Infrastructure Advisory	15.1%
Project Advisory	15.1%
Real Estate Advisory	15.1%
Finance Restructuring Advisory	11.3%
Any other	1.9%
Total	100

iv. 88.2 % of the investment bankers surveyed mostly take into consideration the stability in returns of the stock, while they assist their clients with their investment portfolios. 11.8%

of the respondents take into account corporate governance factors like reputation and history of the promoter, NOC's from the CPCB and certain other green documents.

v. In accessing the potentiality and profitability of projects while financing, 46.2% of the investment bankers take into consideration financial benchmarks, 23.1% of the respondents consider environmental factors, 15.4% consider macroeconomic factors, 11.5% account corporate governance factors and 3.8% of the investment bankers surveyed take into account social factors.

vi. 42.9% of the investment bankers surveyed report financial factors to their clients, 32.1% report corporate governance factors, 10.7% of the investors report environmental factors and social factors each.

vii. 75% of the institutional investors surveyed do not consciously counsel clients to include ESG criteria in their portfolio, while the rest 25% does so.

viii. 64.3% of the institutional investors surveyed do not have any partnership with international framework such as the Equator principles, Climate principles, UNPRI or UNEP FI. 14.3% of the respondents have partnerships with the Equator Principles. 7.1% of the respondents have partnerships with the Climate principles and Carbon Disclosure Project. The remaining 7.1 % consider international partnership with other frameworks such as Carbon credit assessors.

ix. All the investment bankers surveyed revealed that they do not encourage their clients to become signatories of the above mentioned sustainable frameworks while taking investment decisions.

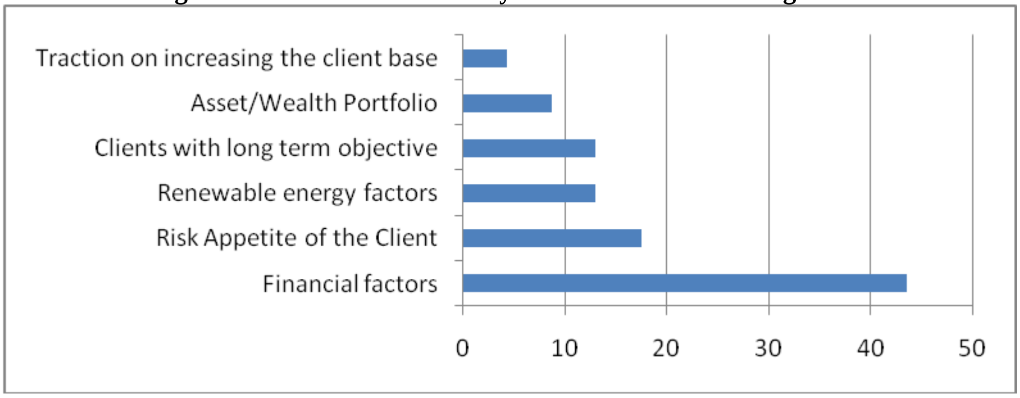
x. The key success factors considered by investment bankers in Mergers & Acquisitions are illustrated below:

Table 7: Key factors considered by investment bankers in Mergers & Acquisitions

Success Factors for M&A	**% of Responses**
Synergies btw acquirer and acquire	22.2%
Intent of acquisition, post integration setup and positioning	19.4%
Perceived long term benefits	11.1%
Financial factors are mostly considered	11.1%
Environmental clearances	11.1%
Only Financial factors	5.6%
Match of vision and long term plans	5.6%
Due diligence and compliance with regulator	5.6%
CG factors	5.6%
HR factors	2.8%
Total	100

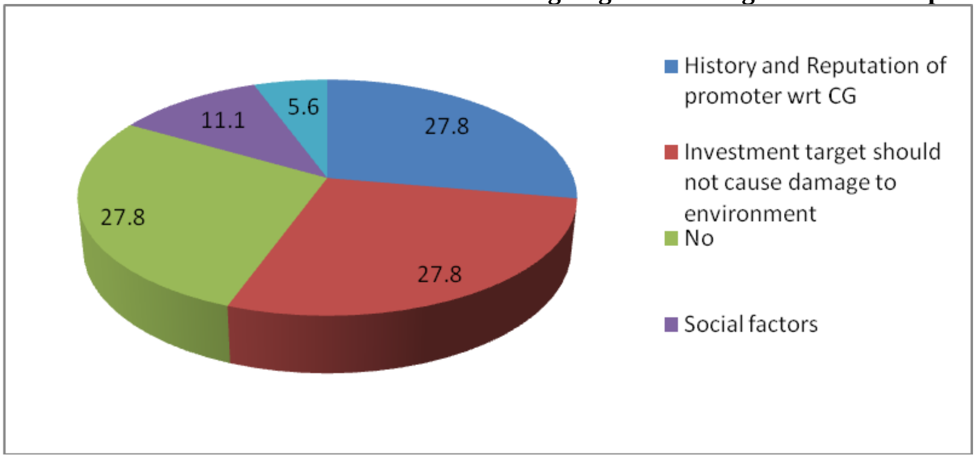
xi. The following pertinent factors are considered by the asset/wealth management division of the investment banking firms surveyed.

Figure 5: Factors considered by the Asset/Wealth management division



xii. According to the investment bankers surveyed, the following are the non-financial factors considered while designing/customizing a portfolio of investment for their clients.

