UNIVERSITY OF CAMBRIDGE
INSTITUTE FOR SUSTAINABILITY LEADERSHIP

Investment Leaders Group

Walking the talk: Understanding consumer demand for sustainable investing

A study by
the Cambridge Institute for
Sustainability Leadership

Publication details

Disclaimer

The opinions expressed here are those of the authors and do not represent an official position of their companies, CISL, the wider University of Cambridge or clients.

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About the partners

University of Cambridge Institute for Sustainability Leadership

The University of Cambridge Institute for Sustainability Leadership (CISL) is a globally influential Institute offering solutions for a sustainable economy. Our Rewiring the Economy plan shows how the economy can be 'rewired' through collaboration between business, government and finance institutions to deliver positive outcomes for people and environment in pursuit of the UN Sustainable Development Goals (SDGs). Our Rewiring Leadership framework sets out our model for the leadership needed to achieve this. Our interdisciplinary research builds the evidence base for practical action.

For over 30 years CISL has empowered business, government and finance leaders to shape their organisations, sectors and public policy towards sustainable economic development. Our global leadership network of nearly 9,000 individuals is now driving transformative and systemic change in every sector and on every continent. We support our clients and network to lead the transformational changes required to rewire the economy through our three interdisciplinary centres for business, policy and finance which draw on CISL's expertise in education and advisory services; acceleration and incubation; collaborative platforms and transdisciplinary research.

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The study of psychology has been organised in various forms in Cambridge for over a century. In 1912 a purpose-built Psychological Laboratory was opened on the Downing Site in the centre of Cambridge. Research and teaching in experimental psychology has continued in the Psychological Laboratory to the present day. The Department's primary objectives are to provide world-class research and teaching in psychology and cognate disciplines. The Department carries out world-class research, which is characterised by its multidisciplinary and collaborative approach. In the current QS World University Rankings, Cambridge is placed third in the world for psychology.

UNIVERSITY OF CAMBRIDGE
The Psychometrics Centre

University of Cambridge Psychometrics Centre

The Psychometrics Centre is a Strategic Research Network at the University of Cambridge dedicated to research, teaching and product development in both pure and applied psychological assessment. Founded in 1989, it has seen significant growth in recent years as a consequence of the explosion of activity in online communication and social networks. The Psychometrics Centre's mission is to establish the University of Cambridge as an international centre of excellence in all forms of psychometric assessment.

UNIVERSITY OF CAMBRIDGE
INSTITUTE FOR SUSTAINABILITY LEADERSHIP

Investment Leaders Group

Investment Leaders Group

The Investment Leaders Group (ILG) is a global network of pension funds, insurers and asset managers committed to advancing the practice of responsible investment. It is a voluntary initiative, driven by its members, facilitated by CISL, and supported by academics in the University of Cambridge.

The ILG's vision is an investment chain in which economic, social and environmental sustainability are delivered as an outcome of the investment process as investors go about generating robust, long-term returns.

*HSBC Bank (UK) Pension Scheme

Contents

Executive summary

The Investment Leaders Group (ILG) commissioned an innovative study from the University of Cambridge on consumer demand for sustainable investment. The research provides insight into how the decision-making behaviour of a sample of 2,000 US citizens is influenced by the availability of information on the environmental and social impact of funds alongside standard financial data. It reveals a strong preference for sustainable investing among the sample, even when a reduction in returns is incurred of between two and three per cent annually.

Introduction to the study

The study was conceived in cooperation with the ILG and two further research groups in the University of Cambridge, the Psychometrics Centre and the Department of Psychology. The study involved a 'virtual investment experiment' designed to reveal real investment choices of the 'investing public', ie retail investors, pension fund policy holders, and savers generally who hold their money in investment funds. For the sake of simplicity all such groups will be referred to as 'savers' throughout this report. The research aims to shed light on consumer demand for sustainable investment to allow financial institutions and intermediaries to respond with relevant disclosure, products and innovation.

The study analysed the decision-making of individual savers by inviting them to choose between pairs of differently specified funds. Based on clearly presented financial and sustainability information, participants in the study were presented with pairs of funds and asked where they would prefer to invest. In order to incentivise real investment behaviour, participants were informed that they had a chance of receiving a significant investment in one of the funds they select.

How is this experiment different?

This innovative study was designed to simulate real investment choices in order to help understand the extent to which savers value sustainability. It fills several large research gaps as set out below.

1. Use of incentive to test savers' revealed preferences for sustainability

Research studies to date have examined self-reported investment intentions, not how people behave when they are investing their own money.[1,2] In this study, participants were told, truthfully, that one of the investment choices they make is real and they may be randomly selected to receive an investment worth US$1,000 into their chosen fund. The aim was to encourage participants to treat all of the choices they made as if they represented a real investment opportunity, making it possible to test whether they value sustainability as an investment aim and, if so, the strength of their preference.[i]

2. Presentation of sustainability information in fund fact sheet format

While the financial performance of funds is readily accessible to the public, their social and environmental impact remains largely opaque, making it difficult for savers to discriminate good sustainability performance. In order to simulate real-world investment experiences, the fund information presented to participants followed a typical fact sheet format with one exception: the addition of sustainability information. The latter was based on a unique format developed by CISL for the ILG known as the Investment Impact Framework[3] (see Box 1), which applies sound science to the task of measuring and communicating the social and environmental performance of funds. In a nutshell, the framework allows savers to quickly understand the alignment of a fund with the 17 United Nations Sustainable Development Goals (SDGs).

Prior to the study, the research team ran focus groups with the public to understand how to present sustainability information clearly and concisely. These provided insight, for example, on whether to provide savers with a single sustainability 'score' (or category) or to break down information by separate social and environmental themes. The focus groups were also helpful in determining whether to provide information in quantitative or qualitative forms (eg ranked A to E), and how to label topics in understandable ways (see Annex A).

