



Evli Podcast Series 3

Transcript

Episode 2: Does responsible investing and ESG narrow investment spaces?

Petter von Bonsdorff: Hello and welcome back to the second episode of Evli podcast — third series. I'm your host, Petter von Bonsdorff. This is Evli.

In episode one, we discussed the changing role of environmental, social and governance; in short, ESG and responsible investments in our industry. We explored why it is the right time to address issues surrounding this matter and we talked about Evli's updated ESG strategy.

In today's episode, we take a deep dive into Evli's way of implementing ESG and RI and discuss how our strategy is intricately linked to customer strategy. To shed light on these topics I'm joined today by my two colleagues, Evli stalwarts Tomas Hildebrandt, Senior Portfolio Manager, and Janne Kujala, Head of Nordic Equity. Welcome to you both.

Janne Kujala: Thank you.

Tomas Hildebrandt: Thank you.

Petter: So, in a slight change of tack during this series I'm going to ask you guys to tell us who you are and what you do at Evli. So, gentlemen, please. Janne, you have been around at Evli for how long now?

Janne: Evli stalwart! In my case, that means I've been here for more than a decade now. I manage equity portfolios that invest in the Finnish and the Swedish stock market. I have a small gap strategy fund that invests in Finland and one that invests in Sweden. Then, I

have more of a generalist Finnish equity fund and a sundry of other direct equity portfolios that I manage – mostly in Finnish equities.

Petter: Okay. So, funds and direct portfolios in Nordic equities?

Janne: That's right. Yes.

Petter: Cool. Thomas, I've seen you for a while at Evli.

Tomas: That's right. I've been here more than 20 years now and I manage institutional portfolios, meaning insurance companies, pension funds, cities and communities and foundations portfolios. They're typically multi-asset and globally diversified portfolios.

Petter: Thank you. So, on the one hand we have globally diversified portfolios, on the other hand, we have a good knowledge of Nordic equities here. Now, let's get started here. So, today we're talking about the implementation of responsible investments across funds and investment spaces and how this benefits the investors, our clients.

Janne, I would like to begin with you. In the first episode with our other colleagues we discussed greenwashing and the idea that it is companies that do the greenwashing. In brief, what's your take on that?

Janne: Companies definitely have an incentive to do greenwashing, which, at least to me, means that you pay lip service on doing good things for the environment, but don't actually do anything concrete. And as it is with a lot of corporate communications, the language that they use is very promotional, you could say. And as an investor, you just have to cut through all that.

It's not that different from how they talk about their strategy or how great they are overall. Over time, you gain the experience of seeing through all that and that works for greenwashing as well. I think one way of making certain whether they are doing anything, or if this is just all talk and no walk, is to see whether they have ESG in their strategy. And preferably that somebody in the executive group has responsibility for this, instead of having somebody in their PR department writing PR material.

Tomas: Yeah, you said it, Janne. Corporate governance is really the key in checking if companies are just looking good or if they are doing good.

Petter: Yeah. You once said, Tomas, it's the easy investor who does green stuff in their strategies. What did you mean by that? I thought it was quite sharp.

Tomas: Well, for the easy investor, it's easy to just buy the greenwash story and that's enough. But if an investor really wants to impact and do some deeply responsible investing, then you have to do more.

Petter: That is what Janne was saying – pretending to be doing something. Going under the lid. Now, if you're looking at executive committees, for example, if they have somebody in the executive committee do you look for reporting on ESG matters as well at the company level?

Janne: Yeah, that's exactly what I do and what I want to see. That is the way to make sure that there is progress going on in the companies. That they are actually following up on what they claim to be doing.

Petter: Yeah. It's interesting to try to call that. When investors come to Evli, Tomas, is it because of our ESG strategy or is it something they learn upon working with us? What's your take over 20 years?