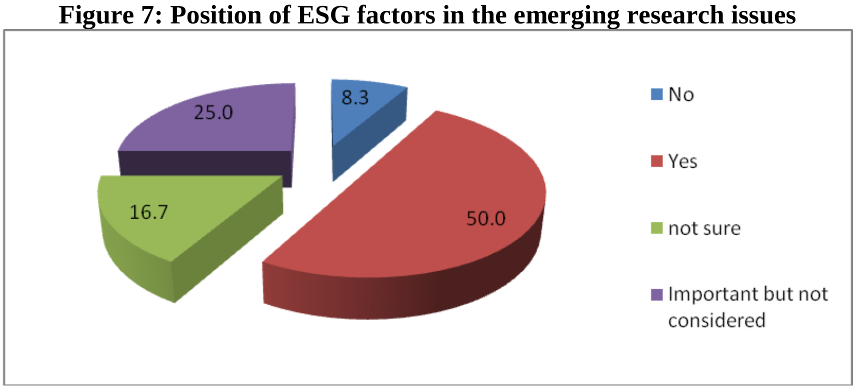
Figure 6: Non-financial factors considered while designing/customizing an investment portfolio



xiii. 55.6% of the investment bankers surveyed do not have any tangible framework which can be embedded in their mainstream assessment. 22.2% of the respondents have a checklist of ESG factors, 11.1% adhere to environmental and social due diligence, while another 11.1% have performance standards framework for evaluation.

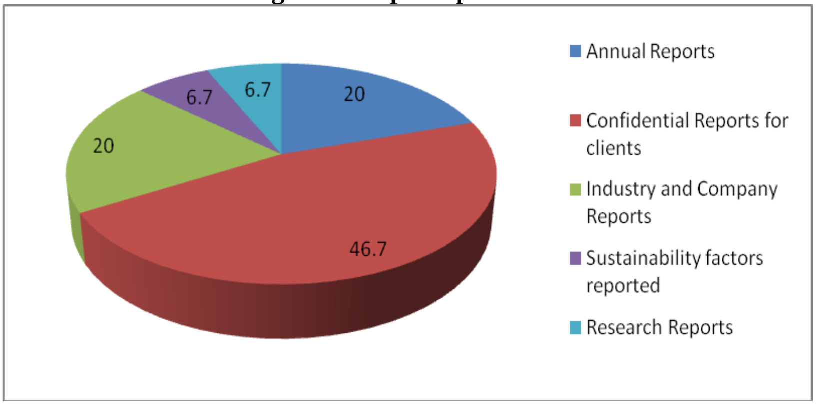
xiv. The following figure illustrates the respondents' position of ESG factors in the emerging research issues.

Figure 7: Position of ESG factors in the emerging research issues



xiv. The reports published by the investment bankers surveyed are illustrated below.

Figure 8: Reports published



xv. 41.7% of the investment bankers agreed to the fact that there can be a model for considering ESG factors. However, 25% of the investors 'did not agree' and for 33.3% of the institutional investors it was 'difficult to say'.

xvi. 66.7% of the investors believed that there can be a realistic framework for the inclusive valuation of ESG factors in investment portfolio. However, the rest 33.3% found it difficult to comment upon.

xvii. The following are the key motivational factors to sustainable investing as believed by investment factors surveyed.

Table 8: Key motivational factors to sustainable investing

Key motivations for sustainable investing	**% of Responses**
Value addition to clients	25.8
Generation of long term returns	25.8
Reputational Concerns	19.4
Inclusive growth and long term sustainability	12.9
Good to do (philanthropy)	12.9
Aspiration of companies to work with foreign investors	3.2
Total	100

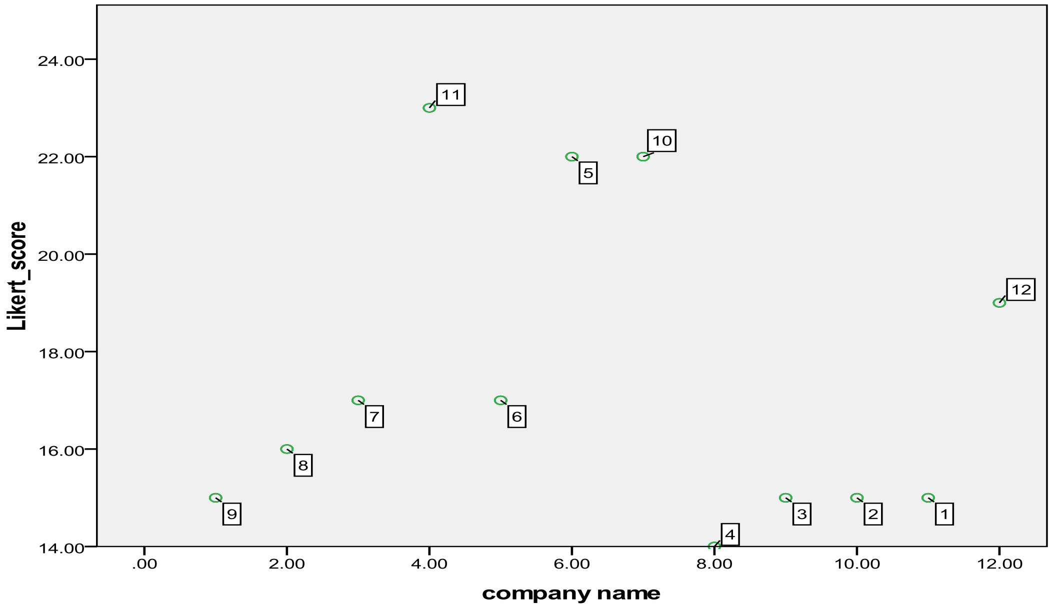
xviii. The following are the key demerits of the concept of sustainable investing as believed by investment factors surveyed.