[i] In this context, sustainability is taken to embrace the social and environmental performance of an investment fund, including the impact of its assets.

3. Quantification of savers' depth of preference using trade-offs

This study explored whether – and if so, how much – participants were willing to trade off investment returns for sustainability. Importantly, there was no assumption in the research team that sustainable investing should lead to lower returns (see a metastudy[4] on this topic which finds a generally positive relationship between financial and sustainability performance). However, in order to understand savers' demand for sustainability the study required decisions over trade-offs to be analysed. As expected, funds with higher financial and sustainability performance were universally preferred. The question, however, was how quickly would savers' interest in sustainability tail off as returns were sacrificed?

Key research findings

The research team conducted the study using a sample of 2,096 US participants, with age, gender and income composition matching the US census. Key results are as follows.

How much do savers value sustainability?

Results found that the median saver would prefer a sustainable fund even if they have to sacrifice up to 2.5 per cent returns. This preference was stronger than expected at the outset of the study and provides robust evidence that information on fund sustainability affects decision-making when presented in a typical fund fact sheet format. It also demonstrates that the general public, without deep expertise of investing, can understand and act on sustainability information when it is presented clearly.

Who values sustainability the most?

Younger people (<35 years old) and inexperienced savers had a particularly strong preference for sustainable investment (after controlling for all other factors). Income level, education and gender had no statistically significant effect on preference for sustainability, and no difference in preference was detected between environmental and social sustainability themes.

What other factors influence fund choices?

Savers showed a stronger preference for avoiding funds rated poorly for sustainability (those rated E on an A–E scale) than for choosing funds with a high sustainability rating (those rated A). It would appear that the avoidance of negative environmental and social impacts is more influential over decision-making than the pursuit of positive impact.

Overall, the study demonstrates that public interest in sustainability does influence investment preferences when suitable information is provided. Combined with increased policy and regulatory attention on sustainable finance, this points to an opportunity for financial institutions and intermediaries to consider how they can meet a large-scale (and latent) consumer demand for sustainable investment.

Introduction to the study

Key principles in decision-making and behavioural economic research

Revealed versus stated preferences

One of the first things that decision-making researchers learn is not to listen to what people say, but to watch what they do. Sometimes people cannot tell you why they made a decision because they do not know themselves. Or sometimes they will explain a decision but it turns out they are deceiving themselves. This can lead to large gaps between words and actions.

The vast majority of research into whether savers (by which we mean retail investors, pension fund policy holders, and people generally who hold money in investment funds) value sustainability is survey-based[1,2] or conducted in focus groups.[5] Savers are asked questions like whether they 'strongly agree' that they prefer their money to be invested in companies that are environmentally sustainable. Such research measures attitudes to sustainability, but there is reason to believe that savers' commitment to sustainability needs a stronger test. It is easy for a saver to say that they prefer sustainable funds because it makes them feel good about themselves and there are no consequences to their choice.

Borrowing from decision-making and behavioural economic research, an incentivised choice experiment was set up to measure savers' behaviour in a situation where they had to choose between pairs of funds, in general a more sustainable investment fund and another fund with better past returns. Research participants were told that one of their choices might be selected to pay out an investment of up to US$1,000 in the selected fund. In other words, savers might experience the result of their decisions. Thus the experiment observes behaviour in a situation with potentially real monetary consequences.

Financial institutions, such as pension funds and insurance companies, have a duty to work on behalf of their savers and policy holders, and hence to reflect their investment preferences. But showing that savers 'strongly agree' that sustainability is important does not tell an investment manager whether it is more important than other factors and to what degree. So, given that investment managers are generally assessed on financial performance (for example their ability to generate returns above a benchmark), it is easy for them to concentrate on these metrics and ignore the environmental and social impacts (i.e. the sustainability) of the companies they put savers' money into.

Communicating impact to savers

Information about the social and environmental impact of a fund is typically complex and inaccessible to the public. Focus groups were therefore run to help design the precise form of the sustainability information to ensure it was clear, understandable and otherwise 'legible' to participants. This resulted in the use of an 'A–E' rating scheme for fund sustainability (A = very positive; E = very negative) similar to the scheme consumers find with electrical appliances (see Annex A). In terms of the nature of the impact information (ie the themes covered) we drew on the framework created by the ILG specifically for this purpose (see Box 1).

Box 1: Investment Impact Framework

All investment has an impact on the real world, not just money labelled 'impact investment' or other categories which are commonly associated with sustainability. To a large extent these impacts – for example job creation or natural resource consumption – are opaque to the public, with limited information available from standard information sources. To address this, the Investment Leaders Group (ILG), in cooperation with the University of Cambridge Institute for Sustainability Leadership (CISL), set out in 2014 to develop a set of measures of the social and environmental impacts of capital ownership and investment. The framework, which was originally published in 2016 as In search of impact: Measuring the full value of capital, was distilled directly from the United Nations (UN) Sustainable Development Goals (SDGs) to allow investors to understand the alignment of their capital with the world's agreed sustainability agenda, and share this in a palatable form with savers.

The framework comprises six impact themes – three social and three environmental – as follows:

Social

- Basic needs – how does my money benefit people living in poverty?
- Wellbeing – how does my money contribute to spending on healthcare, education and other public services?
- Decent work – how does my money support jobs with decent pay and working conditions?

Environmental

- Resource security – how does my money support the efficient use of resources such as wood and metals?
- Healthy ecosystems – how does my money contribute to protecting nature (soil, water and biodiversity)?
- Climate stability – how does my money help to keep global warming below 1.5 degrees Celsius?

