

“Capitalism Revisited. Responsible Investors”

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DO ESG MUTUAL FUNDS DELIVER ON THEIR PROMISES?

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Is the EU Different? A Few Comparisons

- 1. Introduction**
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 - 5. EU Disclosure regulation**
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1. Introduction

- Great paper, informative and innovative!
- Interesting research questions
 - Do ESG funds offer portfolios with real investment exposure to ESG goals?
 - Do they invest and vote differently from other mutual funds?
 - Do they deliver sound performance at reasonable cost, or do they sacrifice returns to promote social causes?

2. US regulation and open questions

- *Disclosure*
 - SEC Names Rule
 - Mutual funds disclose a minimum of information in the summary prospectus
- *Fiduciary duties*
 - DOL's proposed rule (2020) as to fiduciaries of retirement plans trustees
 - The revised rule insists on the need for fiduciaries to base their investment decisions on pecuniary factors

2. US regulation and open questions

- *What does ESG mean?*
 - Absence of a clear definition
 - ESG ratings vary substantially among providers
 - ESG investing can incorporate different strategies
 - Pecuniary benefits do not always characterize ESG funds

3. Excellent empirical research and provocative conclusions

- *Interesting results*
 - ESG funds generally deliver greater ESG exposure in their portfolio allocations
 - They are more likely to oppose management in proxy voting
 - They do not cost more or perform worse than similar non-ESG funds

3. Excellent empirical research and provocative conclusions

- *A few doubts*
 - Maybe ESG funds' performance would be worse if measured on this year's results ...
 - The empirical results are measured on the averages so that greenwashing in individual cases is not excluded a priori
 - Greenwashing is mainly perpetrated by companies!

3. Excellent empirical research and provocative conclusions

- *Implications for regulatory policy*
 - The paper suggests that a regulatory response specifically targeted to ESG funds is unwarranted
 - Regulators should adopt a presumption against ESG-specific interventions in the absence of clear evidence of ESG-specific problems

3. Excellent empirical research and provocative conclusions

- The role of third-party information providers (Morningstar and ESG ratings) in improving the market is notable
 - A privately ordered system of information production would succeed in providing useful information to investors
 - ESG funds offer a promising story for capital market regulation

4. The EU approach to sustainable finance and governance

- The EU regulatory responses to the concerns regarding ESG stewardship must be considered within the emerging regulatory framework of sustainable finance
 - In 2019 the European Commission launched the European Green Deal resetting its commitment to tackling climate and environmental-related challenges

4. The EU approach to sustainable finance and governance

- Actions planned include
 - establishing an EU classification system for sustainable activities
 - clarifying institutional investors' and asset managers' duties
 - incorporating sustainability in prudential requirements
 - strengthening sustainability disclosure and accounting rule-making

5. EU Disclosure regulation

- *EU Taxonomy Regulation (2020)*
 - Establishes a unified classification system for environmentally sustainable activities
 - Provides requirements for marketing financial products as environmentally sustainable investments
 - Aims to create a cross-border market for sustainable investments
 - Addresses concerns about greenwashing

5. EU Disclosure regulation

- *EU Sustainable Finance Disclosure Regulation (SFDR)*
 - Scope and purpose
 - Financial market participants and financial advisers are required to disclose information regarding their approaches to the integration of sustainability risks and the consideration of adverse sustainability impacts
 - Aims to reduce information asymmetries in principal-agent relationships

5. EU Disclosure regulation

- General provisions
 - Pre-contractual and on-going disclosures to end-investors
 - Disclosure regards the way in which sustainability risks are integrated in investment decisions
 - It also concerns the adverse sustainability impacts of portfolio companies and relevant policies

5. EU Disclosure regulation

- Types of ESG investments
 - Article 8
 - a financial product that promotes environmental or social characteristics
 - Article 9
 - a financial product that has sustainable investment as its objective

5. EU Disclosure regulation

- Impact on practice
 - Financial market participants are given wide discretion in classification
 - Article 8 class of products is more crowded than Article 9
 - Manufacturers of products that do not belong to Art. 8 or 9 still integrate sustainability factors in portfolio management (ESG consideration funds?)

6. EU regulation of fiduciary duties

- EU Commission Delegated Acts
 - UCITS and AIFM
 - Obligation to integrate sustainability risks in the management of portfolios

6. EU regulation of fiduciary duties

- Insurance undertakings and distributors
 - Prudent Person Principle: climate and environmental risks should be effectively managed
- Investment firms
 - When identifying conflicts of interest, firms should include those conflicts that stem from the integration of clients' sustainability preferences

7. Is EU regulation of ESG stewardship flawed?

- Limits of the paper from an EU perspective
 - The empirical analysis concerns the US market and regulation
 - EU regulation of sustainable finance has a much broader scope than the problems of ESG funds addressed by the paper

7. Is EU regulation of ESG stewardship flawed?

- Questions addressed by the paper also to the EU policy maker
 - Disclosure regulation is important, but isn't too burdensome?
 - Can the market function with less mandated disclosure?
 - Are third-party information providers good substitutes for disclosure by financial market participants?
 - Are private ordering solutions better than public regulation?

The background features a dark blue field with several light blue circular patterns. These include solid and dashed lines forming circles of various sizes, some with arrows indicating a clockwise direction. A prominent circular scale with numerical markings from 140 to 260 is visible on the left side. A solid orange horizontal bar spans the width of the image, containing the text "Thank you!".

Thank you!