Table 9: Demerits to the concept of sustainable investing

Demerits of sustainable investing	**% of Responses**
No objective assessment of the same which is measurable	4.2
Returns are low keeping in mind the cost involved	20.8
ESG framework is not defined	4.2
Red Tapism	4.2
Absence of a market to accept ESG factors	16.7
Institutional investors are doubtful about profitability in future	29.2
Uncertainty about the regulatory framework	20.8
Total	100

xix. The Likert scores calculated for the investment bankers are illustrated in the figure below. The reliability of the perception based questions has been tested with the efficient of Cronbach's alpha.

Figure 9: Perception of Investment Bankers towards ESG investments



Note: 1.00=RBS, 2.00=SMC Capital, 3.00=Axis Capital, 4.00=Almondz Global Securities, 5.00=Centrum Capital, 6.00=Motilal Oswal, 7.00=ICICI Securities, 8.00=Global Trust, 9.00=IDBI Capital, 10.00=Fortune Financial Services, 11.00=Daiwa Capital, 12.00=IDFC

3. Sustainable Investment scenario in Germany

Germany is one of the foremost nations in the European Union in terms of sustainability investing and sustainable development as a whole. The rate of increase of ESG investments in Germany is manifested by the growth of UNPRI members in all the three categories, namely, Asset Owners, Investment Managers and Professional Service Partners. The German Global Compact Network (DGCN) is quite similar in nature to the UN Global Compact Network and brings together the German Global Compact participants from business, government and civil society committed to implementing and disseminating the 10 principles of the Global Compact and the goals of the United Nations, not only in Germany but worldwide. As a matter of fact, DGCN maintains its close association and cooperation with the UNPRI. The total number of sustainable mutual funds in Germany is on the rise. According to data from Sustainable Business Institute (SBI), total of 384 sustainable mutual funds were licensed for marketing in Germany, Austria and Switzerland. Forum for Sustainable Investment (FNG) estimated the size of sustainable investments in Germany, Switzerland and Austria, to the tune of 103.5 billion euros, as of Dec 2011. The total figure included mutual funds and mandates, sustainability oriented specialists' bank account, customer investments and sustainable certificates. FNG had also calculated the asset overlays in the German speaking countries to the tune of 1055.6 billion euros. Out of this figure, Germany accounted for the highest share of 618.2 billion euros. According to a Deutsche Bank report, sustainable assets equivalent to Euro 400 million is managed by them in individual portfolios, mutual funds and especially themed funds for clients in Germany. In the domain of corporate responsibility, Oekom Research states that sustainability is a major criterion for German companies to operate as they are extremely futuristic in believing that sustainable investments can lead to sustainable development in the longer run (Oekom Research, 2012). The institutional investors in Germany are extremely focused and determined in factoring ESG criteria in their investment decisions. In fact, this was one of the key results of the survey conducted by Union Investment. Moreover, a growing number of institutional investors expect sustainability reporting requirement to increase rapidly and hence they can no longer ignore the pertinent issue of sustainability. Sustainable investing in Germany is much beyond reputational concerns. It has become more of a risk management criterion. The essence of sustainable investing in Germany lies in the hands of the institutional investors who believe that a top-down approach is to be followed in its implementation process in investment decisions. It is a matter of fact that the narrow differences between ESG investing, sustainable investing and SRI investing is ignored by majority of investors and are mostly seen as synonymous terms. The most common approaches followed in sustainable investing are Best in class approach, Engagement and voting, Exclusions, Impact investment, Integration, Norms based screening and sustainable themes. According to Social Investment Research Platform (SIRP), the German government has certain regulations in relation to the fiduciary duty of institutional investors towards ESG investing. The investors have a legal duty to manage investments professionally to ensure highest possible security and sustainable profit, apart from risk diversification and liquidity requirements.

Eurosif conducts socially responsible investment (SRI) surveys in Europe every year with institutional and retail investors. The results from the 2014 survey are more or less consistent with the findings of the 2013 survey. The data has been gathered from 13 distinct European markets. Although the survey has covered a broad range of European countries, we present the major findings in the German market. The study calculates CAGR from 2011 to 2013.

The main findings of the study are as follows:

a. The foremost and overall finding from the survey is that the sustainable and responsible investment strategies in the selected markets including Germany continue to grow at a faster rate than the broader European market.
b. Germany has seen a negative growth of -4% in sustainability themed funds, which cover a wide range of themes from climate change and energy efficiency to forests and water.

c. Germany has indicated a positive growth of 10% in Best-in-class investments, which involve selecting the top percentage of companies within a sector using ESG criteria.
d. Norms based screening in Germany has seen a negative growth of -5%. This strategy involves assessing each company held in the investment portfolio against the specific standards of Environmental, Social and Governance criteria.
e. Using the Exclusion based criteria; Germany has indicated a 20% growth. This strategy also known as negative screening involves removing certain companies from the portfolio based on certain Environment, Social and Governance indicators.
f. ESG integration has seen a slight decline of -2% in Germany. ESG integration actually refers to explicit inclusion by asset managers by factoring ESG risks and opportunities into traditional financial analysis and investment decisions.
g. Engagement and voting has increased by 22% over the mentioned time period.
h. Best in Class and Exclusions are the most popular strategies used by institutional investors in Germany.
i. The report also states that asset managers in Germany take an optimistic view on the future. They expect the market to further grow and believe that institutional investors will continue to be the most important drivers of SRI demand in the German market.