The ILG shares a common vision of the future of impact reporting in which all funds are assessed using a common standard to allow savers to make informed choices about how and where to invest. Its framework aims to help savers choose the services they want based on a fuller understanding of the impact those choices will have.

In order to simulate the style of information on funds that participants might expect to find online or in product marketing, information was presented in a form resembling a 'real world' fund fact sheet. This approach is consistent with the recommendations of the 2018 EU Action Plan on Financing Sustainable Growth, which calls for improved disclosure of environmental, social and governance (ESG) performance of investment products. The European Commission has highlighted the importance of financial institutions better understanding their clients' sustainability preferences in order to achieve this (see Box 2).

Box 2: Mandate to better understand clients' ESG preferences

In January 2019, the European Commission published draft rules on how investment firms and insurance distributors should take sustainability issues into account when providing advice to their clients. The proposals are part of the Commission's Action Plan on Financing Sustainable Growth and amend the EU directive on markets in financial instruments (MiFID II) and the directive on insurance distribution (IDD). Until recently, few financial advisors had asked their clients about their sustainability preferences and whether they would like them to be reflected in product selection.

Quantifying savers' preference using trade-offs

Typically investment managers incorporate sustainability factors into their investment processes when they consider them financially material in order to help them gain a fuller picture of the assets they invest in and consequently reduce risk or enhance returns. A metastudy[4] from researchers at the University of Hamburg and Deutsche Asset Management, examining the relationship between sustainability and financial performance across more than 2,000 academic studies published since 1970, found a generally positive correlation, confirming the value of this approach.

While it is common sense to see why integrating sustainability risks (and opportunities) into investment processes can and should be financially rewarding, this study sought to understand the degree to which savers would accept sub-market returns in exchange for high sustainability performance. Why would we do this when we know that sustainable investment strategies can outperform rather than underperform the market? There are two reasons:

1. Firstly, a neat way to gauge savers' degree of preference for sustainability is to offer it at the expense of another desired outcome, in this case financial reward. By trading off one against the other it is possible to identify thresholds beyond which the desire for sustainability is subdued by the loss of financial reward. Far from implying that sustainable investing is loss-making, this approach reveals the extent to which savers are prepared to go to obtain it – and hence indicates what savers want from their capital. This should be of interest to financial institutions and intermediaries, particularly those acting on behalf of savers.

2. Secondly, not all sustainable investing strategies will necessarily reduce risk or enhance returns, especially over the short term. For example, exclusion strategies which eliminate certain sectors or business practices can affect returns; high concentrations of investments in subsidised green technologies could result in increased risk; and 'impact strategies' which seek positive social and environmental outcomes by definition may target sub-market returns. Again, the degree to which savers want these strategies should be of interest to financial institutions and intermediaries acting on behalf of savers.

For these reasons this study explored savers' responses to situations requiring a trade-off between sustainability and financial returns. To achieve this participants were presented a pair of differently specified funds and asked to choose between them. As expected, funds with higher financial *and* sustainability performance were universally preferred. The question, however, was how quickly would savers' interest in sustainability tail off as returns were sacrificed?

Details of the study design

Literature review

An extensive review was conducted of existing initiatives and studies exploring the value that savers place on sustainability, and how they react to different versions of impact-related information. The review yielded around 25 consumer research reports and 25 academic articles. The former exclusively constituted attitude surveys, whereby respondents were asked to report their opinions on various sustainability issues. The latter divided into two broad categories:

- attitude surveys, similar to the consumer research reports, where respondents reported opinions on sustainability issues
- experimental studies in which participants were asked to imagine they possessed an amount of money to invest among different investment products.

Nearly every study shows that sustainability does matter to savers. All other things being equal, people report that they prefer sustainable to non-sustainable investments. Similarly, in experimental settings they normally choose a sustainable product over a conventional one.

However, the literature reviewed has a number of limitations. Firstly, the majority of the studies consist of attitude surveys which, in this context, offer little insight into how savers would behave in real investment situations. In the field of social science the phenomenon of an 'attitude–behaviour gap' is well observed in which people say one thing and do another. Thus, the findings from attitude surveys that people are interested in sustainability does not guarantee that they will invest accordingly.

The experimental studies we reviewed address this phenomenon to some extent by exploring savers' choices rather than attitudes. However, a number of methodological constraints were apparent:

- None of the experimental studies involved real financial stakes for their participants. As a result, the findings from these imaginary scenarios may still not mimic savers' behaviour in real settings.
- Reliance on relatively small sample sizes, or specific groups (eg students), does not allow for rigorous statistical analyses and sound generalisation.

Besides these methodological limitations, the literature offered conflicting evidence on some issues. For example, it is not clear whether positive and negative sustainability information has a symmetrical impact on people's willingness to invest, or whether one is more influential than the other. Similarly it remains an open question whether people consider sustainability issues more within a long- or short-term investment horizon. Moreover, if savers opt to invest sustainably, is this due to their values and concerns for the world or the fact that they believe it will result in improved financial performance, or both? Lastly, how do personal characteristics such as gender, age, education and level of experience with investment affect choices, and do different impact themes affect savers in different ways?

The present study addresses the inherent methodological caveats of the past literature, in particular by providing a real financial incentive to participants.

Focus groups on presentation of sustainability information

Prior to surveying individual savers, the research team ran focus groups to obtain a cross-section of opinions on how to present sustainability information in a clear, understandable and otherwise 'legible' manner. A group of 35 people was recruited through advertisements on Gumtree, Facebook and in local press in the UK. The vast majority of focus group members reported an interest in the environmental and social impacts of their money, although it was not tested whether this interest would translate into investment choices. Focus group members also reported that they did not feel they had sufficient information to identify sustainable funds, while some felt that they may experience trade-offs with sustainable fund choices (eg poor customer service from providers or higher risks from lower diversification of assets).