Tomas: Well, over 20 years, it's definitely about learning together. A decade ago, the whole ESG and responsible investing thing was taking its baby steps. And today I'd say that there are three types of clients, very much generalising of course. The first group are those for whom the issue is really irrelevant. So, they're looking for return. They're not that interested in ESG issues. That's a minority today. The largest group are clients who are looking for responsibility and ESG more from a risk management perspective and typically for guarding against reputation risks. These kinds of clients might well do some greenwashing just to have a cleaner portfolio. Some of them have more ambitious targets in their investing. Then the third group, of course, are more faith-based investors, who have very clear issues that they want to take into account in their investments and in their portfolios. From my point of view, the situation is a little bit different from Janne. He has a fund with, what do you have? Something like 70 to 100 stocks?

Janne: Altogether? Yeah, maybe.

Tomas: Whereas global portfolios have thousands of equities and bonds in the underlying funds that we use.

Petter: You can't follow all those, can you?

Tomas: That's right. And that's why we need transparency. We want to know exactly where the money is invested. We have to rely on the fund managers that we use. That they are doing their job looking into the companies and managing the funds, according to the principles that they have.

Petter: Is it enough for you that you know these other fund managers are doing that? Or do we demand something more, even from them?

Tomas: Yeah, we regularly demand all the data and we go through their investment processes. We talk with the managers. Of course, within Evli it's much easier than with somebody further away.

Petter: Do you judge them or are you happy with the transparency that they offer?

Tomas: As many of these issues are very complicated, you could say that there are several shades of grey – or green. Some clients may emphasise different issues to another, so our take is to offer a solution that fits most of the clients. If somebody wants to have specific exclusions or some specific tilts in the portfolio, then we have to look for other solutions, but everything is possible.

Petter: Yeah and then you report it further on to the investors. So, thinking about how you narrow your investment space by implementing RI, or responsible investments. Janne, do you need to narrow your space in order to have a responsible portfolio or ESG portfolio? Please.

Janne: From a practical perspective, how it affects my work is mostly in buyer exclusions that are implemented by the clients. They may want to exclude typically alcohol and tobacco and fossil fuels or other activities. In the field that I invest in, which is Finnish and Swedish equities, I don't feel that I really lose that much beyond the exclusions. I think most companies nowadays are taking ESG very seriously and seem to want to behave as responsible corporate citizens. There are, of course, industries that inherently are more problematic. But then again, I think what's important is that the companies themselves address these issues and do better within the confines of what can be done in their particular business. I'm talking about very high emitting industries, such as steel making or cement factories and so forth, which have, for example, big emissions but can have smaller emissions in the future.

Petter: Okay. So, you look at what they can do within the field of ESG in the future, not only what they're reporting today.

Janne: Yeah and also as pertaining to what we talked about earlier, that you can follow what happens to their numbers and how much more efficient they are in producing their wares.

Petter: Ok. Tomas, has your investment space been narrowed?

Tomas: When you implement responsible strategies, you always narrow your investment space to some extent and it's quite obvious because you take an active view on the markets or the world. Today, there are many different techniques to mitigate this, for example, different factors strategies are perfect for this. You can optimise a tracking error and you can do the exclusions with a narrower space. But, in the end, I think it's really a question of the beliefs of investors. The main point being that most of us think that companies which behave, that are responsible, do better in their business. This should lead to better earnings and should lead to a better performance of their equities.

Petter: So, talking about performance: do you say that there is a tangible effect of having an implemented and thought-after ESG strategy? A tangible benefit is to get either better, absolute or relative performance. This is something that concerns a lot of people.

Tomas: That's right. And so far, academic research is still out there but more and more studies are showing that implementing responsible strategies or ESG strategies don't harm your performance. So that's an important thing. In recent years, we have mostly seen that the companies that run into trouble regarding responsibility are hammered in the markets quite quickly.

Janne: ESG investing, at least as I understand it, is about taking into account all the risks and possibilities or opportunities that these companies face because of what's happening to the climate or to the society at large. So, it's also about opportunities. It's not just that you lose something there.

Petter: No, you might find something new.

Tomas: That's right. The interesting cases, I think, are those companies who are trying to make a turnaround, who are revising their strategies in different issues like climate and so on. But, typically, in the mainstream the majority of investments that are in an equity portfolio, of course, have to be high-scoring companies.