Novethic in association with FNG had conducted a market survey with 185 asset owners from 13 countries with 6 trillion euros in assets from June to September, 2014. Out of the total sample of respondents, 20 respondents are from Germany with 1204 billion euros worth assets (Novethic, 2014). The major findings from the survey on German investors are as follows:

a. German signatories to UNPRI are increasing, as compared to the other European counterparts. According to the study, while 12% of the respondents were signatories in 2013, the number increased to 50% in 2014.
b. 80% of the German investors have introduced an ESG strategy. Four out of the five respondents use sector based exclusions and 65% exclude companies implicated in violations of international norms.
c. According to the survey, Germany is still underdeveloped in terms of shareholder engagement. Only 35% of the sample surveyed stated that they had only one direct dialogue with companies in the period considered which mainly focused on governance issues.

In this context, it is highly pertinent to mention about the German Sustainability Code (GSC). The German Council for Sustainable Development attaches great political value to the GSC. Some of the salient goals of the GSC are as follows:

a. Creating a level playing field for sustainability by means of standardized minimum requirements, a frame of reference for making competitive comparisons
b. Mainstreaming sustainability, tapping into new groups of investors for enterprises
c. Facilitating access to sustainability data
d. The application of GSC is voluntary, the set of criteria and the Key Performance Indicators (KPI) is binding
e. The Council assumes no liability for the quality of the information

The Council also demarcates the area of application of the GSC. It is valid for all sizes, organizational and legal forms. As a matter of fact, the Code specifies the KPI's (both by GRI and EFFAS). The Code assures that this binding set of criteria and the KPI's are expected to achieve better comparability between companies, industries and countries. Companies can decide whether to report on the basis of the KPIs of the GRI or EFFAS. The KPI's cover a broad range of strategic areas like Strategy, Process management, Environment and Society.

The University of Hamburg, Germany, had conducted a survey on the analysis of implementation and effectivity of the GSC. The survey was carried out with 163 participants. The responses received involved asset managers (32%), Sell side analyst (10%), Buy side analyst (7%), Asset Owners (1%), Rating agency analyst (1%), others (18%) and no responses (31%). Some of the major findings of the survey are stated as under:

a. Only 24% of the respondents were aware of the GSC. 41% of the respondents did not respond.
b. 8% of the companies had examined the introduction of GSC with the majority of respondents not responding to it.
c. 3% of the companies surveyed had actually implemented GSC across all company levels and 2% of the companies implemented GSC at the asset management levels.
d. 23% of the companies surveyed consider improved reporting standards on non-financial information as necessary.
e. To the question as to why they consider improved reporting standards as necessary on non-financial information, the responses hovered around transparency, improved risk assessment, customer requirements, demand from some investors, lack of uniform guidelines and comparability, to increase reliability and level of detail of company evaluation etc.
f. GSC is mostly used by companies as a good management signal of companies, as a selection criteria for individual titles, enhancement and debasement in evaluation, quantification in evaluation models etc.

g. The main advantages of the GSC include increased transparency, addressing the issue of sustainability in general, reflects social pressure, strengthening sustainability within the company, internationally compatible, suitability for all company sizes etc.

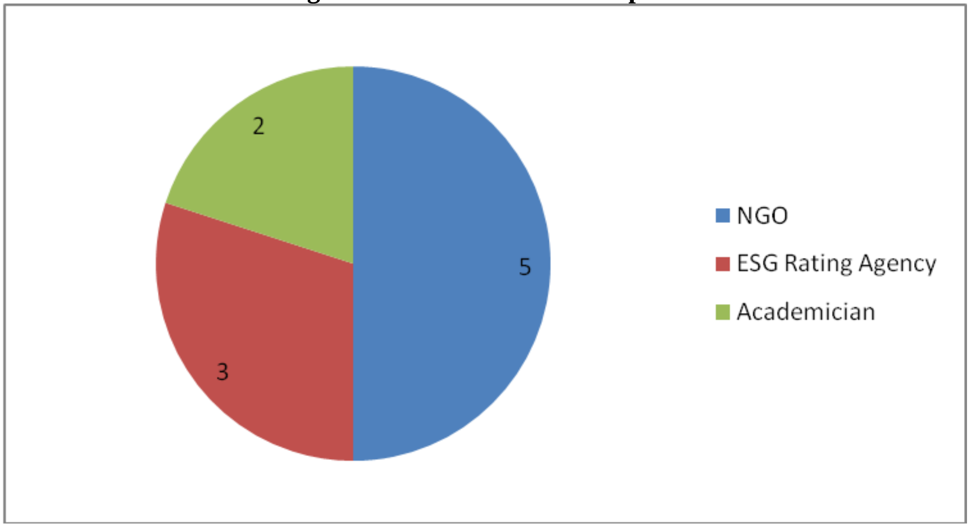
h. Some of the main disadvantages of the GSC as reported by the responding companies include non-representation of sector specific characteristics, unclear interpretation of sustainability by GSC, low level of international compatibility/adaptability, applicability of GSC to only large enterprises, low number of declarations of conformity, absence of a legal framework etc.

i. The most common KPI indicators as was found from the survey are ESG assessment, research for ESG fields, remuneration and performance, ESG business strategy, Greenhouse Gas Emissions, direct energy consumption, Fines/non-financial penalties etc.

3.1 Methodology of the Personal Interviews conducted

The sample of ESG experts in Germany was chosen through a purposive sampling method among academicians, NGO’s and ESG rating agencies in Berlin, Frankfurt and Hamburg. The sample size is small, comprising of 10 experts in the domain of sustainable investments who directly interact with institutional investors. The survey was conducted with the help of an interview schedule wholly based on descriptive questions. The responses have been analysed using appropriate software. The structure of the respondents is illustrated below.