Focus group members found the six themes of the Investment Impact Framework (Box 1) to be understandable and informative, although some required clarification on the surrounding terminology (eg 'revenue from low-income groups' or 'decent work'). They were split as to the best way to visualise the six themes. Some liked a table format, others a 'traffic light' format, and some preferred the 'A–E' colour-coded rating scheme used to convey the energy performance of appliances and buildings (see Annex A). The majority of focus group members preferred a more detailed format which included quantification. Not surprisingly they felt that information should be as simple and minimal as possible to communicate sustainability performance, and favoured plain language rather than specialist terms or jargon.

General study procedure

The study was conducted online, with participants recruited through a market research company, Lucid, between April and May 2019. A sample of 2,096 US residents was provided, with age, gender and income composition matching the US census. Other geographic strategies were clearly possible, but the US represents a good starting point given the scope and scale of its consumer finance market. Participants were not told anything about the study during recruitment. This ensured that they did not elect to participate out of prior interest in sustainability or investing (selection bias).

Participants were invited to click on a link sent to them via email, leading them to an online survey in which they were asked to choose between investment funds. The survey lasted approximately 20 minutes.

Participants were provided with a choice between two funds, one showing a higher sustainability rating, and the other showing equal or superior past annual returns of up to 3 per cent (0 per cent, 0.5 per cent, 1 per cent. 2 per cent and 3 per cent). The proportion of participants choosing the more sustainable fund (and hence willing to sacrifice past returns) was measured. This choice gave rise to the principal findings of the study.

The presentation of fund information mimicked the literature typically used by financial institutions to profile savings products. Hence fund fact sheets (see Figure 1) were presented for each fund, containing details of past returns, risk–reward profile, sector breakdown, country breakdown and key facts including fund size; the only additional information was a sustainability rating. Fund names were of course anonymised so that participants could not look them up. The past returns and sustainability information were crucial to the study, with other elements being randomly varied to ensure the generality of the results.

To incentivise real investment behaviour, participants were informed that five participants in the study would be randomly selected to receive a US$1,000 investment in one of the funds they chose. Although participants were not aware of this during the study, the two real funds were either an S&P 500 index tracker or a broad large- and mid-cap European index tracker.

Finally, the survey provided a free-text field for participants to comment. Two comments are included below and show that participants took the experiment seriously:

"This was interesting and different. I am a lower income senior citizen who has invested a small amount of money in the stock market. I have made a little money but I have also made a lot of mistakes. I want to do right and invest in companies that have moral and ethical convictions like myself but I also have to make some money."

Participant aged 65+

"This was truly fun. Whether I end up winning that US$1,000 in investment or not I really want to say thank you for that experience. The idea that I might win made me focus and try my best."

Participant aged 18–25

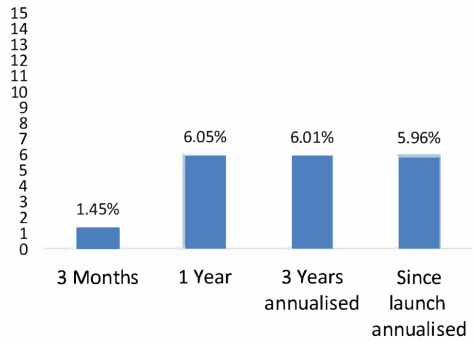
Figure 1: Example fund fact sheet used in study

Fund 1

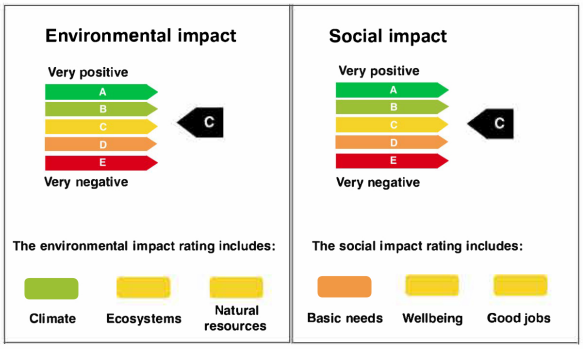
Investment objective and policy

The fund aims to grow your money by investing in shares of companies in a variety of global sectors and countries.

Performance as of June 2018



Environmental and social impact



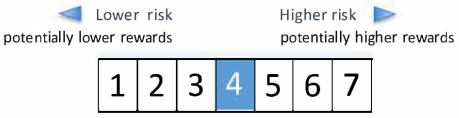
Explanation of the environmental and social impact metrics

Environmental	Social
Climate Does my money help to keep global warming below 2 degrees Celsius?	**Basic needs** Does my money benefit people living in poverty?
Ecosystems Does my money contribute to protecting nature (soil, water, and biodiversity)?	**Wellbeing** Does my money contribute to spending on healthcare, education, and other public services?
Natural resources Does my money support the efficient use of resources such as wood and metals?	**Good jobs** Does my money support jobs with decent pay and working conditions?