Petter: Yeah. But you can always look for new opportunities in companies with revising strategies. I think that sounds very sensible. Now, if we then move forward and focus on customer strategy, I would like to touch on the sensitive topic of inclusion versus exclusion. Tomas, again, systematic over or underperformance with exclusion of companies?

Tomas: Well, I think the question is also about how do you implement your ESG strategy? Is it an ad-hoc ESG strategy, running case by case after issues? Or, do you implement a systematic approach to the ESG issues? If you have a systematic approach, if you have a systematic under or over performance, you can compensate that with something else in that portfolio. If you're working ad-hoc, then it's really difficult.

Janne: What I've seen, especially this year in the Swedish small cap fund that we have, is that we implement exclusions there. We exclude tobacco, adult entertainment, fossil fuels, alcohol and gambling. And this year, the biggest detriment to our relative performance has been gambling stock, which has detracted, I think, close to three percentage points from our performance this year.

Now, it has been a very good year for the fund, but it would have been even a bit better if we didn't implement the exclusions that we have. Despite this very unfortunate experience this year, I wouldn't say either way that exclusions are systematically a bad thing. I think they can work in your favour in other periods. So, over the long term I don't think it will be hurting my performance.

Petter: Ok. Janne, I'm going to poke in a question here, because I think you said, 'unfortunate exclusion.' I mean, is it an exclusion according to plan?

Janne: Yeah, that's right. No, I don't think the exclusion itself is unfortunate. It's just that the events this year didn't really help out in performance in this case.

Petter: Yeah. Now, Janne, you have dealt with a faith-based investor with a responsible portfolio since 2008. Looking back, what demands were placed on you back then? How did you feel when you were told that you have to start to do ESG? What were the demands and what were you looking for?

Janne: Basic demand was pretty much the same as it is today. It's about integrating ESG into the investment process, the difference being, of course, that I didn't have any framework or tools, or any idea initially of how to do all of this. And, I mean, the world was a bit different back then. You didn't have a lot of information from companies. They didn't report their emissions and their gender balance or a lot of other things that are reported nowadays. So, it was a lot harder and you had to try to figure out your own way of doing things. I didn't have anybody to copy or follow. So, you just had to roll up your sleeves and start doing something.

Petter: Did you work with the investor and get guidance from them?

Janne: I don't think I got a lot of guidance from them. It was just more of an expectation that this is something you should be doing. Actually, not an expectation, it was a basically a demand. Over time the demand or the expectations have become stricter and the bar has been set higher. I think that is a good thing, actually. So, we probably have both evolved over this time — the client and Evli as well.

Petter: Yeah, I guess. So, it was a jump into the void actually for you at that point. That's only 12 years ago, which is pretty funny to think about now.

Tomas, the same for you because you have been selecting funds as well. You're also involved in a lot of the undertakings for responsible investments at Evli, all the different initiatives for example. Can you tell us a little bit more about those?

Tomas: Yeah, along with Janne I'd say that we we've been walking along with our clients and learning together. Getting better data, getting better tools, getting more resources to do all of this. And it's an evolution, so to say. We're not ready yet. I think ESG is evolving all the time. As an asset manager, you have to be active on different kinds of issues and fronts. Take part in different investor initiatives or the type of thing that brings more information. You learn with all this and hopefully also make some impact on the companies and on the real underlying issues, not only at the portfolio level, but in the real world.

Petter: Yeah. And that's the highest level of ESG actually that one can receive. That you do really have some impact here.

And this takes us to the end of the second podcast of the Evli podcast series. We were talking about greenwashing in the beginning. We also said that at Evli we don't judge, but we provide a good portion of transparency to our investors. We also discussed that the tangible effects of ESG strategies offer new opportunities rather than hamper portfolio results. All and more that have been discussed will be found at the Evli Hub. There will also be a written blog about the subjects and the blogs will, of course, be even more detailed.

So, thank you, Janne. Thank you, Tomas.

Tomas: Thanks for having me.

Janne: Thank you.

Petter: Pretty good to have you here. My name is Petter Von Bonsdorff. This is Evli.

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