Figure 10: Classification of Experts



3.2 Major findings from the primary survey

i. To the question of whether they believe that there has been an attitudinal or perceptional change towards ESG investing in the recent years, all the 10 experts have agreed to it. According to the experts, the financial economic crisis has been the primary reason wherein institutional investors have understood the importance of good governance and other Environment and Social risk factors. Some experts also believe that strengthening of the regulatory framework has also geared up the process of sustainable investing. There has also been a remarkable increase in the number of green and ethical banks in the country.

ii. When asked about the importance of the UNPRI, 55.6% of the respondents stated that this flagship initiative is indeed 'important'. 44.4% of the respondents believed that the principles were 'extremely important'. According to all the respondents, the principles are very much meaningful for mainstream investors and set the platform for responsible investments. It also enhances the confidence of the future financial managers in sustainable investing. Apart from this, the experts also believed that the UNPRI's gives a possible menu of actions for factoring the E, S and G factors in financial portfolios. Although the importance of the UNPRI's has been accepted by all the experts, there exist certain lacunae in its framework and proper implementation.

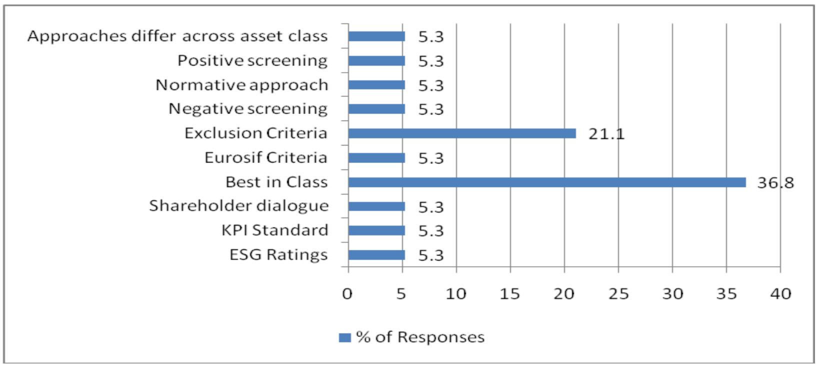
iii. To the question of whether they believed that PRI's offer a possible menu of actions for incorporating E, S and G factors in investment practices across asset classes, 66.7 % said 'yes', 22.2 % said 'no' and 11.1 % of the respondents were 'not sure' about it.

iv. 33.3% of the respondents believed that the Key Performance Indicators (KPI's) were the most important framework for considering the specific Environment, Social and Governance factors in investment portfolios. The KPI's are included in the German Sustainability Code (GSC) which was established by the German Council for Sustainable Development in 2001. There are 19 KPI's for ESG in the broad arenas of Strategy, Process Management, Environment, and Society. The other 66.7% of the respondents, which includes mostly the ESG rating agencies have their own specific indicators which are sector specific and are maintained confidentially.

v. Apart from this, all the respondents believed that the E, S and G factors were complimentary to each other but are industry specific.

vi. The key approaches to ESG integration as practiced are illustrated below:

Figure 11: Main approaches to ESG integration



vii. All the professionals interviewed believed that financial organizations should have an effective ESG management system, so that they can understand the risks and opportunities underlying sustainable investments.

viii. Regarding the requirement of a separate ESG research department for research on sustainable investments, 55.6% replied ‘yes’, 11.1% said ‘no’, 22.2% were ‘not sure’ and 11.1% were ‘neutral’.

ix. The main motivations for sustainable investing in the German financial sector is illustrated in the table below:

Table 10: Motivational factors to sustainable investing in the German Financial sector

Factors	% of Responses
Secured investment independent from crisis	18.2
Add to profits in the long term	27.3
Diversification of risks	22.7
Contribute to the movement of sustainability and sustainable development	9.1
Reputation and public perception	13.6
Institutional investors are becoming more concerned and committed	4.5
Growing market size of sustainable investments	4.5
Total	100

x. The perceived barriers to sustainable investing according to the experts are provided in the table below.

Table 11: Perceived barriers to sustainable investing

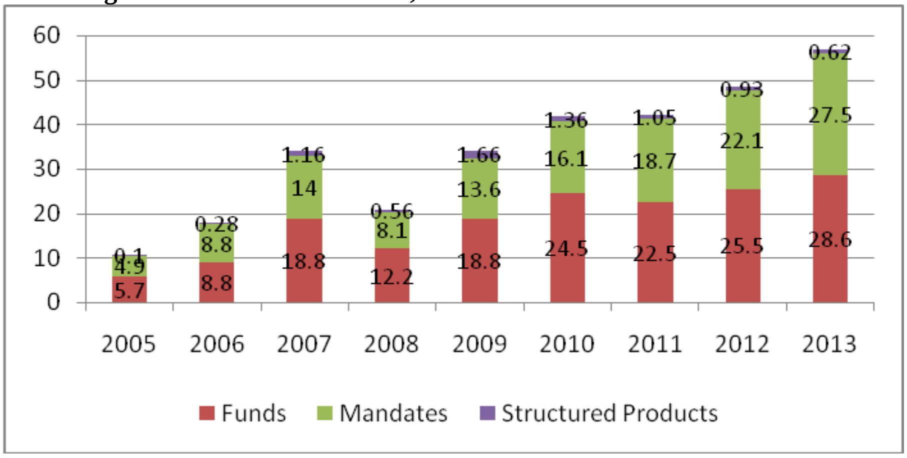
Factors	% of Responses
Lack methods to evaluate ESG risks in portfolios	17.2%
Lack of enforcement from industries and suppliers	10.3%
Lack of ESG awareness among institutional investors	17.2%
Assumption of negative returns from ESG investments by institutional investors	3.4%
Difficult to integrate non-financial factors in valuation models	13.8%
Insufficient studies to prove the positive correlation btw financial performance and ESG factors	13.8%
Lack of a proper framework to integrate ESG factors	17.2%
Cost is a big factor considering the returns	6.9%
Total	100

4. Sustainable Investment market in Switzerland and Austria

4.1. Sustainable Investment scenario in Switzerland

The sustainable investment market in Switzerland has substantially grown over the last five years. According to a report by FNG, the volume of sustainable investment market rose to CHF 56.7 billion in 2013 with a growth rate of 17% over the previous year. The salient contributors to this were investment funds, mandates and structured products. The following figure provides the details and growth of the same.