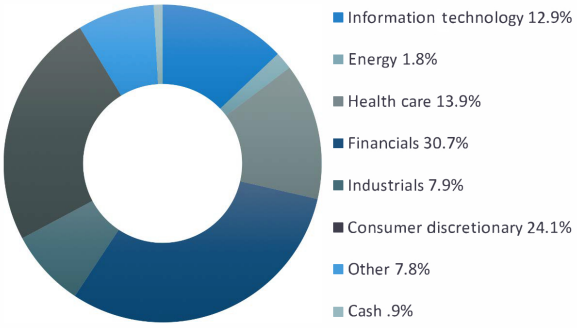
Key facts

Inception date:	14 July 2010
Fund size	$161.6m
Number of holdings	48
ISIN	US##########

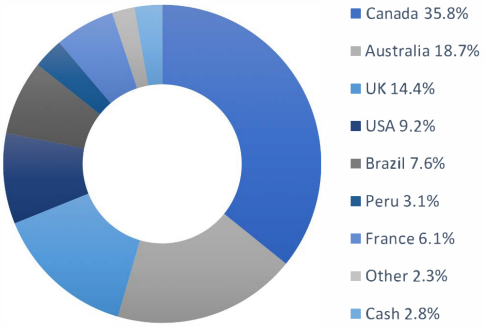
Risk and reward profile



Sector breakdown



Country breakdown



Limitations of study

The research team identified the following limitations to the study:

- **Sample:** the study was conducted with a general US sample. It will be important to test whether the findings generalise to populations in different parts of the world, and to different population segments.
- **Participants' understanding of financial information:** returns were presented in the form of annualised percentages in order to mirror real-world fund fact sheets. Alternatives could be used, for example 'US$30/year additional returns from a US$1,000 investment'.
- **Participants' understanding of sustainability rating:** based on focus groups, information was presented in a similar form to energy performance ratings for consumer goods. However, the team acknowledges that the method of presentation is key: smaller, less eye-catching graphics could reduce attention on the information and vice versa. This is an area of continuing research by the ILG.
- **Incentivised procedure choice:** participants were told, truthfully, that they may be randomly selected to receive an investment worth US$1,000. However, one could argue that some participants may have assumed they would never win it, or that the incentive was weak since participants were not spending their own money. But comments provided by participants suggested that it was taken seriously and group behaviour was consistent with careful decision-making, eg participants chose funds with higher returns, all else being equal.
- **Other considerations:** the study was based on a one-off fund choice. It would be helpful to understand whether participants would stick with their choices as returns varied over time, or switch into or out of sustainable choices as performance unfolds and they experience the consequences of their decisions.

How much do savers value sustainability?

Using an incentivised investment experiment, this study quantified how much savers value sustainability in their fund choices.

Key finding: the median saver would prefer a sustainable fund even if it means having to sacrifice up to 2.5 per cent of annual returns

Figure 2 shows that when the two funds' past returns were equal approximately 75 per cent of savers preferred the more sustainable choice. When the sustainable fund's past returns were decreased, fewer people chose it. This is to be expected. However, what was surprising was the degree of willingness of the participants to back the sustainable fund: the median saver was prepared to do so even if it meant sacrificing a 2.5 per cent annual return.

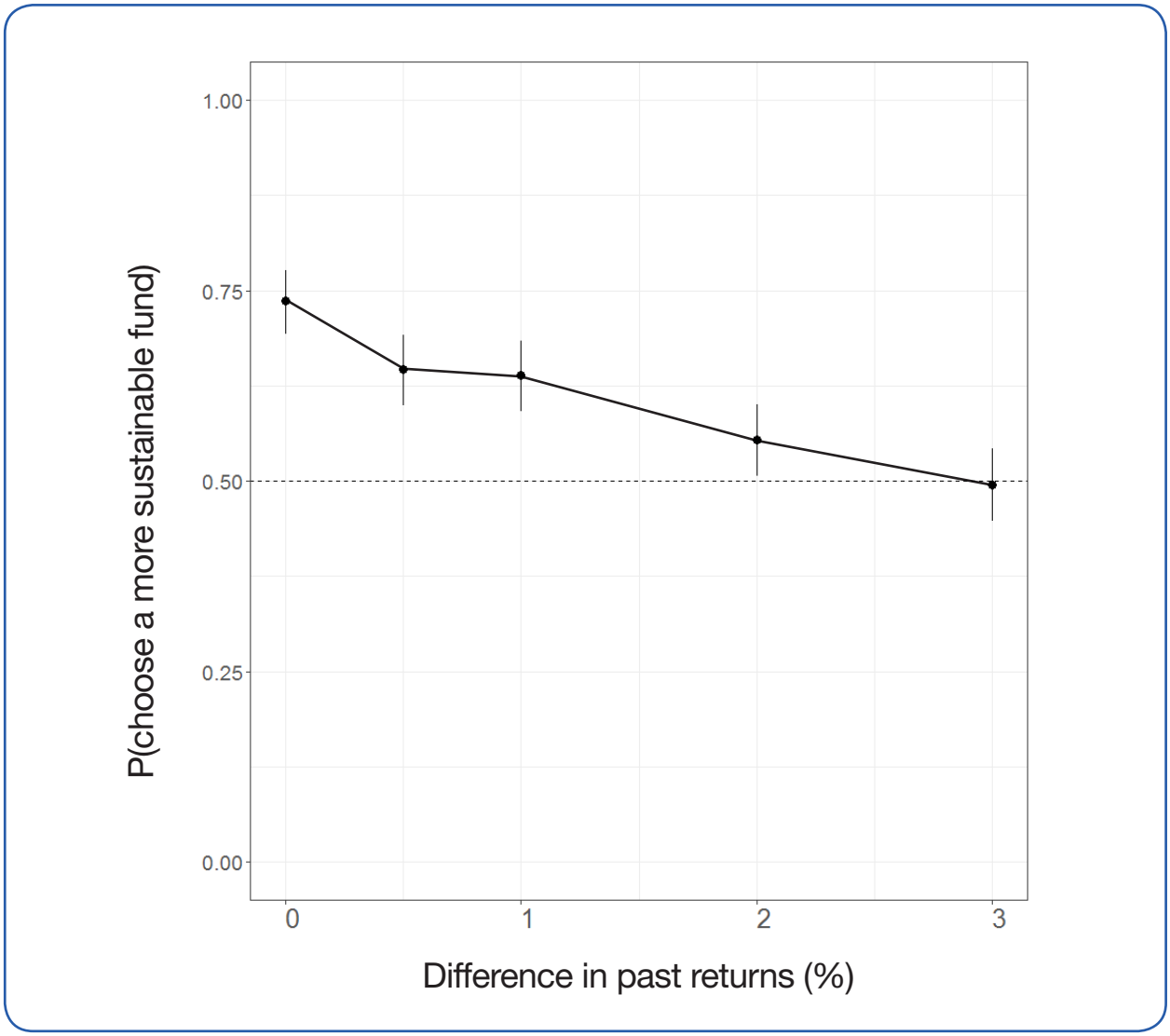
What about the 25 per cent of participants who did not choose the more sustainable fund when past returns were equal? To make the experiment as real as possible, the sector and country breakdown, and risk level, of funds was randomly varied. Participants may therefore have chosen the less sustainable option because they had a preference to invest in certain sectors, geographies or risk levels. Alternatively, they may simply believe that a sustainable fund is likely to do worse in the future regardless of past returns. These or other explanations mean that not everyone can be expected to choose the sustainable fund.