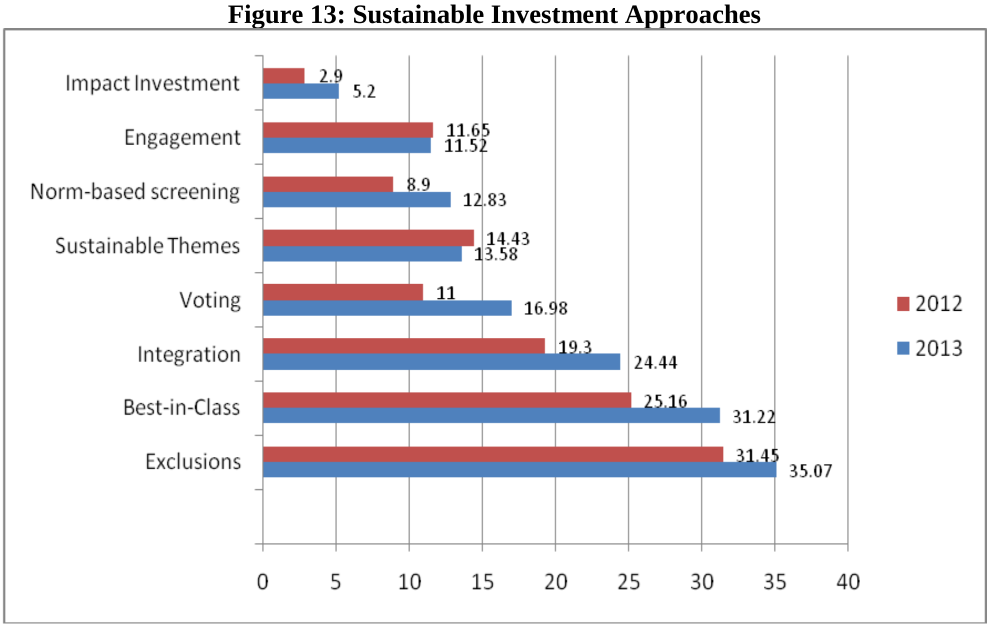
Figure 12: Investment Funds, Mandates and Structured Products



Source: FNG

The High-net-worth individuals (HNWIs) play a very important role in Switzerland. In fact, sustainable investments are increasingly becoming an attractive proposition for HNWIs. The basic motive behind sustainable investments for HNWIs is reputational factors. The strategies used by them include norms-based screening, exclusion criteria and best-in-class approach. The following figure provides the sustainable investment approaches used by the institutional investors in Switzerland.

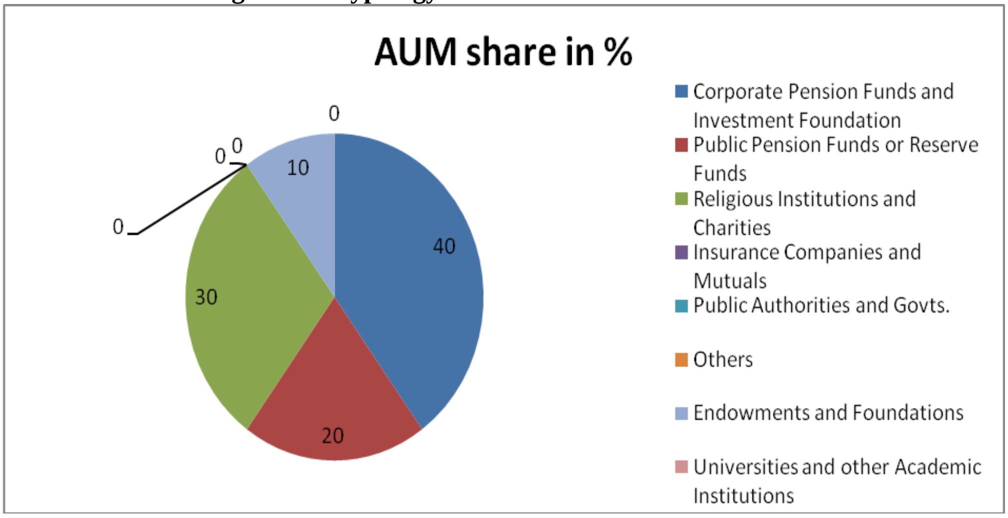
Figure 13: Sustainable Investment Approaches



Source: FNG

The typology of SRI investors in Switzerland is represented in the figure below:

Figure 14: Typology of SRI investors in Switzerland



Source: FNG

The legal and regulatory framework for responsible investments in Switzerland is evolving in a strong manner. “Guidelines for institutional investors governing the exercise of shareholder rights in Swiss listed companies”, a collaborative effort by the institutional investors, proxy advisors and business representatives has been in place. It is meant to facilitate a voluntary agreement concerning the industry’s commitment to the exercise of voting rights. Apart from this, “Klimarappen/Centime Climatique”, an industry initiative to reduce CO2-emissions, or the steering tax on CO2 emissions from fossil fuels, has also been framed. In addition to that, Switzerland has ratified the International Convention on Cluster Munitions (CCM). The corresponding legislation includes the ban of financing such weapons through direct or indirect investments, whereas the latter are prohibited if they are meant to evade direct investments.