Interestingly, despite large numbers of participants showing interest in sacrificing up to three per cent annual returns for the more sustainable fund, one participant injected the following dose of realism:

"I think if you really want to test where money would be put you need to lessen the differences between the two funds (returns-wise). That would ideally help define the 'cut-off' point for an investment with a more ESG focus. In my examples three per cent annually is a HUGE difference, but if it was closer to one per cent then I may look at the ESG fund more... but not for 300 basis points."

Experienced saver participant

Figure 2: Proportion of participants choosing the more sustainable fund as its past returns are varied between zero and three per cent lower than the alternative fund (the y-axis represents the proportion of people choosing the sustainable fund option and the x-axis represents the difference in past returns between the funds).



Who values sustainability the most?

The study tested whether sustainability was particularly valued by different age groups, genders, income levels and other factors. The general statistical approach was as follows:

1. Examine each variable after controlling for all other variables.

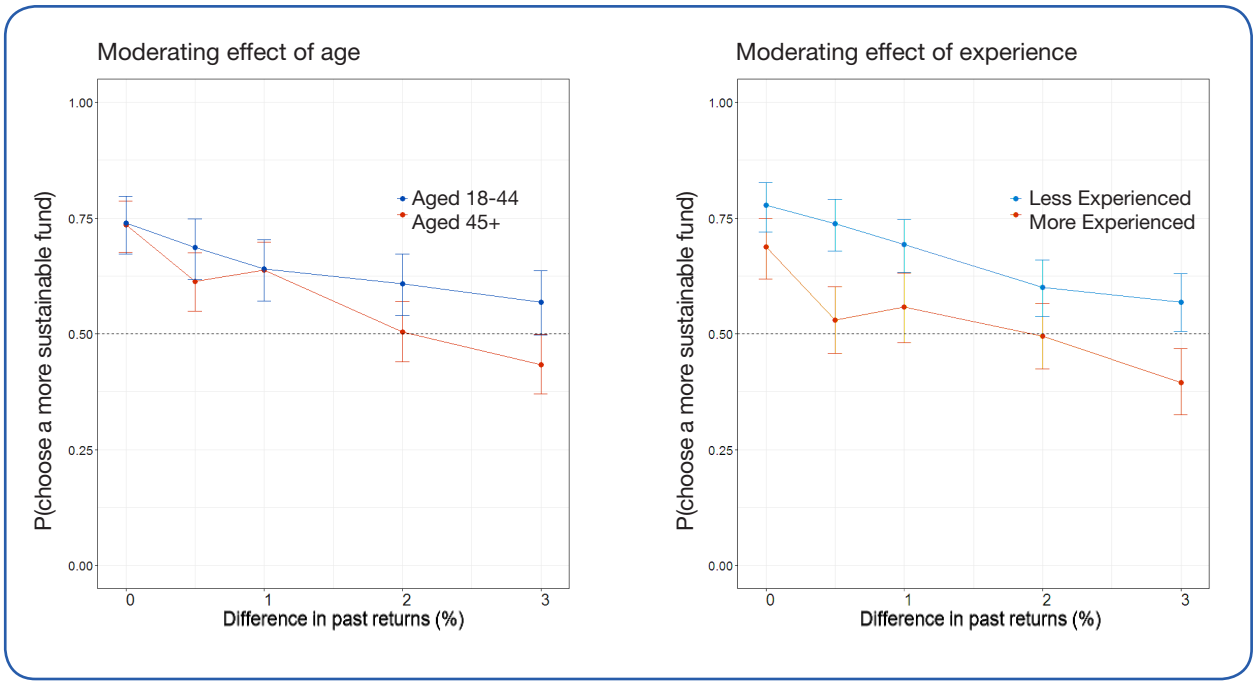
2. Respond to two questions:

   - Is there an effect when the more and less sustainable funds have the same past returns?
   - Does the variable affect sensitivity to differences in past returns?

Finding: younger people have a stronger preference for sustainable funds

Statistical analysis indicated that, after controlling for other variables, younger participants had a stronger preference for sustainability compared to older people.[7] Specifically, younger people were more prepared to sacrifice past returns as illustrated in Figure 3. Note that when the funds have the same past returns, younger and older participants showed a similar level of preference for the more sustainable option, but the older participants were more sensitive to an increasing differences. Correspondingly, the oldest half of the sample were willing to sacrifice around two per cent past returns for sustainability whereas the younger half were willing to sacrifice even beyond three per cent.

Figure 3: Effects of age (left) and experience (right) on preference for sustainability (the y-axis represents the proportion of people choosing the sustainable fund option and the x-axis represents the difference in past returns).



Finding: inexperienced savers have a stronger preference for sustainable funds

Participants were asked to self-report their experience with investing (from 'not at all experienced' to 'extremely experienced'). This parameter is not related to the age of the participants but rather their familiarity with investment practices. Those who answered that they are less experienced had a stronger preference for sustainability between funds with the same past returns, and this preference persisted as the difference in past returns increased. Figure 3 shows that more experienced participants were willing to sacrifice approximately 1.5 per cent past returns for sustainability, whereas the less experienced ones were willing to sacrifice more than three per cent.

Finding: other individual differences did not affect preference for sustainable funds

The study explored whether gender, income and educational level affected preference for sustainability. No differences were found: women and men showed a similar preference for sustainable funds, as did those with higher or lower incomes and those at different educational levels.

What other factors influence fund choices?

The study tested three further factors with potential influence over fund choices:

- whether participants preferred to invest in positively sustainable funds or, alternatively, to avoid funds with negative sustainability ratings
- whether savers particularly value environmental or social sustainability themes
- whether the value placed on sustainability depended on the 'baseline' level of past returns of the less sustainable fund option.

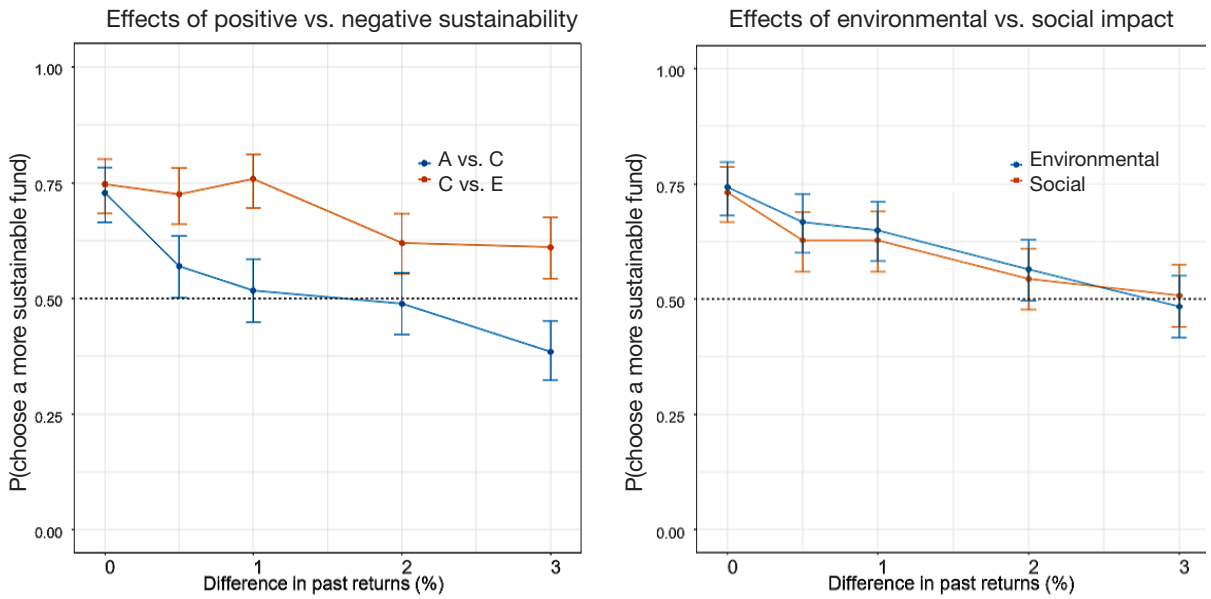
Finding: savers prefer to avoid the most unsustainable funds

The sustainability performance of funds was rated on a five-point scale, from A (very positive) to E (very negative). Two conditions were tested:

- The more sustainable fund is rated A against an alternative fund rated C (this is the positive sustainability condition).
- The more sustainable fund is rated C against an alternative fund rated E (this is the negative sustainability condition).

After controlling for other variables, it was observed that the avoidance of an E rating had a much stronger impact on fund choices than the pursuit of an A rating (see Figure 4). In other words the negative condition was more influential than the positive condition.

Figure 4: Effects of positive vs. negative sustainability (left), and environmental vs. social impact (right), on preference for sustainable funds (the y-axis represents the proportion of people choosing the sustainable fund option and the x-axis represents the difference in past returns).



Finding: there was no difference in preference between environmental and social impact

The format used to communicate fund sustainability had separate ratings for environmental and social impact (see Annex A). These ratings were manipulated so that the more sustainable fund option was better only in its environmental performance or only its social performance in order to test whether one or other of these conditions was more influential. Figure 4 shows that no (statistically significant) evidence to this effect was observed.

Finding: there was no effect of 'baseline' past returns

It was hypothesised that in an investment environment of low average annual returns, savers may be less inclined to give up returns in favour of sustainability. Two levels of 'baseline' past returns were therefore introduced for the less sustainable fund option: nine per cent and six per cent. However, the results showed that this factor did not affect the strength of participants' preference for the sustainable fund option.

Conclusions and reflection

Consumers are ready for sustainable investment

This study sheds light on whether savers value sustainability in a situation with real monetary consequences. The revealed preference test of investor behaviour found that the median saver was willing to sacrifice up to 2.5 per cent past returns to invest in a sustainable fund.

This result is stronger than initially expected. Conversations with investment experts suggested that the trade-off point would be nearer to 0.25–0.5 per cent, with higher figures considered outlandish. Some subgroups in the sample showed an even higher appetite for sustainability than was measured using our survey instrument (which explored only up to three per cent).

The results offer robust evidence that savers value fund sustainability, and that suitably crafted information on the environmental and social impact of funds will influence decision-making. It also demonstrates that the general investing public can understand and act on sustainability information without the need for deep expertise provided that it is presented in a legible manner.