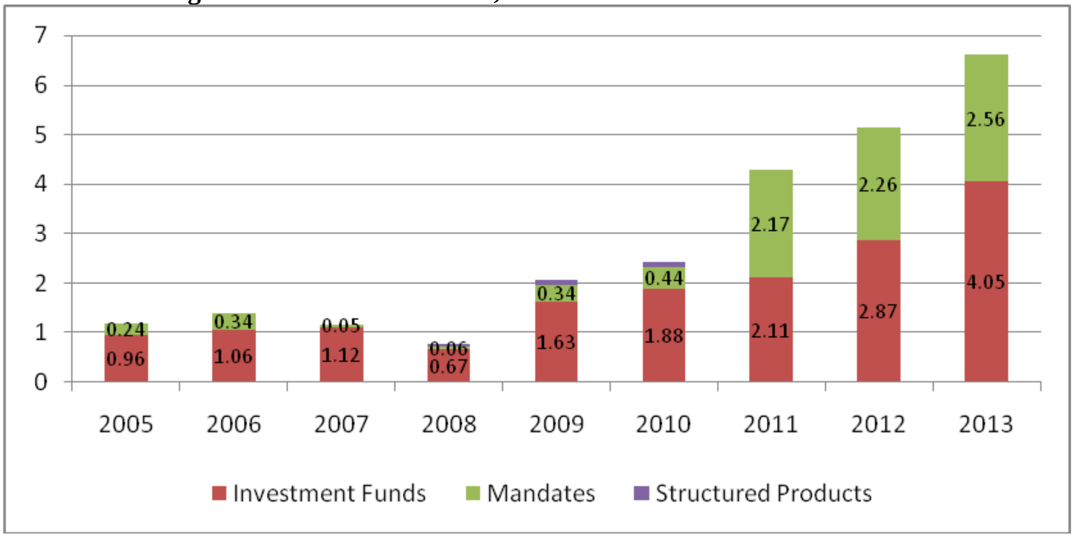
According to a survey by RobecoSam in 2014, the Pension funds in Switzerland are also increasingly factoring the sustainability aka ESG factors in their portfolio. The survey took place across 1200 pension fund members from each of Switzerland’s diverse language regions. The findings of the survey are as follows:

a. Pension fund members in Switzerland are interested in how and where the pension fund invests their money.
b. The overwhelming majority (72%) of the insured members are calling for more sustainable investment strategies from their pension funds.
c. 79% of the pension fund members believe that sustainable investment strategies lead to better long-term investment decisions.

4.2 Sustainable Investment market in Austria

Austria has also taken a strong stand when it comes to sustainable investments. The economy has witnessed a robust growth in the area of sustainable investment funds and mandates. Compared to Germany and Switzerland in the European continent, Austria is leading the way with a 4.5 % share of the sustainable segment. Both in Austria and Switzerland, corporate pension funds are the most frequent investors in sustainable investment solutions. The salient contributors to this were investment funds, mandates and structured products. The following figure provides the details and growth of the same.

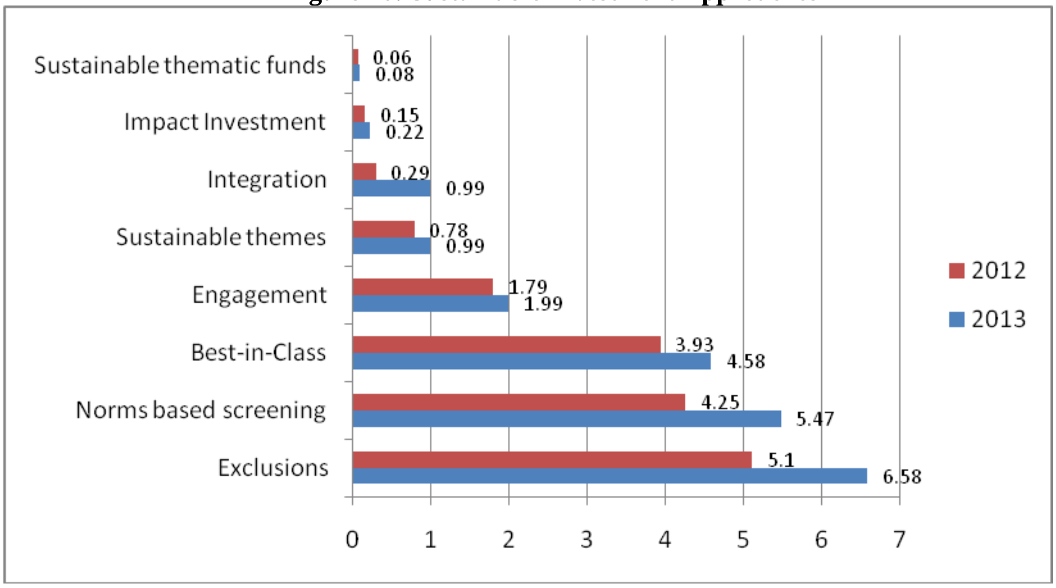
Figure 15: Investment Funds, Mandates and Structured Products



Source: FNG

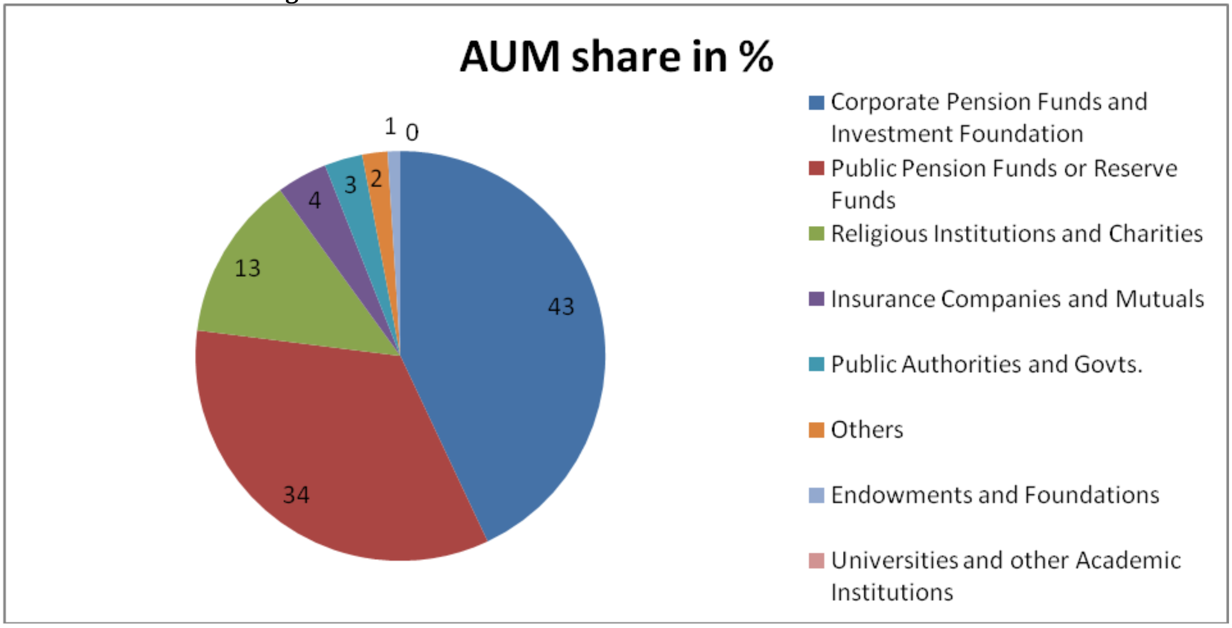
The most prevalent sustainable investment approach followed in Austria is negative screening or exclusions. Apart from this, the other approaches followed are Norms based screening, Best-in-Class, Integration, Engagement and the like. The figure below illustrates the same.

Figure 16: Sustainable Investment Approaches



The majority of SRI investors in Austria comprises of Public Authorities and Governments. The classification of SRI investors is illustrated below.

Figure 17: Classification of SRI investors in Austria



Source: FNG

The key drivers for demand in sustainable investments in Austria include demand from institutional investors, external pressure from NGO's, media and trade unions, legislations, international initiatives, demand from private investors, notion of fiduciary duty and materiality.

5. Limitations of the Study

The study which is mostly based on primary surveys in the Indian and German financial sectors is subject to certain limitations. First of all, the sample size of the survey undertaken in the Indian financial sector is small, comprising of 22 fund managers and 12 investment bankers. If the sample size is expanded, a much broader picture of the trend in ESG investing is likely to be observed. Even in the case of the German financial sector, we had to conduct a purposive sampling with a smaller segment of the academicians, ESG rating agencies and NGO's, as the direct access to the institutional investors in Germany is extremely limited. Even for the case of Switzerland and Austria, we had to depend on the secondary sources of data. Secondly, in almost all the surveys conducted, we had to mostly depend on the opinions of the respondents' as we had limited possibilities to verify their statements apart from the annual reports and factsheets. Thirdly, in all the select European counterparts not much distinction is made between the terms 'ESG investing', 'responsible investing' and 'SRI investing'. As a result of this, valuation of sustainable assets becomes difficult as the individual categories overlap.

6. Concluding Remarks

In the earlier sections, we have tried to provide a commentary on the sustainable investing scenario in India vis-à-vis the developed nations like Germany, Austria and Switzerland. It is evident that the institutional investors in India, especially fund managers and investment bankers, consider the strategic importance of ESG factors in their portfolio construction with governance issues already having caught their active attention. Likert scores, as used, have measured these custodial investors' perceptions vis-à-vis ESG factors. Although the evidences are strong in cases of bigger investment firms with smaller counterparts yet to catch up, this is however no little a fact to be ignored. The leaders in the industry are surely to be followed in the days to come. These firms would be known as trendsetters for obvious reasons. We can reasonably expect the ESG factors to be considered by the finance firms in India in greater scale in near future. As compared to this scenario, German, Swiss and Austrian firms are much ahead. The sustainable investment market in these developed nations is quite large and has been quantified in some research reports. Apart from being aware of the implications of E, S and G factors, there has been adequate quantitative analysis to prove the positive correlation of these factors and financial performance of companies. Hence, for them, 'ESG' is already a hedging tool in their hand. Even the retail and church investors are found considering ESG issues there. The significant increase in the number of green banks and ESG rating agencies especially in Germany corroborate the argument. As has been evident, corporate pension funds are the most prevalent investors in Switzerland and Austria, while in Germany, religious institutions and charitable organizations account for the major share in sustainable investments. However, ESG potential to earn extra layer of income is yet to be fully explored. On the other hand, still miles to go in India. Slow progress may be attributed to our basic risk aversion mindset. At best our findings suggest that, although a bit slow as compared to the west, the developments are evidently in the right direction.

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