The findings of this experiment should encourage financial institutions to offer savers far greater levels of transparency with respect to the sustainability performance of investment products. Robust, scientifically valid and consistent measures of fund environmental and social impact are needed to allow savers to make more informed choices on the basis of what they want their capital to achieve both financially and in society (see Box 1 for an example measurement framework).

Millennials are a key target population

The study confirms that people younger than 35 years old are particularly motivated by sustainable investing, presumably in order to align their investment with personal values. It could be argued that younger people have inherently longer investment horizons as a consequence of their age, particularly with regard to pension products, and so it is easier for them to do without the highest possible returns. Another way to look at this is that millennials will live with the consequences of environmental and social damage for longer than older people and so have most to gain from avoiding further harm.

Savers are particularly keen to avoid negative sustainability impacts

The study found that savers wish to avoid unsustainable investment. This finding is important for financial institutions and intermediaries seeking to offer products which meet their clients' aspirations. The finding that savers are motivated more strongly by the prospect of avoiding harm should not be seen as competing with positive sustainability strategies (indeed it seems complementary), merely that harm avoidance is the stronger motive.

An opportunity exists to align with public policy

The European Commission's Action Plan on Financing Sustainable Growth, the EU directive on markets in financial instruments (MiFID II) and the directive on insurance distribution (IDD) propose that ESG considerations are included in the advice that investment firms and insurance distributors offer to individual clients. This study may be particularly helpful to financial institutions and intermediaries tasked with implementing these proposals. The message is clear: knowing your clients (KYC) means understanding how to furnish them with effective sustainable investing solutions.

The study also informs the debate on appropriate ways to communicate sustainability information to savers and other financial consumers. The European Securities and Markets Authority (ESMA) clearly states that "manufacturers and distributors should specify with a meaningful level of granularity which ESG preferences the investment product fulfils".[8] The focus groups consulted during this study, and prior work by the ILG and CISL on impact measurement (see Box 1), confirm the need to convey complex, quantitative information on fund sustainability to consumers in a simple, concise format usable by non-specialists.

There is more work to be done

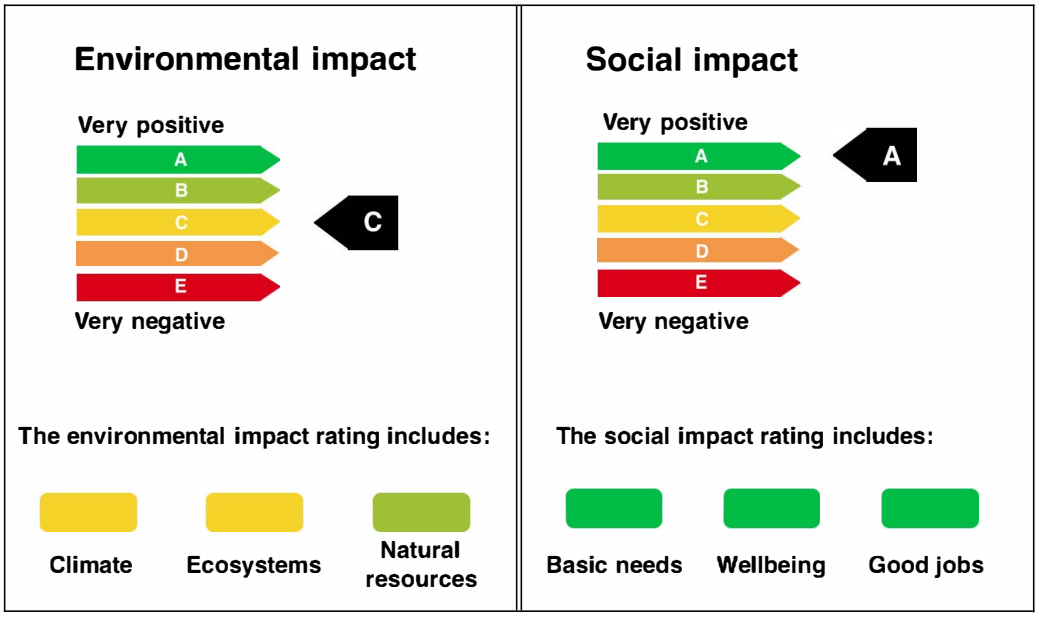
A number of new avenues of research have been opened up by this initial study, as highlighted below:

- Replicate the study with a larger sample (geographically and with superior targeting of groups of interest).
- Explore in more detail differences in behaviour based on gender and income.
- Refine parameters of the study (wider returns differences, alternative baselines, more varied sustainability ratings).
- Continue exploring communication methods for sustainability information.
- Explore perceptions of the relationship between sustainability and returns among savers (beliefs).
- Run the study over time to understand loyalty to fund choices (longitudinal study).

Overall, in confirming market demand for sustainable investing it is hoped that this study will offer valuable insights for financial institutions and intermediaries, while providing reassurance that better communication practices on fund sustainability will be valued by savers. As savers become better acquainted with the issues, and policymakers seek greater disclosure and standardisation in the market, the volume of capital deployed in sustainable funds is likely to grow rapidly and, with it, the contribution of the public to financing the SDGs.

Annex A: representation of fund sustainability performance

There are many possible ways in which fund sustainability can be represented to savers. In order to arrive at a format which is clear, understandable and otherwise 'legible' to the sample of people involved in this study, the formats were tested prior to the study with focus groups. The graphic below shows the format agreed for use in light of the feedback received. This information was included in the fund fact sheets presented to participants.



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[7] Throughout this report, where the results say that there was a difference between groups this has been tested statistically and it indicates that the p value is <.05. When no difference is reported, then p >.05.

[8] European Securities and Markets Authority (2019). Final Report: ESMA's technical advice to the European Commission on integrating sustainability risks and factors in MiFID II. ESMA35-43-1737. Paris, France: European Securities and Markets Authority.